

FASTENAL CO
Form 10-Q
April 15, 2013
Table of Contents

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended March 31, 2013, or

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _____ to _____
Commission file number 0-16125

FASTENAL COMPANY

(Exact name of registrant as specified in its charter)

Minnesota 41-0948415
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)
2001 Theurer Boulevard 55987-0978
Winona, Minnesota (Zip Code)
(Address of principal executive offices)
(507) 454-5374
(Registrant's telephone number, including area code)
Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files.) Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer", "accelerated filer", and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer Accelerated Filer

Non-accelerated Filer (Do not check if a smaller reporting company) Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the last practicable date.

Class	Outstanding at April 9, 2013
Common Stock, par value \$.01 per share	296,686,927

Table of Contents

FASTENAL COMPANY
INDEX

	Page No.
<u>Part 1 Financial Information:</u>	
<u>Consolidated Balance Sheets as of March 31, 2013 and December 31, 2012</u>	<u>1</u>
<u>Consolidated Statements of Earnings for the three months ended March 31, 2013 and 2012</u>	<u>2</u>
<u>Consolidated Statements of Comprehensive Income for the three months ended March 31, 2013 and 2012</u>	<u>3</u>
<u>Consolidated Statements of Cash Flows for the three months ended March 31, 2013 and 2012</u>	<u>4</u>
<u>Notes to Consolidated Financial Statements</u>	<u>5</u>
<u>Management's discussion and analysis of financial condition and results of operations</u>	<u>11</u>
<u>Quantitative and qualitative disclosures about market risk</u>	<u>28</u>
<u>Controls and procedures</u>	<u>28</u>
<u>Part II Other Information:</u>	
<u>Legal Proceedings</u>	<u>29</u>
<u>Risk Factors</u>	<u>29</u>
<u>Exhibits</u>	<u>29</u>

Table of Contents

PART I — FINANCIAL INFORMATION

ITEM 1 — FINANCIAL STATEMENTS

FASTENAL COMPANY AND SUBSIDIARIES

Consolidated Balance Sheets

(Amounts in thousands except share information)

	(Unaudited)	
	March 31, 2013	December 31, 2012
Assets		
Current assets:		
Cash and cash equivalents	\$ 159,240	79,611
Marketable securities	417	354
Trade accounts receivable, net of allowance for doubtful accounts of \$6,728	418,733	372,159
Inventories	700,484	715,383
Deferred income tax assets	14,079	14,420
Other current assets	83,883	97,361
Prepaid income taxes	—	7,368
Total current assets	1,376,836	1,286,656
Property and equipment, less accumulated depreciation	555,734	516,427
Other assets, net	12,726	12,749
Total assets	\$ 1,945,296	1,815,832
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 75,327	78,019
Accrued expenses	126,091	126,155
Income taxes payable	51,679	—
Total current liabilities	253,097	204,174
Deferred income tax liabilities	51,336	51,298
Stockholders' equity:		
Preferred stock, 5,000,000 shares authorized	—	—
Common stock, 400,000,000 shares authorized, 296,686,427 and 296,564,382 shares issued and outstanding, respectively	2,967	2,966
Additional paid-in capital	66,560	61,436
Retained earnings	1,556,987	1,477,601
Accumulated other comprehensive income	14,349	18,357
Total stockholders' equity	1,640,863	1,560,360
Total liabilities and stockholders' equity	\$ 1,945,296	1,815,832

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents

FASTENAL COMPANY AND SUBSIDIARIES

Consolidated Statements of Earnings

(Amounts in thousands except earnings per share)

	(Unaudited)	
	Three months ended	
	March 31,	
	2013	2012
Net sales	\$806,326	768,875
Cost of sales	384,446	374,698
Gross profit	421,880	394,177
Operating and administrative expenses	247,334	232,970
(Gain) loss on sale of property and equipment	(213) 174
Operating income	174,759	161,033
Interest income	447	96
Interest expense	(34) —
Earnings before income taxes	175,172	161,129
Income tax expense	66,124	60,935
Net earnings	\$109,048	100,194
Basic net earnings per share	\$0.37	0.34
Diluted net earnings per share	\$0.37	0.34
Basic weighted average shares outstanding	296,643	295,538
Diluted weighted average shares outstanding	297,652	296,927

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents

FASTENAL COMPANY AND SUBSIDIARIES
 Consolidated Statements of Comprehensive Income
 (Amounts in thousands)

	(Unaudited)	
	Three months ended	
	March 31,	
	2013	2012
Net earnings	\$ 109,048	100,194
Other comprehensive income (loss), net of tax:		
Foreign currency translation adjustments (net of tax of \$0 in 2013 and 2012)	(4,072)	2,940
Change in marketable securities (net of tax of \$0 in 2013 and 2012)	63	23
Comprehensive income	\$ 105,039	103,157

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents

FASTENAL COMPANY AND SUBSIDIARIES

Consolidated Statements of Cash Flows

(Amounts in thousands)

	(Unaudited)	
	Three months ended	
	March 31,	
	2013	2012
Cash flows from operating activities:		
Net earnings	\$ 109,048	100,194
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation of property and equipment	15,152	12,415
(Gain) loss on sale of property and equipment	(213)	174
Bad debt expense	2,045	2,329
Deferred income taxes	379	1,863
Stock based compensation	1,350	1,050
Excess tax benefits from stock based compensation	(954)	—
Amortization of non-compete agreements	26	148
Changes in operating assets and liabilities:		
Trade accounts receivable	(48,619)	(50,617)
Inventories	14,899	(1,734)
Other current assets	13,478	15,536
Accounts payable	(2,692)	2,334
Accrued expenses	(64)	1,134
Income taxes	60,001	44,941
Other	(3,592)	2,421
Net cash provided by operating activities	160,244	132,188
Cash flows from investing activities:		
Purchase of property and equipment	(55,513)	(28,212)
Proceeds from sale of property and equipment	1,267	985
Net increase in marketable securities	(63)	(29)
Increase in other assets	(3)	(57)
Net cash used in investing activities	(54,312)	(27,313)
Cash flows from financing activities:		
Borrowings under line of credit	20,000	—
Payments against line of credit	(20,000)	—
Proceeds from exercise of stock options	2,821	18,285
Excess tax benefits from stock based compensation	954	7,697
Payment of dividends	(29,662)	(50,197)
Net cash used in financing activities	(25,887)	(24,215)
Effect of exchange rate changes on cash	(416)	542
Net increase in cash and cash equivalents	79,629	81,202
Cash and cash equivalents at beginning of period	79,611	117,676
Cash and cash equivalents at end of period	\$ 159,240	198,878
Supplemental disclosure of cash flow information:		
Cash paid during each period for interest	\$ 34	—
Cash paid during each period for income taxes	\$ 6,502	21,828

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents

FASTENAL COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Amounts in thousands except share and per share information and where otherwise noted)

March 31, 2013 and 2012

(Unaudited)

(1) Basis of Presentation

The accompanying unaudited consolidated financial statements of Fastenal Company and subsidiaries (collectively referred to as the Company, Fastenal, or by terms such as we, our, or us) have been prepared in accordance with United States generally accepted accounting principles for interim financial information. They do not include all information and footnotes required by United States generally accepted accounting principles for complete financial statements. However, except as described herein, there has been no material change in the information disclosed in the notes to consolidated financial statements included in our consolidated financial statements as of and for the year ended December 31, 2012. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included.

(2) Marketable Securities

We follow a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets and liabilities (Level 1) and the lowest priority to measurements involving unobservable inputs (Level 3). The three levels of the fair value hierarchy are as follows:

Level 1 inputs are observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 inputs include other inputs that are directly or indirectly observable in the marketplace.

Level 3 inputs are unobservable inputs which are supported by little or no market activity.

The level in the fair value hierarchy within which a fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

The following table presents the placement in the fair value hierarchy of assets that are measured at fair value on a recurring basis:

March 31, 2013:	Total	Level 1	Level 2	Level 3
Common stock	\$417	417	—	—
Total available-for-sale securities	\$417	417	—	—
December 31, 2012:	Total	Level 1	Level 2	Level 3
Common stock	\$354	354	—	—
Total available-for-sale securities	\$354	354	—	—
March 31, 2012:	Total	Level 1	Level 2	Level 3
Common stock	\$347	347	—	—
Government and agency securities	26,847	26,847	—	—
Total available-for-sale securities	\$27,194	27,194	—	—

There were no transfers between levels during the three month periods ended March 31, 2013 and 2012.

As of March 31, 2013, December 31, 2012, and March 31, 2012, our financial assets that are measured at fair value on a recurring basis consisted of common stock and debt securities.

Table of Contents

FASTENAL COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Amounts in thousands except share and per share information and where otherwise noted)

March 31, 2013 and 2012

(Unaudited)

Marketable securities, all treated as available-for-sale securities, consist of the following:

March 31, 2013:	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Common stock	\$ 197	220	—	417
Total available-for-sale securities	\$ 197	220	—	417

December 31, 2012:	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Common stock	\$ 197	157	—	354
Total available-for-sale securities	\$ 197	157	—	354

March 31, 2012:	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Common stock	\$ 197	150	—	347
Government and agency securities	26,857	—	(10)	26,847
Total available-for-sale securities	\$27,054	150	(10)	27,194

The unrealized gains and losses recorded in accumulated other comprehensive income and the realized gains and losses recorded in earnings were immaterial during the periods reported in these consolidated financial statements. Future maturities of our available-for-sale securities consist of the following:

March 31, 2013:	Less than 12 months		Greater than 12 months	
	Amortized cost	Fair value	Amortized cost	Fair value
Common stock	\$ 197	417	—	—
Total available-for-sale securities	\$ 197	417	—	—

Table of Contents

FASTENAL COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Amounts in thousands except share and per share information and where otherwise noted)

March 31, 2013 and 2012

(Unaudited)

(3) Stockholders' Equity

Our authorized, issued, and outstanding shares (share amounts stated in whole numbers) consist of the following:

	Par Value	March 31, 2013	December 31, 2012	March 31, 2012
Preferred Stock	\$.01 /share			
Shares authorized		5,000,000	5,000,000	5,000,000
Shares issued and outstanding		—	—	—
Common Stock	\$.01 /share			
Shares authorized		400,000,000	400,000,000	400,000,000
Shares issued and outstanding		296,686,427	296,564,382	296,071,374

Dividends

On April 9, 2013, our board of directors declared a dividend of \$0.20 per share of common stock. This dividend is to be paid in cash on May 30, 2013 to shareholders of record at the close of business on May 2, 2013. Since 2011 we have paid quarterly dividends and, in 2012, we paid a supplemental dividend late in the year. Our board of directors expect to continue paying quarterly dividends, provided the future determination as to payment of dividends will depend on the financial needs of the Company and such other factors as deemed relevant by the board of directors. The following table presents the dividends either paid previously or declared by our board of directors for future payment:

	2013	2012
First quarter	\$0.10	0.17
Second quarter	\$0.20	0.17
Third quarter		0.19
Fourth quarter		0.21
Supplemental		0.50
Total	\$0.30	1.24

Table of ContentsFASTENAL COMPANY AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Amounts in thousands except share and per share information and where otherwise noted)

March 31, 2013 and 2012

(Unaudited)

Stock Options

The following tables summarize the details of grants made under our stock option plan of options that have been granted and are outstanding, and the assumptions used to value these options. All options granted were effective at the close of business on the date of grant.

Date of grant	Options granted	Option exercise price (strike)	Closing stock price on date of grant	March 31, 2013	
				Options outstanding	Options vested
April 17, 2012	1,235,000	\$54.00	\$49.01	1,152,500	—
April 19, 2011	410,000	\$35.00	\$31.78	370,000	—
April 20, 2010	530,000	\$30.00	\$27.13	330,000	—
April 21, 2009	790,000	\$27.00	\$17.61	520,000	—
April 15, 2008	550,000	\$27.00	\$24.35	254,417	99,417
April 17, 2007	4,380,000	\$22.50	\$20.15	1,963,080	947,330
Total	7,895,000			4,589,997	1,046,747

Date of grant	Risk-free interest rate	Expected life of option in years	Expected dividend yield	Expected stock volatility	Estimated fair value of stock option	
April 17, 2012	0.9	% 5.00	1.4	% 39.25	%	\$13.69
April 19, 2011	2.1	% 5.00	1.6	% 39.33	%	\$11.20
April 20, 2010	2.6	% 5.00	1.5	% 39.10	%	\$8.14
April 21, 2009	1.9	% 5.00	1.0	% 38.80	%	\$3.64
April 15, 2008	2.7	% 5.00	1.0	% 30.93	%	\$7.75
April 17, 2007	4.6	% 4.85	1.0	% 31.59	%	\$5.63

All of the options in the tables above vest and become exercisable over a period of up to eight years. Each option will terminate, to the extent not previously exercised, 13 months after the end of the relevant vesting period.

The fair value of each share-based option is estimated on the date of grant using a Black-Scholes valuation method that uses the assumptions listed above. The expected life is the average length of time over which we expect the employee groups will exercise their options, which is based on historical experience with similar grants. Expected volatilities are based on the movement of our stock over the most recent historical period equivalent to the expected life of the option. The risk-free interest rate is based on the U.S. Treasury rate over the expected life at the time of grant. The dividend yield is estimated over the expected life based on our current dividend payout, historical dividends paid, and expected future cash dividends.

Compensation expense equal to the grant date fair value is recognized for all of these awards over the vesting period. The stock-based compensation expense for the three month periods ended March 31, 2013 and 2012 was \$1,350 and \$1,050, respectively. Unrecognized compensation expense related to outstanding stock options as of March 31, 2013 was \$18,337 and is expected to be recognized over a weighted average period of 4.50 years. Any future changes in estimated forfeitures will impact this amount.

Table of ContentsFASTENAL COMPANY AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Amounts in thousands except share and per share information and where otherwise noted)

March 31, 2013 and 2012

(Unaudited)

Earnings Per Share

The following tables present a reconciliation of the denominators used in the computation of basic and diluted earnings per share and a summary of the options to purchase shares of common stock which were excluded from the diluted earnings calculation because they were anti-dilutive:

Reconciliation	Three-month period	
	2013	2012
Basic weighted average shares outstanding	296,643,014	295,538,402
Weighted shares assumed upon exercise of stock options	1,008,946	1,388,821
Diluted weighted average shares outstanding	297,651,960	296,927,223

Summary of anti-dilutive options excluded	Three-month period	
	2013	2012
Options to purchase shares of common stock	1,168,083	—
Weighted average exercise price of options	\$54.00	\$0.00

Any dilutive impact summarized above would relate to periods when the average market price of our stock exceeded the exercise price of the potentially dilutive option securities then outstanding.

(4) Income Taxes

Fastenal, or one of its subsidiaries, files income tax returns in the United States federal jurisdiction, numerous states, and various local and foreign jurisdictions. With limited exceptions, we are no longer subject to income tax examinations by taxing authorities for taxable years before 2009 in the case of United States federal and non-United States examinations and 2008 in the case of state and local examinations.

As of March 31, 2013 and 2012, the Company had \$7,661 and \$5,517, respectively, of liabilities recorded related to unrecognized tax benefits. Included in this liability for unrecognized tax benefits is an immaterial amount for interest and penalties, both of which we classify as a component of income tax expense. The Company does not anticipate its total unrecognized tax benefits will change significantly during the next 12 months.

(5) Operating Leases

We lease certain pick-up trucks under operating leases. These leases have a non-cancellable lease term of one year, with renewal options for up to 72 months. The pick-up truck leases include an early buy out clause we generally exercise, thereby giving the leases an effective term of 28-36 months. Certain operating leases for vehicles contain residual value guarantee provisions which would become due at the expiration of the operating lease agreement if the fair value of the leased vehicles is less than the guaranteed residual value. The aggregate residual value guarantee related to these leases is approximately \$49,433. We believe the likelihood of funding the guarantee obligation under any provision of the operating lease agreements is remote, except for a \$137 loss on disposal reserve provided at March 31, 2013. Our fleet also contains vehicles we estimate will settle at a gain. Gains on these vehicles will be recognized when we sell or dispose of the vehicle or at the end of the lease term.

Table of Contents

FASTENAL COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Amounts in thousands except share and per share information and where otherwise noted)

March 31, 2013 and 2012

(Unaudited)

(6) Contingencies

As of March 31, 2013 there were no material litigation matters that we consider to be probable or reasonably estimable.

(7) Subsequent Events

On April 9, 2013, our board of directors declared a dividend of \$0.20 per share. This dividend is discussed in footnote

(3) 'Stockholders' Equity'.

Table of Contents

ITEM 2 — MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following is management's discussion and analysis of certain significant factors which have affected our financial position and operating results during the periods included in the accompanying consolidated financial statements. (Dollar amounts are stated in thousands except for per share amounts and where otherwise noted.)

BUSINESS AND OPERATIONAL OVERVIEW:

Fastenal is a North American leader in the wholesale distribution of industrial and construction supplies. We distribute these supplies through a network of approximately 2,700 company owned stores. Most of our customers are in the manufacturing and non-residential construction markets. The manufacturing market includes both original equipment manufacturers (OEM) and maintenance and repair operations (MRO). The non-residential construction market includes general, electrical, plumbing, sheet metal, and road contractors. Other users of our product include farmers, ranchers, truckers, railroads, mining companies, federal, state, and local governmental entities, schools, and certain retail trades. Geographically, our stores and customers are primarily located in North America.

In the past decade, we have experienced periods of inflation and deflation related to steel prices (this is meaningful to our business because approximately 45% of our sales consist of some type of fastener – nuts, bolts, screws, etc. – most of which are made of steel). In the period from 2003 to the fall of 2008, we experienced inflation in steel prices, this was most pronounced in 2008. In the fourth quarter of 2008, and throughout much of 2009, we experienced deflation in steel prices. When the swings are dramatic, this can hurt our gross margins because we are selling expensive inventory on the shelf at declining prices. This hurt our gross margins in 2009. The drop in energy costs (this is meaningful to our business because we are a store based distributor with a large trucking fleet) over the same period provided some relief, but it was small in comparison to the impact of the steel deflation. The deflation of 2009 ended and these conditions normalized and allowed our gross margins to recover into a more normal range beginning in 2010. (See later discussion on gross margins.)

Similar to previous quarters, we have included comments regarding several aspects of our business:

1. Monthly sales changes, sequential trends, and end market performance – a recap of our recent sales trends and some insight into the activities with different end markets.
2. Growth drivers of our business – a recap of how we grow our business.
3. Profit drivers of our business – a recap of how we increase our profits.
4. Statement of earnings information – a recap of the components of our income statement.
5. Operational working capital, balance sheet, and cash flow – a recap of the operational working capital utilized in our business, and the related cash flow.

While reading these items, it is helpful to appreciate several aspects of our marketplace: (1) it's big, the North American marketplace for industrial supplies is estimated to be in excess of \$160 billion per year (and we have expanded beyond North America), (2) no company has a significant portion of this market, (3) many of the products we sell are individually inexpensive, (4) when our customer needs something quickly or unexpectedly our local store is a quick source, (5) the cost to manage and procure these products can be significant, and (6) the cost to move these products, many of which are bulky, can also be significant.

Our motto is Growth through Customer Service. This is important given the points noted above. We believe in efficient markets – to us, this means we can grow our market share if we provide the greatest value to the customer. We believe our ability to grow is amplified if we can service our customer at the closest economic point of contact.

The concept of growth is simple – find more customers every day and increase your activity with them. However, execution is hard work. First, we recruit service minded individuals to support our customers and their business. Second, we operate in a decentralized fashion to help identify the greatest value for our customers. Third, we build a great machine behind the store to operate efficiently and to help identify new business solutions. Fourth, we do these things every day. Finally, we strive to generate strong profits; these profits produce the cash flow necessary to fund the growth and to support the needs of our customers.

Table of Contents

SALES GROWTH:

Net sales and growth rates in net sales were as follows:

	Three-month period			
	2013	2012		
Net sales	\$806,326	768,875		
Percentage change	4.9	% 20.0		%

The increase in net sales in the first three months of 2013 and 2012 came primarily from higher unit sales. Our growth in net sales was impacted by inflationary price changes in our non-fastener products and some price deflation in our fastener products, but the net impacts were limited. Our growth in net sales was not meaningfully impacted by the introduction of new products or services, with one exception, our FAST SolutionsSM (industrial vending) initiative did stimulate faster growth (discussed later in this document). The higher unit sales resulted primarily from increases in sales at older store locations (discussed below and again later in this document) and to a lesser degree the opening of new store locations in the last several years. The growth in net sales at the older store locations was due to the growth drivers of our business (discussed later in this document), and, in the case of 2012, the moderating impacts of the recessionary environment. The change in currencies in foreign countries (primarily Canada) relative to the United States dollar lowered our daily sales growth rate by 0.1% in the first three months of 2013 and 2012.

Our sales growth of 4.9% in the first quarter of 2013 was impacted by the loss of one business day versus the prior year (63 days versus 64). Our sales growth adjusted to a daily basis was 6.5% in the first quarter of 2013; the calendar change also impacted the sales by store age shown in the table below. We believe our sales growth was held back partially due to the global economic policy uncertainty.

The stores opened greater than two years represent a consistent 'same store' view of our business (store sites opened as follows: 2013 group – opened 2011 and earlier, and 2012 group – opened 2010 and earlier). However, the impact of the economy is best reflected in the growth performance of our stores opened greater than five years (store sites opened as follows: 2013 group – opened 2008 and earlier, and 2012 group – opened 2007 and earlier) and opened greater than ten years (store sites opened as follows: 2013 group – opened 2003 and earlier, and 2012 group – opened 2002 and earlier). These two groups of stores are more cyclical due to the increased market share they enjoy in their local markets. The daily sales change for each of these groups was as follows:

Store Age	Three-month period			
	2013	2012		
Opened greater than 2 years	4.8	% 17.4		%
Opened greater than 5 years	3.6	% 16.2		%
Opened greater than 10 years	1.9	% 14.4		%

Note: The age groups above are measured as of the last day of each respective calendar year.

SALES BY PRODUCT LINE:

The mix of sales from the original fastener product line and from the other product lines was as follows:

	Three-month period			
	2013	2012		
Fastener product line	43.0	% 45.5		%
Other product lines	57.0	% 54.5		%
	100.0	% 100.0		%

Table of Contents

MONTHLY SALES CHANGES, SEQUENTIAL TRENDS, AND END MARKET PERFORMANCE

Note – Daily sales are defined as the sales for the period divided by the number of business days (in the United States) in the period.

This section focuses on three distinct views of our business – monthly sales changes, sequential trends, and end market performance. The first discussion regarding monthly sales changes provides a good mechanical view of our business based on the age of our stores. The second discussion provides a framework for understanding the sequential trends (that is, comparing a period to the immediately preceding period) in our business. Finally, we believe the third discussion regarding end market performance provides insight into activities with our various types of customers.

MONTHLY SALES CHANGES:

All company sales – During the months in 2013, 2012, and 2011, all of our selling locations, when combined, had daily sales growth rates of (compared to the same month in the preceding year):

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
2013	6.7	% 8.2	% 5.1	%								
2012	21.3	% 20.0	% 19.3	% 17.3	% 13.1	% 14.0	% 12.1	% 12.0	% 12.9	% 6.8	% 8.2	% 9.7
2011	18.8	% 21.5	% 22.8	% 23.2	% 22.6	% 22.5	% 22.4	% 20.0	% 18.8	% 21.4	% 22.2	% 21.2

Stores opened greater than two years – Our stores opened greater than two years (store sites opened as follows: 2013 group – opened 2011 and earlier, 2012 group – opened 2010 and earlier, and 2011 group – opened 2009 and earlier) represent a consistent 'same-store' view of our business. During the months in 2013, 2012, and 2011, the stores opened greater than two years had daily sales growth rates of (compared to the same month in the preceding year):

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
2013	5.0	% 6.5	% 3.4	%								
2012	18.8	% 17.1	% 16.8	% 14.5	% 10.1	% 11.1	% 9.1	% 8.6	% 9.8	% 3.8	% 5.1	% 6.6
2011	16.0	% 18.4	% 19.4	% 19.6	% 19.2	% 19.1	% 18.7	% 16.5	% 15.2	% 18.0	% 18.5	% 17.5

Stores opened greater than five years – The impact of the economy, over time, is best reflected in the growth performance of our stores opened greater than five years (store sites opened as follows: 2013 group – opened 2008 and earlier, 2012 group – opened 2007 and earlier, and 2011 group – opened 2006 and earlier). This group is more cyclical due to the increased market share they enjoy in their local markets. During the months in 2013, 2012, and 2011, the stores opened greater than five years had daily sales growth rates of (compared to the same month in the preceding year):

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
2013	3.2	% 5.6	% 2.3	%								
2012	17.4	% 15.8	% 15.7	% 13.7	% 9.0	% 10.2	% 8.3	% 7.9	% 8.5	% 2.6	% 4.6	% 5.6
2011	15.3	% 17.9	% 19.2	% 19.1	% 17.9	% 18.2	% 17.3	% 15.2	% 14.5	% 17.0	% 17.4	% 16.9

There are three distinct influences to our growth: (1) execution, (2) currency fluctuations, and (3) economic fluctuations. This discussion centers on (2) and (3). First off, currency – the change in currencies in foreign countries (primarily Canada) relative to the United States dollar impacted our growth over the last several years. During 2011 it lifted our growth by 0.7%, in 2012 it lowered our growth by 0.1% (by quarter the impact was down 0.1%, 0.4%, and 0.2% in the first, second, and third quarters, respectively, and then up in the fourth quarter by 0.2%) and in the first quarter of 2013 it lowered our growth by 0.1%.

Regarding economic fluctuations, in 2011 we enjoyed strong growth. This reflected the strengthening economic environment being experienced by our customers. While the strength did not apply to all customers and to all geographies we serve, it was strong enough to produce acceptable results. During 2012, the growth in the first three and a half months generally continued the relative strength we saw in 2011. Then we experienced two distinct economic slowdowns. The first occurred in the late April/May time frame, and then moderated until September. The second occurred in the October/November time frame. This was exaggerated by an unusual business day comparison in October (23 days in 2012 versus 21 days in 2011 - the maintenance portion of our business is often linked to monthly spend patterns, which are not as business day dependent, this can dilute the daily growth picture given the change in business day divisor) and the impact of Hurricane Sandy. During the first three months of 2013, the weakness has continued. Both January and February experienced some negative impact from weather, and January

experienced a very weak start due to extended holiday shutdown. However, with the benefit of hindsight, we believe the economic activity of our customers slowed from January to February and slowed further from February to March. This is evident in the two and five year comparisons above.

Table of Contents

SEQUENTIAL TRENDS:

We find it helpful to think about the monthly sequential changes in our business using the analogy of climbing a stairway – This stairway has several predictable landings where there is a pause in the sequential gain (i.e. April, July, and October to December), but generally speaking, climbs from January to October. The October landing then establishes the benchmark for the start of the next year.

History has identified these landings in our business cycle. They generally relate to months with impaired business days (certain holidays). The first landing centers on Easter, which alternates between March and April (Easter occurred in March in 2013, and in April in 2012 and 2011), the second landing centers on July 4th, and the third landing centers on the approach of winter with its seasonal impact on primarily our construction business and with the Christmas / New Year holidays. The holidays we noted impact the trends because they either move from month-to-month or because they move around during the week.

The table below shows the pattern to our sequential change in our daily sales. The line labeled 'Past' is an historical average of our sequential daily sales change for the period 1998 to 2003. We chose this time frame because it had similar characteristics, a weaker industrial economy in North America, and could serve as a benchmark for a possible trend line. The '2013', '2012', and '2011' lines represent our actual sequential daily sales changes. The '13Delta', '12Delta', and '11Delta' lines indicate the difference between the 'Past' and the actual results in the respective year.

	Jan.(1)	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Cumulative change from Jan. to Mar.	
Past	0.9	% 3.3	% 2.9	% -0.3	% 3.4	% 2.8	% -2.3	% 2.6	% 2.6	% -0.7	% 6.2	%
2013	-0.4	% 2.0	% 3.4	%							5.4	%
13Delta	-1.3	% -1.3	% 0.5	%							-0.8	%
2012	-0.3	% 0.5	% 6.4	% -0.8	% 0.5	% 2.5	% -2.7	% 1.3	% 4.3	% -4.8	% 7.0	%
12Delta	-1.2	% -2.8	% 3.5	% -0.5	% -2.9	% -0.3	% -0.4	% -1.3	% 1.7	% -4.1	% 0.8	%
2011	-0.2	% 1.6	% 7.0	% 0.9	% 4.3	% 1.7	% -1.0	% 1.4	% 3.4	% 0.7	% 8.7	%
11Delta	-1.1	% -1.7	% 4.1	% 1.2	% 0.9	% -1.1	% 1.3	% -1.2	% 0.8	% 1.4	% 2.5	%

(1) The January figures represent the percentage change from the previous October, whereas the remaining figures represent the percentage change from the previous month.

A graph of the sequential daily sales change pattern discussed above, starting with a base of '100' in the previous October and ending with the next October, would be as follows:

Table of Contents

END MARKET PERFORMANCE:

Fluctuations in end market business – The sequential trends noted above were directly linked to fluctuations in our end markets. To place this in perspective – approximately 50% of our business has historically been with customers engaged in some type of manufacturing. The daily sales to these customers grew, when compared to the same period in the prior year, as follows:

	Q1	Q2	Q3	Q4	Annual	
2013	7.0	%				
2012	20.3	% 15.8	% 14.0	% 9.7	% 14.9	%
2011	15.5	% 18.5	% 18.3	% 21.0	% 20.0	%

Our manufacturing business consists of two subsets: the industrial production business (this is business where we supply products that become part of the finished goods produced by our customers) and the maintenance portion (this is business where we supply products that maintain the facility or the equipment of our customers engaged in manufacturing). The industrial business is more fastener centered, while the maintenance portion is represented by all product categories.

The best way to understand the change in our industrial production business is to examine the results in our fastener product line. From a company perspective, sales of fasteners grew, when compared to the same period in the prior year, as follows (note: this information includes all end markets):

	Q1	Q2	Q3	Q4	Annual	
2013	1.7	%				
2012	15.4	% 8.0	% 6.0	% 2.6	% 7.8	%
2011	15.4	% 18.1	% 13.6	% 15.9	% 15.7	%

By contrast, the best way to understand the change in the maintenance portion of the manufacturing business is to examine the results in our non-fastener product lines. From a company perspective, sales of non-fasteners grew, when compared to the same period in the prior year, as follows (note: this information includes all end markets):

	Q1	Q2	Q3	Q4	Annual	
2013	10.8	%				
2012	25.1	% 21.1	% 18.0	% 13.6	% 19.2	%
2011	26.5	% 27.3	% 26.9	% 27.4	% 27.0	%

The non-fastener business demonstrated greater relative resilience when compared to our fastener business and to the distribution industry in general, due to our strong FAST SolutionsSM (industrial vending) program; this is discussed in greater detail later in this document. However, this business has not been immune to the impact of a weakening industrial environment.

The patterns related to the industrial production business, as noted above, are influenced by the movements noted in the Purchasing Manufacturers Index ('PMI') published by the Institute for Supply Management (<http://www.ism.ws/>), which is a composite index of economic activity in the manufacturing sector. The PMI in 2013, 2012, and 2011 was as follows:

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
2013	53.1	54.2	51.3									
2012	53.7	51.9	53.3	54.1	52.5	50.2	50.5	50.7	51.6	51.7	49.9	50.2
2011	59.2	59.6	59.3	59.4	53.5	55.8	52.3	53.2	53.2	51.5	52.3	52.9

For background to readers not familiar with the PMI index, it is a monthly indicator of the economic health of the manufacturing sector. Five major indicators that influence the PMI index are new orders, inventory levels, productions, supplier deliveries, and the employment environment. When a PMI of 50 or higher is reported, this indicates expansion in the manufacturing industry compared to the previous month. If the PMI is below 50, this represents a contraction in the manufacturing sector. (Note – the Institute for Supply Management made annual adjustments to reflect seasonal factors for the PMI index effective for the January 2013 report. This table represents the updated PMI index.)

Table of Contents

Our non-residential construction customers have historically represented 20% to 25% of our business. The daily sales to these customers grew, when compared to the same period in the prior year, as follows:

	Q1	Q2	Q3	Q4	Annual		
2013	2.9	%					
2012	17.1	%	12.7	% 8.2	% 4.2	% 10.3	%
2011	17.7	%	15.8	% 15.8	% 17.4	% 17.1	%

We believe the weakness in the economy in the fourth quarter of 2012 and the first quarter of 2013, particularly in the non-residential construction market, was amplified by the economic policy uncertainty in the United States.

A graph of the sequential daily sales trends to these two end markets in 2013, 2012, and 2011, starting with a base of '100' in the previous October and ending with the next October, would be as follows:

Manufacturing

Non-Residential Construction

Table of Contents**GROWTH DRIVERS OF OUR BUSINESS**

We grow by continuously adding customers and by increasing the activity with each customer. We believe this growth is enhanced by our close proximity to our customers, which allows us to provide a range of services and product availability that our competitors can't easily match. Historically, we expanded our reach by opening stores at a very fast pace. These openings were initially in the United States, but expanded beyond the United States beginning in the mid 1990's.

In our first ten years of being public (1987 to 1997), we opened stores at a rate approaching 30% per year. In the next ten years, we opened stores at an annual rate of approximately 10% to 15% and, over the last five years, at a rate of approximately 3% to 8% (we currently expect to open approximately 65 to 80 stores in 2013, or approximately 2.5% to 3.0%). As we gained proximity to more customers, we continued to diversify our growth drivers. This was done to provide existing store personnel with more tools to grow their business organically, and the results of this are reflected in our earlier discussion on sales growth at stores opened greater than five years. In the early 1990's, we began to expand our product lines, and we added new product knowledge to our bench. This was our first big effort to diversify our growth drivers. The next step began in the mid to late 1990's when we began to add sales personnel with certain specialties or focus. This began with our National Accounts group in 1995, and, over time, has expanded to include individuals dedicated to: (1) sales related to our internal manufacturing division, (2) government sales, (3) internet sales, (4) specific products (most recently metalworking), and (5) FAST SolutionsSM (industrial vending). Another step occurred at our sales locations (this includes Fastenal stores as well as strategic account stores and in-plant locations) and at our distribution centers, and began with a targeted merchandising and inventory placement strategy that included our 'Customer Service Project' approximately ten years ago and our 'Master Stocking Hub' initiative approximately five years ago. This strategy allowed us to better target where to stock certain products (local store, regional distribution center, master stocking hub, or supplier) and allowed us to improve our fulfillment, lower our freight costs, and improve our ability to serve a broader range of customers. During 2013, we intend to expand our store based inventory around select industries (with an emphasis on fasteners and safety products).

Our FAST SolutionsSM (industrial vending) operation is a rapidly expanding component of our business. We believe industrial vending is the next logical chapter in the Fastenal story; we also believe it has the potential to be transformative to industrial distribution, and that we have a 'first mover' advantage. We are investing aggressively to maximize this advantage. At our investor day in May 2011, we discussed our progress with industrial vending. In addition to our discussion regarding progress, we discussed our goals with the rollout of the industrial vending machines. One of the goals we identified related to our rate of 'machine signings' (the first category below) – our goal was simple, sign 2,500+ machines per quarter (or an annualized run rate of 10,000 machines). In 2012, we hit our annual goal of 10,000 machines during July, and the momentum has continued as we finished the year. We intend to continue our aggressive push with FAST SolutionsSM (industrial vending) and, to this end, established an internal goal to sign 30,000 machines in 2013, or 2,500 per month rather than per quarter. This is an aggressive goal, but we believe we can hit this run rate during 2013. In addition, during 2012 we developed plans to (1) reinvigorate our fastener growth and (2) improve the performance (i.e. sales growth) at under-performing locations. These plans centered on expanding our sales team for our industrial production business, improving our delivery systems for our other fastener business, and expanding the team that supports under-performing stores and districts.

During 2013 we have several distribution initiatives. The first centers on a multi-year initiative to add significant automation. Currently, our facilities in Indianapolis, IN, Denton, TX, and Winona, MN contain the most extensive automation. In addition, we have plans to begin utilizing a new 'highly automated' distribution facility adjacent to our existing Indianapolis facility for replenishing our industrial vending machines. It may seem odd to see these initiatives listed under the category of 'growth drivers' versus 'efficiency or profit drivers'; however, we see these changes as enhancing our fill rates and as freeing up time at the store, both of which help drive sales growth.

Table of Contents

The following table includes some statistics regarding our industrial vending business.

		Q1	Q2	Q3	Q4	Annual
Number of vending machines in contracts signed during the period ¹	2013	5,728				
	2012	4,568	4,669	5,334	5,591	20,162
	2011	1,405	2,107	2,246	2,084	7,842
Cumulative machines installed ²	2013	25,447				
	2012	9,798	13,036	17,013	21,095	
	2011	2,659	3,867	5,642	7,453	
Percent of installed machines that are a FAST 5000 (our most common helix vending machine) ³	2013	54.3	%			
	2012	70.1	% 66.2	% 60.2	% 57.2	%
	2011	78.6	% 76.0	% 74.7	% 72.8	%
Percent of total net sales to customers with vending machines ⁴	2013	27.5	%			
	2012	17.8	% 20.8	% 23.2	% 25.8	%
	2011	8.9	% 10.5	% 13.1	% 15.7	%
Daily sales growth to customers with vending machines ⁵	2013	23.9	%			
	2012	33.9	% 34.3	% 32.9	% 28.6	%
	2011	50.6	% 43.9	% 42.5	% 40.7	%

¹ This represents the gross number of machines signed during the quarter, not the number of contracts.

² This represents the number of machines installed and dispensing product on the last day of the quarter.

³ This information is intended to highlight the mix change in the machines deployed as our business expands beyond the flagship FAST 5000 machine.

⁴ The percentage of total sales (vended and traditional) to customers currently using a vending solution.

⁵ The growth in total sales (vended and traditional) to customers currently using a vending solution compared to the same period in the preceding year.

Table of Contents

PROFIT DRIVERS OF OUR BUSINESS

We grow our profits by continuously working to grow sales and to improve our relative profitability. We also grow our profits by allowing our inherent profitability to shine through – we refer to this as the 'pathway to profit'. The distinction is important.

We achieve improvements in our relative profitability by increasing our gross margin, by structurally lowering our operating expenses, or both. We advance on the 'pathway to profit' by increasing the average store size (measured in terms of monthly sales), and by allowing the changing store mix to improve our profits. This is best explained by comparing the varying profitability of our 'traditional' stores in the table below. The average store size for the group, and the average age, number of stores, and pre-tax earnings data by store size for the first quarter of 2013, 2012, and 2011, respectively, were as follows:

Sales per Month	Average Age (Years)	Number of Stores	Percentage of Stores	Pre-Tax Earnings Percentage	
Three months ended March 31, 2013					Average store sales = \$88,267
\$0 to \$30,000	5.4	261	9.8	% -11.6	%
\$30,001 to \$60,000	8.2	771	29.0	% 13.9	%
\$60,001 to \$100,000	10.9	765	28.8	% 22.5	%
\$100,001 to \$150,000	12.8	437	16.4	% 25.5	%
Over \$150,000	16.0	305	11.5	% 29.0	%
Strategic Account/Overseas Store		121	4.5	%	
Company Total		2,660	100.0	% 21.7	%

Three months ended March 31, 2012