



Fastenal Company (FAST)

Updated October 15th, 2019 by Eli Inkrot

Key Metrics

Current Price:	\$36	5 Year CAGR Estimate:	4.2%	Volatility Percentile:	76.1%
Fair Value Price:	\$28	5 Year Growth Estimate:	7.0%	Momentum Percentile:	93.2%
% Fair Value:	128%	5 Year Valuation Multiple Estimate:	-4.8%	Growth Percentile:	70.7%
Dividend Yield:	2.4%	5 Year Price Target	\$39	Valuation Percentile:	23.3%
Dividend Risk Score:	C	Retirement Suitability Score:	D	Total Return Percentile:	25.2%

Overview & Current Events

Fastenal began in 1967 when Bob Kierlin and four friends pooled together \$30,000 to open the first store. The original intent was to dispense nuts and bolts via vending machine, but it would take a few decades before that idea got off the ground. The company went public in 1987, and today provides fasteners, tools and supplies to its customers via 2,146 public branches, 1,076 active Onsite locations and over 88,000 industrial vending devices. The \$20 billion market cap company employs nearly 22,200 people and generates over \$5 billion in annual sales.

On October 11th, 2019 Fastenal reported Q3 2019 results for the period ending September 30th, 2019. For the quarter, the company reported net sales of \$1.379 billion, a 7.8% increase compared to the year ago period, driven by one additional selling day, higher unit sales and strong performance from the industrial vending and Onsite locations. Net earnings for the quarter totaled \$213.5 million, an 8.0% year-over-year increase, with earnings-per-share coming in at \$0.37 against \$0.34 previously. During the first nine months of 2019, Fastenal has signed 16,713 industrial vending units and 283 Onsite locations, bringing the totals up to 88,327 and 1,076 respectively. Meanwhile, the number of public branches has continued to decline from 2,261 locations in Q3 2018 to 2,146 locations in Q3 2019.

Total debt on the balance sheet equaled \$445 million or 14.7% of total capital, compared to 14.4% in Q3 2018.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$0.31	\$0.45	\$0.61	\$0.71	\$0.76	\$0.84	\$0.89	\$0.87	\$1.01	\$1.31	\$1.40	\$1.96
DPS	\$0.18	\$0.21	\$0.33	\$0.37	\$0.40	\$0.50	\$0.56	\$0.60	\$0.64	\$0.77	\$0.86	\$1.00
Shares¹	590	590	591	593	594	592	579	578	575	572	572	570

All of the numbers above reflect the May 22nd, 2019 two-for-one stock split.

From 2008 through 2018, Fastenal grew earnings-per-share by an average compound rate of 10.6% per annum. This was driven by a variety of factors, including sales basically doubling over this period, an improvement in margins and most recently as a result of tax reform. We are forecasting strong growth, 7% annually, but not quite as robust as in the past.

Fastenal is in the midst of a transformation from the traditional public branches leading the business to Onsite locations and vending devices heading the growth story (public store count topped out in 2014 and has since been declining, while on-site and vending have increased materially). We believe this is a prudent move, establishing stickier relationships with customers. This is especially true since only about 15% of the company's business is from walk-in customers while the remaining 85% is business-to-business.

On the flip side, the large, national accounts that the company is pursuing are tougher for margins, but this should be made up for in incremental volume. Moreover, the company is exposed to a fair amount of cyclical as over half of the business is in construction and heavy manufacturing.

¹ In millions.

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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	28.6	27.9	28.2	31.7	32.3	27.9	23.2	25.3	23.3	20.8	25.5	20.0
Avg. Yld.	2.0%	1.6%	1.9%	1.6%	1.6%	2.1%	2.7%	2.7%	2.7%	2.8%	2.4%	2.5%

Over the past decade shares of Fastenal have traded hands with an average P/E ratio of 27 times earnings. Even during the depths of the recession, shares did not trade below 15 times earnings. And since 2010 you would be hard pressed to find shares trading under 20 times earnings. Fastenal, it seems, has always traded at a premium valuation.

This premium has implications on the shareholder return side, as the dividend yield will remain average (even with an elevated payout ratio) and share buybacks do not look particularly attractive. (The last time a meaningful number of shares were retired was in 2015, when the company took on debt to buy shares that had dropped from 28 times earnings down to 21 or 22.) With our slightly cautious fair value assumption, this could imply a moderate headwind.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	58%	47%	54%	52%	53%	60%	63%	69%	63%	59%	61%	51%

