

FASTENAL CO
Form 10-K
February 09, 2010
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SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

☒ **Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the fiscal year ended December 31, 2009,

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)

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Minnesota
(State or other jurisdiction of
incorporation or organization)

41-0948415
(I.R.S. Employer
Identification No.)

2001 Theurer Boulevard

Winona, Minnesota
(Address of principal executive offices)

55987-0978
(Zip Code)
(507) 454-5374

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value \$.01 per share	The NASDAQ Stock Market

Securities registered pursuant to Section 12(g):

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act: Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act: Yes ☐ No ☒

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

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.

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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 ☒

The aggregate market value of the Common Stock held by non-affiliates of the registrant as of June 30, 2009, the last business day of the registrant's most recently completed second fiscal quarter, was \$4,385,653,845, based on the closing sale price of the Common Stock on that date. For purposes of determining this number, all executive officers and directors of the registrant as of June 30, 2009 are considered to be affiliates of the registrant. This number is provided only for the purposes of this report on Form 10-K and does not represent an admission by either the registrant or any such person as to the status of such person.

As of February 5, 2010, the registrant had 147,430,712 shares of Common Stock issued and outstanding.

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ANNUAL REPORT ON FORM 10-K

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DOCUMENTS INCORPORATED BY REFERENCE

Portions of our Proxy Statement for the annual meeting of shareholders to be held Tuesday, April 20, 2010 (Proxy Statement) are incorporated by reference in Part III.

FORWARD LOOKING STATEMENTS

This Form 10-K and other portions of our 2009 Annual Report to Shareholders of which this Form 10-K forms a part contain statements that are not historical in nature and that are intended or may be interpreted to be, and are hereby identified as, forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995 (the Reform Act), including statements regarding (1) the goals of our long-term growth strategy, pathway to profit, at the time the strategy was implemented, including planned decreases in the rate of new store openings from our then historic rate, planned additions to our outside sales personnel, the expected funding of such additions out of cost savings resulting from the slowing of the rate of new store openings, the growth in average store sales expected to result from this strategy, our ability to capture leverage and working capital efficiency expected to result from this strategy, and our ability to achieve our pre-tax profit and operating margin goals and increase overall productivity as a result of this strategy, (2) the effect of the current economic setback on our pathway to profit strategy, including the expected time frame for returning our rate of new store openings to the range initially established by the strategy and the anticipated delay in achieving the financial goals of the strategy, (3) our ability to return to sales growth in the near future, (4) our ability to improve gross margins in 2010, (5) our working capital goals and expected returns on total assets when working capital is appropriately managed, (6) the future payment of dividends, (7) 2010 capital expenditures, (8) the expansion of foreign operations and the growth expected to result from that expansion, (9) new distribution center openings, (10) markets for North American stores, (11) expansion of owned store locations, (12) addition of new products, (13) the percentage of net sales expected to be contributed by manufacturing and support services, (14) protection from economic downturns believed to be provided by the number of our customers and varied markets they represent, (15) our ability to mitigate the effects of rising fuel prices, (16) the funding of our expansion plans, (17) the typical time required before new stores become profitable and achieve operating results comparable to existing stores, (18) the rate of growth, and variability, of sales at older store locations, (19) the expected amount of future compensation expense resulting from existing stock options, (20) growth in our market share and our ability to capitalize upon that growth in the future, and (21) the expected impact of the Holo-Krome acquisition on sales in 2010. In addition, certain statements in our future filings with the Securities and Exchange Commission, in our press releases and in oral statements made by or with approval of our executive officers constitute or will constitute forward-looking statements under the Reform Act. Certain risks and uncertainties that could cause actual results to differ materially from those predicted in such forward-looking statements are described below. We assume no obligation to update either such forward-looking statements or the discussion of such risks and uncertainties.

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CERTAIN RISK AND UNCERTAINTIES

The following factors are among those that could cause our actual results to differ materially from those predicted in the forward-looking statements described above: (1) a prolonged downturn, or further deterioration, in the economy or in the manufacturing or commercial construction industries, changes in the expected rate of new store openings, difficulties in successfully attracting and retaining additional qualified outside sales personnel, and difficulties in changing our sales process could adversely impact our ability to achieve the goals of our pathway to profit initiative or the expected time frame for achieving those goals, (2) a prolonged downturn, or further deterioration, in the economy or in the manufacturing or commercial construction industries could prolong our sales contraction, (3) a prolonged downturn, or further deterioration, in the economy or in the manufacturing or commercial construction industries, a change in our purchasing patterns, a significant change in commodity prices, or increased competitive pressure on our selling prices could adversely affect our ability to improve gross margins in 2010, (4) a prolonged downturn, or further deterioration, in the economy or in the manufacturing or commercial construction industries, a change, from that projected, in the number of North American markets able to support stores, or an inability to recruit and retain qualified employees could cause the rate of new store openings to change from that expected, (5) a prolonged downturn, or further deterioration, in the economy or in the manufacturing or commercial construction industries, a change in accounts receivable collections, a change in raw material costs, a change in buying patterns, or a change in vendor production lead times could cause us to fail to attain our goals regarding working capital and rates of return on assets, (6) changes in our financial condition or results of operations could cause us to modify our dividend practices, (7) changes in the rate of new store openings could cause us to modify our planned 2010 capital expenditures, (8) difficulty in adapting our business model to different foreign business environments could alter our plans regarding expansion of foreign operations and negatively impact the growth expected to result from that expansion, (9) a change in our store format or the presence of a competitor's store could alter our projections regarding the number of markets for North American stores, (10) availability of cost-effective real estate, changes in our cash position, a change in distribution technology, or a change in our distribution model could delay the opening of new distribution centers as our number of stores increases, (11) changes in the commercial real estate market, a change in our cash position, or a change in our business model could cause us to change our plans regarding expansion of owned store locations, (12) changes in our cash position, a change in our business model or a change in the manufacturing or commercial construction industries could cause us to alter the introduction of new products, (13) an economic downturn across multiple industries and geographic regions could negate the protections thought to be provided to us by the number of our customers and the varied markets they represent, (14) our ability to pass freight costs on to our customers could be adversely impacted by, in the short term, changes in fuel prices and by competitive selling pressures, (15) a change in our ability to generate free cash flow resulting from a slowdown in our sales or our inability to manage expenses could negatively impact the funding of our expansion plans, (16) an upturn or downturn in the economy could alter, from historic norms, the time it typically takes a new store to achieve profitability or operating results comparable to existing stores and the rate of growth, and variability, of sales at older store locations, (17) a change in accounting for stock-based compensation or the assumptions used could change the amount of stock-based compensation recognized, (18) changes in our competitors' business models could negatively impact the growth of our market share and our ability to capitalize on that growth in the future, and (19) a strengthening of the economy or an improvement in the manufacturing and commercial construction industries could change the impact of the Holo-Krome acquisition on our 2010 sales. A discussion of other risks and uncertainties which could cause our operating results to vary from anticipated results or which could materially adversely affect our business, financial condition, or operating results is included later in this Form 10-K under the heading entitled Item 1A. Risk Factors.

