Fastener Distributor Index – Report #125 May 2022

Written by R.W. Baird analyst David J. Manthey, CFA with Quinn Fredrickson, CFA 6/7/22

Key Takeaway:

The May seasonally adjusted Fastener Distributor Index (FDI) was essentially unchanged vs. last month, remaining in modest growth territory at **52.7**. Container/import logistics constraints and slowing growth were consistent themes among respondents. The pricing indices were also stable but at very high levels, as higher import costs and raw material pressures continue to drive out-sized fastener pricing. The Forward-Looking Indicator (FLI) was also consistent with last month at **55.4**, as higher employment levels offset a weaker six-month outlook. Net, we believe growth and overall market conditions in May were stable m/m, with the overall index indicative of continued but moderating growth.

Fastener Distribution Trends: May 2022

FASTENER DISTRIBUTION AT A GLANCE
May 2022

	---------- Index Values							----------		Rate of
	May	**Apr**	**Mar**	**Feb**	**Jan**	**Dec**	**Nov**	**Oct**	**Direction**	**Change**
ISM PMI (Manufacturing)	56.1	55.4	57.1	58.6	57.6	58.7	61.1	60.8	Growing	Faster
FDI	**52.7**	**52.6**	**57.2**	**56.0**	**52.7**	**56.2**	**57.6**	**56.1**	Growing	Faster
FLI	**55.4**	**55.1**	**65.4**	**55.6**	**62.8**	**63.7**	**64.0**	**64.5**	Growing	Faster
(Other Metrics)										
Sales	56.3	60.5	75.2	79.1	64.5	75.7	76.6	58.5	Growing	Slower
Employment	62.9	53.1	62.1	48.3	55.0	54.7	63.6	65.2	Growing	Faster
Supplier Deliveries	69.4	68.8	69.7	72.4	71.7	79.7	78.8	75.8	Growing	Faster
Respondent Inventories	62.9	59.4	50.0	56.9	41.7	46.9	53.0	51.5	Growing	Faster
Customer Inventories	27.4	29.7	21.2	25.9	18.3	15.6	15.2	21.2	Declining	Faster
Pricing, month-to-month	77.4	78.1	83.3	81.0	81.7	85.9	83.3	84.8	Growing	Slower
Pricing, year-to-year	95.2	95.3	95.5	94.8	95.0	96.9	95.5	95.5	Growing	Slower
				Higher	Same	Lower				
6-Month Outlook -May				26%	52%	23%				

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, conducted with 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 stable with last month. The seasonally adjusted May FDI (52.7) was virtually unchanged m/m (April 52.6), consistent with growth but at a more measured pace vs. earlier this year/2H21. The sales index was a touch lower sequentially which participants seemingly attributed to difficulties getting overseas containers/materials into ports amid further slowdowns from China. Pricing remained stable at a very high level, supported by rising container/freight costs in addition to ongoing raw material cost pressures. Overall, growth and market conditions remained positive but slowing relative to earlier this year and 2H21.

