

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2012

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 1-5684

W.W. Grainger, Inc.

(Exact name of registrant as specified in its charter)

Illinois

(State or other jurisdiction of incorporation or organization)

36-1150280

(I.R.S. Employer Identification No.)

100 Grainger Parkway, Lake Forest, Illinois

(Address of principal executive offices)

60045-5201

(Zip Code)

(847) 535-1000

(Registrant's telephone number including area code)

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

Title of each class

Common Stock \$0.50 par value

Name of each exchange on which registered

New York Stock Exchange
Chicago Stock Exchange

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 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 website, 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 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 the definitions 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 [] Smaller reporting company []

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes No

The aggregate market value of the voting common equity held by nonaffiliates of the registrant was \$12,756,537,599 as of the close of trading as reported on the New York Stock Exchange on June 30, 2012. The Company does not have nonvoting common equity.

The registrant had 69,522,640 shares of the Company's common stock outstanding as of January 31, 2013.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the proxy statement relating to the annual meeting of shareholders of the registrant to be held on April 24, 2013, are incorporated by reference into Part III hereof.

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PART I

Item 1: Business

The Company

W.W. Grainger, Inc., incorporated in the State of Illinois in 1928, is a broad-line distributor of maintenance, repair and operating (MRO) supplies and other related products and services used by businesses and institutions primarily in the United States and Canada, with expanding global operations. In this report, the words “Grainger” or “Company” mean W.W. Grainger, Inc. and its subsidiaries.

Grainger uses a multichannel business model to provide customers with a range of options for finding and purchasing products, utilizing sales representatives, direct marketing materials, catalogs and eCommerce. Grainger serves approximately 2 million customers worldwide through a network of highly integrated branches, distribution centers, websites and export services.

In 2012, Grainger acquired one business in the United States and one in Brazil. Techni-Tool, Inc., a business acquired in the United States, is a specialist distributor serving manufacturers in the electronics, telecommunications and medical services industries. AnFreixo S.A., the business acquired in Brazil, is a former subsidiary of the Votorantim Group, and is a broad-line distributor of MRO supplies in Brazil. Results for both business are consolidated with Grainger from the respective acquisition dates.

Grainger has centralized business support functions that provide coordination and guidance in the areas of accounting and finance, business development, communications and investor relations, compensation and benefits, information systems, health and safety, global supply chain functions, human resources, risk management, internal audit, legal, real estate, security, tax and treasury. These services are provided in varying degrees to all business units.

Items are regularly added to and deleted from Grainger’s product lines on the basis of customer demand, market research, recommendations of suppliers, sales volumes and other factors.

Grainger’s two reportable segments are the United States and Canada and they are described further below. Other businesses include operations in Europe, Asia, Latin America and other U.S. operations. These businesses generate revenue through the distribution of maintenance, repair and operating supplies and products and provide related services. For segment and geographical information and consolidated net sales and operating earnings see “Item 7: Management’s Discussion and Analysis of Financial Condition and Results of Operations” and Note 16 to the Consolidated Financial Statements.

United States

The United States business offers a broad selection of maintenance, repair and operating supplies and other related products and services through local branches, sales representatives, catalogs and the Internet. A combination of product breadth, local availability, speed of delivery, detailed product information and competitively priced products and services is provided by this business. Products offered include material handling equipment, safety and security supplies, lighting and electrical products, power and hand tools, pumps and plumbing supplies, cleaning and maintenance supplies, forestry and agriculture equipment, building and home inspection supplies, vehicle and fleet components and many other items primarily focused on the facilities maintenance market. Services offered include inventory management and energy efficiency solutions.

The United States business operates in all 50 states through a network of 369 branches and sales representatives. The branches are located in close proximity to the majority of U.S. businesses and serve the immediate needs of customers in their local markets by allowing them to pick up items directly from the branches. Branches range in size from small branches to large master branches. The branch network has approximately 4,700 employees who primarily fulfill counter and will-call product purchases and provide customer service. An average branch is 23,000 square feet in size, has 13 employees and handles about 170 transactions per day. In the normal course of business, Grainger continually reviews the effectiveness of its branch network. In 2012, three branches were opened and two branches were closed.

The logistics network in the United States is comprised of 15 distribution centers (DCs) of various sizes. Automated equipment and processes in the larger DCs allow them to handle the majority of the customer shipping for next-day product availability and replenish the branches that provide same day availability.

Customers range from small and medium-sized businesses to large corporations, government entities and other institutions. They are primarily represented by purchasing managers or workers in facilities maintenance departments and service shops across a wide range of industries such as manufacturing, hospitality, transportation, government, retail, healthcare and education. Sales in 2012 were made to approximately 1.4 million customers averaging 106,000 daily transactions. No single customer accounted for more than 2% of total sales.

The business has a sales force of almost 2,700 professionals who help businesses and institutions select the right products to find immediate solutions to maintenance problems and to reduce operating expenses and improve cash

flows. The composition of the sales force changed during the year with more sales representatives focused on acquiring additional business from existing medium-sized customers, as well as acquiring new business across the United States.

Another area in which the United States business helps customers be more productive is through inventory management services. A comprehensive program was launched in 2006 called KeepStock® that includes on-site services and vendor-managed inventory. During the past several years, the program has expanded to more than 20,000 customers and approximately 40,000 unique customer installations.

Customers can also purchase products through Grainger.com. More customers are migrating to online and electronic purchasing and Grainger continues to enhance its eCommerce platform. eCommerce revenues were \$2.2 billion in 2012, an increase of 17% versus 2011. Grainger.com provides access to almost 950,000 products and serves as a prominent channel for the United States business. Grainger.com provides real-time price and product availability and detailed product information, and offers advanced features such as product search and compare capabilities. For customers with sophisticated electronic purchasing platforms, Grainger utilizes technology that allows these systems to communicate directly with Grainger.com. Customers can also purchase products through several other branded websites.

The majority of the products sold by the United States business are well recognized national branded products. In addition, 22% of 2012 sales were of private label items bearing Grainger's registered trademarks, such as DAYTON® motors, power transmission, HVAC and material handling, SPEEDAIRE® air compressors, AIR HANDLER® air filtration equipment, TOUGH GUY® cleaning products, WESTWARD® tools, CONDOR® safety products and LUMAPRO® lighting products. Grainger has taken steps to protect these trademarks against infringement and believes that they will remain available for future use in its business. The United States business purchases products for sale from more than 2,600 key suppliers, most of which are manufacturers. Through a global sourcing operation, the business procures competitively priced, high-quality products produced outside the United States from approximately 360 suppliers. Grainger sells these items primarily under the private label brands listed above. No single supplier comprised more than 5% of total purchases and no significant difficulty has been encountered with respect to sources of supply.

The Grainger catalog, most recently issued in February 2013, offers approximately 570,000 facilities maintenance and other products, an increase of 160,000 from the prior year, and is used by customers to assist in product selection. Approximately 2 million copies of the catalog were produced. In addition, Grainger's United States business issues targeted catalogs for its multiple branded products, as well as other marketing materials.

Grainger estimates the United States market for facilities maintenance and related products to be approximately \$118 billion, of which Grainger's share is approximately 6%.

Canada

Acklands–Grainger is Canada's leading broad-line distributor of industrial and safety supplies. A combination of product breadth, local availability, speed of delivery, detailed product information and competitively priced products and services is provided by this business.

The Canadian business serves customers through 172 branches, sales and service representatives and 6 DCs across Canada. Acklands–Grainger distributes tools, fasteners, safety supplies, instruments, welding and shop equipment, and many other items. During 2012, approximately 15,500 sales transactions were completed daily. A comprehensive catalog, printed in both English and French, was most recently issued in February 2013. The catalog has more than 116,000 products and is used by customers to assist in product selection. In addition, customers can purchase products through Acklandsgrainger.com, a fully bilingual website. Grainger estimates the Canadian market for facilities maintenance and related products to be approximately \$14 billion, of which Acklands–Grainger's share is approximately 8%.

Other Businesses

Included in other businesses are the operations in Europe, Asia, Latin America and other U.S. operations. The more significant businesses in this group are described below.

Fabory

Fabory, acquired in 2011, is a European distributor of fasteners, tools and industrial supplies. Fabory is headquartered in Tilburg, the Netherlands, and has more than 100 locations in 14 countries. Customers have access to more than 90,000 products through a catalog and through Fabory.com. Grainger estimates the European market (in which Fabory has its primary operations) for facilities maintenance and related products to be approximately \$35 billion, of which Grainger's share is approximately 1%.

Japan

Grainger operates in Japan through its 52% interest in MonotaRO Co. MonotaRO provides small and mid-sized domestic businesses with products that help them operate and maintain their facilities. MonotaRO is a catalog and web-based direct marketer with approximately 80% of orders being conducted through Monotaro.com. MonotaRO has no branches or sales force and fulfills all orders from two DCs. Grainger estimates the Japanese market for facilities maintenance and related products to be approximately \$57 billion, of which Grainger's share is less than 1%.

Mexico

Grainger's operations in Mexico provide local businesses with maintenance, repair and operating supplies and other related products primarily from Mexico and the United States. Mexico distributes products through a network of branches and one DC where customers have access to approximately 116,000 products through a Spanish-language catalog and through Grainger.com.mx. Grainger estimates the Mexican market for facilities maintenance and related products to be approximately \$10 billion, of which Grainger's share is approximately 1%.

Brazil

In 2012, Grainger acquired 100% of the shares of AnFreixo S.A., a former subsidiary of the Votorantim Group, a broad-line distributor of MRO supplies in Brazil. This operation offers approximately 170,000 products for sale. Grainger estimates the Brazilian market for facilities maintenance and related products to be approximately \$21 billion, of which Grainger's share is less than 1%.

Seasonality

Grainger's business in general is not seasonal, however, there are some products that typically sell more often during the winter or summer season. In any given month, unusual weather patterns, i.e., unusually hot or cold weather, could impact the sales volumes of these products, either positively or negatively.

Competition

Grainger faces competition in all markets it serves, from manufacturers (including some of its own suppliers) that sell directly to certain segments of the market, wholesale distributors, catalog houses, retail enterprises and Internet-based businesses. Grainger provides local product availability, a broad product line, sales representatives, competitive pricing, catalogs (which include product descriptions and, in certain cases, extensive technical and application data), and electronic and Internet commerce technology. Other services such as inventory management and energy efficiency solutions to assist customers in lowering their total facilities maintenance costs are also offered. Grainger believes that it can effectively compete with manufacturers on small orders, but manufacturers may have an advantage in filling large orders. There are several large competitors, although the majority of the market is served by small local and regional competitors.

Employees

As of December 31, 2012, Grainger had approximately 22,400 employees, of whom approximately 21,100 were full-time and 1,300 were part-time or temporary. Grainger has never had a major work stoppage and considers employee relations to be good.