PRESENTATION OF DOLLAR AMOUNTS

All dollar amounts in this Form 10-K are presented in thousands, except for share and per share information or unless otherwise noted.

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Fastenal Company (together with our wholly owned subsidiaries, hereinafter referred to as Fastenal or the Company or by terms such as we, our, or us) began as a partnership in 1967, and was incorporated under the laws of Minnesota in 1968. As of December 31, 2009, we had 2,369 store locations located in the United States (50 states), Puerto Rico, Canada (10 provinces), Mexico (25 states), Singapore, China, The Netherlands, Hungary, and Malaysia, and employed 8,491 people at these store locations. In addition, there were 3,554 people employed in various support positions. These support roles consisted of distribution and manufacturing (2,187 people) and administrative and sales support (1,367 people).

We sell industrial and construction supplies in a wholesale and retail fashion. As of December 31, 2009 these industrial and construction supplies were grouped into ten product lines described further below.

We operated 14 distribution centers in North America as of December 31, 2009 from which we distribute products to our store and in-plant locations.

Our Internet address for corporate and investor information is www.fastenal.com. The information contained on this website or connected to our website is not incorporated by reference into this Annual Report on Form 10-K and should not be considered part of this report.

Development of the Business

Fastenal began in 1967 with a marketing strategy of supplying threaded fasteners to customers in small, medium-sized, and, in subsequent years, large cities. We believe our success can be attributed to our ability to offer our customers a full line of products at convenient locations and to the high quality of our employees.

We opened our first store in Winona, Minnesota, a city with a population of approximately 25,000. The following table shows our consolidated net sales for each fiscal year during the last ten years and the number of our store locations at the end of each of the last ten years:

	2009	2008	2007	2006	2005	2004	2003	2002	2001	2000
Net sales (in millions)	\$ 1,930.3	2,340.4	2,061.8	1,809.3	1,523.3	1,238.5	994.9	905.4	818.3	755.6
Number of stores at year end	2,369	2,311	2,160	2,000	1,755	1,533	1,314	1,169	1,025	897

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As of December 31, we operated store locations in:

Geographic location	2009	2008
United States	2,153	2,097
Puerto Rico	9	8
Canada	169	169
Mexico	32	33
Singapore	1	1
The Netherlands	1	2
China	2	1
Hungary	1	
Malaysia	1	
	2,369	2,311

We have closed 29 stores in our history, and of these locations, we subsequently reopened in six of these markets when the expansion of our product line or the expansion of our distribution network improved profitability of stores in these markets. Of the remaining 23 closed stores, 21 of these stores have a store located within ten miles of the originally closed store location.

We select new locations for our stores based on their proximity to our distribution network, population statistics, and employment data for manufacturing and construction. Historically, we have disclosed that we intend to continue opening new store locations and expect the rate of new store openings to be approximately 7% to 10% per year (calculated on the ending number of stores in the previous year). Given the recent economic slowdown, we decreased this range to 2% to 5% in 2009, but we expect to return to the 7% to 10% rate of annual openings in the latter half of 2010.

We stock all new stores with inventory drawn from all of our product lines. Subsequent to opening, store personnel may supplement the inventory offering to customize the selection to the needs of our local customer base.

We currently have several versions of store locations. The majority of our stores operate as a Fastenal store and stock our expected inventory format. During the 2002 to 2005 period, this format was referred to as the CSP (or Customer Service Project) format. The CSP project was a significant store re-merchandising project during these years.

We believe, based on the demographics of the marketplace in North America, that there is sufficient potential in this geographic area to support at least 3,500 total stores. Many of the new store locations may be in cities in which we currently operate. Fastenal has not operated outside of North America long enough to assess the market potential of those markets.

In addition to the Fastenal store type discussed above, we also operate strategic account stores, strategic account sites, and in-plant sites. A strategic account store is a unique location that sells to multiple large customers and we include these in our store count. A strategic account site is essentially the same, but it typically operates out of an existing store location, rather than a unique location; therefore, it is not included in our store count. An in-plant site is a selling unit located in or near a customer's facility that sells product solely to that customer. In-plant sites are not included in the store count numbers as they represent a customer subset of a store.

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We opened the following stores in the last five years:

	2009	2008	2007	2006	2005
United States	62	138	141	210	198
Puerto Rico	1				
Canada	2	21	11	25	17
Mexico	1	2	9	10	5
Singapore					
The Netherlands					1
China	1				1
Hungary	1				
Malaysia	1				
Total openings	69	161	161	245	222

We plan to open additional stores outside of the United States in the future. The stores located outside the United States contributed approximately 8% of our consolidated net sales in 2009, with approximately 72% of this amount attributable to our Canadian operations.

No assurance can be given that any of the expansion plans described above will be achieved, or that new store locations, once opened, will be profitable.

It has been our experience that near-term profitability has been adversely affected by the opening of new store locations. This adverse effect is due to the start-up costs and the time necessary to generate a customer base. A new store generates its sales from direct sales calls, a slow process involving repeated contacts. As a result of this process, sales volume builds slowly and it typically requires ten to twelve months for a new store to achieve its first profitable month, although this time frame has been longer in the current economic downturn. Of the 33 stores opened in the first quarter of 2009, 11 were profitable in the fourth quarter of 2009.

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The data in the following table shows the change in the average sales of our stores from 2008 to 2009 based on the age of each store. The stores opened in 2009 contributed approximately \$15,172 (or approximately 0.8%) of our consolidated net sales in 2009, with the remainder coming from stores opened prior to 2009.

Age of stores on December 31, 2009	Year opened	Number of stores in group on December 31, 2009	Closed stores ¹	Average sales 2008	Average sales 2009	Percent Change
0 1 year old	2009	69		\$	\$ 220 ²	%
1 2 years old	2008	161		601 ²	465	
2 3 years old	2007	161		543	512	(5.7)
3 4 years old	2006	243	2/0	601	503	(16.4)
4 5 years old	2005	220	2/0	684	557	(18.5)
5 6 years old	2004	217	1/1	815	656	(19.4)
6 7 years old	2003	148	3/0	818	650	(20.5)
7 8 years old	2002	139	1/2	886	732	(17.3)
8 9 years old	2001	125	1/1	1,186	901	(24.1)
9 10 years old	2000	87	0/1	1,077	863	(19.9)
10 11 years old	1999	44		1,301	1,028	(21.0)
11 12 years old	1998	118	0/2	1,233	969	(21.4)
12 16 years old	1994-1997	384	0/2	1,279	977	(23.7)
16+ years old	1967-1993	253		2,205	1,766	(19.9)

¹ We closed ten stores and nine stores and converted one store and two stores in 2009 and 2008, respectively. The respective average sales above were calculated assuming the store closed mid year. The number of closed locations is noted in the table above as 2009 number/2008 number.