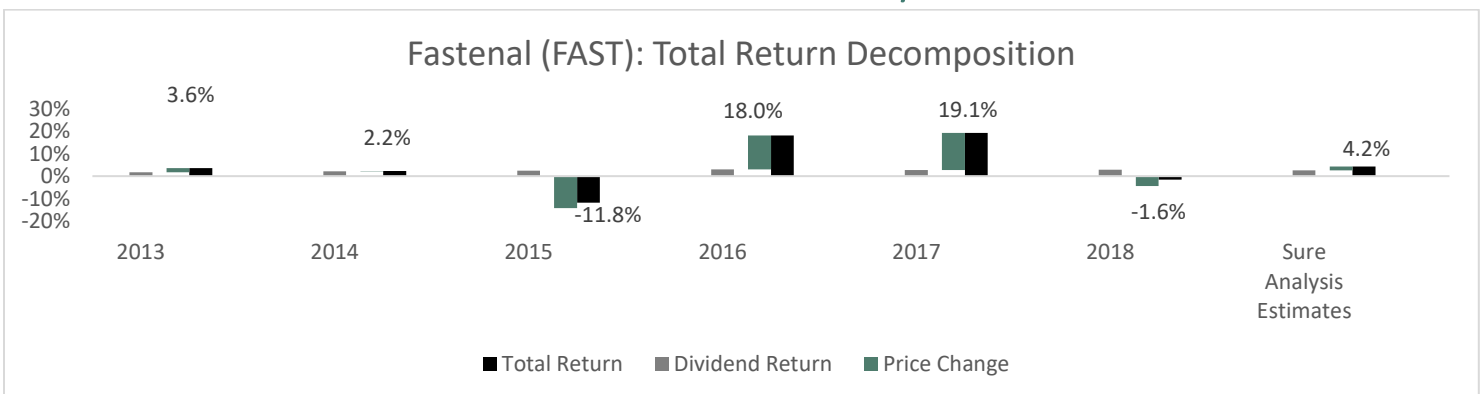
Fastenal has a first mover competitive advantage in its industrial vending and Onsite locations, creating a very sticky and well-attuned customer relationship with high switching costs. Moreover, the company's scale allows for the company to continue on its growth path, adjusting to business preferences and reliably delivering needed goods.

During the last recession, Fastenal reported earnings-per-share of \$0.39, \$0.48, \$0.31 and \$0.45 for the 2007 through 2010 period. Moreover, the dividend kept on increasing during this time. While we note some cyclical possibilities in the construction industry, thus far the company has proven itself to be well prepared to survive financial storms. We note that the dividend payout ratio is elevated, but we believe this is reasonable considering the strong financial position.

Final Thoughts & Recommendation

Shares are up 20% since our last report, while our earnings expectations are unchanged. Fastenal has proven itself to be a great business, with earnings and dividends growing consistently over the years. Moreover, the company is executing moves to better cement itself as a go-to supplier. It's the sort of business that you would be proud to own. However, on the security side you have to get comfortable with the elevated valuation. Total return potential comes in at just 4.2% per annum, driven by 7% growth and a 2.4% dividend offset by a moderate valuation headwind. We are enthused about the quality of the business and future growth prospects, but we are not overly excited about the security's intermediate-term investment merits and continue to rate shares as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	1930	2269	2767	3134	3326	3734	3869	3962	4391	4965
Gross Profit	983	1175	1434	1615	1719	1897	1949	1965	2164	2399
Gross Margin	50.9%	51.8%	51.8%	51.5%	51.7%	50.8%	50.4%	49.6%	49.3%	48.3%
SG&A Exp.	687	745	859	941	1007	1111	1122	1170	1283	1400
D&A Exp.	40	41	45	54	64	73	87	104	127	138
Operating Profit	297	430	575	673	712	787	827	795	881	999
Operating Margin	15.4%	18.9%	20.8%	21.5%	21.4%	21.1%	21.4%	20.1%	20.1%	20.1%
Net Profit	184	265	358	421	449	494	516	499	579	752
Net Margin	9.6%	11.7%	12.9%	13.4%	13.5%	13.2%	13.3%	12.6%	13.2%	15.1%
Free Cash Flow	254	167	148	258	210	310	395	330	465	498
Income Tax	113	165	217	254	265	293	310	290	295	235

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	1327	1468	1685	1816	2076	2359	2532	2669	2911	3322
Cash & Equivalents	165	144	118	80	59	114	129	113	117	167
Accounts Receivable	214	270	339	372	414	462	468	500	608	714
Inventories	508	557	646	715	784	869	913	993	1093	1279
Goodwill & Int. Ass.										
Total Liabilities	137	186	226	255	303	444	731	736	814	1019
Accounts Payable	53	60	74	78	91	104	126	109	148	194
Long-Term Debt	0	0	0	0	0	90	365	390	415	500
Shareholder's Equity	1191	1283	1459	1560	1773	1915	1801	1933	2097	2303
D/E Ratio	0	0	0	0	0	0	0.2	0.2	0.2	0.2

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	14.0%	19.0%	22.7%	24.0%	23.1%	22.3%	21.1%	19.2%	20.7%	24.1%
Return on Equity	15.8%	21.5%	26.1%	27.9%	26.9%	26.8%	27.8%	26.7%	28.7%	34.2%
ROIC	15.8%	21.5%	26.1%	27.9%	26.9%	26.2%	24.8%	22.2%	23.9%	28.3%
Shares Out.										
Revenue/Share										
FCF/Share										

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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