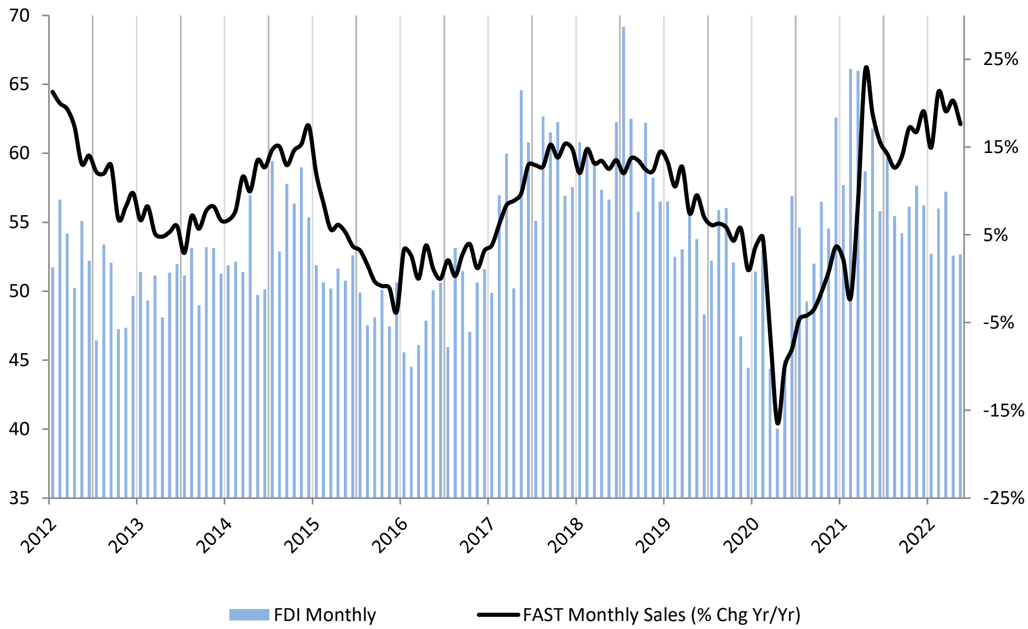
FLI continues to signal growth. The seasonally adjusted FLI came in at 55.4, very similar to last month's 55.1 and signaling continued growth ahead. Relative to April, a stronger employment reading was offset by a weaker six-month outlook and higher respondent inventory levels. Regarding the outlook, respondents were fairly evenly divided between those expecting higher activity levels (26%) and those expecting lower (23%) over the next six months compared to today; this is the first time the outlook has been this divided since just prior to the onset of the COVID-19 driven recession (December 2019). That said, with multiple participants noting backlogs of orders and delays fulfilling orders due to port congestion, we still think the FDI is likely to remain in growth mode near term.

FDI employment index improves. The FDI employment index came in at 62.9 after dipping down to just 53.1 last month. No comments were registered this month on labor shortages, perhaps implying some improvement in this area when coupled with the quantitative improvement seen in the index. The broader economy in May saw +390,000 job additions compared to economists' expectation for +328,000. Average hourly earnings rose +5.2% y/y as competition for workers remains intense.

Demand remains strong despite several headwinds. Overall, commentary this month focused on continued growth and strong demand despite numerous logistics constraints. As one participant said, "*Incoming sales remain very strong, although they did tail off a bit from April. Lead times are starting to stretch out as we work to catch up on the record-breaking sales of the previous few months. At the halfway point of our fiscal year, we have already surpassed last year's total sales. Now the challenge is to get material and tooling in house in a timely manner in order to produce the parts on time for our customers.*" Slowing growth was also seen by this participant who said, "*Our sales numbers are still performing at historical levels but thinking the industry will see slower growth the remainder of the year.*" Lastly, issues at the port appear to be increasing ahead of the busy Summer peak (expected to be in mid-June), with most attributing this to lockdowns in China. As one respondent commented, "*[We're] still having logistics issues getting containers in from overseas in a timely manner. One delay after another! Lockdown in China has also created major delays in getting material shipped!*" The rising cost associated with imports has not had a uniformly negative effect, however, as another participant noted, "*As a domestic manufacturer of fasteners, we hear that our costing is closer than ever before to import costing*."