Website Access to Company Reports

Grainger makes available, through its website, free of charge, its Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements and amendments to those reports, as soon as reasonably practicable after this material is electronically filed with or furnished to the Securities and Exchange Commission. This material may be accessed by visiting grainger.com/investor.

Item 1A: Risk Factors

The following is a discussion of significant risk factors relevant to Grainger's business that could adversely affect its financial position or results of operations.

Weakness in the economy could negatively impact Grainger's sales growth. Economic and industry trends affect Grainger's business environments. Economic downturns can cause customers, both domestic and international, to idle or close facilities, delay purchases and otherwise reduce their ability to purchase Grainger's products and services as well as their ability to make full and timely payments. Thus, a significant or prolonged slowdown in economic activity in the United States, Canada or any other major world economy could negatively impact Grainger's sales growth and results of operations.

The facilities maintenance industry is highly fragmented, and changes in competition could result in a decreased demand for Grainger's products and services. There are several large competitors in the industry, although most of the market is served by small local and regional competitors. Grainger faces competition in all markets it serves, from manufacturers (including some of its own suppliers) that sell directly to certain segments of the market, wholesale distributors, catalog houses, retail enterprises and Internet-based businesses. Competitive pressures could adversely affect Grainger's sales and profitability.

Volatility in commodity prices may adversely affect operating margins. Some of Grainger's products contain significant amounts of commodity-priced materials, such as steel, copper, petroleum derivatives or rare earth minerals, and are subject to price changes based upon fluctuations in the commodities market. Increases in the price of fuel could also drive up transportation costs. Grainger's ability to pass on increases in costs depends on market conditions. The inability to pass along cost increases could result in lower operating margins. In addition, higher prices could impact demand for these products, resulting in lower sales volumes.

Unexpected product shortages could negatively impact customer relationships, resulting in an adverse impact on results of operations. Grainger's competitive strengths include product selection and availability. Products are purchased from more than 4,600 key suppliers located in various countries around the world, no one of which accounted for more than 5% of total purchases. Historically, no significant difficulty has been encountered with respect to sources of supply; however, disruptions could occur due to factors beyond Grainger's control, such as economic downturns, political unrest, trade issues, etc., any of which could adversely affect a supplier's ability to manufacture or deliver products. If Grainger were to experience difficulty in obtaining products, there could be a short-term adverse effect on results of operations and a longer-term adverse effect on customer relationships and Grainger's reputation. In addition, Grainger has strategic relationships with key vendors. In the event Grainger were unable to maintain those relations, there might be a loss of competitive pricing advantages which could, in turn, adversely affect results of operations.

The addition of new product lines could impact future sales growth. Grainger is continuing in a multiyear product line expansion program. The continued success of this program is expected to be a driver of growth. Its success will depend on Grainger's ability to accurately forecast market demand, obtain products from suppliers and effectively integrate these products into the supply chain. As such, there is a risk that the product line expansion program will not deliver the expected results, which could negatively impact anticipated future sales growth.

Disruptions in Grainger's supply chain could result in an adverse impact on results of operations. A disruption within Grainger's logistics or supply chain network, including damage, destruction, and other events which would cause one or more of the distribution centers to become non-operational, could adversely affect Grainger's ability to deliver inventory in a timely manner, impair Grainger's ability to meet customer demand for products and result in lost sales or damage to Grainger's reputation. Such a disruption could adversely impact the results of operations.

Interruptions in the proper functioning of information systems could disrupt operations and cause unanticipated increases in costs and/or decreases in revenues. The proper functioning of Grainger's information systems, including its websites, is critical to the successful operation of its business. Grainger continues to invest in software, hardware and network infrastructures in order to effectively manage its information systems and websites. Although Grainger's information systems are protected with robust backup and security systems, including physical and software safeguards and remote processing capabilities, information systems are still vulnerable to natural disasters, power losses, computer viruses, telecommunication failures and other problems. If critical information systems fail or otherwise become unavailable, among other things, Grainger's ability to process orders, maintain proper levels of inventories, collect accounts receivable and disburse funds could be adversely affected. Any such interruption of Grainger's information systems could also subject Grainger to additional costs.

Breaches of information systems security could damage Grainger's reputation, disrupt operations, increase costs and/or decrease revenues. Through Grainger's sales and eCommerce channels, Grainger collects and stores confidential information that customers provide to, among other things, purchase products or services, enroll in promotional programs and register on the website. Grainger also acquires and retains information about suppliers and employees in the normal course of business. Despite instituted safeguards for the protection of such information, computer hackers may attempt to penetrate Grainger's or its vendors' information systems and, if successful, misappropriate confidential customer, supplier, employee or other business information. In addition, a Grainger employee, contractor or other third party with whom Grainger does business may attempt to circumvent security measures in order to obtain such information or inadvertently cause a breach involving such information. Loss of customer, supplier, employee or other business information could disrupt operations, damage Grainger's reputation, and expose Grainger to claims from customers, suppliers, financial institutions, regulators, payment card associations, employees and other persons, any of which could have an adverse effect on Grainger, its financial condition and

results of operations. In addition, compliance with tougher privacy and information security laws and standards may result in significant additional expense due to increased investment in technology and the development of new operational processes.

Fluctuations in foreign currency have an effect on reported results of operations. Foreign currency exchange rates and fluctuations have an impact on sales, costs and cash flows from international operations, and could affect reported financial performance.

Acquisitions involve a number of inherent risks, any of which could result in the benefits anticipated not being realized and could have an adverse effect on results of operations. Acquisitions, both foreign and domestic, involve various inherent risks, such as uncertainties in assessing the value, strengths, weaknesses, liabilities and potential profitability of acquired companies. There is a risk of potential losses of key employees of an acquired business and of an inability to achieve identified operating and financial synergies anticipated to result from an acquisition. Additionally, problems could arise from the integration of the acquired business including unanticipated changes in the business or industry, or general economic conditions that affect the assumptions underlying the acquisition. Any one or more of these factors could cause Grainger to not realize the benefits anticipated to result from the acquisitions or have a negative impact on the fair value of the reporting units. Accordingly, goodwill and intangible assets recorded as a result of acquisitions could become impaired.

In order to compete, Grainger must attract, retain and motivate key employees, and the failure to do so could have an adverse effect on results of operations. In order to compete and have continued growth, Grainger must attract, retain and motivate executives and other key employees, including those in managerial, technical, sales, marketing and support positions. Grainger competes to hire employees and then must train them and develop their skills and competencies. Grainger's operating results could be adversely affected by increased costs due to increased competition for employees, higher employee turnover or increased employee benefit costs.

Grainger's continued success is substantially dependent on positive perceptions of Grainger's reputation. One of the reasons why customers choose to do business with Grainger and why employees choose Grainger as a place of employment is the reputation that Grainger has built over many years. To be successful in the future, Grainger must continue to preserve, grow and leverage the value of Grainger's brand. Reputational value is based in large part on perceptions of subjective qualities. Even an isolated incident, or the aggregate effect of individually insignificant incidents, can erode trust and confidence, particularly if they result in adverse publicity, governmental investigations or litigation, and as a result, could tarnish Grainger's brand and lead to adverse effects on Grainger's business.

Grainger's business is subject to various government regulations. Grainger's business is subject to a wide array of laws and regulations in every jurisdiction where it operates, and compliance with these laws and regulations increases the cost of doing business. Grainger is subject to a variety of laws and regulations, including without limitation import and export requirements, the Foreign Corrupt Practices Act, tax laws (including U.S. taxes on foreign subsidiaries), foreign exchange controls and cash repatriation restrictions, data privacy requirements, labor laws and anti-competition regulations, and is also subject to audits and inquiries in the ordinary course of business. As a government contractor selling to federal, state and local government entities, Grainger is also subject to a wide variety of additional laws and regulations. Changes to the legal and regulatory environments could increase the cost of doing business, and such costs may increase in the future as a result of changes in these laws and regulations or in their interpretation. Furthermore, Grainger has implemented policies and procedures designed to facilitate compliance with these laws and regulations, but there can be no assurance that employees, contractors or agents will not violate such laws and regulations or Grainger's policies. Any such violations could individually or in the aggregate materially adversely affect Grainger's financial condition or operating results.

Item 1B: Unresolved Staff Comments

None.

Item 2: Properties

As of December 31, 2012, Grainger's owned and leased facilities totaled approximately 27 million square feet, an increase of approximately 2% from December 31, 2011. The United States business and Acklands–Grainger accounted for the majority of the total square footage. Grainger believes that its properties are generally in excellent condition, well maintained and suitable for the conduct of business.

A brief description of significant facilities follows:

Location	Facility and Use (6)	Size in Square Feet (in 000's)
United States (1)	369 United States branch locations	8,357
United States (2)	15 Distribution Centers	6,699
United States (3)	Other facilities	3,709
Canada (4)	185 Acklands–Grainger facilities	2,890
Other Businesses (5)	Other facilities	3,923
Chicago Area (2)	Headquarters and General Offices	1,349
	Total Square Feet	26,927

- (1) United States branches consist of 273 owned and 96 leased properties located throughout the U.S. Branches range in size from approximately 1,400 to 109,000 square feet. Most leases expire between 2013 and 2020.
- (2) These facilities are primarily owned.
- (3) These facilities include both owned and leased locations, consisting of storage facilities, office space and idle properties, including a one million square foot facility for a new distribution center in Illinois. Operations at this facility began to be phased in during the fourth quarter of 2012 and will be fully operational in 2013.
- (4) Acklands–Grainger facilities consist of general offices, distribution centers and branches located throughout Canada, of which 64 are owned and 121 leased.
- (5) These facilities include owned and leased locations in Europe, Asia, Latin America and other U.S. operations.
- (6) Owned facilities are not subject to any mortgages.

Item 3: Legal Proceedings

Information on specific and significant legal proceedings is set forth in Note 18 to the Consolidated Financial Statements included under Item 8.

Item 4: Mine Safety Disclosures

Not applicable.

PART II

Item 5: Market for Registrant's Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities

Market Information and Dividends

Grainger's common stock is listed on the New York Stock Exchange and the Chicago Stock Exchange, with the ticker symbol GWW. The high and low sales prices for the common stock and the dividends declared and paid for each calendar quarter during 2012 and 2011 are shown below.