² The average sales include sales of stores open for less than the full fiscal year.

As of December 31, 2009, we operated distribution centers in or near Winona, Minnesota; Indianapolis, Indiana; Dallas, Texas; Atlanta, Georgia; Scranton, Pennsylvania; Modesto, California; Seattle, Washington; Akron, Ohio; Salt Lake City, Utah; Greensboro, North Carolina; Kansas City, Kansas; Toronto, Ontario (Canada); Edmonton, Alberta (Canada); and Monterrey, Nuevo Leon (Mexico). These 14 distribution centers give us over 2.6 million square feet of distribution capacity. These distribution centers are located so as to permit twice-a-week to five times-a-week deliveries to our stores using our trucks and overnight delivery by surface common carrier. As the number of stores increases, we intend to add new distribution centers.

Our Information Systems department is responsible for developing, implementing and maintaining computer based technology used to support business functions within Fastenal. Corporate, e-Business and distribution center systems are primarily supported from a central location(s), while each store uses a locally installed Point-Of-Sale (POS) system. The systems consist of both customized and purchased software. A dedicated Wide Area Network (WAN) is used to provide connectivity between systems and authorized users.

Trademarks and Service Marks

We conduct business under various trademarks and service marks, including: Fastenal®, FAS-N-IT®, FNL®, Blackstone®, Rock River®, Blue Global®, Fastenal Racing®, FNL G9®, Equiprite®, Clean Choice®, Bodyguard®, Profitter®, Dynaflo®, FMT®, Tritan®, Caliber®, PowerPhase®, and, as of December 19, 2009, Holo-Krome®. We utilize a variety of designs and tag lines in connection with each of these marks, including *First In Fasteners*. Although we do not believe our operations are substantially dependent upon any of our trademarks or service marks, we consider the Fastenal name and our other trademarks and service marks to be valuable to our business.

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Products

Our original product offerings were fasteners and other industrial and construction supplies, many of which are sold under the Fastenal® product name. This product line, which we refer to as the fastener product line, consists of two broad categories: threaded fasteners, such as bolts, nuts, screws, studs, and related washers; and miscellaneous supplies, such as paints, various pins and machinery keys, concrete anchors, batteries, sealants, metal framing systems, wire rope, strut, private-label stud anchors, rivets, and related accessories.

Threaded fasteners are used in most manufactured products and building projects, and in the maintenance and repair of machines and structures. Many aspects of the threaded fastener market are common to all cities. Variations from city to city that do exist typically relate to the types of businesses operating in a market or to the environmental conditions in a market. Therefore, we open each store with a broad selection of base stocks of inventory and then allow the local store and district leaders to tailor the additional inventory to the local market demand as it develops.

Threaded fasteners accounted for approximately 90% of the fastener product line sales in 2009, 2008, and 2007 and approximately 45%, 46%, and 46% of our consolidated net sales in 2009, 2008, and 2007, respectively. Concrete anchors make up the largest portion of the miscellaneous supply items included in the fastener product line. Most concrete anchors use threaded fasteners as part of the completed anchor assembly.

Since 1993, we have added additional product lines. These product lines are sold through the same distribution channel as the original fastener product line. Our product lines include the following:

Product line:	Year introduced	Approximate number of stock items	Private label product name
Fasteners	1967	410,000	Fastenal®, FNL G9®, Rock River®
Tools	1993	136,000	Fastenal®, Blackstone®, Rock River®
Cutting tools	1996	251,000	Blackstone®, FMT , Tritan
Hydraulics & pneumatics	1996	64,000	Fastenal®, Profitter®, Dynaflo
Material handling	1996	18,000	EquipRite , Caliber
Janitorial supplies	1996	16,000	Clean Choice®
Electrical supplies	1997	25,000	PowerPhase
Welding supplies ¹	1997	34,000	Blackstone
Safety supplies	1999	30,000	Fastenal®, Bodyguard
Metals	2001	12,000	Fastenal®

¹ We do not sell welding gases.

We plan to continue to add other products in the future.

Inventory Control

Our inventory stocking levels are determined using our computer systems, our sales personnel at the store, district, and region levels, and our product managers. The data used for this determination is derived from sales activity from all of our stores, from individual stores, and from different geographic areas. It is also derived from vendor information and from customer demographic information. The computer system monitors the inventory level for all stock items and triggers replenishment, or prompts a buyer to purchase, as necessary, based on an established minimum-maximum level. All stores stock a base inventory and may expand beyond preset inventory levels as deemed appropriate by their district managers. Inventories in distribution centers are established from computerized data for the stores served by the respective centers. Inventory quantities are continuously re-balanced utilizing an automated transfer mechanism we call inventory re-distribution .

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Manufacturing and Support Services Operations

In 2009, approximately 94.5% of our consolidated net sales were attributable to products manufactured by other companies to industry standards. The remaining 5.5% related to products manufactured, modified or repaired by our manufacturing division or our support services. The manufactured products consist primarily of non-standard sizes of threaded fasteners made to customers' specifications. The services provided by the support services group include, but are not limited to, items such as tool repair, band saw blade welding, third-party logistics, and light manufacturing. We engage in these activities primarily as a service to our customers and expect these activities in the future to continue to contribute in the range of 4% to 10% of our consolidated net sales.

Sources of Supply

We use a large number of suppliers for the approximately 996,000 standard stock items we distribute. Most items distributed by our network can be purchased from several sources, although preferred sourcing is used for some stock items to facilitate quality control. No single supplier accounted for more than 5% of our purchases in 2009.

Geographic Information

Information regarding our revenues and certain assets by geographic location is set forth in note 8 to the Notes to Consolidated Financial Statements included later in this Form 10-K under the heading "Item 8. Financial Statements and Supplementary Data". Foreign currency fluctuations, changes in trade relations, or fluctuations in the relative strength of foreign economies could impact our ability to procure products overseas at competitive prices and our foreign sales.