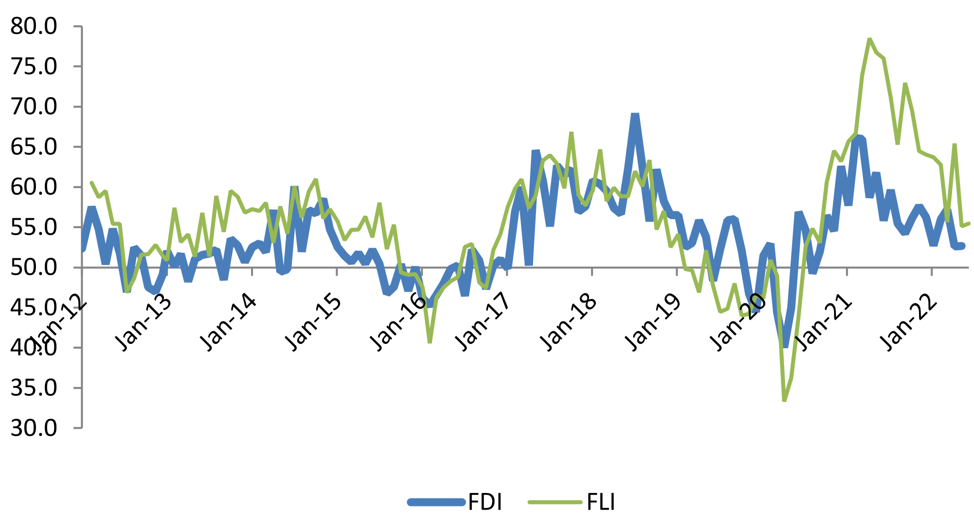
Fastenal's +17.6% overall May daily sales growth came in above our +16.6% estimate and normal seasonality. Consistent with the FDI, fastener sales were again very strong (but moderating) at +20.0% y/y (compared to last month's +25.5% growth), while safety was +15.6% and other non-fasteners were +16.1%. Looking ahead to June daily sales, we model overall daily sales +18.8% y/y. This would again be slightly better than normal seasonality given the solid FLI reading and recent strong ISM/manufacturing capacity utilization readings. FAST will report June daily sales in conjunction with 2Q22 earnings on July 13.

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

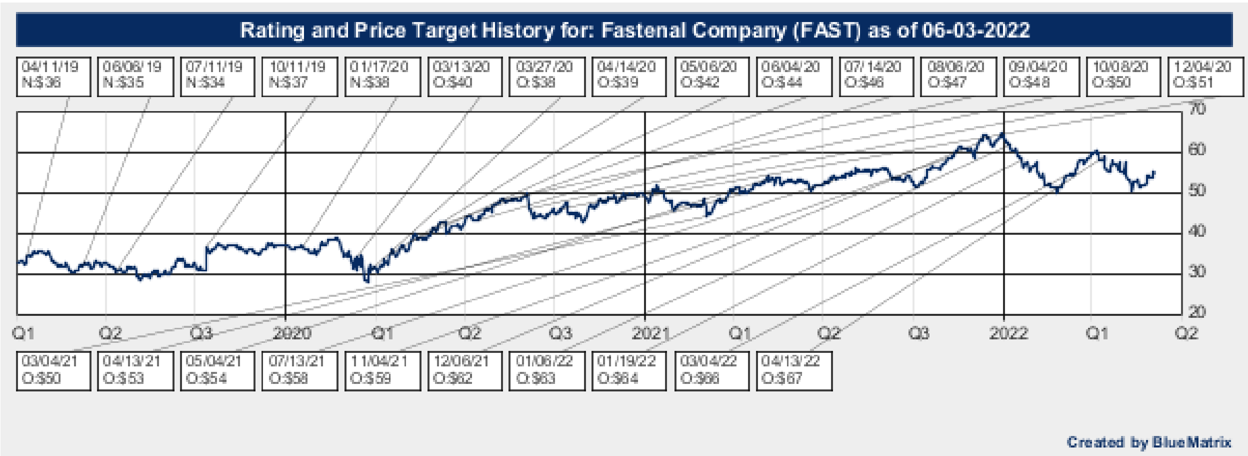
Fastenal: Risks include economic sensitivity, pricing power, relatively high valuation, secular gross margin pressures, success of vending and on-site initiatives, and ability to sustain historical growth.