	Quarters	Prices		Dividends
		High	Low	
2012	First	\$221.84	\$184.37	\$0.66
	Second	221.00	172.50	0.80
	Third	211.36	176.50	0.80
	Fourth	218.23	184.78	0.80
	Year	\$221.84	\$172.50	\$3.06
2011	First	\$140.17	\$129.01	\$0.54
	Second	154.68	137.75	0.66
	Third	165.55	124.33	0.66
	Fourth	193.21	141.36	0.66
	Year	\$193.21	\$124.33	\$2.52

Grainger expects that its practice of paying quarterly dividends on its common stock will continue, although the payment of future dividends is at the discretion of Grainger's Board of Directors and will depend upon Grainger's earnings, capital requirements, financial condition and other factors.

Holders

The approximate number of shareholders of record of Grainger's common stock as of January 31, 2013, was 820 with approximately 126,300 additional shareholders holding stock through nominees.

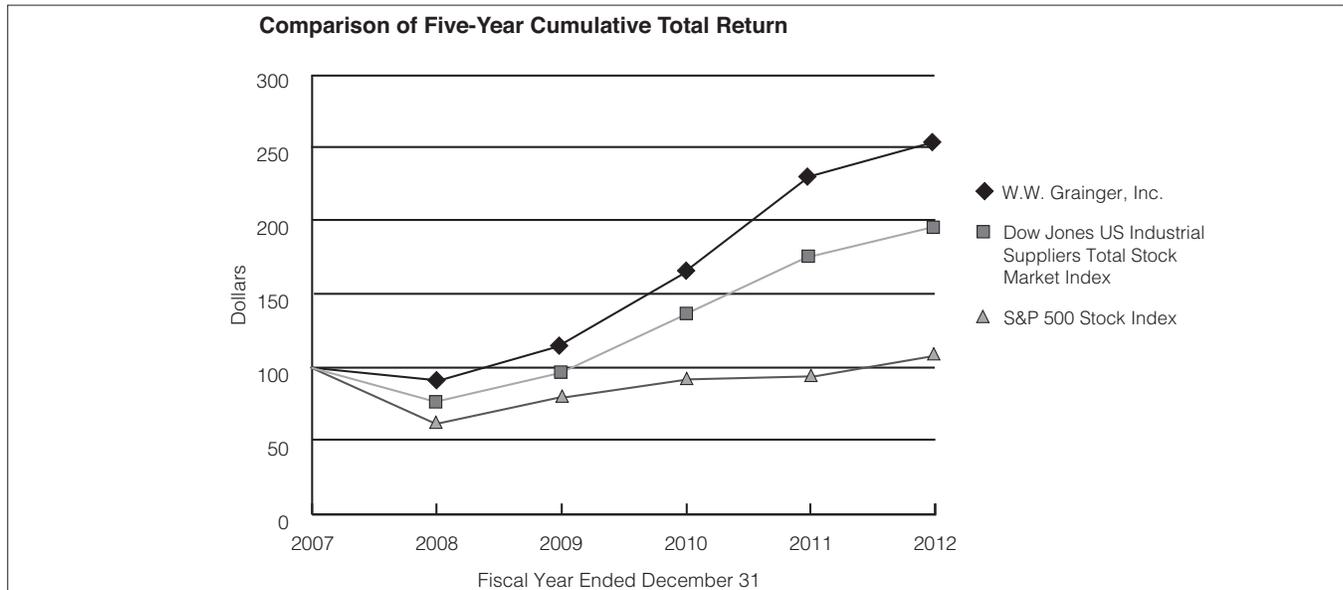
Issuer Purchases of Equity Securities – Fourth Quarter

Period	Total Number of Shares Purchased (A)	Average Price Paid per Share (B)	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (C)	Maximum Number of Shares That May Yet Be Purchased Under the Plans or Programs
Oct. 1 – Oct. 31.....	27,500	202.46	27,500	5,564,009 shares
Nov. 1 – Nov. 30	53,489	191.00	53,489	5,510,520 shares
Dec. 1 – Dec. 31	169,851	194.56	169,851	5,340,669 shares
Total	250,840	194.67	250,840	

- (A) There were no shares withheld to satisfy tax withholding obligations.
- (B) Average price paid per share includes any commissions paid and includes only those amounts related to purchases as part of publicly announced plans or programs.
- (C) Purchases were made pursuant to a share repurchase program approved by Grainger's Board of Directors on July 28, 2010. The program has no specified expiration date. Activity is reported on a trade date basis.

Company Performance

The following stock price performance graph compares the cumulative total return on an investment in Grainger common stock with the cumulative total return of an investment in each of the Dow Jones US Industrial Suppliers Total Stock Market Index and the S&P 500 Stock Index. It covers the period commencing December 31, 2007, and ending December 31, 2012. The graph assumes that the value for the investment in Grainger common stock and in each index was \$100 on December 31, 2007, and that all dividends were reinvested.



	December 31,					
	2007	2008	2009	2010	2011	2012
W.W. Grainger, Inc.....	\$100	\$92	\$115	\$167	\$231	\$253
Dow Jones US Industrial Suppliers Total Stock Market Index.....	100	78	98	137	176	198
S&P 500 Stock Index.....	100	63	80	92	94	109

Item 6: Selected Financial Data

	2012	2011	2010	2009	2008
	(In thousands of dollars, except for per share amounts)				
Net sales	\$8,950,045	\$8,078,185	\$7,182,158	\$6,221,991	\$6,850,032
Net earnings attributable to					
W.W. Grainger, Inc.	689,881	658,423	510,865	430,466	475,355
Net earnings per basic share	9.71	9.26	7.05	5.70	6.07
Net earnings per diluted share	9.52	9.07	6.93	5.62	5.97
Total assets	5,014,598	4,716,062	3,904,377	3,726,332	3,515,417
Long-term debt (less current maturities) and other long-term liabilities	817,229	603,858	747,404	722,334	719,878
Cash dividends paid per share	\$ 3.06	\$ 2.52	\$ 2.08	\$ 1.78	\$ 1.55

Net earnings for 2012 included a \$0.66 per share expense related to the settlement of disputes involving the General Services Administration (GSA) and United States Postal Service (USPS) contracts. See Note 18 to the Consolidated Financial Statements. Results also included a \$0.18 per share expense due to restructuring charges primarily related to improving the long-term performance of the businesses in Europe, India and China, a \$0.04 per share expense due to an impairment charge and a \$0.03 per share expense related to U.S. branch closures. When combined, these items had a net expense effect of \$0.91 per share.

Net earnings for 2011 included a \$0.16 per share expense for U.S. branch closures, a \$0.12 per share benefit related to the settlement of prior year tax reviews and a \$0.07 per share benefit for a gain on the sale of the MRO Korea Co., Ltd. joint venture, which when combined, resulted in a net benefit of \$0.03 per share.

There were two non-cash items included in 2010 earnings, a \$0.28 per share benefit from a change to the paid time off policy and a \$0.15 per share tax expense related to the tax treatment of retiree healthcare benefits following the passage of the Patient Protection and Affordable Care Act, which when combined, resulted in a net benefit of \$0.13 per share. Results for 2009 included a \$0.37 per share non-cash gain from the MonotaRO transaction in September 2009.

For further information see “Item 7: Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

Item 7: Management’s Discussion and Analysis of Financial Condition and Results of Operations

Overview

General. Grainger is a broad-line distributor of maintenance, repair and operating supplies, and other related products and services used by businesses and institutions. Grainger’s operations are primarily in the United States and Canada, with an expanding presence in Europe, Asia and Latin America. Grainger uses a multichannel business model to provide customers with a range of options for finding and purchasing products utilizing sales representatives, catalogs and direct marketing materials and eCommerce. Grainger serves approximately 2 million customers worldwide through a network of highly integrated branches, distribution centers, multiple websites and export services.

Grainger’s two reportable segments are the United States and Canada. The United States segment reflects the results of Grainger’s U.S. operating segment. The Canada segment reflects the results for Acklands–Grainger Inc., Grainger’s Canadian operating segment. Other Businesses include operations in Europe, Asia, Latin America and other U.S. operations, which are not material individually.

Business Environment. Several economic factors and industry trends tend to shape Grainger’s business environment. The overall economy and leading economic indicators provide general insight into projecting Grainger’s growth. Grainger’s sales tend to correlate with Gross Domestic Product (GDP), Industrial Production, Exports, Business Investment, Business Inventory for the United States and Oil prices for Canada. The table below provides these estimated indicators for 2012 and 2013:

	United States		Canada	
	Estimated 2012	Forecasted 2013	Estimated 2012	Forecasted 2013
GDP	2.2%	1.9%	1.9%	1.6%
Industrial Production	3.7%	2.4%	0.5%	0.3%
Exports	3.2%	2.4%	3.4%	3.5%
Business Investment	7.7%	3.8%	5.4%	4.4%
Business Inventory	2.5%	2.2%	—	—
Oil prices	—	—	\$102/barrel	\$95/barrel

Source: Global Insight (February 2013)

The Bureau of Economic Analysis reported the GDP (advance estimate released on January 30, 2013) decreased at an annual rate of 0.1% in the fourth quarter of 2012. Grainger’s results reflected this as sales growth slowed in the fourth quarter, particularly with a sudden decrease in sales the last third of December. Sequentially, Grainger’s sales growth declined in each of the four quarters of 2012.

The light and heavy manufacturing customer sectors, which comprised approximately 27% of Grainger’s total 2012 sales, have historically correlated with manufacturing employment levels and manufacturing production. Manufacturing employment levels in the United States increased approximately 1.5% from December 2011 to December 2012, while manufacturing output increased 1.5%. These increases contributed to a low double-digit percent increase in the heavy manufacturing customer sector and a high single-digit percent increase in the light manufacturing customer sector for Grainger in 2012.

Outlook. During 2013, Grainger plans to continue to make investments in growth drivers such as sales force and product line expansion, eCommerce, inventory management services and international expansion.

While indicators on a macro basis point to a softer economy in 2013, Grainger believes it will continue to outperform these metrics. On January 24, 2013, Grainger reiterated the 2013 earnings per share guidance of \$10.85 to \$12.00 and raised the 2013 sales guidance to a new range of 3 to 9 percent growth. Grainger’s previous 2013 sales guidance was 2 to 8 percent growth issued on November 14, 2012. The increase in sales guidance reflects the December 31, 2012, acquisition of Techni-Tool, Inc., which had sales of \$88 million in 2011.

Matters Affecting Comparability. There were 255 sales days in 2012, 255 in 2011 and 254 in 2010.

Grainger completed several acquisitions throughout 2012 and 2011, all of which were immaterial individually and in the aggregate. Grainger’s operating results have included the results of each business acquired since the respective acquisition dates.

