Demand

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DEMAND—A MANAGEMENT NEWSLETTER FOR WHOLESALE DISTRIBUTION

Demand: Building Momentum

Inside this issue...

Welcome back to *Demand* — a management newsletter for wholesale distribution!

Many thanks to the numerous readers who enthusiastically supported Issue I. We are working hard to continue to exceed your high expectations!

This edition of *Demand* takes us “back to the future” with a case study presenting W.W. Grainger’s electronic commerce initiative and the frequently overlooked success of Grainger.com.

Grainger’s product focus might not apply to your business, but their experience and results are highly relevant to your information technology, marketing and customer service investment and strategy decisions. Enjoy!

Grainger.com — their success offers a rare glimpse into a profitable electronic commerce site

Grainger.com — A Case Study

When W.W. Grainger first established its online presence with Grainger.com in 1995, it saw itself as a pioneer in e-commerce that would “take Internet to the next level.” The company planned to utilize the Internet to grow its share of the fragmented MRO market and to show businesses how technology could reduce procurement costs. Group president Don Bielinski envisioned a time when online commerce would become so pervasive that the company would no longer print paper catalogs. Six years later, Grainger has emerged from its e-commerce initiatives a stronger company with a significantly improved cost structure and customer service function. Despite taking an after-tax charge of $38 million in the second quarter of 2001 related to electronic commerce investments, a rigorous analysis of Grainger’s operating results provides valuable insight into a successful “electronic business” in wholesale distribution. *(cont’d on p. 2)*

International

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Grainger.com — A Case Study (cont'd from p. 1)

Distribution management need only look to the success of Grainger.com, the company's flagship website, to recognize the strong foundation that Grainger has built in B2B e-commerce. Booking revenue of $267 million in 2000, the website was expected to bring in **$400 million in sales in 2001** (2001 actual results not available at press time). Grainger.com sales have a compounded annual growth rate of 166% between 1997 and 2001 and account for almost 10 percent of total sales. According to CEO Richard Keyser, 190,000 Grainger customers are buying online, with 135 of them purchasing products through e-procurement systems. The company has discovered that online purchasing translates to more sales, more often. Grainger claims that its Internet customers make four times as many transactions and purchase from twice as many product categories compared to all Grainger customers. Not only do customers who buy online increase their spending via all channels, they also **spend an average of $240 online versus $130 off-line**, on a per order basis. All of these figures are documented in W.W. Grainger's SEC filings and corporate reports (available at investor.grainger.com).

"Grainger claims that its Internet customers make four times as many transactions and purchase from twice as many product categories..."

What accounts for Grainger.com's success when so many other dot.coms struggled to stay alive during the past two years? According to Gartner, a Connecticut-based business and technology research firm, the most successful dot.com businesses have been those backed by traditional brick-and-mortar storefronts and human customer service. Transitioning to the Internet has allowed the company to leverage its huge inventory and its reputation as one of the leading MRO distributors in North America. While Grainger spun off its other websites into Material Logic, a separate business, it kept Grainger.com as a part of its core operations and undertook aggressive efforts to integrate the site into its existing sales. In addition to sending direct mailings to customers and posting the site address on its general catalog, Grainger employed its territory managers to personally help existing customers register on Grainger.com and set up personal lists that allowed them to order supplies with just a few clicks. The company also required its 5,500 field employees to learn the features of Grainger.com and to serve as "on-the-spot" product experts.

Throughout its transition to the Internet, the company continued to maintain its top-notch quality customer service. One of its customers, for instance, is pleased with the quick follow-ups, claiming that a Grainger rep will reply to his e-mail within two hours. Regional distribution centers, which are notified when customers register on Grainger.com, often send representatives to make introductions to new customers. The company's efforts to expand the website's functionality have also contributed to customer acceptance and satisfaction. Customer profiles, personal lists, multi-criteria search, order tracking via UPS, and two-step ordering via express checkout are just some of the perks customers gain by ordering online. Reflecting Grainger's multi-channel "call, click, or stop by" sales approach, the "will call" option allows customers to order online and pick up purchases at any branch. Customers can also place orders 24 hours a day, a feature that has resulted in an astounding **25% of orders being placed after-hours**. All these features translate to enormous cost savings for customers who buy online. One of Grainger's largest accounts, paper products manufacturer Weyerhaeuser, spends $300,000 in processing costs on purchases through Grainger.com and $2.4 million in processing costs for the remaining third of the goods it buys from other distributors. *(cont'd on pg. 3)*

"All these features translate to enormous cost savings for customers who buy online."

Grainger.com — A Case Study (cont'd from p. 2)

The convenience and cost savings associated with ordering on Grainger's website have encouraged customers to purchase more, **generating almost 11% incremental revenue** for the company. Grainger also benefits from lower processing costs per order, with online orders costing Grainger 4 percent less than orders made over the phone or fax. The company has progressed towards automation of the online ordering process, which will allow it reduce its headcount.

Like other distributors, Grainger has suffered from a weak economy and reduced demand. November 2001 sales were 10 percent below sales for the same period during 2000. Grainger.com sales, however, remain strong, and the company is optimistic about the future. Generating more efficiency and savings for both customers and distributors, Grainger.com clearly represents the future of MRO procurement. The continuing success of Grainger.com reflects the proven financial and operating benefits realized when companies systematically integrate new technology into their businesses. While arguably expanding beyond its core business in initiating e-commerce efforts, Grainger serves as a powerful example for distribution managers looking to reduce costs and improve customer service during a challenging economic environment.

