# <u>Fastener Distributor Index – Report #133 January 2023</u>

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#### **Key Takeaway:**

The seasonally adjusted *Fastener Distributor Index* (FDI) began 2023 with another sub-50 reading, albeit modestly improved over the previous month with a reading of **47.7**. Commentary was mixed as some respondents pointed to still-strong customer backlogs and solid demand, while others saw significant slowing and cancellation of large blanket orders. Looking ahead, the *Forward-Looking Indicator* (FLI) continued to retreat further with a downbeat **41.4** reading, suggesting participants largely expect further softening. Overall, the FDI/FLI continue to suggest a slowing demand backdrop for fasteners.

Fastener Distribution Trends: January 2023

FASTENER DISTRIBUTION AT A GLANCE January 2023											
	Index Values										
	Jan	Dec	Nov	Oct	Sep	Aug	Jul	Jun	May	Direction	Change
ISM PMI (Manufacturing)	47.4	48.4	49.0	50.2	50.9	52.8	52.8	53.0	56.1	Declining	Faster
FDI	47.7	43.8	54.9	44.3	47.6	52.6	46.1	53.8	52.7	Declining	Slower
FLI	41.4	45.0	42.0	42.2	47.5	47.4	58.1	51.5	55.4	Declining	Faster
(Other Metrics)											
Sales	44.7	37.9	59.8	27.9	43.9	51.9	43.2	65.5	56.3	Declining	Slower
Employment	48.1	50.0	57.9	53.6	47.8	53.4	62.5	59.1	62.9	Declining	Faster
Supplier Deliveries	44.4	40.3	47.4	46.4	54.3	55.2	52.1	65.2	69.4	Declining	Slower
Respondent Inventories	72.2	71.0	72.4	69.6	58.7	72.4	66.7	63.6	62.9	Growing	Faster
Customer Inventories	55.6	45.2	55.3	48.2	39.1	46.6	27.1	28.8	27.4	Growing	Faster
Pricing, month-to-month	53.7	58.1	52.6	53.6	52.2	65.5	68.8	68.2	77.4	Growing	Slower
Pricing, year-to-year	74.1	75.8	78.9	87.5	87.0	91.4	91.7	90.9	95.2	Growing	Slower
	Higher Same Lower										
6-Month Outlook - January						37%	30%	33%			

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.

Source: Baird, FCH Sourcing Network, Institute for Supply Management

**About the Fastener Distributor Index (FDI).** The FDI is a monthly survey of North American fastener distributors, produced and conducted by the **FCH Sourcing Network** and **Baird**. It offers insights into current fastener industry trends/outlooks. Similarly, the Forward-Looking Indicator (FLI) is based on a weighted average of four forward-looking inputs from the FDI survey. This indicator is designed to provide directional perspective on future expectations for fastener market conditions. As diffusion indexes, values above 50.0 signal strength, while readings below 50.0 signal weakness. Over time, results should be directly relevant to **Fastenal (FAST)** and broadly relevant to other industrial distributors such as **W.W. Grainger (GWW)** and **MSC Industrial (MSM)**.

### **Key Points:**

**FDI slightly improves vs. last month but remains well into contractionary levels.** The seasonally adjusted January FDI (47.7) slightly improved off last month's 43.8 reading – which was the lowest reading since April 2020. However, the index remains <50, indicating conditions continued to worsen vs. last month – just at a slower rate than in December. The sales index told a similar story, coming in at 44.7 vs. 37.9 last month. 37% of respondents this month saw sales above seasonal expectations vs. just 16% last month. The sales index and customer inventory index drove the slight m/m overall improvement in the FDI, with employment slightly worse vs. last month.

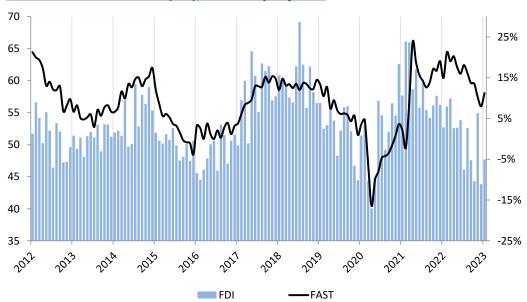
**FLI continues to decelerate.** The FLI registered a 41.4 reading, retreating further from last month's 45.0 reading and signaling additional slowing is likely ahead (still sub-50). In addition to weaker employment, higher respondent and customer inventory levels drove the continued drop in the FLI. The six-month outlook was modestly improved, however, with 37% of respondents anticipating higher activity levels six months from now vs. today compared to 26% in December. This level of optimism nonetheless remains below the 44% average seen over the past two years. Conversely, 33% expect lower activity levels (December was 29%) vs. an average of just ~19% over the past two years. Finally, 30% expect a continuation of December trends over the next six months. Expectations for a mild recession and slowing demand in certain markets were commonly expressed outlook themes.

**FDI employment reading also slightly softer m/m.** The FDI employment index came in at 48.1 for January vs. 50.0 last month. Employment levels continue to be seen as generally at appropriate levels (81% of responses), while just 7% said employment levels were too high and 11% said they were too low. Turning to the overall economy, the January jobs report came in well above expectations. 517,000 jobs were added vs. economist expectations for +187,000. A cooling labor market remains key toward the Federal Reserve eventually pausing rate hikes, but to this point the labor market has remained persistently strong.

Outlook improves for third consecutive month but still muted, overall. Forward-looking commentary suggested general expectations for softening throughout 2023, with degrees of variance +/-. One respondent anticipates a mild recession with some geographic differences: "I believe there will be a mild recession this summer, but I do not expect it to affect all areas of the country equally. I think Southern Florida (for example) will be largely spared. I think parts of California and New York will be hammered." Others see a relatively balanced outlook, with some markets seeing growth and others contracting: "Large blanket orders that were placed due to manufacturer/wire extended lead times in 22Q4 we have received requests to cancel from our customers. Working to balance the cancellations has led to good discussions with customers. Good customers are more open to working together this year compared to past years. We see market sectors that will be slow until 23Q4 while other markets continue to grow. Box of chocolates." Still others remain optimistic based on customer backlogs: "I'm hearing all this doom and gloom from the press, but I'm not seeing it with the orders from my customers. Many of my customers have 6-9 month backlogs."

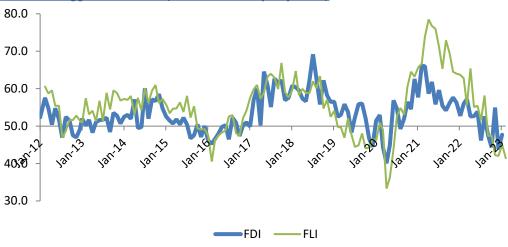
**Fastenal** reported January daily sales growth of +11.2%, nicely exceeding our +6.2% estimate and in line with normal seasonality. This included +11.6% y/y growth in fasteners, +6.2% safety growth, and +14.1% other non-fastener growth. Looking forward, we model overall February daily sales growth of +9.3% y/y – moderating vs. January which is consistent with deceleration in the FLI. Looking at 2023 overall, we generally model slightly weaker-than-seasonally-normal sales given the string of sub-50 FDI/FLI readings, a sub-50 ISM PMI, and an over-arching assumption that recession hits in 2H23.

## Fastener Distributor Index (FDI); Seasonally Adjusted



\*FAST March 2020 – December 2021 Monthly Sales Presented as ex. Safety Products Source: Baird, FCH Sourcing Network, Company reports

## 1-Month Lagged FDI vs. FLI (Both Seasonally Adjusted)



Source: Baird, FCH Sourcing Network

## **Risk Synopsis**

Fastenal: Risks include economic sensitivity, pricing power, relatively high valuation, secular gross margin pressures, success of vending and on-site initiatives, and ability to sustain historical growth.

Industrial Distribution: Risks include economic sensitivity, pricing power, online pressure/competitive threats, global sourcing, and exposure to durable goods manufacturing.

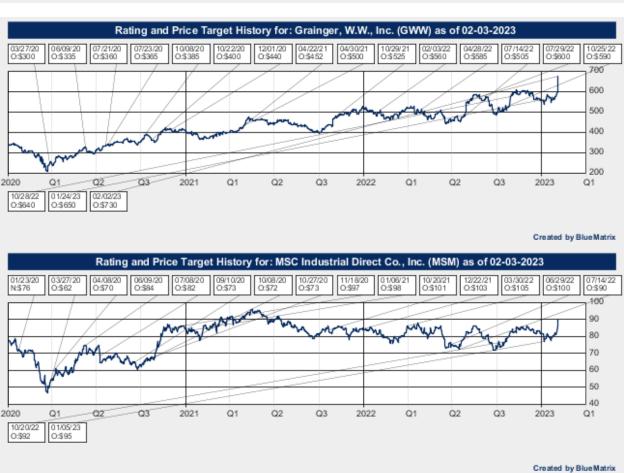
# **Appendix – Important Disclosures and Analyst Certification**

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All stock prices below are as of 2/6/2023.

Fastenal Company (FAST-\$53.22-Neutral) W.W. Grainger Inc. (GWW-\$674.40 -Outperform) MSC Industrial Direct Co. Inc (MSM-\$88.85 -Outperform) (See recent research reports for more information)





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