Results of Operations

The following table is included as an aid to understanding changes in Grainger's Consolidated Statements of Earnings:
For the Years Ended December 31,

	As a Percent of Net Sales			Percent Increase/(Decrease) from Prior Year	
	2012	2011	2010	2012	2011
	Net sales.....	100.0%	100.0%	100.0%	10.8%
Cost of merchandise sold	56.2	56.5	58.2	10.2	9.4
Gross profit.....	43.8	43.5	41.8	11.5	16.8
Operating expenses.....	31.2	30.5	29.9	13.3	14.6
Operating earnings	12.6	13.0	11.9	7.5	22.3
Other income (expense).....	(0.1)	—	(0.1)	—	(86.5)
Income taxes	4.7	4.8	4.7	8.8	13.2
Noncontrolling interest	0.1	0.1	—	12.3	194.0
Net earnings attributable to W.W. Grainger, Inc.	7.7%	8.1%	7.1%	4.8%	28.9%

2012 Compared to 2011

Grainger's net sales of \$8,950 million for 2012 increased 11% when compared with net sales of \$8,078 million for 2011. The 11% daily increase for the year consisted of the following contributors:

	Percent Increase/(Decrease)
Volume.....	6 %
Business acquisitions	3 %
Price.....	3 %
Foreign exchange.....	(1)%
Total.....	11 %

Sales to all customer end-markets increased for 2012. The increase in net sales was led by growth in sales to heavy and light manufacturing customers, followed by diversified commercial services customers. Refer to the *Segment Analysis* below for further details.

Gross profit of \$3,916 million for 2012 increased 12%. The gross profit margin for 2012 was 43.8%, up 0.3 percentage points versus 2011, primarily driven by price increases exceeding product cost increases, partially offset by customer mix.

Operating expenses of \$2,785 million for 2012 increased 13% from \$2,458 million for 2011. Operating expenses in 2012 included a \$76 million expense related to the settlement of disputes involving the GSA and USPS contracts. Also included was \$24 million of expense related to branch closure costs, restructuring charges related to improving the long-term performance of the businesses in Europe, India and China and an impairment charge for Grainger Lighting Services (formerly known as Alliance Energy Solutions), an acquisition completed in November 2009. The year 2011 included \$18 million of branch closure costs. Excluding these expenses from both years, operating expenses increased 10%, primarily driven by the Fabory and AnFreixo acquisitions and incremental growth-related spending on new sales representatives, eCommerce and advertising primarily in the United States.

Operating earnings of \$1,131 million for 2012 increased 7% from \$1,052 million for 2011. Excluding the expenses mentioned above for both years, operating earnings increased 15%, primarily due to higher sales and gross profit margins, and operating expenses increasing at a slightly slower rate than sales.

Net earnings attributable to Grainger for 2012 increased by 5% to \$690 million from \$658 million in 2011. The increase in net earnings primarily resulted from an increase in operating earnings. Diluted earnings per share of \$9.52 in 2012 were 5% higher than \$9.07 for 2011, due to increased net earnings.

The table below reconciles reported diluted earnings per share determined in accordance with generally accepted accounting principles in the United States to adjusted diluted earnings per share, a non-GAAP measure. Management believes adjusted diluted earnings per share is an important indicator of operations because it excludes items that may not be indicative of core operating results. Because non-GAAP financial measures are not standardized, it may not be possible to compare this financial measure with other companies' non-GAAP financial measures having the same or similar names.

	Twelve Months Ended December 31,		Percent
	2012	2011	
Diluted earnings per share reported.....	\$ 9.52	\$9.07	5%
GSA/USPS settlement.....	0.66	—	
Restructuring.....	0.18	—	
Goodwill impairment.....	0.04	—	
Charge for U.S. branch closures.....	0.03	0.16	
Settlement of prior year tax reviews.....	—	(0.12)	
Gain on sale of joint venture.....	—	(0.07)	
Subtotal.....	<u>0.91</u>	<u>(0.03)</u>	
Diluted earnings per share adjusted.....	<u>\$10.43</u>	<u>\$9.04</u>	15%

Segment Analysis

The following comments at the reportable segment and other business unit level include external and intersegment net sales and operating earnings. See Note 16 to the Consolidated Financial Statements.

United States

Net sales were \$6,926 million for 2012, an increase of \$425 million, or 7%, when compared with net sales of \$6,501 million for 2011. The 7% daily increase for the year consisted of the following contributors:

	Percent Increase/(Decrease)
Volume.....	4%
Price.....	3%
Total.....	<u>7%</u>

Sales to all customer end-markets increased for 2012. The increase was led by growth in sales to heavy and light manufacturing customers, followed by diversified commercial services customers.

The segment gross profit margin increased 0.3 percentage points in 2012 over 2011, primarily driven by price increases exceeding product cost increases, partially offset by customer mix.

Operating expenses were up 8% for 2012 versus 2011. The 2012 year included a \$76 million expense related to the settlement of disputes involving the GSA and USPS contracts. Also included was \$10 million of expense primarily related to branch closure costs and an impairment charge for Grainger Lighting Services (formerly known as Alliance Energy Solutions), an acquisition completed in November 2009. The 2011 year included costs for the closure of 35 branches of \$18 million. Excluding these expenses from both years, operating expenses increased 4%, primarily driven by an incremental \$70 million in growth-related spending on new sales representatives, eCommerce and advertising.

For the segment, operating earnings of \$1,133 million for 2012 increased 6% over \$1,066 million in 2011. Excluding the expenses mentioned above in both years, operating earnings were up 12%. The improvement in operating earnings for 2012 was due to an increase in net sales and gross profit margin, and operating expenses increasing at a slower rate than sales.

Canada

Net sales were \$1,106 million for 2012, an increase of \$113 million, or 11%, when compared with \$993 million for 2011. In local currency, daily sales increased 12% for 2012. The 11% daily increase for the year consisted of the following contributors:

	Percent Increase/(Decrease)
Volume.....	11 %
Price.....	1 %
Foreign exchange.....	(1)%
Total.....	<u>11 %</u>

The increase in net sales was led by growth to oil and gas, commercial and construction customers.

The gross profit margin increased 0.2 percentage points in 2012 over 2011, primarily driven by price increases exceeding product cost increases, partially offset by unfavorable customer and product mix.

Operating expenses increased 9% in 2012. In local currency, operating expenses increased 10% primarily due to higher volume-related payroll and travel costs, and higher advertising and depreciation expense, partially offset by lower occupancy costs.

Operating earnings of \$127 million for 2012 were up \$20 million, or 18%, versus 2011. In local currency, operating earnings increased 19%. The increase in earnings was due to strong sales growth, an improved gross profit margin and expense leverage.

Other Businesses

Net sales for other businesses, which include operations in Europe, Asia, Latin America and other U.S. operations were up 55% for 2012. The sales increase was due primarily to a full year of sales from Fabory, acquired in August 2011, and incremental sales from AnFreixo, acquired in April 2012, as well as strong growth from the businesses in Japan and Mexico.

Operating earnings for other businesses were \$20 million for 2012 compared to \$31 million for 2011. The decrease was primarily due to restructuring charges related to improving the long-term performance of the businesses in Europe, India and China. Excluding these charges, operating earnings were up \$3 million, primarily driven by improved performance in Japan and Mexico, partially offset by losses from the acquired businesses in Europe and Brazil, along with losses in some start-up businesses in developing markets.

Other Income and Expense

Other income and expense was \$13 million of expense in 2012 compared with \$1 million of expense in 2011. The following table summarizes the components of other income and expense (in thousands of dollars):

	For the Years Ended December 31,	
	2012	2011
Interest income (expense) – net	\$(13,418)	\$(7,023)
Equity in net income of unconsolidated entities	—	314
Gain on sale of investment in unconsolidated entity	—	7,639
Other non-operating income	1,866	709
Other non-operating expense	(1,784)	(2,541)
	<u>\$(13,336)</u>	<u>\$ (902)</u>

Net interest expense increased in 2012 due to higher average debt outstanding, higher average interest rates and interest expense related to capital leases for the acquired business in Europe.

In 2011, Grainger divested its 49% ownership in the MRO Korea Co., Ltd. joint venture, resulting in a gain of approximately \$8 million.

Income Taxes

Income taxes of \$419 million in 2012 increased 9% as compared with \$385 million in 2011. Grainger's effective tax rates were 37.5% and 36.6% in 2012 and 2011, respectively. The 2011 rate benefited from a tax law change in Japan and the settlement of various tax reviews. Excluding these benefits in 2011, the effective tax rate was 38.1%. The effective tax rate in 2012 benefited primarily from a lower blended state tax rate. Grainger is currently projecting an effective tax rate of 37.3% to 37.7% for 2013.

2011 Compared to 2010

Grainger's net sales of \$8,078 million for 2011 increased 13% when compared with net sales of \$7,182 million for 2010. There was one more selling day in 2011 versus 2010. The 12% daily increase for the year consisted of the following contributors:

	Percent Increase/(Decrease)
Volume	8 %
Business acquisitions	2 %
Price.....	2 %
Foreign exchange.....	1 %
Oil spill cleanup in the Gulf of Mexico	(1)%
Total	<u>12 %</u>

Sales to all customer end-markets except one increased for 2011. The overall increase in net sales was led by a mid-teen percent increase to heavy manufacturing customers, followed by a high single-digit increase in light manufacturing. The agriculture and mining customer end-market declined due to the difficult comparison from the oil spill in 2010. Refer to the *Segment Analysis* below for further details.

Gross profit of \$3,511 million for 2011 increased 17%. The gross profit margin for 2011 was 43.5%, up 1.7 percentage points versus 2010. The gross profit margin was favorably affected by price increases exceeding product cost increases, a decline in sales of low margin sourced products and lower excess and obsolete inventory requirements.

Operating expenses of \$2,458 million for 2011 increased 15% from \$2,145 million for 2010. Operating expenses increased primarily driven by volume-related costs, expenses from the Fabory acquisition and incremental spending on Grainger's growth programs. The 2011 year also included approximately \$18 million of costs related to the closure of branches in the United States. In addition, 2010 benefited by \$33 million from a paid time off policy change, which reduced the related liability.

Operating earnings of \$1,052 million for 2011 increased 22% from \$860 million for 2010. The increase in operating earnings was due to higher sales and an improved gross profit margin, partially offset by operating expenses increasing at a faster rate than sales.

Net earnings attributable to Grainger for 2011 increased by 29% to \$658 million from \$511 million in 2010. The increase in net earnings for 2011 primarily resulted from an increase in operating earnings. Diluted earnings per share of \$9.07 in 2011 were 31% higher than \$6.93 for 2010, due to increased net earnings and fewer shares outstanding.

The table below reconciles reported diluted earnings per share determined in accordance with generally accepted accounting principles in the United States to adjusted diluted earnings per share, a non-GAAP measure. Management believes adjusted diluted earnings per share is an important indicator of operations because it excludes items that may not be indicative of core operating results. Because non-GAAP financial measures are not standardized, it may not be possible to compare this financial measure with other companies' non-GAAP financial measures having the same or similar names.

