



Fastenal Company (FAST)

Updated January 17th, 2020 by Eli Inkrot

Key Metrics

| | | | | | |
|-----------------------------|------|--|-------|----------------------------------|----------|
| Current Price: | \$37 | 5 Year CAGR Estimate: | 4.6% | Market Cap: | \$21.2B |
| Fair Value Price: | \$29 | 5 Year Growth Estimate: | 7.0% | Ex-Dividend Date: | 01/30/20 |
| % Fair Value: | 127% | 5 Year Valuation Multiple Estimate: | -4.7% | Dividend Payment Date: | 02/28/20 |
| Dividend Yield: | 2.7% | 5 Year Price Target | \$41 | Years Of Dividend Growth: | 20 |
| Dividend Risk Score: | C | Retirement Suitability Score: | D | Last Dividend Increase: | 13.6% |

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 2,114 public branches, 1,114 active Onsite locations and over 89,000 industrial vending devices. The \$21 billion market cap company employees nearly 22,000 people and generates over \$5 billion in annual sales.

On January 17th, 2020 Fastenal reported Q4 and full year 2019 results for the period ending December 31st, 2019. For the quarter, the company reported net sales of \$1.277 billion, a 3.7% increase compared to the year ago period, driven by higher unit sales and strong performance from the industrial vending and Onsite locations. Net earnings for the quarter totaled \$178.7 million, a 5.9% year-over-year increase, with earnings-per-share coming in at \$0.31 against \$0.29 previously. For the year revenue equaled \$5.334 billion, a 7.4% increase compared to the \$4.965 billion generated in 2018. Net earnings equaled \$790.9 million or \$1.38 per share compared to \$1.31 previously.

During 2019 Fastenal signed 21,857 industrial vending units and 362 Onsite locations, bringing the totals up to 89,937 and 1,114 respectively. Meanwhile, the number of public branches has continued to decline from 2,227 locations in Q4 2018 to 2,114 locations in Q4 2019. Total debt on the balance sheet equaled \$345 million or 11.5% of total capital, compared to 17.8% at the end of Q4 2018.

Growth on a Per-Share Basis

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2025 |
|---------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|---------------|
| EPS | \$0.45 | \$0.61 | \$0.71 | \$0.76 | \$0.84 | \$0.89 | \$0.87 | \$1.01 | \$1.31 | \$1.38 | \$1.45 | \$2.03 |
| DPS | \$0.21 | \$0.33 | \$0.37 | \$0.40 | \$0.50 | \$0.56 | \$0.60 | \$0.64 | \$0.77 | \$0.87 | \$1.00 | \$1.22 |
| Shares¹ | 590 | 591 | 593 | 594 | 592 | 579 | 578 | 575 | 572 | 574 | 574 | 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 Onsite 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 cyclicity as over half of the business is in construction and heavy manufacturing.

¹ In millions.

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Valuation Analysis

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | Now | 2025 |
|-----------|------|------|------|------|------|------|------|------|------|------|------|------|
| Avg. P/E | 27.9 | 28.2 | 31.7 | 32.3 | 27.9 | 23.2 | 25.3 | 23.3 | 20.8 | 22.7 | 25.5 | 20.0 |
| Avg. Yld. | 1.6% | 1.9% | 1.6% | 1.6% | 2.1% | 2.7% | 2.7% | 2.7% | 2.8% | 2.8% | 2.7% | 3.0% |

Over the past decade shares of Fastenal have traded hands with an average P/E ratio of 26 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 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2025 |
|--------|------|------|------|------|------|------|------|------|------|------|------|------|
| Payout | 47% | 54% | 52% | 53% | 60% | 63% | 69% | 63% | 59% | 63% | 69% | 60% |

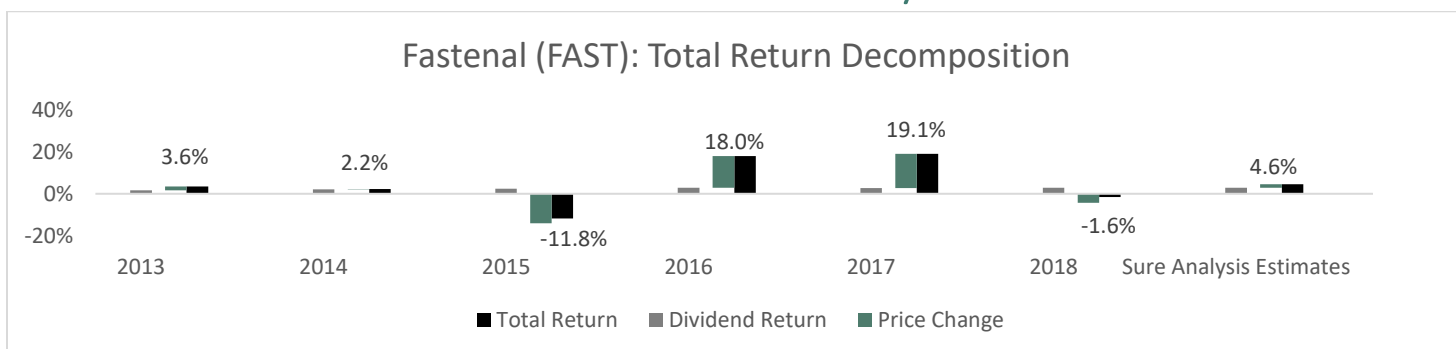
Fastenal has a first mover competitive advantage in its industrial vending and Onsite locations, creating a very sticky and well-attuned customer relationship with high switching costs. Moreover, the company's scale allows for the company to continue on its growth path, adjusting to business preferences 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 3% since our last report. 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 4.6% per annum, driven by 7% growth and a 2.7% 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 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|------|
| Revenue | 2269 | 2767 | 3134 | 3326 | 3734 | 3869 | 3962 | 4391 | 4965 | |
| Gross Profit | 1175 | 1434 | 1615 | 1719 | 1897 | 1949 | 1965 | 2164 | 2399 | |
| Gross Margin | 51.8% | 51.8% | 51.5% | 51.7% | 50.8% | 50.4% | 49.6% | 49.3% | 48.3% | |
| SG&A Exp. | 745 | 859 | 941 | 1007 | 1111 | 1122 | 1170 | 1283 | 1400 | |
| D&A Exp. | 41 | 45 | 54 | 64 | 73 | 87 | 104 | 127 | 138 | |
| Operating Profit | 430 | 575 | 673 | 712 | 787 | 827 | 795 | 881 | 999 | |
| Operating Margin | 18.9% | 20.8% | 21.5% | 21.4% | 21.1% | 21.4% | 20.1% | 20.1% | 20.1% | |
| Net Profit | 265 | 358 | 421 | 449 | 494 | 516 | 499 | 579 | 752 | |
| Net Margin | 11.7% | 12.9% | 13.4% | 13.5% | 13.2% | 13.3% | 12.6% | 13.2% | 15.1% | |
| Free Cash Flow | 167 | 148 | 258 | 210 | 310 | 395 | 330 | 465 | 498 | |
| Income Tax | 165 | 217 | 254 | 265 | 293 | 310 | 290 | 295 | 235 | |

Balance Sheet Metrics

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|---------------------------------|------|------|------|------|------|------|------|------|------|------|
| Total Assets | 1468 | 1685 | 1816 | 2076 | 2359 | 2532 | 2669 | 2911 | 3322 | |
| Cash & Equivalents | 144 | 118 | 80 | 59 | 114 | 129 | 113 | 117 | 167 | |
| Accounts Receivable | 270 | 339 | 372 | 414 | 462 | 468 | 500 | 608 | 714 | |
| Inventories | 557 | 646 | 715 | 784 | 869 | 913 | 993 | 1093 | 1279 | |
| Goodwill & Int. Ass. | | | | | | | | | | |
| Total Liabilities | 186 | 226 | 255 | 303 | 444 | 731 | 736 | 814 | 1019 | |
| Accounts Payable | 60 | 74 | 78 | 91 | 104 | 126 | 109 | 148 | 194 | |
| Long-Term Debt | 0 | 0 | 0 | 0 | 90 | 365 | 390 | 415 | 500 | |
| Shareholder's Equity | 1283 | 1459 | 1560 | 1773 | 1915 | 1801 | 1933 | 2097 | 2303 | |
| D/E Ratio | 0 | 0 | 0 | 0 | 0 | 0.2 | 0.2 | 0.2 | 0.2 | |

Profitability & Per Share Metrics

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|------|
| Return on Assets | 19.0% | 22.7% | 24.0% | 23.1% | 22.3% | 21.1% | 19.2% | 20.7% | 24.1% | |
| Return on Equity | 21.5% | 26.1% | 27.9% | 26.9% | 26.8% | 27.8% | 26.7% | 28.7% | 34.2% | |
| ROIC | 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.

Disclaimer

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