INDEX TO FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

December 31, 2017, 2016 and 2015

MANAGEMENT'S ANNUAL REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of W.W. Grainger, Inc. (Grainger) is responsible for establishing and maintaining adequate internal control over financial reporting. Grainger's internal control system was designed to provide reasonable assurance to Grainger's management and Board of Directors regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements under all potential conditions. Therefore, effective internal control over financial reporting provides only reasonable, and not absolute, assurance with respect to the preparation and presentation of financial statements.

Grainger's management assessed the effectiveness of Grainger's internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). Based on its assessment under that framework and the criteria established therein, Grainger's management concluded that Grainger's internal control over financial reporting was effective as of December 31, 2017.

Ernst & Young LLP, an independent registered public accounting firm, has audited Grainger's internal control over financial reporting as of December 31, 2017, as stated in their report, which is included herein.

Report of Independent Registered Public Accounting Firm

To the Shareholders and the Board of Directors of
W.W. Grainger, Inc. and Subsidiaries

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of W.W. Grainger, Inc. and subsidiaries (the Company) as of December 31, 2017 and 2016, the related consolidated statements of earnings, comprehensive earnings, and shareholders' equity and cash flows for each of the three years in the period ended December 31, 2017, and the related notes (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company at December 31, 2017 and 2016, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2017, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated February 26, 2018 expressed an unqualified opinion thereon.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Ernst & Young LLP

We have served as the Company's auditor since 2005.

Chicago, Illinois
February 26, 2018

Report of Independent Registered Public Accounting Firm

To the Shareholders and the Board of Directors of
W.W. Grainger, Inc. and Subsidiaries

Opinion on Internal Control over Financial Reporting

We have audited W.W. Grainger, Inc. and subsidiaries' internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 Framework) (the COSO Criteria). In our opinion, W.W Grainger, Inc. and subsidiaries (the Company) maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated balance sheets of the Company as of December 31, 2017 and 2016, and the related consolidated statements of earnings, comprehensive earnings, and shareholders' equity and cash flows for each of the three years in the period ended December 31, 2017 and the related notes and our report dated February 26, 2018 expressed an unqualified opinion thereon.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of effectiveness of the internal control over financial reporting included in the accompanying Management's Annual Report on Internal Controls over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects.

Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Ernst & Young LLP
Chicago, Illinois
February 26, 2018

W.W. Grainger, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF EARNINGS
(In thousands of dollars, except for share and per share amounts)

	For the Years Ended December 31,		
	2017	2016	2015
Net sales	$ 10,424,858	$ 10,137,204	$ 9,973,384
Cost of merchandise sold	6,327,301	6,022,647	5,741,956
Gross profit	4,097,557	4,114,557	4,231,428
Warehousing, marketing and administrative expenses	3,048,895	2,995,060	2,931,108
Operating earnings	1,048,662	1,119,497	1,300,320
Other income and (expense):			
Interest income	2,570	717	1,166
Interest expense	(80,458)	(66,332)	(33,571)
Loss from equity method investment	(37,771)	(31,193)	(11,740)
Other, net	2,321	(3,631)	(5,470)
Total other expense	(113,338)	(100,439)	(49,615)
Earnings before income taxes	935,324	1,019,058	1,250,705
Income taxes	312,881	386,220	465,531
Net earnings	622,443	632,838	785,174
Less: Net earnings attributable to noncontrolling interest	36,713	26,910	16,178
Net earnings attributable to W.W. Grainger, Inc.	$ 585,730	$ 605,928	$ 768,996
Earnings per share:			
Basic	$ 10.07	$ 9.94	$ 11.69
Diluted	$ 10.02	$ 9.87	$ 11.58
Weighted average number of shares outstanding:			
Basic	57,674,977	60,430,892	65,156,864
Diluted	57,983,167	60,839,930	65,765,121

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

W.W. Grainger, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS
(In thousands of dollars)