	Twelve Months Ended December 31,		Percent
	2011	2010	
Diluted earnings per share reported	\$ 9.07	\$6.93	31%
Charge for U.S. branch closures.....	0.16	—	
Settlement of prior year tax reviews	(0.12)	—	
Gain on sale of joint venture.....	(0.07)	—	
Paid time off policy change.....	—	(0.28)	
Write-down of deferred tax asset	—	0.15	
Subtotal	<u>(0.03)</u>	<u>(0.13)</u>	
Diluted earnings per share adjusted.....	<u>\$ 9.04</u>	<u>\$6.80</u>	33%

Segment Analysis

The following comments at the reportable segment and other business unit level include external and intersegment net sales and operating earnings. See Note 16 to the Consolidated Financial Statements.

United States

Net sales were \$6,501 million for 2011, an increase of \$481 million, or 8%, when compared with net sales of \$6,020 million for 2010. The 8% daily increase for the year consisted of the following contributors:

	Percent Increase/(Decrease)
Volume.....	7 %
Price.....	3 %
Gulf of Mexico 2010 oil spill cleanup.....	(2)%
Total.....	<u>8 %</u>

Sales to all customer end-markets except one increased for 2011. The overall increase in net sales was led by a mid-teen percent increase to heavy manufacturing customers and a high single-digit increase to light manufacturing customers. The agriculture and mining customer end-market declined due to the difficult comparisons from the oil spill in 2010.

The segment gross profit margin increased 1.7 percentage points in 2011 over 2010. The gross profit margin benefited from price increases exceeding product cost increases, a decline in sales of low margin sourced products and a lower excess and obsolete inventory requirement.

Operating expenses were up 10% for 2011 versus 2010. Operating expenses increased driven by volume and growth-related spending including new sales representatives, eCommerce, advertising and incremental expenses for the new distribution center in northern California. The 2011 year also included costs for the closure of 35 branches. In addition, 2010 included a \$30 million benefit that resulted from a paid time off policy change, which reduced the related liability. Excluding the branch closure costs from 2011 and the 2010 benefit, operating expenses increased 7%.

For the segment, operating earnings of \$1,066 million for 2011 increased 16% over \$920 million in 2010. The improvement in operating earnings for 2011 was due to an increase in net sales and gross profit margin, partially offset by operating expenses increasing at a faster rate than sales.

Canada

Net sales were \$993 million for 2011, an increase of \$172 million, or 21%, when compared with \$821 million for 2010. Daily sales were up 20%. In local currency, daily sales increased 15% for 2011. The 20% daily increase for the year consisted of the following contributors:

	<u>Percent Increase/(Decrease)</u>
Volume	12%
Foreign exchange	5%
Acquisitions	3%
Total	<u>20%</u>

The increase in net sales was led by growth to heavy manufacturing, retail, oil and gas, and agriculture and mining customers.

The gross profit margin increased 2.3 percentage points in 2011 over 2010, primarily driven by lower product costs and stronger sales of private label products, which carry higher margins.

Operating expenses increased 10% in 2011. In local currency, operating expenses increased 5% primarily due to increased payroll and benefits costs driven by higher bonus expense, headcount and incremental costs for acquisitions made over the last year. Non-payroll related expenses also increased driven by volume-related occupancy and warehouse costs.

Operating earnings of \$108 million for 2011 were up \$61 million, or 130%, versus 2010. In local currency, operating earnings increased 121% due to higher sales, an improved gross profit margin and operating expenses increasing at a slower rate than sales.

Other Businesses

Net sales for other businesses, which include operations in Europe, Asia, Latin America and other U.S. operations, were up 66% for 2011. The increase in net sales was due primarily to Fabory, acquired in August of 2011, along with strong growth from all the other international businesses. Operating earnings for other businesses were \$31 million for 2011 compared to \$12 million for 2010. The increase was primarily driven by improved performance in Japan and Mexico.

Other Income and Expense

Other income and expense was \$1 million of expense in 2011 compared with \$7 million of expense in 2010. The following table summarizes the components of other income and expense (in thousands of dollars):

	<u>For the Years Ended December 31,</u>	
	<u>2011</u>	<u>2010</u>
Interest income (expense) – net	\$(7,023)	\$(6,972)
Equity in net income (loss) of unconsolidated entity	314	(182)
Gain on sale of investment in unconsolidated entity	7,639	—
Other non-operating income	709	1,608
Other non-operating expense	(2,541)	(1,151)
	<u>\$ (902)</u>	<u>\$(6,697)</u>

The reduction in net expense was primarily attributable to a gain of \$8 million in the fourth quarter of 2011 related to the divestiture of Grainger's 49% ownership in the MRO Korea Co., Ltd. joint venture.

Income Taxes

Income taxes of \$385 million in 2011 increased 13% as compared with \$340 million in 2010. Grainger's effective tax rates were 36.6% and 39.8% in 2011 and 2010, respectively. The 2011 rate benefited from a tax law change in Japan and the settlement of various tax reviews. The 2010 effective tax rate included a tax expense related to the U.S. healthcare legislation enacted in the first quarter of 2010. Excluding these items in both years, the effective tax rate for 2011 was 38.1% compared to 39.1% in 2010, primarily the result of lower state tax expense and higher earnings in foreign jurisdictions with lower tax rates in 2011.

Financial Condition

Grainger expects its strong working capital position, cash flows from operations and borrowing capacity to continue, allowing it to fund its operations, including growth initiatives, capital expenditures, acquisitions and repurchase of shares, as well as to pay cash dividends.

Cash Flow

Fiscal year 2012 compared with fiscal year 2011

Cash from operating activities continues to serve as Grainger's primary source of liquidity. Net cash flows from operations in 2012 were \$816 million and increased \$70 million from \$746 million in 2011. The primary driver of the improvement was an increase in net earnings of \$32 million as well as an increase of \$38 million in net non-cash expenses.

Net cash used in investing activities of \$306 million in 2012 was driven by net cash expended for property, buildings, equipment and software of \$241 million and net cash paid for business acquisitions of \$65 million. Additional information regarding capital spending is detailed in the *Capital Expenditures* section below. Net cash used in investing activities was \$229 million less than in 2011 due primarily to a decrease in net cash paid for business acquisitions of \$294 million versus 2011.

Net cash used in financing activities of \$394 million in 2012 increased \$217 million from \$177 million in 2011. The increase was primarily due to higher treasury shares repurchases and higher dividends paid in 2012 versus 2011. Cash paid for treasury share purchases was \$341 million in 2012 versus \$151 million in 2011, an increase of \$190 million. Cash dividends paid were \$220 million in 2012, an increase of \$39 million versus 2011.

Fiscal year 2011 compared with fiscal year 2010

Cash from operating activities served as Grainger's primary source of liquidity. Net cash flows from operations in 2011 were \$746 million and increased \$150 million from \$596 million in 2010. The primary driver of the improvement was an increase in net earnings of \$153 million. Higher accounts receivable and inventory balances, driven by growth in sales volumes and a new distribution center in northern California, partially offset by an increase in accounts payable, reduced the operating cash flow from net earnings.

Net cash used in investing activities of \$535 million in 2011 was driven by net cash expended for property, buildings, equipment and software of \$190 million and net cash paid for business acquisitions of \$359 million. Additional information regarding capital spending is detailed in the *Capital Expenditures* section below. Net cash used in investing activities was \$366 million more than in 2010 due primarily to an increase in net cash paid for business acquisitions of \$297 million versus 2010.

Net cash used in financing activities of \$177 million in 2011 decreased \$401 million from \$579 million in 2010. The decrease was primarily due to lower treasury shares repurchases in 2011 versus 2010. Cash paid for treasury share purchases was \$151 million in 2011 versus \$505 million in 2010, a reduction of \$354 million.

Working Capital

Internally generated funds are the primary source of working capital and funds used in business expansion, supplemented by debt. In addition, funds are expended to support growth initiatives, as well as for business and systems development and other infrastructure improvements.

Working capital consists of current assets (less non-operating cash) and current liabilities (less short-term debt and current maturities of long-term debt). Working capital was \$1,604 million at December 31, 2012, compared with \$1,438 million at December 31, 2011. At these dates, the ratio of current assets to current liabilities was 2.6 and 2.4, respectively. The \$166 million increase in working capital and higher current ratio was primarily related to higher accounts receivable and inventory balances, lower accrued compensation and benefits, and lower accounts payable.

Capital Expenditures

In each of the past three years, a portion of operating cash has been used for additions to property, buildings, equipment and capitalized software as summarized in the following table (in thousands of dollars):

	For the Years Ended December 31,		
	2012	2011	2010
Land, buildings, structures and improvements.....	\$ 57,929	\$ 51,249	\$ 61,001
Furniture, fixtures, machinery and equipment.....	145,483	118,228	50,152
Subtotal	203,412	169,477	111,153
Capitalized software	46,448	27,465	15,971
Total.....	<u>\$249,860</u>	<u>\$196,942</u>	<u>\$127,124</u>

In 2012, significant capital investments were made to build new distribution centers in the United States and for distribution center expansion in Canada. In addition, Grainger continued to invest in the improvement of the eCommerce platform, new and existing international businesses, and for the normal recurring replacement of equipment.

In 2011, significant expenditures were made to build new distribution centers in the United States and for distribution center expansion in Canada. Also, a large investment was made to update and improve the eCommerce platform in the United States business. Finally, Grainger continued to invest in new and existing international businesses, as well as for normal recurring replacement of equipment.

In 2010, significant capital expenditures included investments in the distribution center network in the U.S. and Canada. Additional expenditures were for normal recurring replacement of equipment.

In 2013, capital expenditures are expected to range from \$280 million to \$350 million. Projected spending includes continued investments in the supply chain, technology infrastructure and in eCommerce. Grainger expects to fund 2013 capital spending from operating cash.

Debt

Grainger maintains a debt ratio and liquidity position that provides flexibility in funding working capital needs and long-term cash requirements. In addition to internally generated funds, Grainger has various sources of financing available, including bank borrowings under lines of credit. Refer to Note 6 and Note 7 to the Consolidated Financial Statements included in Item 8. Total debt as a percent of total capitalization was 15.3% and 15.9% as of December 31, 2012 and 2011, respectively. The reduction in total debt as a percent of total capitalization was primarily due to increased retained earnings associated with strong earnings in 2012. Grainger believes any circumstances that would trigger early payment or acceleration with respect to any outstanding debt obligations would not have a material impact on its results of operations or financial position.