Customers and Marketing

We believe our success can be attributed to our ability to offer customers a full line of quality products at convenient locations, and to the superior service orientation and expertise of our employees. Most of our customers are in the construction and manufacturing markets. The construction market includes general, electrical, plumbing, sheet metal, and road contractors. The manufacturing market includes both original equipment manufacturers and maintenance and repair operations. Other users of our products include farmers, truckers, railroads, mining companies, federal, state and local governmental entities, schools, and certain retail trades. During the fourth quarter of 2009, our total number of active customer accounts (defined as accounts having purchase activity within the last 90 days) was approximately 356,000.

During each of the three years ended December 31, 2009, no one customer accounted for a significant portion of our sales. We believe that our large number of customers together with the varied markets that they represent, provide some protection to us from economic downturns.

Store personnel generate a significant portion of our sales through direct calls on customers. Because of the nature of our business, we make limited use of the more expensive forms of mass media advertising such as television, radio, and newspapers. The forms of advertising we use include signs, catalogs, and direct mailings.

Competition

Our business is highly competitive. Competitors include both large distributors located primarily in large cities and smaller distributors located in many of the same cities in which we have stores. We believe that the principal competitive factors affecting the markets for our products are customer service, price, and convenience.

Some competitors use vans to sell their products in markets away from their main warehouses, while others rely on mail order, websites, or telemarketing sales. We, however, believe that the convenience provided to customers by operating stores in small, medium, and large markets, each offering a wide variety of products, is a competitive selling advantage and that the large number of stores in a given area, taken together with our ability to provide frequent deliveries to such stores from centrally located distribution centers, makes possible the prompt and efficient distribution of products. Having trained personnel at each store also enhances our ability to compete (see "Employees" below).

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Employees

As of December 31, 2009, we employed a total of 12,045 full and part-time employees, 8,491 of whom were employed at a store location, 2,187 of whom were employed in one of our distribution centers, manufacturing operations, or service operations, and the remaining 1,367 of whom were employed at one of our administrative support facilities or home office.

We believe the quality of our employees is critical to our ability to compete successfully in the markets we currently serve and to our ability to open new stores in new markets. We foster the growth and education of skilled employees throughout the organization by operating training programs and by decentralizing decision-making. Wherever possible, promotions are from within our organization. For example, most new store managers are promoted from an outside sales position and district managers (who supervise a number of stores) are usually former store managers.

The Fastenal School of Business (our internal corporate university program) develops and delivers a comprehensive array of industry and company specific education and training programs that are offered to all Fastenal employees. Our school of business provides core curricula focused on key competencies determined to be critical to the success of our employees' performance. In addition, we provide specialized educational tracks within various institutes of learning. These institutes of learning are advanced levels that provide specific concentrations of education and development and have been designed to focus on the critical aspects of our business. These institutes provide a focused educational experience to enhance employee performance in relevant business areas such as leadership, effective store best practices, sales and marketing, product education, and distribution.

Our sales personnel are compensated with a modest base salary and an incentive bonus arrangement that places emphasis on achieving increased sales on a store and regional basis, while still attaining targeted levels of, among other things, gross profit and collections. As a result, a significant portion of our total employment cost varies with sales volume. We also pay incentive bonuses to our leadership personnel based on one or more of the following factors: sales growth, profit growth (before and after taxes), profitability, and return on assets, and to our other personnel for achieving pre-determined departmental, project, and cost containment goals.

None of our employees are subject to a collective bargaining agreement and we have experienced no work stoppages. We believe our employee relations are good.

Available Information

Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act are available free of charge on or through our website at www.fastenal.com as soon as reasonably practicable after such reports have been filed with or furnished to the SEC.

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ITEM 1A. RISK FACTORS

In addition to the other information in this Form 10-K, the following factors should be considered in evaluating our business. Our operating results depend upon many factors and are subject to various risks and uncertainties. The material risks and uncertainties known to us which may cause the operating results to vary from anticipated results or which may negatively affect our operating results and profitability are as follows:

A downturn in the economy and other factors may affect customer spending, which has harmed and could continue to harm our operating results.

In general, our sales represent spending on discretionary items or consumption needs by our customers. This spending is affected by many factors, including, among others:

general business conditions,

business conditions in our principal markets,

interest rates,

inflation,

liquidity in credit markets,

taxation,

fuel prices and electrical power rates,

unemployment trends,

terrorist attacks and acts of war, and

other matters that influence customer confidence and spending.

A downturn in either the national or local economy where our stores operate or changes in any of the other factors described above could negatively impact sales at our stores and their level of profitability.

This risk has come to bear during the last four months of 2008 and all of 2009. As the economic condition in North America has weakened significantly, our customers, which operate principally in various manufacturing, non-residential construction, and services sectors, have experienced a pronounced slowdown that has adversely impacted our sales and operating results. A lag in these sectors, even as the general economy improves, would continue to adversely impact our business.

Our current estimate for total store market potential in North America could be incorrect.

One of our primary growth strategies is to grow our business through the introduction of stores into new markets. Based on a snapshot of current marketplace demographics in the U.S., Canada, and Mexico, we currently estimate there is potential market opportunity in North America to

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support approximately 3,500 stores. We cannot guarantee that our market potential estimates are accurate or that we will open stores to reach the full market opportunity. In addition, a particular local market's ability to support a store may change because of a change in our store format or the presence of a competitor's store.

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We may be unable to meet our goals regarding new store openings.

Our growth, in part, is primarily dependent on our ability to attract new customers. Historically, the most effective way to attract new customers has been opening new stores. Our current business strategy focuses on opening stores at a rate of approximately 7% to 10% each year, although the economic slowdown in the latter 4 months of 2008 and all of 2009 caused us to adjust this rate to 2% to 5% for 2009. We anticipate returning to our historical rate of 7% to 10% in the second half of 2010. Failure to open stores at this rate could negatively impact our long-term growth.

Our current business strategy pathway-to-profit , which involves reducing our rate of new store openings and using the money saved to add outside sales personnel to existing stores, has not yet proven successful on a long-term basis.

In April 2007, we introduced our pathway to profit strategy. This strategy involves slowing our annual new store openings from our historical rate of 13% to 18% to approximately 7% to 10%. The funds saved by opening fewer stores would be invested in additional outside sales personnel, with the goal of increasing our average annual per store sales, capturing earnings leverage, and increasing our pre-tax operating margin. At the time we introduced this strategy, we believed that, over the five year period from 2007 to 2012, we could grow our average store sales to \$125 thousand per month and grow our pre-tax operating margin from 18% to 23%. The economic weakness that dramatically worsened in the fall of 2008 and continued into 2009 caused us to alter this strategy during 2009 by temporarily slowing our annual new store openings to a range of approximately 2% to 5% and temporarily stopping headcount additions except at newly opened stores and stores that are growing. Because of this economic setback, we believe that the time required to achieve our goals for pathway to profit will be delayed 24 to 30 months. However, we cannot assure even these delayed results. A more prolonged downturn in the economy than expected, the prospect of future economic deterioration, difficulty in successfully attracting and retaining qualified outside sales personnel, and failure to successfully change our selling process could further adversely impact our ability to grow average store sales, capture earnings leverage, and achieve desired pre-tax earnings results.