	For the Years Ended December 31,		
	2017	2016	2015
Net earnings	$ 622,443	$ 632,838	$ 785,174
Other comprehensive earnings:			
Foreign currency translation adjustments, net of reclassification (see Note 6 and Note 13)	92,711	(38,729)	(154,096)
Postretirement benefit plan remeasurement, net of tax expense $29,172 (see Note 9 and Note 13)	46,543	—	—
Postretirement benefit plan reclassification, net of tax (expense) benefit of $(1,017), $6,991 and $(17,013)	2,043	(12,453)	27,846
Other	—	885	1,300
Comprehensive earnings, net of tax	763,740	582,541	660,224
Less: Comprehensive earnings attributable to noncontrolling interest:			
Net earnings	36,713	26,910	16,178
Foreign currency translation adjustments	3,677	906	(532)
Comprehensive earnings attributable to W.W. Grainger, Inc.	$ 723,350	$ 554,725	$ 644,578

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

W.W. Grainger, Inc. and Subsidiaries
CONSOLIDATED BALANCE SHEETS
(In thousands of dollars, except for share and per share amounts)

	As of December 31,	
ASSETS	2017	2016
CURRENT ASSETS		
Cash and cash equivalents	$ 326,876	$ 274,146
Accounts receivable - net	1,325,186	1,223,096
Inventories – net	1,429,199	1,406,470
Prepaid expenses and other assets	86,667	81,766
Prepaid income taxes	38,061	34,751
Total current assets	3,205,989	3,020,229
PROPERTY, BUILDINGS AND EQUIPMENT	3,444,660	3,411,502
Less: Accumulated depreciation and amortization	2,052,693	1,990,611
Property, buildings and equipment – net	1,391,967	1,420,891
DEFERRED INCOME TAXES	22,362	64,775
GOODWILL	543,903	527,150
INTANGIBLES – NET	569,115	586,126
OTHER ASSETS	70,918	75,136
TOTAL ASSETS	$ 5,804,254	$ 5,694,307
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Short-term debt	$ 55,603	$ 386,140
Current maturities of long-term debt	38,709	19,966
Trade accounts payable	731,582	650,092
Accrued compensation and benefits	254,560	212,525
Accrued contributions to employees’ profit-sharing plans	92,682	54,948
Accrued expenses	313,766	290,207
Income taxes payable	19,759	15,059
Total current liabilities	1,506,661	1,628,937
LONG-TERM DEBT (less current maturities)	2,248,036	1,840,946
DEFERRED INCOME TAXES AND TAX UNCERTAINTIES	111,710	126,101
EMPLOYMENT-RELATED AND OTHER NONCURRENT LIABILITIES	110,114	192,555
SHAREHOLDERS' EQUITY		
Cumulative preferred stock – $5 par value – 12,000,000 shares authorized; none issued or outstanding	—	—
Common stock – $0.50 par value – 300,000,000 shares authorized; issued 109,659,219 shares	54,830	54,830
Additional contributed capital	1,040,493	1,030,256
Retained earnings	7,405,192	7,113,559
Accumulated other comprehensive losses	(134,674)	(272,294)
Treasury stock, at cost – 53,330,356 and 50,854,905 shares, respectively	(6,675,709)	(6,128,416)
Total W.W. Grainger, Inc. shareholders’ equity	1,690,132	1,797,935
Noncontrolling interest	137,601	107,833
Total shareholders' equity	1,827,733	1,905,768
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 5,804,254	$ 5,694,307

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

W.W. Grainger, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands of dollars)