Commitments and Other Contractual Obligations

At December 31, 2012, Grainger's contractual obligations, including estimated payments due by period, are as follows (in thousands of dollars):

	Payments Due by Period				
	Total Amounts Committed	Less than 1 Year	1-3 Years	4-5 Years	More than 5 Years
Debt obligations.....	\$ 564,644	\$ 97,596	\$ 62,136	\$389,964	\$ 14,948
Interest on debt.....	39,408	12,679	15,920	7,955	2,854
Operating lease obligations.....	231,687	54,456	87,554	50,521	39,156
Purchase obligations:					
Uncompleted additions to property, buildings and equipment.....	85,475	78,560	6,915	—	—
Commitments to purchase inventory	352,795	352,795	—	—	—
Other purchase obligations	204,869	145,992	58,194	683	—
Other liabilities	344,190	176,068	21,465	23,088	123,569
Total	<u>\$1,823,068</u>	<u>\$918,146</u>	<u>\$252,184</u>	<u>\$472,211</u>	<u>\$180,527</u>

Purchase obligations for inventory are made in the normal course of business to meet operating needs. While purchase orders for both inventory purchases and non-inventory purchases are generally cancelable without penalty, certain vendor agreements provide for cancellation fees or penalties depending on the terms of the contract.

Other liabilities represent future payments for profit sharing plans and employee benefits plans as determined by actuarial projections, and other employee benefit plans. Other employment-related benefits costs of \$45 million have not been included in this table as the timing of benefit payments is not statistically predictable. See Note 9 to the Consolidated Financial Statements.

See also Note 7 and Note 10 to the Consolidated Financial Statements for further detail related to the interest on long-term debt and operating lease obligations, respectively.

Grainger has recorded a noncurrent liability of approximately \$43 million for tax uncertainties and interest at December 31, 2012. This amount is excluded from the table above, as Grainger cannot make reliable estimates of these cash flows by period. See Note 14 to the Consolidated Financial Statements.

Off-Balance Sheet Arrangements

Grainger does not have any material exposures to off-balance sheet arrangements. Grainger does not have any variable interest entities or activities that include non-exchange-traded contracts accounted for at fair value.

Critical Accounting Estimates

The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses in the financial statements. Management bases its estimates on historical experience and other assumptions, which it believes are reasonable. If actual amounts are ultimately different from these estimates, the revisions are included in Grainger's results of operations for the period in which the actual amounts become known.

Accounting policies are considered critical when they require management to make assumptions about matters that are highly uncertain at the time the estimates are made and when there are different estimates that management reasonably could have made, which would have a material impact on the presentation of Grainger's financial condition, changes in financial condition or results of operations.

Note 1 to the Consolidated Financial Statements describes the significant accounting policies used in the preparation of the Consolidated Financial Statements. The most significant areas involving management judgments and estimates follow. Actual results in these areas could differ materially from management's estimates under different assumptions or conditions.

Allowance for Doubtful Accounts. Grainger considers several factors to estimate the allowance for uncollectible accounts receivable including the age of the receivables, the percent past due and the historical ratio of actual write-offs to the age of the receivables. The analyses performed also take into consideration economic conditions that may have an impact on a specific industry, group of customers or a specific customer. Based on analysis of actual historical write-offs of uncollectible accounts receivable, Grainger's estimates and assumptions have been materially accurate in regards to the valuation of its allowance for doubtful accounts. However, write-offs could be materially different than the reserves established if business or economic conditions change or actual results deviate from historical trends, and Grainger's estimates and assumptions may be revised as appropriate to reflect these changes. For fiscal years 2012, 2011 and 2010, actual results did not vary materially from estimated amounts.

Inventory Reserves. Grainger establishes inventory reserves for obsolete inventory. Grainger regularly reviews inventory to evaluate continued demand and identify any obsolete or excess quantities. Grainger records provisions for the difference between excess and obsolete inventory and its estimated realizable value. Estimated realizable value is based on anticipated future product demand, market conditions and liquidation values. As Grainger's inventory consists of approximately 1.2 million stocked products, it is not practical to quantify the actual disposition of excess and obsolete inventory against estimated amounts at a SKU level and no individual SKU is material. There were no material differences noted between reserve levels compared to the level of write-offs historically. Grainger's methodology for estimating reserves is continually evaluated based on current experience and the methodology provides for a materially accurate level of reserves at any reporting date. Actual results could differ materially from projections and require changes to reserves which could have a material effect on Grainger's results of operations based on significant changes in product demand, market conditions or liquidation value. If business or economic conditions change, Grainger's estimates and assumptions may be revised as appropriate. For fiscal years 2012, 2011 and 2010, actual results did not vary materially from estimated amounts.

Goodwill and Indefinite Lived Intangible Assets. Grainger's business acquisitions result in the recording of goodwill and identified intangible assets which affect the amount of amortization expense and possibly impairment write-downs that may occur in future periods. Grainger annually reviews goodwill and intangible assets that have indefinite lives for impairment in the fourth quarter and when events or changes in circumstances indicate the carrying value of these assets might exceed their current fair values. Grainger tests for goodwill impairment at the reporting unit level and first performs a qualitative assessment of factors such as a reporting unit's current performance and overall economic factors to determine if it is more likely than not that the goodwill might be impaired and whether it is necessary to perform the two-step quantitative goodwill impairment test. Grainger completed the annual impairment testing using

the qualitative approach for all of its reporting units and the two-step quantitative test for two of its reporting units. Grainger recorded an impairment of \$4 million reducing the carrying value of goodwill to \$13 million for one of them. The estimated fair value of the other reporting unit with the carrying value of goodwill of \$125 million exceeded its carrying value and no indication of impairment existed as of the test date.

Grainger uses the discounted cash flow method to derive the fair value of a reporting unit. The discounted cash flow method requires considerable management judgment, assumptions and estimates regarding future profitability and cash flows of its reporting units and general market conditions, including terminal growth rate and discount rate assumptions. Due to the inherent uncertainties associated with these unobservable Level 3 inputs, the results of these tests may differ and impairment charges could occur in future periods. While Grainger will continue to consider the economic environment and other pertinent factors that may have an adverse effect on its reporting units, there can be no assurance that Grainger's estimates and assumptions regarding forecasted cash flows or other inputs used in forecasting the fair value of future cash flows will prove to be accurate projections.

Stock Incentive Plans. Grainger maintains stock incentive plans under which a variety of incentive grants may be awarded to employees and directors. Grainger uses a binomial lattice option pricing model to estimate the fair value of stock option grants. The model requires projections of the risk-free interest rate, expected life, volatility, expected dividend yield and forfeiture rate of the stock option grants. The fair value of options granted used the following assumptions:

	For the Years Ended December 31,		
	2012	2011	2010
Risk-free interest rate.....	1.1%	2.6%	2.9%
Expected life.....	6 years	6 years	6 years
Expected volatility.....	25.9%	24.6%	24.7%
Expected dividend yield.....	1.6%	1.8%	2.0%

The risk-free interest rate is selected based on yields from U.S. Treasury zero-coupon issues with a remaining term approximately equal to the expected term of the options being valued. The expected life selected for options granted during each year presented represents the period of time that the options are expected to be outstanding based on historical data of option holders' exercise and termination behavior. Expected volatility is based upon implied and historical volatility of the closing price of Grainger's stock over a period equal to the expected life of each option grant. Historical information is also the primary basis for selection of the expected dividend yield assumptions. Because stock option compensation expense is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures, using historical forfeiture experience. The amount of stock option compensation expense is significantly affected by the valuation model and these assumptions. If a different valuation model or different assumptions were used, the stock option compensation expense could be significantly different from what is recorded in the current period.

Compensation expense for other stock-based awards is based upon the closing market price on the last trading date preceding the date of the grant. Because the expense for other stock-based awards should reflect the awards ultimately expected to vest, it has been reduced for estimated forfeitures, using historical forfeiture experience.

For additional information concerning stock incentive plans, see Note 11 to the Consolidated Financial Statements.

Postretirement Healthcare Benefits. Postretirement healthcare obligation and net periodic cost are dependent on assumptions and estimates used in calculating such amounts. The assumptions used include, among others, discount rates, assumed rates of return on plan assets and healthcare cost trend rates, and certain employee-related factors, such as turnover, retirement age and mortality rates. Changes in these and other assumptions (caused by conditions in equity markets or plan experience, for example) could have a material effect on Grainger's postretirement benefit obligation and expense, and could affect its results of operations and financial condition. These changes in assumptions may also affect voluntary decisions to make additional contributions to the trust established for funding the postretirement benefit obligation.

The discount rate assumptions used by management reflect the rates available on high-quality fixed income debt instruments as of December 31, the measurement date, of each year. A lower discount rate increases the present value of benefit obligations and net periodic benefit costs. As of December 31, 2012, Grainger decreased the discount rate used in the calculation of the postretirement plan obligation from 4.5% to 4.0% to reflect the decrease in market interest rates. Grainger estimates that this decrease could reduce 2013 pretax earnings by approximately \$5 million. However, other changes in assumptions may increase, decrease or eliminate this effect.

Grainger considers the long-term historical actual return on plan assets and the historical performance of the Standard & Poor's 500 Index and the Total International Composite Index in developing its expected long-term return on plan assets. In 2012, Grainger maintained the expected long-term rate of return on plan assets of 6.0% (net of tax) based on the historical average of long-term rates of return.

A 1 percentage point change in assumed healthcare cost trend rates would have had the following effects on December 31, 2012 results (in thousands of dollars):

	1 Percentage Point	
	Increase	(Decrease)
Effect on total of service and interest cost.....	\$ 8,909	\$ (6,670)
Effect on accumulated postretirement benefit obligation.....	35,541	(28,647)

During the fourth quarter 2012, Grainger implemented an Employer Group Waiver Plan (EGWP) and a secondary supplemental “wrap-around” plan for its Medicare eligible retiree medical plan participants, and the Part D Retiree Drug Subsidy (RDS) was eliminated effective January 1, 2013. As a result of the implementation of the EGWP program, the benefit obligation is no longer reduced by Part D RDS as of December 31, 2012. The EGWP program does not alter the benefits expected to be provided to the plan participants and is recognized as an actuarial gain for the year ended December 31, 2012. As a result of this change, Grainger’s postretirement benefit obligation was reduced by \$19 million as of December 31, 2012. Grainger estimates that this change could increase 2013 pretax earnings by approximately \$5 million.

During the fourth quarter 2012, Grainger also implemented plan design changes effective January 1, 2013. Employees hired after January 1, 2013 will not be eligible for retiree health benefits. Active participants in the plan as of December 31, 2012 will remain eligible for retiree health benefits with the employee contribution structure modified for certain employees based on retirement eligibility. As a result of this plan amendment, Grainger’s postretirement benefit obligation declined \$84 million as of December 31, 2012. Grainger estimates that this plan amendment could increase 2013 pretax earnings by approximately \$20 million.

Grainger may terminate or modify the postretirement plan at any time, subject to the provisions of the Employee Retirement Income Security Act of 1974 (ERISA) and the Internal Revenue Code, as amended. In the event the postretirement plan is terminated, all assets of the Group Benefit Trust inure to the benefit of the participants. The foregoing assumptions are based on the presumption that the postretirement plan will continue. Were the postretirement plan to terminate, different actuarial assumptions and other factors might be applicable.

Grainger has used its best judgment in making assumptions and estimates and believes such assumptions and estimates used are appropriate. Changes to the assumptions may be required in future years as a result of actual experience or new trends or plan changes and, therefore, may affect Grainger’s retirement plan obligations and future expense. For additional information concerning postretirement healthcare benefits, see Note 9 to the Consolidated Financial Statements.

Insurance Reserves. Grainger retains a significant portion of the risk of certain losses related to workers’ compensation, general liability and property losses through the utilization of high deductibles and self-insured retentions. There are also certain other risk areas for which Grainger does not maintain insurance.

Grainger is responsible for establishing accounting policies on insurance reserves. Although it relies on outside parties to project future claims costs, it retains control over actuarial assumptions, including loss development factors and claim payment patterns. Grainger performs ongoing reviews of its insured and uninsured risks, which it uses to establish the appropriate reserve levels. In calculating the liability, historical trends, claims experience and loss development patterns are analyzed and appropriate loss development factors are applied to the incurred costs associated with the claims made.

The use of assumptions in the analysis leads to fluctuations in required reserves over time. Any change in the required reserve balance is reflected in the current period’s results of operations. Grainger believes its estimates are reasonable based on the information currently available and the methodology used to estimate these reserves has been consistently applied. There were no material adjustments based on Grainger’s historical experience in 2012, 2011 and 2010. If actual trends, including the nature, severity or frequency of claims differ from Grainger’s estimates, or if business or economic conditions change, Grainger’s estimates and assumptions may be revised as appropriate and the results of operations could be materially impacted.

Income Taxes. Grainger recognizes deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial reporting and tax bases of assets and liabilities, using enacted tax rates in effect for the year in which the differences are expected to reverse. The tax balances and income tax expense recognized by Grainger are based on management’s interpretations of the tax laws of multiple jurisdictions. Income tax expense reflects Grainger’s best estimates and assumptions regarding, among other items, the level of future taxable income, interpretation of tax laws and tax planning opportunities, and uncertain tax positions. Future rulings by tax authorities and future changes in tax laws and their interpretation, changes in projected levels of taxable income and future tax planning strategies could impact the actual effective tax rate and tax balances recorded by Grainger.

Contingent Liabilities. At any time, Grainger may be subject to investigations, legal proceedings, or claims related to the ongoing operation of its business, including claims both by and against Grainger. Such proceedings typically involve claims related to product liability, contract disputes, wage and hour laws, employment practices, regulatory compliance or other actions brought by employees, consumers, competitors, suppliers or governmental entities. Grainger routinely assesses the likelihood of any adverse outcomes related to these matters on a case by case basis, as well as the potential ranges of losses and fees. Grainger establishes accruals for its potential exposure, as appropriate, for claims against Grainger when losses become probable and reasonably estimable. Where Grainger is able to reasonably estimate a range of potential losses, Grainger records the amount within that range that constitutes Grainger's best estimate. Grainger also discloses the nature of and range of loss for claims against Grainger when losses are reasonably possible and material. These accruals and disclosures are determined based on the facts and circumstances related to the individual cases and require estimates and judgments regarding the interpretation of facts and laws, as well as the effectiveness of strategies or other factors beyond Grainger's control.

Other. Other significant accounting policies, not involving the same level of measurement uncertainties as those discussed above, are nevertheless important to an understanding of the financial statements. Policies such as revenue recognition, depreciation, intangibles, long-lived assets, fair value measurements and valuations, and warranties require judgments on complex matters that are often subject to multiple external sources of authoritative guidance such as the Financial Accounting Standards Board and the Securities and Exchange Commission. Possible changes in estimates or assumptions associated with these policies are not expected to have a material effect on the financial condition or results of operations of Grainger. More information on these additional accounting policies can be found in Note 1 to the Consolidated Financial Statements.

Inflation

Inflation during the last three years has not had a significant effect on operations. The predominant use of the last-in, first-out (LIFO) method of accounting for inventories and accelerated depreciation methods for financial reporting and income tax purposes result in a substantial recognition of the effects of inflation in the financial statements.

Some of Grainger's products contain significant amounts of commodity-priced materials, such as steel, copper, petroleum derivatives or rare earth minerals, and are subject to price changes based upon fluctuations in the commodities market. Grainger has been able to successfully pass on cost increases to its customers minimizing the effect of inflation on results of operations.

Grainger believes the most positive means to combat inflation and advance the interests of investors lie in the continued application of basic business principles, which include improving productivity, maintaining working capital turnover and offering products and services that can command appropriate prices in the marketplace.

Forward-Looking Statements

This Form 10-K contains statements that are not historical in nature but concern future results and business plans, strategies and objectives and other matters that may be deemed to be "forward-looking statements" under the federal securities laws. Grainger has generally identified such forward-looking statements by using words such as "anticipate, anticipated, assumed, assumes, assumption, assumptions, believe, believes, can, continue, continued, continues, continues to believe it has complied, continuing, could, estimate, estimated, estimates, expect, expectation, expected, expects, forecast, forecasts, if, intend, intended, intends, maintains, may, might, no assurance, plans, predict, predictable, presumption, project, projected, projecting, projection, projections, potential, potentially, reasonably likely, scheduled, should, strategy, tend, tended, timing and outcome are uncertain, unanticipated, will, will be realized, and would" or similar expressions.

Grainger cannot guarantee that any forward-looking statement will be realized, although Grainger does believe that its assumptions underlying its forward-looking statements are reasonable. Achievement of future results is subject to risks and uncertainties that could cause Grainger's results to differ materially from those which are presented.

Factors that could cause actual results to differ materially from those presented or implied in a forward-looking statement include, without limitation: higher product costs or other expenses; a major loss of customers; loss or disruption of source of supply; increased competitive pricing pressures; failure to develop or implement new technologies or business strategies; the outcome of pending and future litigation or governmental or regulatory proceedings; investigations, inquiries, audits and changes in laws and regulations; disruption of information technology or data security systems; general industry or market conditions; general global economic conditions; currency exchange rate fluctuations; market volatility; commodity price volatility; labor shortages; litigation involving appropriate payment for wages; facilities disruptions or shutdowns; higher fuel costs or disruptions in transportation services; natural and other catastrophes; unanticipated weather conditions; and the factors identified in Item 1A, Risk Factors.

Caution should be taken not to place undue reliance on Grainger's forward-looking statements and Grainger undertakes no obligation to publicly update the forward-looking statements, whether as a result of new information, future events or otherwise.

Item 7A: Quantitative and Qualitative Disclosures About Market Risk

Grainger may use financial instruments to reduce its exposure to adverse fluctuations in foreign currency exchange rates and interest rates as part of its overall risk management strategy. The derivative positions reduce risk by hedging certain underlying economic exposures. Because of the high correlation between the hedging instrument and the underlying exposure, fluctuations in the value of the instruments are generally offset by reciprocal changes in the value of the underlying exposure. Grainger does not enter into derivative financial instruments for trading or speculative purposes. See Note 8 and Note 13 to the Consolidated Financial Statements for additional information on Grainger's derivative activities.

Foreign Currency Exchange Rates

Grainger's international subsidiaries generate revenue and expenses in their local currencies. Grainger's consolidated earnings are subject to foreign currency translation exposure upon conversion of a foreign entity's statement of earnings from the functional currency to the reporting currency, which is the U.S. dollar. For 2012, a uniform 10% strengthening of the U.S. dollar relative to foreign currencies that affect Grainger's international subsidiaries would have resulted in a \$7 million decrease in net earnings. Comparatively, in 2011 a uniform 10% strengthening of the U.S. dollar relative to foreign currencies that affect Grainger's international subsidiaries would have resulted in an \$8 million decrease in net earnings. A uniform 10% weakening of the U.S. dollar would have resulted in an \$8 million increase in net earnings for 2012, as compared with an increase in net earnings of \$9 million for 2011. This sensitivity analysis of the effects of changes in foreign currency exchange rates does not factor in future potential changes in sales levels or local currency prices or costs.

Interest Rates

Grainger is subject to interest rate risk related to its variable rate debt portfolio. Grainger may enter into interest rate swap agreements to manage those risks. Based on Grainger's variable rate debt and derivative instruments outstanding, a 1 percentage point increase in interest rates paid by Grainger would have resulted in a decrease to net earnings of approximately \$2 million for 2012 and \$3 million for 2011. A 1 percentage point decrease in interest rates would have resulted in an increase to net earnings of approximately \$2 million for 2012 and \$3 million for 2011. This sensitivity analysis of the effects of changes in interest rates on long-term debt does not factor in future potential changes in long-term debt levels.

Commodity Price Risk

Grainger has limited primary exposure to commodity price risk on certain products for resale, but does not purchase commodities directly.

Item 8: Financial Statements and Supplementary Data

The financial statements and supplementary data are included on pages 29 to 60. See the Index to Financial Statements and Supplementary Data on page 28.

Item 9: Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

None.

Item 9A: Controls and Procedures**Disclosure Controls and Procedures**

Grainger carried out an evaluation, under the supervision and with the participation of its management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of Grainger's disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that Grainger's disclosure controls and procedures were effective as of the end of the period covered by this report.

Internal Control Over Financial Reporting**(A) Management's Annual Report on Internal Control Over Financial Reporting**

Management's report on Grainger's internal control over financial reporting is included on page 29 of this Report under the heading Management's Annual Report on Internal Control Over Financial Reporting.

(B) Attestation Report of the Registered Public Accounting Firm

The report from Ernst & Young LLP on its audit of the effectiveness of Grainger's internal control over financial reporting as of December 31, 2012, is included on page 30 of this Report under the heading Report of Independent Registered Public Accounting Firm.

(C) Changes in Internal Control Over Financial Reporting

There have been no changes in Grainger's internal control over financial reporting during the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, Grainger's internal control over financial reporting.

Item 9B: Other Information

None.

PART III

Item 10: Directors, Executive Officers and Corporate Governance

The information required by this item is incorporated by reference to Grainger's proxy statement relating to the annual meeting of shareholders to be held April 24, 2013, under the captions "Directors," "Board of Directors and Board Committees" and "Section 16(a) Beneficial Ownership Reporting Compliance." Information required by this item regarding executive officers of Grainger is set forth below under the caption "Executive Officers."

