

COMPANIES MENTIONED

Applied Industrial

AIT - \$47.27 - Hold

Fastenal

FAST - \$49.15 - Hold

W.W. Grainger

GWW - \$268.96 - Hold

MSC Industrial Direct

MSM - \$78.06 - Hold

BB&TCM's Fastener Distributor Index: Intrigue in an Otherwise Subdued October**KEY TAKEAWAY**

On the surface, little changed with the FDI in October. The index rose and was back above 50, but given the weak reading in September that was not surprising. Pricing is still subdued. This seems to accurately reflect on-the-ground demand, as Fastenal and Applied Industrial both noted demand through October was weak. The month was intriguing in a sense. Employment got better, while inventory dynamics seemed to move more favorably. Whether this is a precursor to a better overall FDI is still unclear. But it certainly is worth watching.

KEY POINTS

About the Fastener Distributor Index (FDI). The FDI is a monthly survey of NorAm fastener distributors, conducted with the **FCH Sourcing Network**. It offers insights into current trends/outlooks. As a diffusion index, figures above 50 signal strength and below 50 signal weakness. It should be directly relevant to Fastenal and broadly relevant to other distributors (W.W. Grainger, MSC Industrial).

October FDI: Is That Progress? October's 52.7 improved on September's 45.4. We are not surprised, as conditions really did not justify such a weak September. The volatile Sales component swung favorably, reversing the plunge in September. And taking Sept./Oct. together the average is still sluggish (49.0). Yet, it was the highest level since March. Employment was a bit perkier. Respondent Inventories are still "too high" but to a lesser degree than we have seen all year (so drew down). And Customer Inventories are still "too low" but to a lesser degree than we have seen all year (so a bit of re-stocking). *The number is not great, viewed in the context of the prior month. However, some favorable movement in employment and inventory data is encouraging. There is no reason to move off our cautious stance. But perhaps there is cause to watch a bit more carefully.*

The outlook remains favorable. In October, ~54% of respondents still see better conditions in six months (same as September) while just ~4%, think things will worsen (vs. 6% in September). *There remains little fear that the business cycle will take a turn for the worse any time soon; sentiment remains favorable.*

Price: still at low levels, likely to stay there (based on supplemental). As in September (and August), sequential and annual price readings improved in October, but the lion's share of respondents still report no change. Pricing continues to run in the low single digits. Our supplemental question this month asked respondents what they expected to realize in pricing in 2014. Most (~54%) expect pricing in 2014 to look much like it has in 2013: "flattish". But 32% expect to realize pricing of 3%-plus, far better than those that expect to see pricing fall by 3% or more (4%). *More of the same is expected from pricing in 2014, which is to say minimal. But at least there is little expectation for material pricing pressure.*

What does this mean for other distributors? As yet, the strong PMI readings have not been mimicked by the FDI. Based on the company reports that have come out, the FDI is giving a more reliable picture of the environment facing fastener distributors. **Fastenal**, for instance, reported October DSRs that we would consider a disappointment. **Applied Industrial**, when it reported, noted conditions through October remained difficult. Comments from respondents were mixed. *Clearly, the first month of Q4'13 has started slowly.*