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"Online orders cost Grainger 4 percent less…"

"The first step is a willingness to understand what value you bring to your customers."

Grainger.com Case Study Epilogue Q&A for Distribution Firms:

1. Our company is not a catalog house and we do not cater towards their type of customer. How is this case relevant?

Grainger.com demonstrates how a distributor utilizes their website to reduce order-related costs and provide information (e.g., product information, order status, marketing materials, etc.) to the customer quickly and efficiently. These reduced costs and information-related benefits certainly apply to you — regardless of the technical complexity of your products and your sales process.

2. We are a small distributor that does not have the ability to spend a lot of money marketing our website. How can you expect customers to find us on the web to make something like this worthwhile?

You can achieve this the same way Grainger does. Utilize your salespeople to guide customers to your web site and show them how to place their orders. If your salespeople have comfort that they will be compensated equally for online orders from their accounts, they will play an important role in marketing your website…as will the customers they train.

3. I understand there may be benefits from e-commerce, but don't they come at a large price? How can I be sure this will be a good investment?

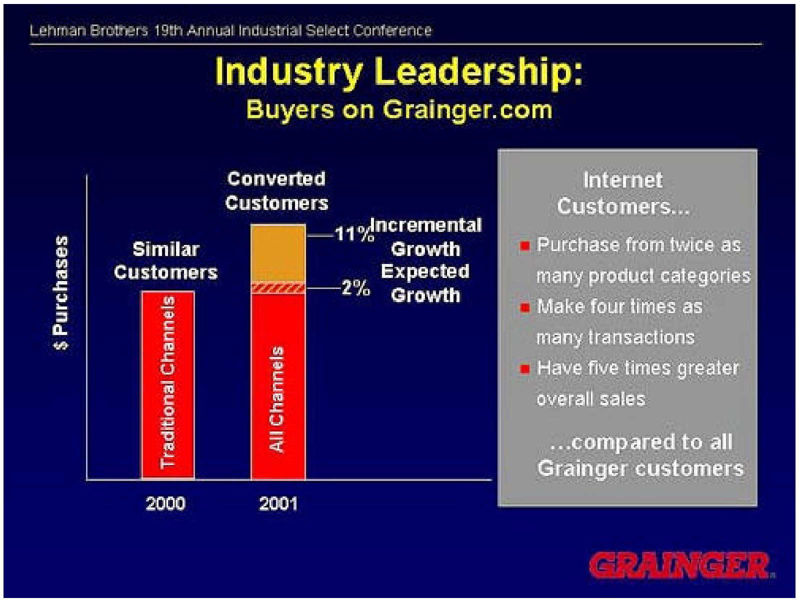
Evaluate your e-commerce project with the rigor of a publicly-traded distribution company (large write-offs notwithstanding). Capture all the sources of value and cost on a spreadsheet and project. Use conservative assumptions and consult with the smartest people you know. The results will surprise you.

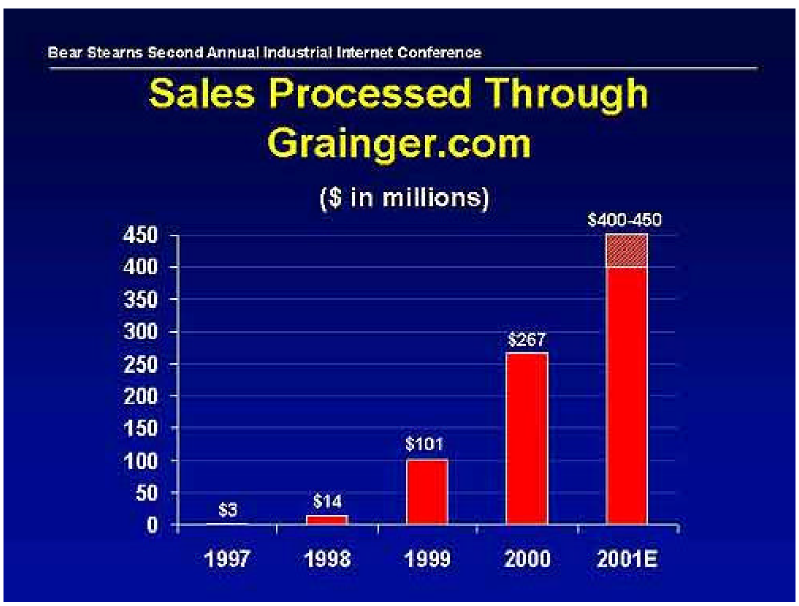
4. Many consultants and technology vendors position e-commerce as a panacea for declining margins and financial performance. How can this be true?

E-commerce investments can reduce operating expenses and improve worker productivity, but there are significant additional investments related to marketing, pricing strategy and service management which can drive improved financial performance in wholesale distribution.

Grainger.com — Buyers and Sales Processed Statistics

Just The Facts — slides from Grainger Investor Relations





Industry Leadership and Sales Processed Through Grainger.com - Incremental Internet Customers are not a myth!

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Know a website that has had similar success to Grainger.com? Email Mark Warnken at mark.warnken@oxinternational.com to share your success story.