Q2 2017 Earnings Call

W.W. Grainger, Inc.

GRAINGER

July 19, 2017

Safe Harbor Statement and Non-GAAP Financial Measures

All statements in this communication, other than those relating to historical facts, are “forward-looking statements.” These forward-looking statements are not guarantees of future performance and are subject to a number of assumptions, risks and uncertainties, many of which are beyond our control, which could cause actual results to differ materially from such statements. These statements include, but are not limited to, statements about future strategic plans and future financial and operating results. Important factors that could cause actual results to differ materially from our expectations include, among others: 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; the implementation, timing and success of our strategic pricing initiatives; the outcome of pending and future litigation or governmental or regulatory proceedings, including with respect to wage and hour, anti-bribery and corruption, environmental, advertising, privacy and cybersecurity matters; 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; facilities disruptions or shutdowns; higher fuel costs or disruptions in transportation services; natural and other catastrophes; unanticipated weather conditions; loss of key members of management; our ability to operate, integrate and leverage acquired businesses; changes in credit ratings; changes in effective tax rates and other factors which can be found in our filings with the Securities and Exchange Commission, including our most recent periodic reports filed on Form 10-K and Form 10-Q, which are available on our Investor Relations website. Forward-looking statements are given only as of the date of this communication and we disclaim any obligation to update or revise any forward-looking statement, whether as a result of new information, future events or otherwise, except as required by law.

Additional information relating to certain non-GAAP financial measures referred to in this presentation, including adjusted operating earnings, adjusted segment operating earnings, adjusted net earnings and adjusted diluted earnings per share, is available in the appendix to this presentation and our most recent earnings release.

DG Macpherson

Chief Executive Officer

Q2 2017 Reported Results – Total Company

($ in millions)	**Q2 2017**	**Q2 2016**	**% vs. PY**
Sales	$ 2,615	$ 2,564	2%
GP	1,040	1,040	0%
Op Expense	808	734	10%
Op Earnings	$ 232	$ 306	-24%
EPS	**$ 1.67**	**$ 2.79**	**-40%**

(% of sales)	**Q2 2017**	**Q2 2016**	**bps vs. PY**
GP Margin	39.8%	40.6%	(80)
Op Expense	30.9%	28.7%	220
Op Margin	8.9%	11.9%	(300)

- Reported results affected by:
  - Colombia wind-down:
    - OE: -$42M
    - EPS: -$0.71
  - Canada restructuring:
    - OE: -$20M
    - EPS: -$0.35
- The remaining slides reference adjusted results, which exclude items outlined in our Q2 press release.

Q2 2017 Adjusted Results – Total Company

($ in millions)	Q2 2017	Q2 2016	% vs. PY
Sales	$ 2,615	$ 2,564	2%
GP	1,043	1,051	-1%
Op Expense	748	728	3%
Op Earnings	$ 294	$ 323	-9%
EPS	**$ 2.74**	**$ 2.89**	**-5%**

(% of sales)	Q2 2017	Q2 2016	bps vs. PY
GP Margin	39.9%	41.0%	(110)
Op Expense	28.7%	28.4%	30
Expense/COGS	47.6%	48.1%	(50)
Op Margin	11.2%	12.6%	(140)

- Sales up 2% vs. prior year
  - Volume up 7%
  - Price down 3%
  - FX down 1%
  - Holiday timing down 1%
- GP margin decline driven by customer response to U.S. pricing actions
- Operating expense leverage on higher volume (Expense/COGS)

Q2 2017 Adjusted Results – Other Businesses

($ in millions)	**Q2 2017**	**Q2 2016**	**% vs. PY**
Sales	$ 527	$ 474	11%
Op Earnings	$ 27	$ 30	-8%

(% of sales)	**Q2 2017**	**Q2 2016**	**bps vs. PY**
Op Margin	5.2%	6.3%	(110)

- Sales up 11% vs. prior year
  - Price and volume up 14%
  - FX headwind 3%, primarily due to British pound
- Online businesses (Zoro and MonotaRO) delivered 23% sales growth and operating margin improvement of 50 basis points
- Cromwell operating margin under pressure due to Brexit/economic uncertainties