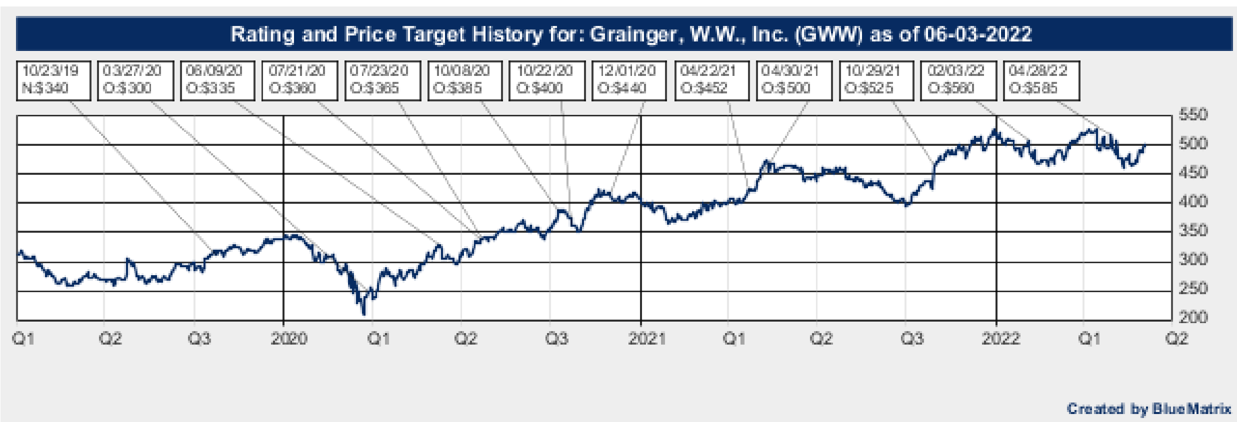
Industrial Distribution: Risks include economic sensitivity, pricing power, online pressure/competitive threats, global sourcing, and exposure to durable goods manufacturing.

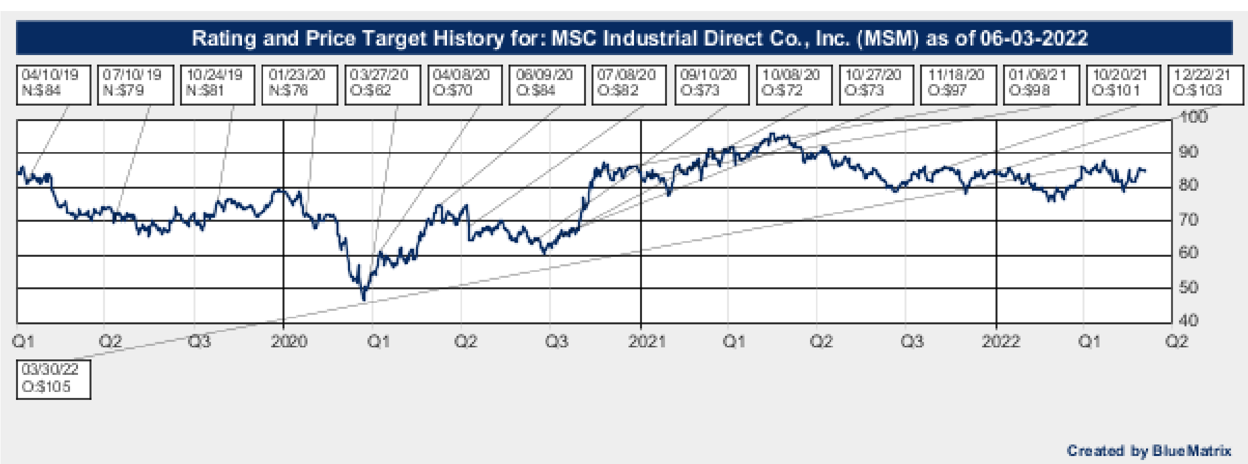
Appendix – Important Disclosures and Analyst Certification

Covered Companies Mentioned
All stock prices below are as of 6/6/2022.

Fastenal Company (FAST-$54.96-Outperform)
W.W. Grainger Inc. (GWW-$498.96-Outperform)
MSC Industrial Direct Co. Inc (MSM-$85.22-Outperform)
(See recent research reports for more information)







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