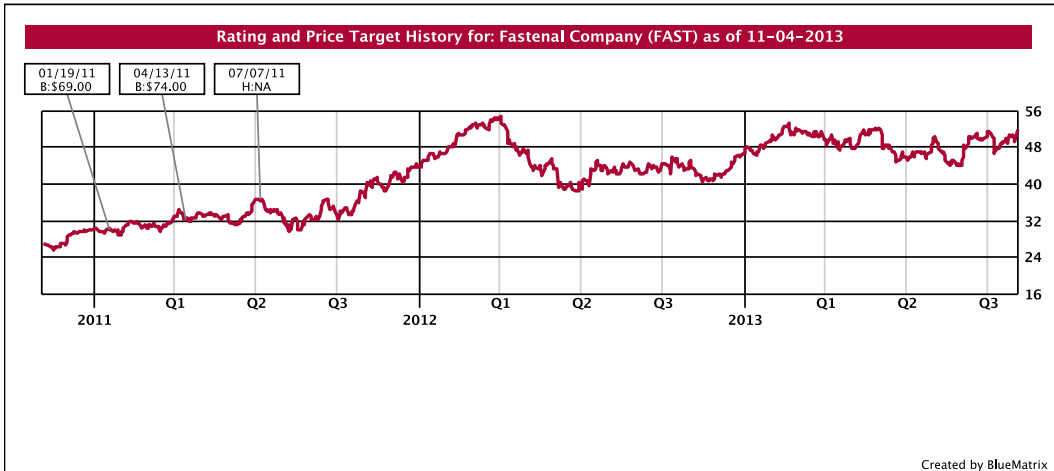
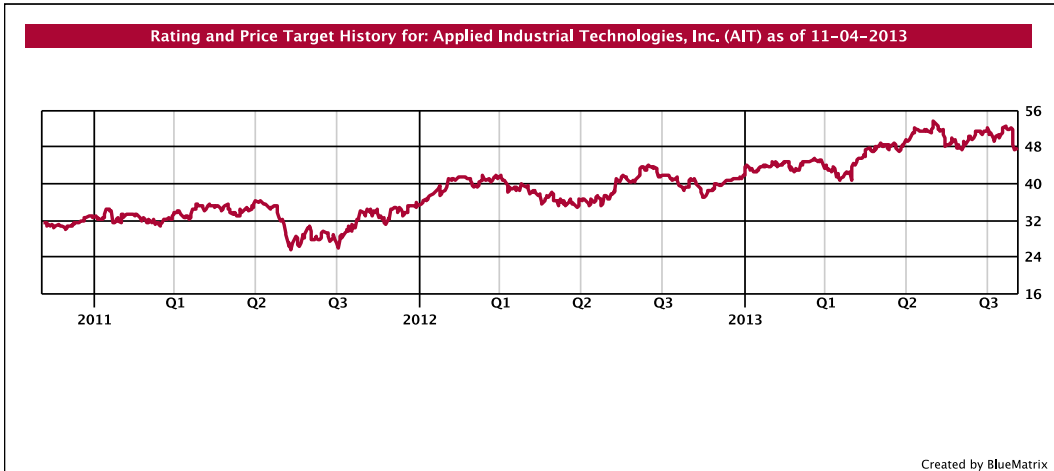
FASTENER DISTRIBUTION AT A GLANCE												
October 2013												
	----- Index Values -----										Sep.-->Oct.	
	Oct.	Sep.	Aug.	July	June	May	Apr.	Mar.	Feb.	Jan.	Change	Direction
PMI (Overall mftring sector)	56.4	56.2	55.7	55.4	50.9	49.0	50.7	51.3	54.2	53.1	0.2	Growing
FDI (Fastener distribution)	52.7	45.4	50.8	49.7	51.3	52.4	51.6	52.8	48.7	56.9	7.3	Growing
Sales	73.2	42.9	58.1	58.3	50.0	63.9	68.8	58.3	48.7	82.8	30.4	Growing
Employment	53.6	50.0	50.0	51.4	57.1	56.9	45.3	56.9	56.4	60.3	3.6	Growing
Supplier Deliveries	44.6	52.9	59.7	56.9	60.7	51.4	53.1	52.8	47.4	44.8	(8.2)	Speeding Up
Respondent Inventories	55.4	62.9	66.1	62.5	69.6	55.6	60.9	68.1	60.3	65.5	(7.5)	Too High
Customer Inventories	39.3	35.7	35.5	31.9	37.5	37.5	39.1	43.1	42.3	39.7	3.6	Too Low
Pricing, month-to-month	55.4	54.3	56.5	52.8	48.2	56.9	54.7	50.0	52.6	56.9	1.1	Higher
Pricing, year-to-year	62.5	62.9	62.9	55.6	58.9	65.3	65.6	56.9	62.8	60.3	(0.4)	Higher
	<u>Higher</u>	<u>Same</u>	<u>Lower</u>									
6-Month Outlook - Oct.	54%	43%	4%									

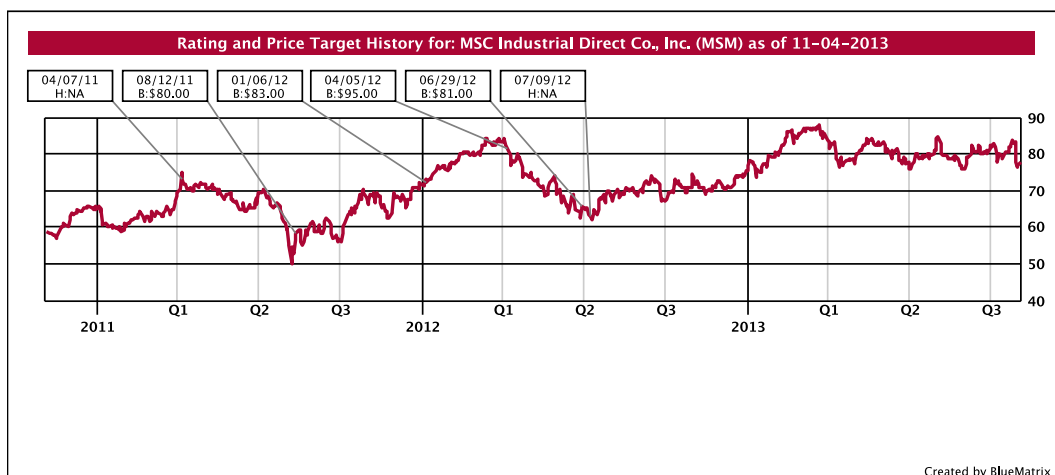
FDI and Pricing are diffusion indexes. At 50, the performance of the category listed met expectations. A reading above 50 suggests the category outperformed expectations, while a reading below 50 suggests the category underperformed expectations.

Sources: BB&T Capital Markets' estimates, FCH Sourcing Network, Institute for Supply Management

IMPORTANT DISCLOSURES

Price Chart





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B: Buy **H:** Hold **UW:** Underweight **NR:** Not Rated **NA:** Not Applicable **NM:** Not Meaningful **SP:** Suspended

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