Changes in customer or product mix, downward pressure on sales prices, and changes in volume of orders could cause our gross margin percentage to fluctuate or decline in the future.

Changes in our customer or product mix, downward pressure on sales prices, and changes in the volume of our orders could cause our gross margin percentage to fluctuate or decline. From time to time we have experienced changes in product mix. For example, marketing activities to existing customers and needs communicated to us from existing and prospective customers have caused us to change our product mix in the past. When we change our product mix, there can be no assurance that we will be able to maintain our historical gross margins. In addition, gross margins can deteriorate if we experience downward pressure on sales prices as a result of deflation, pressures on customers to reduce costs or increased competition, as was the case in 2009. Furthermore, reductions in our volume of purchases, as also happened in 2009, can adversely impact gross margins by reducing vendor volume allowances.

Opening stores in new markets presents increased risks that may prevent us from being profitable in these new locations.

We intend to open stores in new markets pursuant to our growth strategy. New stores do not typically achieve operating results comparable to our existing stores until after several years of operation, and stores in new markets face additional challenges to achieving profitability. A new store generates its sales from direct sales calls, a slow process involving repeated contacts. In new markets, we have less familiarity with local customer preferences and customers in these markets are less familiar with Fastenal's name and capabilities. In addition, entry into new markets may bring us into competition with new, unfamiliar competitors. We cannot assure success in operating our stores in new markets on a profitable basis.

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New store openings may negatively impact our operating results.

While new stores build the infrastructure for future growth, the first year sales in new stores are low, and the added expenses relating to payroll, occupancy, and transportation costs can impact our ability to leverage earnings. It has been our experience that new stores take approximately ten to twelve months to achieve profitability. We cannot assure you that we will be successful in operating our new stores on a profitable basis.

The ability to identify new products and products lines, and integrate them into our store and distribution network, may impact our ability to compete and our sales and margins.

Our success depends in part on our ability to develop product expertise at the store level and identify future products and product lines that complement existing products and product lines and that respond to our customers' needs. We may not be able to compete effectively unless our product selection keeps up with trends in the markets in which we compete or trends in new products. In addition, our ability to integrate new products and product lines into our stores and distribution network could impact sales and margins.

Increases in energy costs and the cost of raw materials used in our products could impact our cost of goods and distribution and occupancy expenses, which may result in lower operating margins.

Costs of raw materials used in our products (e.g., steel) and energy costs have fluctuated during the last several years. Increases in these costs result in increased production costs for our vendors. These vendors typically look to pass their increased costs along to us through price increases. The fuel costs of our distribution and store operations have fluctuated as well. While we typically try to pass increased vendor prices and fuel costs through to our customers or to modify our activities to mitigate the impact, we may not be successful. Failure to fully pass any such increased prices and costs through to our customers or to modify our activities to mitigate the impact would have an adverse effect on our operating margins.

Our ability to successfully attract and retain qualified personnel to staff our stores could impact labor costs, sales at existing stores, and the rate of new store openings.

Our success depends in part on our ability to attract, motivate, and retain a sufficient number of qualified employees, including store managers, outside sales personnel, and other store associates, who understand and appreciate our culture and are able to adequately represent this culture to our customers. Qualified individuals of the requisite caliber and number needed to fill these positions may be in short supply in some areas, and the turnover rate in the industry is high. If we are unable to hire and retain personnel capable of consistently providing a high level of customer service, as demonstrated by their enthusiasm for our culture and product knowledge, our sales could be materially adversely affected. Additionally, competition for qualified employees could require us to pay higher wages to attract a sufficient number of employees. An inability to recruit and retain a sufficient number of qualified individuals in the future may also delay the planned openings of new stores. Any such delays, material increases in employee turnover rates at existing stores, or increases in labor costs, could have a material adverse effect on our business, financial condition or operating results.

Inclement weather and other disruptions to the transportation network could impact our distribution system.

Our ability to provide efficient distribution of core business products to our store network is an integral component of our overall business strategy. Disruptions at distribution centers or shipping ports, due to events such as the hurricanes of 2005 and the longshoremen's strike on the West Coast in 2002, may affect our ability to both maintain core products in inventory and deliver products to our customers on a timely basis, which may in turn adversely affect our results of operations. In addition, severe weather conditions could adversely affect demand for our products in particularly hard hit regions.

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We are exposed to foreign currency exchange rate risk, and changes in foreign exchange rates could increase our costs to procure products and our foreign sales.

Because the functional currency related to most of our foreign operations is the applicable local currency, we are exposed to foreign currency exchange rate risk arising from transactions in the normal course of business, such as sales to third party customers and purchases from suppliers denominated in foreign currencies. In addition, fluctuations in the relative strength of foreign economies could impact our ability to procure products overseas at competitive prices and our foreign sales. Our primary exchange rate exposure is with the Canadian dollar.

We may not be able to compete effectively against our competitors, which could harm our business and operating results.

The industrial, construction, and maintenance supply industry, although consolidating, still remains a large, fragmented industry that is highly competitive. Our current or future competitors include companies with similar or greater market presence, name recognition, and financial, marketing, and other resources, and we believe they will continue to challenge us with their product selection, financial resources, and services. Increased competition in markets in which we have stores or the adoption by competitors of aggressive pricing strategies and sales methods could cause us to lose market share or reduce our prices or increase our spending, thus eroding our margins.

Our revenues and net income may be adversely affected by economic conditions, political situations, and changing laws and regulations in foreign countries, over which we have no control.

We obtain certain of our products, and our suppliers obtain certain of their products, from China, Taiwan, South Korea, Mexico, and other foreign countries. Our vendors could discontinue selling products manufactured in foreign countries at any time for reasons that may or may not be in our control or the vendor's control, including foreign government regulations, political unrest, war, disruption or delays in shipments, changes in local economic conditions and trade issues. Our operating results and inventory levels could suffer if we are unable to promptly replace a vendor who is unwilling or unable to satisfy our requirements with a vendor providing equally appealing products.

The industrial, construction, and maintenance supply industry is consolidating, which could cause it to become more competitive and could negatively impact our business.