	For the Years Ended December 31,		
	2017	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net earnings	$ 622,443	$ 632,838	$ 785,174
Provision for losses on accounts receivable	16,376	16,216	10,181
Deferred income taxes and tax uncertainties	(5,048)	(5,884)	4,076
Depreciation and amortization	264,064	248,857	227,967
Impairment of goodwill, intangible and other assets	28,186	52,318	—
Net (gains) losses from sales of assets and business divestitures	(8,795)	(18,521)	2,765
Stock-based compensation	32,661	35,735	46,861
Losses from equity method investment	37,771	31,193	11,740
Change in assets and liabilities – net of business acquisitions and divestitures:			
Accounts receivable	(103,126)	(45,600)	(3,085)
Inventories	(4,915)	(4,403)	(37,737)
Prepaid expenses and other assets	(5,024)	18,641	15,788
Trade accounts payable	72,332	72,882	23,130
Other current liabilities	112,445	(3,937)	(24,101)
Current income taxes payable	3,967	(3,513)	6,943
Accrued employment-related benefits cost	(6,380)	7,542	(27,721)
Other – net	(400)	(10,281)	(5,872)
Net cash provided by operating activities	1,056,557	1,024,083	1,036,109
CASH FLOWS FROM INVESTING ACTIVITIES:			
Additions to property, buildings and equipment and intangibles	(237,283)	(284,249)	(373,868)
Proceeds from sales of assets and business divestitures	120,228	55,023	14,857
Equity method investment	(34,754)	(34,103)	(20,382)
Cash paid for business acquisitions	—	(159)	(464,431)
Other – net	5,726	1,224	466
Net cash used in investing activities	(146,083)	(262,264)	(843,358)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net (decrease) increase in commercial paper	(369,766)	39,748	325,000
Borrowings under lines of credit	73,781	36,055	54,770
Payments against lines of credit	(43,256)	(37,358)	(78,559)
Proceeds from issuance of long-term debt	401,764	515,985	1,307,183
Payments of long-term debt	(39,301)	(262,248)	(52,838)
Proceeds from stock options exercised	47,418	34,125	60,885
Payments for employee taxes withheld from stock awards	(27,884)	(21,107)	(46,205)
Excess tax benefits from stock-based compensation	—	11,905	27,553
Purchase of treasury stock	(605,431)	(789,773)	(1,400,071)
Cash dividends paid	(304,473)	(302,971)	(306,474)
Net cash used in financing activities	(867,148)	(775,639)	(108,756)
Exchange rate effect on cash and cash equivalents	9,404	(2,170)	(20,503)
NET CHANGE IN CASH AND CASH EQUIVALENTS:	52,730	(15,990)	63,492
Cash and cash equivalents at beginning of year	274,146	290,136	226,644
Cash and cash equivalents at end of year	$ 326,876	$ 274,146	$ 290,136
Supplemental cash flow information:			
Cash payments for interest (net of amounts capitalized)	$ 78,043	$ 63,143	$ 31,591
Cash payments for income taxes	$ 334,647	$ 359,506	$ 442,486

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

W.W. Grainger, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(In thousands of dollars, except for per share amounts)

	Common Stock	Additional Contributed Capital	Retained Earnings	Accumulated Other Comprehensive Earnings (Losses)	Treasury Stock	Noncontrolling Interest
Balance at January 1, 2015	$ 54,830	$ 948,340	$6,335,990	$ (96,673)	$ (4,032,615)	$ 74,229
Exercise, settlement and vesting of stock based compensation awards	—	(22,781)	—	—	62,835	460
Stock based compensation expense	—	42,643	—	—	—	163
Tax benefits on stock-based compensation awards	—	31,614	—	—	—	—
Purchase of treasury stock	—	—	—	—	(1,399,931)	(140)
Net earnings	—	—	768,996	—	—	16,178
Other comprehensive losses	—	—	—	(124,418)	—	(532)
Cash dividends paid ($4.59 per share)	—	660	(302,856)	—	—	(4,278)
Balance at December 31, 2015	$ 54,830	$ 1,000,476	$6,802,130	$ (221,091)	$ (5,369,711)	$ 86,080
Exercise, settlement and vesting of stock based compensation awards	—	(18,137)	—	—	41,307	58
Stock based compensation expense	—	34,915	—	—	—	441
Tax benefits on stock-based compensation awards	—	12,284	—	—	—	—
Purchase of treasury stock	—	—	—	—	(800,012)	(130)
Net earnings	—	—	605,928	—	—	26,910
Other comprehensive (losses) earnings	—	—	—	(51,203)	—	3,664
Cash dividends paid ($4.83 per share)	—	718	(294,499)	—	—	(9,190)
Balance at December 31, 2016	$ 54,830	$ 1,030,256	$7,113,559	$ (272,294)	$ (6,128,416)	$ 107,833
Exercise, settlement and vesting of stock based compensation awards	—	(22,906)	—	—	60,273	206
Stock based compensation expense	—	32,514	—	—	—	137
Purchase of treasury stock	—	—	—	—	(607,566)	(114)
Net earnings	—	—	585,730	—	—	36,713
Other comprehensive (losses) earnings	—	—	—	137,620	—	3,831
Cash dividends paid ($5.06 per share)	—	629	(294,097)	—	—	(11,005)
Balance at December 31, 2017	$ 54,830	$ 1,040,493	$7,405,192	$ (134,674)	$ (6,675,709)	$ 137,601

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