Q2 2017 Adjusted Results – Canada

($ in millions)	**Q2 2017**	**Q2 2016**	**% vs. PY**
Sales	$ 189	$ 194	-3%
Op Earnings	$ -7	$ -10	26%

(% of sales)	**Q2 2017**	**Q2 2016**	**bps vs. PY**
Op Margin	-3.8%	-5.1%	130

- Sales down 3% vs. prior year
  - Up 2% in local currency
- Trends improving
- Announced restructuring including closure of 59 of 144 branches
- On track to reach a break even run rate during Q4 2017

GRAINGER

Q2 2017 Adjusted Results – United States

($ in millions)	Q2 2017	Q2 2016	% vs. PY
Sales	$ 1,999	$ 1,979	1%
Op Earnings	$ 312	340	-8%

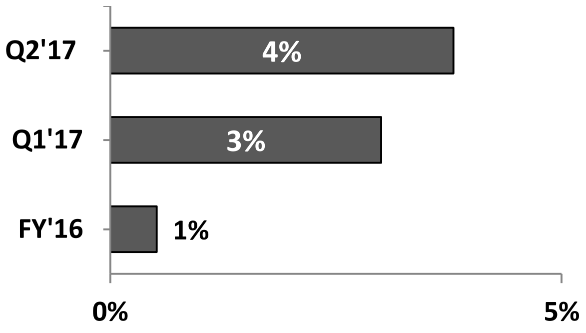
(% of sales)	Q2 2017	Q2 2016	bps vs. PY
Op Margin	15.6%	17.2%	(160)

- Sales up 1% vs. prior year
  - Volume up 5%
  - Price down 4%
- Operating expense up 2% on 5% volume growth
- Operating margin decline driven by pricing actions

U.S. Business – Volume Response to Pricing Actions

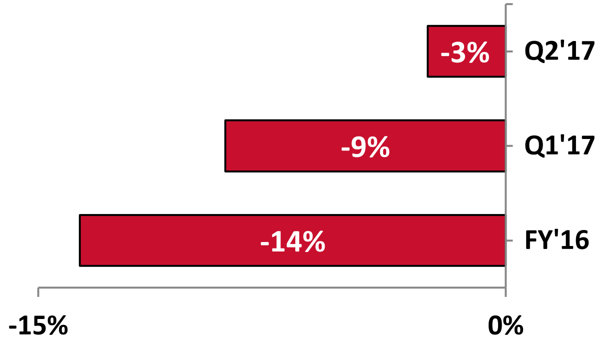
U.S. Large – pricing actions proof points[1]

Total volume growth on $6.1 billion of revenue



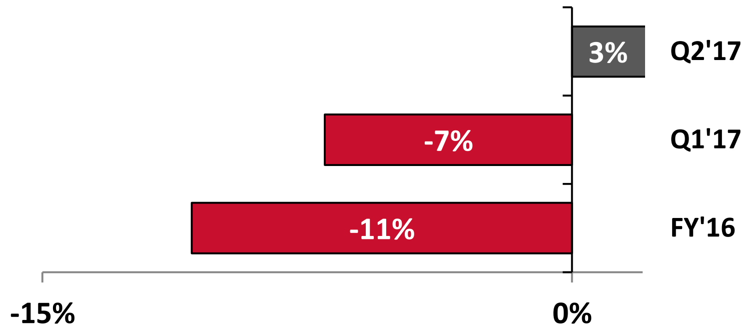
Spot buy volume growth

(~30% of volume)



U.S. Medium – pricing actions proof points[1]

Total volume growth on $0.9 billion of revenue



Pricing actions enabling share gains with Medium

- ~50% of Medium volume on more competitive pricing (Web or Red Pass)
- Medium Red Pass customers achieving double digit growth year-to-date
- All Medium customer volume will be competitively priced in August
- Launch digital marketing in August to drive Medium customer acquisition

1. U.S. Large and Medium total product COGS dollars (excludes freight, rebates and other adjustments) used as a proxy for volume