The industrial, construction and maintenance supply industry in North America is consolidating. This consolidation is being driven by customer needs and supplier capabilities, which could cause the industry to become more competitive as greater economies of scale are achieved by suppliers. Customers are increasingly aware of the total costs of fulfillment and of the need to have consistent sources of supply at multiple locations. We believe these customer needs could result in fewer suppliers as the remaining suppliers become larger and capable of being a consistent source of supply.

There can be no assurance that we will be able in the future to take advantage effectively of the trend toward consolidation. The trend in our industry toward consolidation could make it more difficult for us to maintain operating margins. Furthermore, as our industrial and construction customers face increased foreign competition, and potentially lose business to foreign competitors or shift their operations overseas in an effort to reduce expenses, we may face increased difficulty in growing and maintaining our market share and growth prospects.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

None.

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We own seven facilities in Winona, Minnesota. These facilities are as follows:

Purpose	Approximate Square Feet
Distribution center and home office	213,000
Manufacturing facility	100,000
Computer support center	13,000
Winona store	15,000
Winona product support and support services facility	55,000
Rack and shelving storage	42,000
Multi-building complex which houses certain operations of the distribution group and home office support group	30,000

We also own the following facilities, excluding store locations, outside of Winona, Minnesota:

Purpose	Location	Approximate Square Feet
Distribution center	Indianapolis, Indiana	414,000 ¹
Storage facility and office building	Indianapolis, Indiana	419,000
Distribution center	Atlanta, Georgia	198,000
Distribution center	Dallas, Texas	176,000 ²
Distribution center	Scranton, Pennsylvania	160,000
Distribution center	Akron, Ohio	102,000
Distribution center	Kansas City, Kansas	300,000
Distribution center	Toronto, Ontario, Canada	62,000
Distribution center	Greensboro, North Carolina	250,000
Distribution center	Modesto, California	320,000
Manufacturing facility	Rockford, Illinois	100,000

¹ In addition, this facility has an auxillary building which contains an automated storage and retrieval system with capacity of 52,000 pallet locations.

² In addition, this facility has an auxillary building which contains an automated storage and retrieval system with capacity of 14,000 pallet locations.

In addition, we own 172 buildings that house our store locations in various cities throughout North America and are in the process of building or renovating another 2 owned store locations for future use.

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All other buildings we occupy are leased. Leased stores range from approximately 3,500 to 10,000 square feet, with lease terms of up to 60 months (most lease terms are for 36 to 48 months). We also lease the following:

Purpose	Location	Approximate Square Feet	Lease Expiration Date	Remaining Lease Renewal Options
Distribution center	Seattle, Washington	55,000	April 2011	None
Distribution center	Salt Lake City, Utah	22,000	July 2012	None
Distribution center	Monterrey, Nuevo Leon, Mexico	14,000	September 2010	None
Distribution center	Edmonton, Alberta, Canada	18,000	July 2013	None
Manufacturing facility	West Hartford, Connecticut	200,000	December 2011	None

If economic conditions are suitable, we will, in the future, consider purchasing store locations to house our older stores. It is anticipated the majority of new store locations will continue to be leased. It is our policy to negotiate relatively short lease terms to facilitate relocation of particular store operations, when desirable. Our experience has been that space suitable for our needs and available for leasing is more than sufficient.

ITEM 3. LEGAL PROCEEDINGS

A discussion of our policies with respect to legal proceedings is discussed in the management's discussion and analysis and our legal proceedings and other loss contingencies as described in Note 10 of the consolidated financial statements. The description of our legal proceedings in Note 10 of the consolidated financial statements to this filing is incorporated herein by reference.

On October 18, 2007, a complaint was filed in the United States District Court for the Northern District of California against Fastenal on behalf of two former employees claiming to represent all employees employed in the store position of Assistant General Manager in the United States within three years prior to the filing date (four years for California employees). The suit alleged Fastenal misclassified its Assistant General Managers as exempt for purposes of the overtime provisions of the Fair Labor Standards Act and California, Oregon, and Pennsylvania state statutes. This suit also alleged that Assistant General Managers in California did not receive sufficient meal breaks and paid rest periods under the California Labor Code. An opt-in class was certified for this action.

On August 29, 2008, we issued a press release announcing a preliminary agreement to settle the class action lawsuit noted above. While we deny the allegations underlying the lawsuit, we agreed to enter into the settlement agreement in order to avoid significant legal fees, the uncertainty of a jury trial, distractions to our operations, and other expenses and management time that would have to be devoted to protracted litigation. The settlement, which received court approval in 2009, fully resolves all claims brought by the plaintiffs in this lawsuit. Pursuant to the settlement, we made a cash payment of \$10 million in the fourth quarter of 2009 to cover claims by eligible class members, plaintiff attorneys' fees and costs, and payments to the named plaintiffs and their attorneys. The expense for this settlement was recorded in the third quarter of 2008. We do not expect the settlement to have any material impact on our operating results going forward.

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In early February 2010, we received a letter from a fastener supplier dated January 26, 2010. This letter threatened to sue us for our alleged violation of an exclusive distribution arrangement this supplier believes exists between our organizations. In addition, this supplier provided a press release and a video regarding the claim that they threatened to make public unless we agreed to mediation of the claim. We have performed a preliminary internal review during the last several days to understand (1) who this supplier is and (2) the nature of our relationship with this supplier. While we have had only a limited time to investigate this matter, we have determined that this supplier manufactures a niche type of fastener and that the total volume of purchases by us, from all suppliers, over the purported term of this alleged exclusivity arrangement of this niche type of fastener does not exceed \$1 million. Based on our preliminary inquiry, we believe it is remote that this claim would have a material adverse impact on our financial position, cash flow, or results of operations. While we are not required to disclose this matter under the rules of the SEC, we believe that disclosure is prudent due to the alleged amount of the claim and the threat to make these allegations public.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Not applicable.

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The executive officers of Fastenal Company are:

Name	Employee of Fastenal since	Age	Position
Willard D. Oberton	1980	51	Chief Executive Officer, President, and Director
Daniel L. Florness	1996	46	Executive Vice President and Chief Financial Officer
Nicholas J. Lundquist	1979	52	Executive Vice President-Sales
Leland J. Hein	1985	49	Executive Vice President-Sales
Steven A. Rucinski	1980	52	Executive Vice President-Sales
Reyne K. Wisecup	1988	47	Executive Vice President-Human Resources and Director
James C. Jansen	1992	39	Executive Vice President-Operations

Mr. Oberton has been our chief executive officer and president since December 2002. From July 2001 through December 2002, Mr. Oberton was our president and chief operating officer. Mr. Oberton has also served as one of our directors since June 1999.

Mr. Florness has been our executive vice-president and chief financial officer since December 2002. From June 1996 to November 2002, Mr. Florness was our chief financial officer.