Grainger has adopted a code of ethics that applies to the principal executive officer, principal financial officer and principal accounting officer. This code of ethics is incorporated into Grainger's business conduct guidelines for directors, officers and employees. Grainger intends to satisfy the disclosure requirement under Item 5.05 of Form 8-K relating to its code of ethics by posting such information on its website at www.grainger.com/investor. A copy of the code of ethics incorporated into Grainger's business conduct guidelines is also available in print without charge to any person upon request to Grainger's Corporate Secretary. Grainger has also adopted Operating Principles for the Board of Directors, which are available on its website and are available in print to any person who requests them.

Executive Officers

Following is information about the Executive Officers of Grainger including age as of March 1, 2013. Executive Officers of Grainger generally serve until the next annual election of officers, or until earlier resignation or removal.

Name and Age	Positions and Offices Held and Principal Occupation and Employment During the Past Five Years
Laura D. Brown (49)	Senior Vice President, Communications and Investor Relations, a position assumed in 2010 after serving as Vice President, Global Business Communications, a position assumed in 2009 and Vice President, Investor Relations, a position assumed in 2008. Previously, Ms. Brown served as Vice President, Marketing, a position assumed in 2005. After joining Grainger in 2000, she served in various management positions including Vice President, Finance and Vice President, Internet Business Analysis and Supplier Management.
Court D. Carruthers (40)	Senior Vice President and President, Grainger U.S., a position assumed in 2012 after serving as President, Grainger International, a position assumed in 2009, and Senior Vice President of Grainger, a position assumed in 2007. Previously, Mr. Carruthers served as President of Acklands-Grainger Inc., a position assumed in 2006. Prior to assuming the last-mentioned position, he served as Vice President, National Accounts and Sales of Acklands-Grainger Inc., a position assumed in 2002 when he joined that company.
Timothy M. Ferrarell (55)	Senior Vice President and Chief Information Officer, a position assumed in June 2007. Prior to this role, Mr. Ferrarell served as Senior Vice President, Enterprise Systems, since June 2001, and took on responsibility for Enterprise Processes in 2006. He has served in increasingly responsible roles since joining Grainger in 1990 including Vice President, Quality and Business Planning, Vice President, Marketing Communications, Vice President, Product Line Development, and Director, Product Management.
Joseph C. High (58)	Mr. High joined Grainger as Senior Vice President, Chief People Officer in June 2011. Prior to joining Grainger, Mr. High was the Senior Vice President of Human Resources at Owens Corning in Toledo, Ohio, a position assumed in 2004.
John L. Howard (55)	Senior Vice President and General Counsel, a position assumed in 2000.
Gregory S. Irving (54)	Vice President and Controller, a position assumed in 2008. Previously, Mr. Irving served as Vice President, Finance, for Acklands-Grainger Inc. since 2004. After joining Grainger in 1999 he served in various management positions including Vice President, Financial Services and Director, Internal Audit.
Ronald L. Jadin (52)	Senior Vice President and Chief Financial Officer, a position assumed in 2008. Previously, Mr. Jadin served as Vice President and Controller, a position assumed in 2006 after serving as Vice President, Finance. Upon joining Grainger in 1998, he served as Director, Financial Planning and Analysis.
Donald G. Macpherson (45)	Senior Vice President and President, Global Supply Chain and Corporate Strategy, a position assumed in 2012 after serving as Senior Vice President, Global Supply Chain, a position assumed in 2008. Mr. Macpherson joined Grainger in 2008 as Senior Vice President, Supply Chain. Before joining Grainger, he was Partner and Director of the Boston Consulting Group, a global management consulting firm and advisor on business strategy.

Michael A. Pulick (48)	Senior Vice President and President, Grainger International, a position assumed in 2012 after serving as Senior Vice President and President, Grainger U.S., a position assumed in 2008. Previously, Mr. Pulick served as Senior Vice President of Customer Service, a position assumed in 2006. After joining Grainger in 1999, Mr. Pulick has held a number of increasingly responsible positions in Grainger's supplier and product management areas including Vice President, Product Management and Vice President, Merchandising.
James T. Ryan (54)	Chairman of the Board, President and Chief Executive Officer of Grainger, positions assumed in 2009, 2006 and 2008, respectively. Mr. Ryan became Chief Operating Officer and was appointed to Grainger's Board of Directors in 2007. Prior to that, Mr. Ryan served as Group President, a position assumed in 2004. He has served Grainger in increasingly responsible roles since 1980, including Executive Vice President, Marketing, Sales and Service; Vice President, Information Services; President, Grainger.com; and President, Grainger Parts.

Item 11: Executive Compensation

The information required by this item is incorporated by reference to Grainger's proxy statement relating to the annual meeting of shareholders to be held April 24, 2013, under the captions "Board of Directors and Board Committees," "Director Compensation," "Report of the Compensation Committee of the Board" and "Compensation Discussion and Analysis."

Item 12: Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required by this item is incorporated by reference to Grainger's proxy statement relating to the annual meeting of shareholders to be held April 24, 2013, under the captions "Ownership of Grainger Stock" and "Equity Compensation Plans."

Item 13: Certain Relationships and Related Transactions, and Director Independence

The information required by this item is incorporated by reference to Grainger's proxy statement relating to the annual meeting of shareholders to be held April 24, 2013, under the captions "Election of Directors" and "Transactions with Related Persons."

Item 14: Principal Accounting Fees and Services

The information required by this item is incorporated by reference to Grainger's proxy statement relating to the annual meeting of shareholders to be held April 24, 2013, under the caption "Audit Fees and Audit Committee Pre-Approval Policies and Procedures."

PART IV

Item 15: Exhibits and Financial Statement Schedules

- (a) 1. Financial Statements. See Index to Financial Statements and Supplementary Data.
- 2. Financial Statement Schedules. The schedules listed in Reg. 210.5-04 have been omitted because they are either not applicable or the required information is shown in the consolidated financial statements or notes thereto.
- 3. Exhibits
 - (3) (a) Restated Articles of Incorporation, incorporated by reference to Exhibit 3(i) to Grainger's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998.
 - (b) Bylaws, as amended February 17, 2010, incorporated by reference to Exhibit 3(b) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2009.
 - (4) Instruments Defining the Rights of Security Holders, Including Indentures
 - (a) No instruments which define the rights of holders of Grainger's Industrial Development Revenue Bonds are filed herewith, pursuant to the exemption contained in Regulation S-K, Item 601(b)(4)(iii). Grainger hereby agrees to furnish to the Securities and Exchange Commission, upon request, a copy of any such instrument.
 - (10) Material Contracts
 - (a) (i) A Credit Agreement with Wachovia Bank, National Association, as administrative agent, and other lenders, incorporated by reference to Exhibit 10 to Grainger's Quarterly Report on Form 10-Q for the quarter ended March 31, 2008.
 - (b) Compensatory Plans or Arrangements
 - (i) Director Stock Plan, as amended, incorporated by reference to Exhibit 10(c) to Grainger's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006.
 - (ii) 1990 Long-Term Stock Incentive Plan, as amended, incorporated by reference to Exhibit 10(a) to Grainger's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006.

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- (iii) 2001 Long-Term Stock Incentive Plan, as amended, incorporated by reference to Exhibit 10(b) to Grainger's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006.
 - (iv) Form of Indemnification Agreement between Grainger and each of its directors and certain of its executive officers, incorporated by reference to Exhibit 10(b)(i) to Grainger's Quarterly Report on Form 10-Q for the quarter ended March 31, 2009.
 - (v) Frozen Executive Death Benefit Plan, as amended, incorporated by reference to Exhibit 10(b)(v) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2007.
 - (1) First amendment to the Frozen Executive Death Benefit Plan, incorporated by reference to Exhibit 10(b)(v)(1) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2008.
 - (2) Second amendment to the Frozen Executive Death Benefit Plan, incorporated by reference to Exhibit 10(b)(iv)(2) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2009.
 - (vi) Supplemental Profit Sharing Plan, as amended, incorporated by reference to Exhibit 10(viii) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2003.
 - (vii) Supplemental Profit Sharing Plan II, as amended, incorporated by reference to Exhibit 10(b)(ix) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2007.
 - (viii) Voluntary Salary and Incentive Deferral Plan, as amended, incorporated by reference to Exhibit 10(b)(xi) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2007.
 - (ix) Summary Description of the 2013 Directors Compensation Program.
 - (x) 2005 Incentive Plan, as amended, incorporated by reference to Exhibit 10(d) to Grainger's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006.
 - (xi) 2010 Incentive Plan, incorporated by reference to Exhibit B of Grainger's Proxy Statement dated March 12, 2010.
 - (xii) Form of Stock Option Award Agreement between Grainger and certain of its executive officers, incorporated by reference to Exhibit 10(xiv) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2005.
 - (xiii) Form of Stock Option Award and Restricted Stock Unit Agreement between Grainger and certain of its executive officers, incorporated by reference to Exhibit 10(xv) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2005.
 - (xiv) Form of Stock Option Award Agreement between Grainger and certain of its executive officers, incorporated by reference to Exhibit 10(b)(xvi) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2009.
 - (xv) Form of Stock Option and Restricted Stock Unit Agreement between Grainger and certain of its executive officers, incorporated by reference to Exhibit 10(b)(xvii) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2009.
 - (xvi) Form of Restricted Stock Unit Agreement between Grainger and certain of its executive officers, incorporated by reference to Exhibit 10(b)(xviii) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2010.
 - (xvii) Form of 2010 Performance Share Award Agreement between Grainger and certain of its executive officers, incorporated by reference to Exhibit 10(b)(xviii) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2011.
 - (xviii) Form of 2011 Performance Share Award Agreement between Grainger and certain of its executive officers, incorporated by reference to Exhibit 10(b)(xix) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2011.
 - (xix) Form of 2012 Performance Share Award Agreement between Grainger and certain of its executive officers.
 - (xx) Letter of Agreement – Long-Term International Assignment to Mr. Court D. Carruthers dated December 22, 2011, incorporated by reference to Exhibit 10(b) (xxi) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2011.
 - (xxi) Summary Description of the 2013 Management Incentive Program.

(xxii) Incentive Program Recoupment Agreement, incorporated by reference to Exhibit 10(b)(xxv) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2009.

(xxiii) Form of Change in Control Employment Agreement between Grainger and certain of its executive officers incorporated by reference to Exhibit 10(b)(xxvii) to Grainger's Annual Report on Form 10-K for the year ended December 31, 2010.

(21) Subsidiaries of Grainger.

(23) Consent of Independent Registered Public Accounting Firm.

(31) Rule 13a – 14(a)/15d – 14(a) Certifications

(a) Chief Executive Officer certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

(b) Chief Financial Officer certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

(32) Section 1350 Certifications

Chief Executive Officer and Chief Financial Officer certifications pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.