

■ **Reports Digest**

**Signs of Optimism Start to Appear in Distributors' Quarterly Reports**

*This article is based on comments made during distributors' quarterly earnings calls.*

Fourth quarter 2009 continued to be tough on distributors. While the recession has technically come to an end, recovery remains elusive. However, signs of improvement are appearing, and companies are starting to plan for the future rather than staying focused on the now.

"It's the expectation that we are at the beginning of an economic recovery based on GDP numbers that are being reported out of the U.S. and Europe. Certainly parts of Asia and Latin America," said Bob Eck, president and CEO of electrical, electronic wire/cable and fasteners distributor Anixter International, Glenview, IL. "As you look at the world and see economic recovery, it's our expectation that we will begin to see pickup as a direct result."

**Business Expansion**

Perhaps as a result, in the fourth quarter, acquisition chatter picked up and some large deals were completed. Arrow Electronics, Melville, NY, completed the acquisition of A. E. Petsche, and Avnet expanded its presence in Southeast Asia with the acquisition of Sunshine Stock Joint Company in Vietnam.

But few executives were willing to claim the mergers and acquisitions arena was ready to return to more normal levels of activity.

"I think it's still an environment where if you don't need to sell your business right now, you're probably not going to be overly interested in doing that," said William DeLaney, CEO of Houston, TX-based foodservice distributor Sysco.

Dennis Letham, Anixter's CFO, agrees: "There just really isn't much activity out there in the smaller-sized deals. Certainly we all see the paper every day, and we've seen the bigger deals that have gotten done

■ **Sales Trends**

**A Selection of Reports from Various Wholesale Sectors**

	Prev. Qtr.	Current Qtr.
<b>United Stationers</b>	↓ 6.8%	↓ 5.5%
<b>Owens &amp; Minor</b>	↑ 13.9%	↑ 11%
<b>Motion Industries</b>	↓ 22%	↓ 18%
<b>Reliance Steel &amp; Aluminum</b>	↓ 51.8%	↓ 39%
<b>Watsco Inc.</b>	↓ 15%	↑ 18%
<b>W.W. Grainger</b>	↓ 14%	↑ 3%
<b>Fastenal Co.</b>	↓ 21.7%	↓ 12.5%
<b>MSC Industrial Direct (1Q)</b>	↓ 21.1%	↓ 12%
<b>Anixter</b>	↓ 20%	↓ 18.8%
<b>Interline Brands</b>	↓ 12.5%	↓ 11.4%
<b>Praxair</b>	↓ 20%	↑ .004%
<b>Avnet (2Q)</b>	↓ 3.1%	↑ 13.2%

*Numbers include acquisitions. All current-quarter numbers fourth-quarter 2009 unless otherwise specified. More earnings at [www.www.mdm.com](http://www.www.mdm.com).*

recently, but there does seem to be a dearth of small deals in the market that fit with our strategy and our business model."

That said, Anixter is "open to assessing" opportunities as they arise, Letham said.

"One of the old sayings in M&A is you've got have a willing buyer and a willing seller," Avnet CEO Roy Vallee said. Avnet is headquartered in Phoenix, AZ. "And during the downturn I guess I would describe Avnet as a reluctant buyer. Now if you fast-forward, we're actually quite comfortable with capital markets. Therefore we are interested in making investments. On the seller side, there are still substantial

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**About This Report**

This is the MDM Public Distributor Report, provided on a quarterly basis to subscribers of Modern Distribution Management.

On the first three pages, you will find recent sales figures from various sectors, as well as a Reports Digest, with information you can use from public distributor and manufacturer reports and earnings calls, distilled by MDM.

On page three of this Public Distributor Report, we feature Airgas, which is fighting off a \$7 billion takeover attempt by Air Products.

The latest numbers for dozens of public distributors across various wholesale sectors are on the back page and provided by Robert W. Baird & Co.

We hope you will view this quarterly feature as another way to gather ideas, stay on top of the moves of your largest competitors, and hone your business plan.

strategic pressures in distribution and they tend to favor global scale and scope.

"I'm reasonably comfortable that our M&A activity will be picking up over the next few quarters," Vallee said.

In the meantime, distributors said they will continue to focus on organic growth and expansion outside of acquisitions. Winona, MN-based Fastenal announced plans to add new stores at a rate of around 20 stores per month during the second half of 2010. "We can do that. We've done that for years. We're going to invest aggressively to grow," said Dan Fiorness, CFO. The first half of the year will be focused on increasing average existing store size.

### Price Pressures/Commodities

Uncertainty in commodity markets continued to have an impact on distributors in the fourth quarter. "Steel prices are pretty much flat and down in summer, and they've actually started rising through the last four months of the year," Fastenal CEO Will Oberton said.

But forecasting future prices is difficult. "We anticipate a little bit of inflation in steel but it's really hard to tell because it has a lot to do with what happens with the economy and the world, mainly China," Oberton says. Inflation is expected to have some positive impact on Fastenal's margins in the second or third quarter of 2010.

The other problem with forecasting the impact of commodity pricing is the lag time between spot market prices and product price increases, Anixter's Letham said. "In the current environment where product demand remains

comparatively weak, there remains an estimated five- to six-month lag," he said.

Copper prices had a negative impact on Anixter's sales during every quarter of 2009, though the fourth quarter showed some improvement. Recent increases in the spot price of copper has led to some price increases, Eck said.

Sysco COO Kenneth Spitler called the price environment tough. "We're used to being the market leader so we're used to staving off price attacks. It's been a lot more frequent, and of course the customer base gets more upset, so we've had to be cautiously defensive, but there's definitely an uptick to it," Spitler said.

### Outlook for 2010

While the outlook for the economy remains somewhat murky, cautious optimism is returning to the conversation as more companies are willing to include forecast discussion in their earnings releases.

"Being a Midwesterner and an accountant makes me a truly conservative person. So for me to come out and say something positive into the future is a pretty rare event," said Fastenal's Fiorness. "But when I look at the trends, as of last October ... our sequential numbers not only make sense but are making us more positive in our outlook."

Pharmaceutical distributor Owens & Minor, Richmond, VA, announced it expected revenue growth in the range of 4 percent to 6 percent in the next year. Avnet also forecast single-digit growth in 2010, with higher growth in emerging markets. - *Jenel Stelton-Holtmeier*

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**Publisher**  
Thomas P. Gale  
tom@mdm.com

**Editor**  
Lindsay Konzak  
lindsay@mdm.com

**Associate Publisher**  
Craig Riley  
craig@mdm.com

**Associate Editor**  
Jenel Stelton-Holtmeier  
jenel@mdm.com

### Contact Information

Questions, comments, article proposals, address changes or subscription service to:

Gale Media, Inc.  
3100 Arapahoe Avenue, Ste 500A, Boulder, CO 80303  
Tel: 303-443-5060 Fax: 303-443-5059  
Website: <http://www.mdm.com>

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Published twice monthly; \$345/yr., \$365 U.S. funds other countries; \$169 each additional subscription to a company (\$189 other countries). Six-month and two-year terms are now available. For group subscription rates and site licenses, please contact Hadley Fable at 303-443-5060.

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ISSN 0544-6538

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■ *Distributor Focus*

## The Back & Forth Between Airgas and Air Products

Air Products took its fight for Airgas public this month – though it has been courting the industrial gases and hardgoods distributor since October. Airgas has rejected each offer; the latest offer is for \$60 per share in an all-cash deal. The value of the transaction is \$7 billion, including \$5.1 billion of equity and \$1.9 billion of debt.

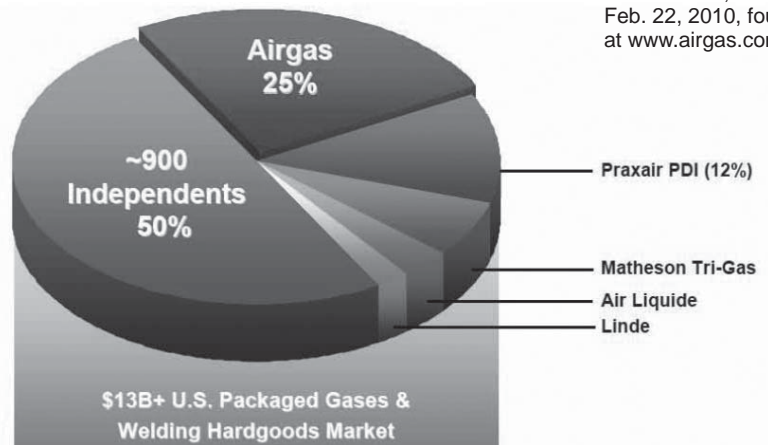
“The Airgas Board of Directors is unanimous in its belief that the Air Products offer significantly undervalues Airgas and fails to reflect the value of our industry-leading position and future growth prospects,” said CEO Peter McCausland in an announcement encouraging shareholders not to tender their shares. Showing the market may agree with that assessment, on Feb. 24, Airgas shares were trading above \$63.

Despite Airgas’ continued rejections of the attempted takeover, Air Products told analysts at the Barclays 2nd Annual Industrial Select Conference that it is “committed to completing the transaction” through all necessary paths, including divestments to comply with regulatory requirements, legal moves and a proxy contest.

In an “open letter to Airgas employees” posted at [www.airgasoffer.com](http://www.airgasoffer.com), CEO John McGlade said: “You might be wondering why we are looking to return to the U.S. packaged gas business. In 2002, our U.S. packaged gas business had limited breadth and scope and at that time, we examined our strategic priorities and decided to exit that business in order to focus on other areas where we could grow and improve our company.”

McGlade says packaged gas is a growth area and that Airgas can grow quickly on a global scale with Air Products’ international reach.

How Airgas Views the Market



Source: Airgas Presentation, Feb. 22, 2010, found at [www.airgas.com](http://www.airgas.com)

### From Airgas’ 3Q Earnings Call

Quotes from CEO Peter McCausland:

#### M&A Plans

“Acquisition activity has been slow as potential sellers assess their business in the wake of the downturn. However, our pipeline has been recovering as the anticipation of improving business conditions has stirred some interest.”

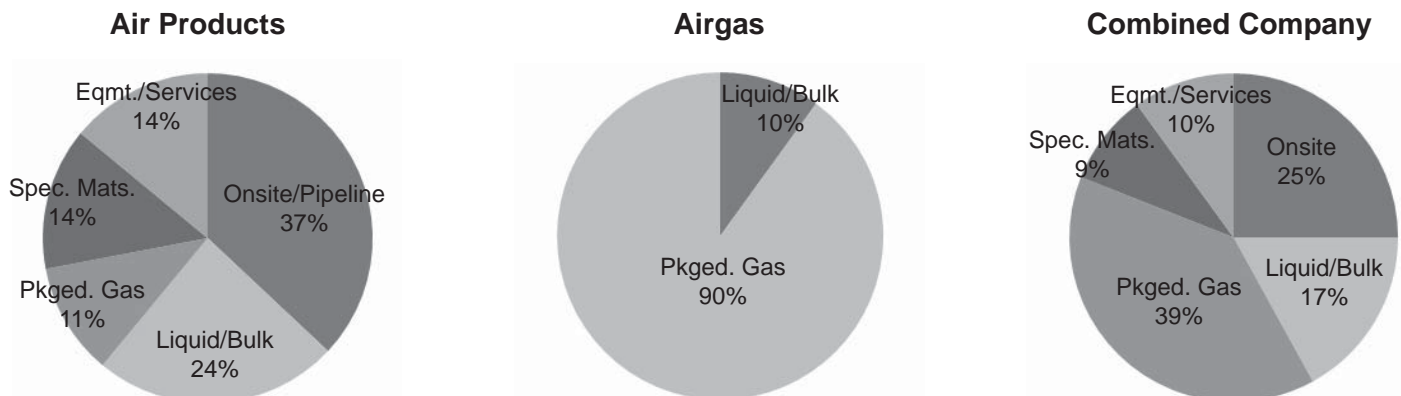
#### Cross-Selling Opportunities

“Safety products present a strong cross-sell opportunity as the value in vendor consolidation is greater for our customers in today’s economy.”