Mr. Lundquist has been one of our executive vice presidents - sales since November 2007. Mr. Lundquist's responsibilities include complete sales and operational oversight over a substantial portion of our business. From December 2002 to November 2007, Mr. Lundquist was our executive vice president and chief operating officer.

Mr. Hein has been one of our executive vice presidents - sales since November 2007. Mr. Hein's responsibilities include complete sales and operational oversight over a substantial portion of our business. Prior to November 2007, Mr. Hein served in various sales leadership roles, most recently serving as leader of our Winona and Kansas City based regions.

Mr. Rucinski has been one of our executive vice presidents - sales since November 2007. Mr. Rucinski's responsibilities include complete sales and operational oversight over our international business. Prior to November 2007, Mr. Rucinski served in various sales leadership roles, most recently serving as leader of national accounts.

Ms. Wisecup has been our executive vice president - human resources since November 2007. Prior to November 2007, Ms. Wisecup served in various support roles, most recently serving as director of employee development. Ms. Wisecup has served as one of our directors since 2000.

Mr. Jansen has been our executive vice president - operations since January 2010. Mr. Jansen's responsibilities include distribution development as well as manufacturing. From November 2007 to January 2010, Mr. Jansen was our executive vice president - internal operations. From June 2005 to November 2007, Mr. Jansen served as leader of systems development (this role encompassed both information systems and distribution systems development). From April 1999 to June 2005, Mr. Jansen was the leader of our Dallas, Texas based region.

The executive officers are elected by our board of directors for a term of one year and serve until their successors are elected and qualified. None of our executive officers are related to any other such executive officer or to any of our other directors.

Table of Contents**PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS, AND ISSUER PURCHASES OF EQUITY SECURITIES****Common Stock Data**

Our shares are traded on The NASDAQ Stock Market under the symbol **FAST**. As of February 1, 2010, there were approximately 1,500 recordholders of our common stock, which includes nominees or broker dealers holding stock on behalf of an estimated 104,000 beneficial owners.

The following table sets forth, by quarter, the high and low closing sale price of our shares on The NASDAQ Stock Market for 2009 and 2008.

2009:	High	Low	2008:	High	Low
First quarter	\$ 37.53	26.16	First quarter	\$ 46.94	33.13
Second quarter	\$ 38.74	32.15	Second quarter	\$ 51.76	43.16
Third quarter	\$ 40.13	30.56	Third quarter	\$ 55.45	42.23
Fourth quarter	\$ 42.19	34.50	Fourth quarter	\$ 45.25	31.87

In 2009, we paid semi-annual dividends of \$.35 and \$.37 per share. In 2008, we paid semi-annual dividends of \$.25 and \$.27 per share. In December 2008, we paid a special one-time dividend of \$.27 per share. On January 18, 2010, we announced a semi-annual dividend of \$.40 per share to be paid on February 26, 2010 to shareholders of record at the close of business on February 15, 2010. We expect that we will continue to pay comparable semi-annual cash dividends in the foreseeable future, provided that any future determination as to payment of dividends will depend upon our financial condition and results of our operations and such other factors as are deemed relevant by our board of directors.

Issuer Purchases of Equity Securities

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs
October 1-31, 2009	600,000	\$ 37.32	600,000	1,400,000
November 1-30, 2009	500,000	\$ 37.42	1,100,000	900,000
December 1-31, 2009			1,100,000	900,000
Total	1,100,000	\$ 37.37	1,100,000	900,000

The Fastenal Company Common Stock Comparative Performance Graph

Set forth below is a graph comparing, for the five years ended December 31, 2009, the yearly cumulative total shareholder return on our common stock with the yearly cumulative total shareholder return of the S&P Composite Index and an index (the Peer Group Index) of a group of peer companies selected by us (the Peer Group). The companies in the Peer Group are Lawson Products, Inc., MSC Industrial Direct Co., Inc. Airgas, Inc., and W.W. Grainger, Inc. Fastenal is not included in the Peer Group.

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In calculating the yearly cumulative total shareholder return of the Peer Group Index, the shareholder returns of the companies included in the Peer Group are weighted according to the stock market capitalization of such companies at the beginning of each period for which a return is indicated.

The comparison of total shareholder returns in the performance graph assumes that \$100 was invested on December 31, 2004 in Fastenal Company, the S&P Composite Index and the Peer Group Index, and that dividends were reinvested when and as paid.

Comparison of Five Year Cumulative Total Return Among Fastenal Company,

Peer Group Index, and S&P Composite Index

	2004	2005	2006	2007	2008	2009
Fastenal Company	100.00	128.46	118.97	135.50	119.07	145.40
Peer Group Index	100.00	104.91	121.48	128.16	80.74	102.11
S&P Composite Index	100.00	112.91	118.37	144.17	124.37	155.90

ITEM 6. SELECTED FINANCIAL DATA

Incorporated herein by reference is Ten-Year Selected Financial Data on page 5 of Fastenal's 2009 Annual Report to Shareholders of which this Form 10-K forms a part, a portion of which is filed as Exhibit 13 to this Form 10-K.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion in conjunction with our consolidated financial statements and related notes appearing elsewhere in this Form 10-K. Certain tabular information will not foot due to rounding.

Business Overview Fastenal is a North American leader in the wholesale distribution of industrial and construction supplies. We operate stores primarily located in North America. On December 31, 2009, we operated 2,369 company-owned or leased store locations.

Most of our customers are in the manufacturing and construction markets. The manufacturing market includes both original equipment manufacturers and maintenance and repair operations. The construction market includes general, electrical, plumbing, sheet metal, and road contractors. Other users of our products include farmers, truckers, railroads, mining companies, federal, state, and local governmental entities, schools, and certain retail trades. Geographically, our customers are primarily located in North America.

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Similar to our first three quarterly reports in 2009, this annual report's discussion contains some additional points not typically covered in our reports in previous years. We believe these are important aspects that require added emphasis.

As we saw in the previous fifteen months, the weakened economy continues to have a substantial impact on our business. These impacts continue to negatively affect our sales, particularly related to our industrial production business (business where we supply products that become part of the finished goods produced by others) and, as the year progressed, our non-residential construction business. To place this in perspective sales to our manufacturing customers (historically approximately 50% of sales) contracted approximately 10.1% in the fourth quarter and 18.8% for the year versus the same periods in 2008. This contraction is less severe in the maintenance portion of our manufacturing sales (business where we supply products that maintain the facility or the equipment of our customers engaged in manufacturing), but more severe in the production business. Our non-residential construction business (historically 20% to 25% of sales) contracted approximately 24.7% in the fourth quarter and 19.4% for the year versus the same periods in 2008. The remaining business (sales to other resellers, government business, transportation/warehousing, other industries, and in-store retail sales) produced better results as a group, but unfortunately, doesn't have enough impact to offset the manufacturing and construction impact. The annual 2009 sales growth/contraction compared to 2008 sales for the remaining business was as follows: Sales to other resellers 26% contraction, government business 16% growth, transportation/warehousing 3% contraction, all other industries combined 0% growth, and in-store retail sales 14% contraction.