Expense Management

Drivers of 2019 productivity

- Continue expense leverage trend
- Cost take-out of $100 to $125 million
  - **U.S.: $80 to $95 million (net of marketing investment):**
    - Contact center consolidation
    - Volume driven expense efficiency (DC scale)
    - Reduced complexity due to pricing actions
    - Fulfillment
  - **Canada: $20 to $30 million:**
    - Closing 59 of 144 branches in 2017
  - **International**
    - Colombia business wind-down

U.S. incremental expense: 2017 - 2019

- Assumes 6% to 8% annual volume growth from 2017 to 2019
  - Volume variable expense: +$60 to +$90 million
  - Inflationary expenses: +$80 to +$85 million
  - Cost takeout, net of incremental marketing investment: -$80 to -$95 million

Reiterating 2017 Guidance (Adjusted)

	Low	Mid	High
Sales *($ billions)*	**$10.2**	**$10.4**	**$10.5**
% vs. prior year	1%	2.5%	4%
GP Margin	**38.8%**	**39.1%**	**39.4%**
bps vs. prior year	(190)	(160)	(130)
Op. Margin	**10.4%**	**10.7%**	**11.2%**
bps vs. prior year	(210)	(170)	(130)
EPS	**$10.00**	**$10.65**	**$11.30**

GRAINGER®

Note: Reiterating guidance issued on 4/18/2017 as of 7/19/2017. Reference slide 21 for GAAP vs. non-GAAP reconciliation.

2017 and 2019 Operating Margin Guidance Remains Unchanged

	2017E	2019E
U.S.	14% - 15%	15% - 16%
Canada	(6)% - (4)%	2% - 4%
Other Businesses	6% - 7%	8 - 10%
Company	**10% - 11%**	**12% - 13%**

2019 Outlook:

- Total company 2019 operating margin guidance unchanged from November 2016 analyst meeting
- U.S. price deflation offset by better mix and continued cost productivity
- Canada volume and pricing improves along with significant cost takeout

Note: Company includes unallocated expenses and eliminations.

Closing Remarks

- Quarter results were as expected
- Seeing growth from U.S. pricing actions in the places that will help us grow profitably in the future – Medium customers and Large customer spot buy
- Portfolio is in a much better place given our actions (Colombia)
- Actions in Canada intended to speed the path to double digit operating margin for the business – we will provide frequent updates

Q&A

Appendix

Price reduction impact on GP% (hypothetical example)

	Prior Year	Current Year	Variance	Change
Sales	**$100.0**	**$95.0**	**-$5.0**	**-5.0%**
COGS	$60.0	$60.0	$0	
COGS %	60.0%	63.2%	3.2%	
Gross Profit	$40.0	$35.0	-$5.0	
GP%	**40.0%**	**36.8%**	**-3.2%**	**-320 bps**

A price reduction of 5% would have a GP% impact of ***less than*** -500 basis points (all else equal)

Quarterly Sales

	Q2 2017 Sales vs. Q2 2016			
	Company	United States	Canada	Other Businesses
Volume	7%	5%	2%	14%
Price	-3%	-4%	-1%	
Seasonal	0%	0%	0%	
Holiday timing	-1%	-1%	-1%	
Intercompany sales	n/a	1%	0%	
Foreign exchange	-1%	n/a	-5%	-3%
Wildfire impact	n/a	n/a	2%	
Change vs. Prior	**2%**	**1%**	**-3%**	**11%**
% of Company Revenue	100%	73%	7%	20%

Note: 64 selling days in both quarters

	Q2 2017 Daily Sales by Month			
	Company	United States	Canada	Other Businesses
April	1%	0%	-11%	10%
May	3%	3%	-2%	11%
June	2%	0%	5%	12%
Q2	**2%**	**1%**	**-3%**	**11%**

GRAINGER

Q2 2017 U.S. Sales By Customer End Market

- Natural Resources and Retail were up in the mid-single digits;
- Heavy Manufacturing and Reseller were up in the low single digits;
- Commercial and Government were flat;
- Light Manufacturing was down in the low single digits;
- Contractor was down in the mid-single digits.

Selling Days – 2017 vs. 2016

Month	2017	2016	Difference
January	21	20	1
February	20	21	-1
March	23	23	0
1Q	**64**	**64**	**0**
April	20	21	-1
May	22	21	1
June	22	22	0
2Q	**64**	**64**	**0**
July	20	20	0
August	23	23	0
September	20	21	-1
3Q	**63**	**64**	**-1**
October	22	21	1
November	21	21	0
December	20	21	-1
4Q	**63**	**63**	**0**
Full Year	**254**	**255**	**-1**

Q2 2017 Branch Summary

	Second Quarter 2017 Branch Summary				
	Branches 3/31/2017	**Opened**	**Closed**	**Branches 6/30/2017**	**Distribution Centers 6/30/2017**
United States	284	2	0	286	18
Canada	151	0	2	149	5
Other Businesses					
Fabory	70	0	0	70	2
Mexico	18	0	0	18	2
Cromwell	62	0	0	62	1
Colombia	6	0	0	6	1
China	0	0	0	0	1
Puerto Rico	5	0	0	5	0
Dominican Republic	1	0	0	1	0
Japan	0	0	0	0	2
Brazil	0	0	0	0	1
Peru	1	0	0	1	0
Total Other Businesses	163	0	0	163	10
Total	598	2	2	598	33

GAAP to Non-GAAP Reconciliations

	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016	%
Operating earnings reported	$ 232,065	$ 305,589	(24)%
Branch gains (United States)	(13,438)	(15,376)	
Restructuring (United States)	13,541	6,024	
Restructuring (Canada)	20,485	8,055	
Inventory reserve adjustment (Canada)	—	9,847	
Restructuring (Other Businesses)	41,510	—	
Restructuring (Unallocated expense)	—	8,947	
Subtotal	62,098	17,497	
Operating earnings adjusted	$ 294,163	$ 323,086	(9)%

	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016	%
Segment operating earnings adjusted			
United States	312,392	339,586	
Canada	(7,242)	(9,839)	
Other Businesses	27,288	29,724	
Unallocated expense	(38,275)	(36,385)	
Segment operating earnings adjusted	$ 294,163	$ 323,086	(9)%
Company operating margin adjusted	11.2%	12.6 %	

	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016	%
Net earnings reported	$ 97,921	$ 172,676	(43)%
Branch gains (United States)	(8,419)	(9,622)	
Restructuring (United States)	11,161	3,770	
Restructuring (Canada)	16,498	5,922	
Inventory reserve adjustment (Canada)	—	7,240	
Restructuring (Other Businesses)	43,969	—	
Restructuring (Unallocated expense)	—	5,599	
Discrete tax item	—	(7,075)	
Subtotal	63,209	5,834	
Net earnings adjusted	$ 161,130	$ 178,510	(10)%
Diluted earnings per share reported	$ 1.67	$ 2.79	(40)%
Pretax adjustments:			
Branch gains (United States)	(0.23)	(0.25)	
Restructuring (United States)	0.23	0.10	
Restructuring (Canada)	0.35	0.13	
Inventory reserve adjustment (Canada)	—	0.16	
Restructuring (Other Businesses)	0.71	—	
Restructuring (Unallocated expense)	—	0.15	
Total pretax adjustments	1.06	0.29	
Tax effect (1)	0.01	(0.08)	
Discrete tax item	—	(0.11)	
Total, net of tax	1.07	0.10	
Diluted earnings per share adjusted	$ 2.74	$ 2.89	(5)%

GRAINGER

(1) The tax impact of adjustments is calculated based on the income tax rate in each applicable jurisdiction, subject to deductibility limitations and the company's ability to realize the associated tax benefits.

IR Contacts

Laura D. Brown
Senior Vice President, Communications & Investor Relations
Laura.Brown@grainger.com
847.535.0409

Irene Holman
Senior Director, Investor Relations
Irene.Holman@grainger.com
847.535.0809

Michael P. Ferreter
Senior Manager, Investor Relations
Michael.Ferreter@grainger.com
847.535.1439