#### Margin Pressure

“What we’re seeing is the end of recession, beginning of recovery, normal price competition. We’re not concerned about it, and our gross margins have actually improved.”

### Air Products’ View of Proposed Combined Company



Source: Air Products Presentation, Feb. 17, 2010, found at [www.airproducts.com](http://www.airproducts.com)

## Distribution Financial Metrics and Trading Multiples

(Data as of Dec. 31, 2009)

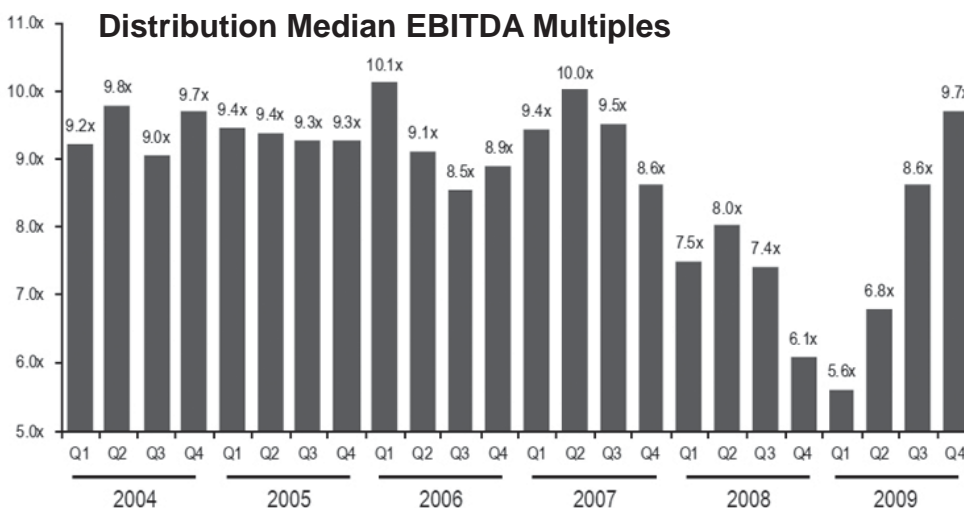
(\$ in millions)

Company	Ticker	Enterprise Value	LTM					EV to LTM Sales	EV to LTM EBITDA	ROIC	Working Capital/Sales
			Sales	Sales Growth	Gross Margin	EBITDA	EBITDA Margin				
Airgas Inc. *	ARG	\$5,523	\$4,012	(8.3%)	54.8%	\$690	17.2%	1.4 x	8.0 x	8.5%	6.9%
AM Castle & Co.	CAS	392	953	(36.5%)	12.8%	13	1.3%	0.4	N/M	N/M	23.7%
Anixter International Inc. *	AXE	2,350	5,223	(15.3%)	22.9%	252	4.8%	0.4	9.3	7.5%	24.8%
Applied Industrial Technologies Inc.	AIT	956	1,817	(14.1%)	26.9%	113	6.2%	0.5	8.5	11.1%	17.2%
Barnes Group Inc. *	B	1,271	1,043	(27.3%)	35.5%	122	11.7%	1.2	10.4	5.9%	22.2%
Beacon Roofing Supply Inc. *	BECN	1,007	1,734	(2.8%)	23.7%	140	8.1%	0.6	7.2	9.4%	16.1%
BlueLinx Holdings Inc.	BXC	426	1,782	(41.7%)	11.1%	(21)	N/M	0.2	N/M	N/M	13.3%
Builders FirstSource, Inc. *	BLDR	342	759	(26.9%)	21.2%	(46)	N/M	0.5	N/M	N/M	9.2%
Bunzl plc	BNZL	4,843	7,415	(2.4%)	21.2%	500	6.7%	0.7	9.7	12.6%	5.5%
DXP Enterprises Inc.	DXPE	296	639	(10.3%)	29.0%	43	6.8%	0.5	6.8	7.0%	18.4%
Fastenal Co. *	FAST	5,981	1,999	(13.7%)	51.9%	365	18.3%	3.0	16.4	20.4%	33.2%
Genuine Parts Co.	GPC	6,201	10,106	(9.1%)	29.6%	752	7.4%	0.6	8.2	14.8%	22.0%
Houston Wire & Cable Company *	HWCC	228	267	(28.9%)	21.2%	16	5.9%	0.9	14.4	9.5%	33.8%
Hutig Building Products Inc.	HBPI	45	477	(34.2%)	17.4%	(27)	N/M	0.1	N/M	N/M	8.6%
Interline Brands Inc. *	IBI	806	1,082	(11.2%)	37.0%	85	7.8%	0.7	9.5	5.8%	21.1%
Kaman Corp.	KAMN	657	1,194	(1.3%)	26.2%	68	5.7%	0.6	9.6	9.9%	27.3%
Lawson Products Inc.	LAWS	140	396	(21.4%)	57.2%	12	3.0%	0.4	11.9	3.5%	17.5%
MSC Industrial Direct Co. Inc. *	MSM	2,936	1,490	(16.3%)	46.2%	232	15.6%	2.0	12.7	16.4%	23.9%
Park-Ohio Holdings Corp.	PKOH	392	763	(28.5%)	14.2%	38	5.0%	0.5	10.3	3.9%	28.7%
Pool Corp *	POOL	1,183	1,568	(14.1%)	29.2%	107	6.8%	0.8	11.1	11.0%	19.2%
Reliance Steel & Aluminum Co.	RS	4,167	6,188	(25.3%)	23.5%	372	6.0%	0.7	11.2	5.0%	16.9%
Rexel SA	RXL	7,471	17,290	1.0%	23.9%	668	3.9%	0.4	11.2	4.0%	11.4%
Smith International Inc.	SII	10,159	9,291	(7.2%)	28.6%	1,331	14.3%	1.1	7.6	9.6%	32.2%
Watsco Inc. *	WSO	1,705	1,773	0.6%	24.4%	83	4.7%	1.0	20.4	6.8%	29.0%
WESCO International Inc. *	WCC	1,755	4,921	(20.2%)	19.7%	232	4.7%	0.4	7.6	9.7%	13.4%
Wolseley plc	WOS	7,524	24,082	(26.3%)	27.5%	350	1.5%	0.3	N/M	N/M	7.9%
WW Grainger Inc. *	GWW	7,120	6,181	(10.0%)	43.9%	801	13.0%	1.2	8.9	19.3%	16.5%
Median		\$1,271	\$1,773	(14.1%)	26.2%	\$122	6.5%	0.6 x	9.7 x	9.4%	18.4%

\* = Companies covered by Baird Research

The table above highlights key financial metrics and trading multiples for 27 publicly traded distributors in the industrial and building products industries.

The chart below illustrates historical median EBITDA multiples for the above companies calculated using LTM EBITDA as of the quarter shown and the enterprise value as of the last day of the quarter. Please see Definitions at bottom of page.



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### Definitions

LTM means latest twelve months. Enterprise Value ("EV") means market capitalization of a company's equity plus preferred stock plus total interest bearing debt (including capitalized leases) net of any cash or cash equivalents. EBITDA means earnings before interest, taxes, depreciation and amortization. In certain cases earnings have been adjusted for certain disclosed income or expense items considered to be non-recurring in nature. ROIC means return on invested capital and is defined as tax-effected EBIT divided by the sum of the book value of equity plus net debt. Working Capital is calculated as current assets, less cash, minus current liabilities excluding short-term borrowings and current portion of long-term debt.