On a sequential basis, our daily average sales to our manufacturing customers improved each month since May 2009 (with the exception of July and December 2009 due to the holiday impact) versus the previous month. This trend was the first sequential improvement since September 2008. However, this improvement was partially offset by continued weakening in our non-residential construction business.

Sometimes our comments are an effort to share our perspective regarding the trends with you, our shareholder. The discussion above is an attempt to provide insight into activities with types of customers and the discussion under the headings Financial Overview and Monthly Daily Sales Change later gives a somewhat mechanical view of our business. Another way to think about our business is to compare our growth during a year to the act of climbing a stairway. This stairway has several predictable landings (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 (i.e. certain holidays). The first landing centers on Easter, which alternates between March and April (it was in April in 2009), 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 on 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 the sequential change in our daily sales (see definition of daily sales later in this report). The line labeled Past is an historical average of the results 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 2009 line is our actual results and the Delta line is the difference between the Past and 2009.

	Jan. ¹	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Past	0.9%	3.3%	2.9%	(0.3)%	3.4%	2.8%	(2.3)%	2.6%	2.6%	(0.7)%	(4.7)%	(6.0)%
2009	(18.3)%	(2.6)%	(1.4)%	(4.9)%	2.7%	1.7%	(3.6)%	5.5%	3.3%	(0.7)%	(2.0)%	(9.0)%
Delta	(19.2)%	(5.9)%	(4.3)%	(4.6)%	(0.7)%	(1.1)%	(1.3)%	2.9%	0.7%	0.0%	2.7%	(3.0)%

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

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In the October 2008 to January 2009 time frame, our economy dug a big hole, and pulled our sales results from daily average sales growth of 11.9% in October to a contraction of 8.5% in January. The Delta, or spread between the benchmark and the 2009 actual, in the February 2009 to April 2009 time frame averaged a negative 5.0%. This increased the daily sales contraction to 21.0% in April. The Delta from May 2009 to July 2009 was not as significant, averaging a negative 1.1%; while this period was still painful, it began to show what we believe was the bottom of the drop. Finally, in the period from August 2009 to December 2009, the Delta improved further, and averaged a positive 0.7%. Historically, we are hesitant to provide much forward looking commentary as we believe we are better able to provide value to our shareholders by managing the business and not by trying to predict the economy; however, our confidence in our ability to see year-over-year sales growth in the near future is buoyed by these trends.

During 2009, we attempted to balance long-term opportunities for growth with the necessary short-term reactions to the current reality. In this regard, we previously slowed our store openings for 2009 to a range of 2% to 5% new stores and we stopped adding any headcount except for store openings and for stores that are growing. Over the last several years, our pathway to profit initiative has slowly altered our cost structure in that a greater portion is now variable versus fixed. This continues to help us today as we navigate through the current economic environment. As discussed in our third quarter report, we began to stabilize our store total headcount in that quarter and in October 2009 we began the steps to increase our rate of store openings. Assuming our confidence continues to be supported by an economy that is stable, we plan to continue increasing the rate of store openings, as we did in the fourth quarter of 2009, with the goal of resuming our historical rate of openings of 7% to 10% in the second half of 2010. This plan allows us to focus on the three drivers of our business: (1) average store size, which ultimately drives our level of profitability, (2) store headcount, and (3) store, or unit, growth. The last two drive our ability to grow our sales long-term.

Our balance sheet continues to be very strong and our operations have good cash generating characteristics. During 2009, we tried to manage it well. During 2009, we generated \$306,070 (or 166.0% of net earnings) of operating cash flow; the comparable figure was \$259,898 (or 92.9% of net earnings) in 2008. Our first quarter typically has stronger cash flow characteristics due to the timing of tax payments; this benefit reverses itself in the second, third, and fourth quarters as income tax payments go out in April, June, September, and December. The remaining amounts of cash flow from operating activities are largely linked to the pure dynamics of a distribution business and its strong correlation to working capital.

As we planned, our capital expenditures for 2009 were down from 2008. This primarily related to the Indianapolis, IN distribution expansion and to our new distribution center location near Dallas, TX. Most of the expenditures for these two locations occurred in 2008 and the first half of 2009. As indicated in our 2008 annual report, we expected our capital expenditures would drop from approximately \$95,000 in 2008 to \$65,000 in 2009. The actual 2009 figure came in at \$52,538 with the difference being driven by lower capital expenditures for computer software and equipment, real estate, and vehicles. In 2010, we expect our capital expenditures will drop to approximately \$40,000. Again, this reduction is driven by a significant drop in expenditures for the aforementioned Indianapolis and Dallas facilities. This reduction will be partially offset by some added spending for computer equipment and vehicles in 2010 and some potential real estate purchases for our manufacturing and distribution operations.

The strong free cash flow in 2009 (operating cash flow less net capital expenditures) allowed us to increase our first dividend payment (declared January 2009 and paid in March 2009) by 40% (from \$.25 per share in 2008 to \$.35 per share in 2009). This strong free cash flow also allowed us to increase our second dividend payment (declared July 2009 and paid in August 2009) by 37% (from \$.27 per share in 2008 to \$.37 per share in 2009). Given the economic environment, we are satisfied with our cash flow for 2009. As announced on January 18, 2010, our Board of Directors declared a dividend of \$.40 per share to be paid in February 2010; this represents a 14.3% increase over our first dividend in 2009.

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Financial Overview During 2009, 2008, and 2007, the weakness of the global industrial environment negatively impacted our business. The impact of the economy is best reflected in the growth performance of our stores opened greater than ten years (2009 group reflects stores opened in 1999 and earlier) and opened greater than five years (2009 group reflects stores opened in 2004 and earlier). These two groups of stores are more cyclical due to the increased market share they enjoy in their local markets. The stores opened greater than two years (2009 group reflects stores opened in 2007 and earlier) represent a consistent same-store view of our business. The net sales change for each of the groups was as follows:

Store Age	2009	2008	2007
Opened greater than 10 years	(21.1)%	6.9%	4.4%
Opened greater than 5 years	(20.6)%	7.8%	6.1%
Opened greater than 2 years	(19.5)%	9.6%	7.3%

Net Sales Net sales and percentage change in net sales were as follows: