W.W. Grainger (GWW)

Company Overview (Sector: Industrials/ Industrial Distribution)

W.W. Grainger distributes more than 1.6 million maintenance, repair, and operations, or MRO, products that are sourced from 5,000 suppliers. The company serves its 3.2 million customers through its online and electronic purchasing platforms, vending machines, catalog distribution, and its network of almost 600 global branches. In recent years, Grainger has invested in its e-commerce capabilities, and the firm is the 11th-largest e-commerce site in North America. W.W. Grainger, Inc. was founded in 1927 and is based in Lake Forest, Illinois.
Investor Relations: **http://invest.grainger.com**

Operations at a Glance

(million USD)	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	TTM
Operating CF	469	530	732	596	746	816	986	960	990	1,003	1,032
Cap Ex	197	181	142	127	197	250	272	387	374	284	310
FCF	**271**	**349**	**590**	**469**	**549**	**566**	**714**	**572**	**616**	**719**	**722**
Cap Ex / OCF	42%	34%	19%	21%	26%	31%	28%	40%	38%	28%	30%
CROIC	12.3%	13.6%	21.9%	17.4%	17.5%	15.8%	18.8%	15.5%	14.5%	17.8%	17.4%

Source: Edgar Online; OldSchoolValue.com

Dividends

W.W. Grainger is a dividend champion with a 46 year dividend raising streak. Considering the quality of this company the current yield is pretty attractive in this market environment even if growth rates are slowing down.

Dividend Yield	Most Recent Raise	3-yr DGR	5-yr DGR	10-yr DGR
3.01%	4.92%	10.4%	13.9%	15.8%

Key dates and the next raise:
Payable September 1; ex-div August 10
The company typically announces dividend increases in April.
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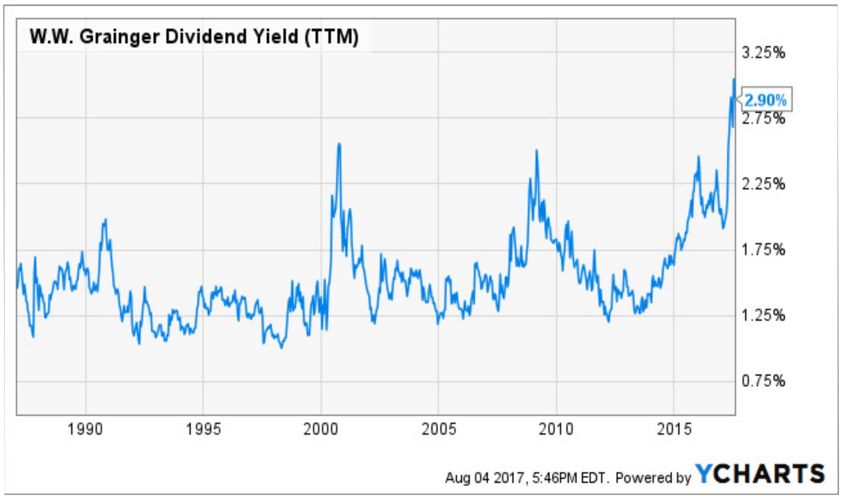
Most recent relevant management comment:
Not too many meaningful comments. Mostly some general messages like the one after the most recent raise: "Consistently increasing the dividend demonstrates our commitment to shareholder value. At the same time, we will continue to manage the business to drive long-term results." (Jim Ryan, Chairman, April 26, 2017)

My take on the dividend profile:
Whenever GWW offered a starting yield above 3% the total returns that followed were extraordinary. Coverage ratios are fine and even with a temporarily (?) slowing growth this stock can be the cornerstone of a portfolio that focuses on reliable dividends.

Valuation

	current	3yr	5yr	10yr	15yr	20yr
P/E	15.5	20.1	19.3	19.9	19.2	19.7
P/OCF	10.6	14.0	15.2	16.1	15.2	14.6
P/FCF	14.8	19.5	23.8	22.6	22.5	21.4
P/EBITDA	7.2	9.6	9.6	10.1	9.9	9.8

Source: S&P Capital IQ, FAST Graphs
Current figures are based on blended ratios, meaning a weighted average of the most recent actual reported earnings plus the closest quarterly forecast earnings. (This is not the same as the often stale TTM data. See the definition of 'blended P/E' in Glossary for more info.)



The historical chart of the trailing twelve month (TTM) dividend yield is backward looking by definition, while dividend yields mentioned in the other sections of this analysis are based on the forward 12-month dividend figures. This explains the difference.

Opinion

Grainger is the prime example of how Amazon can disrupt a business model. Historically, the company issued massive product catalogs to purchasing managers and relied on a steady flow of foot traffic and phone calls to its brick-and-mortar branches. Pricing was not transparent so customers didn't really know what fair prices for the products were. Amazon is looking to change all of this, bringing low-cost inventory from thousands of business supply vendors online, where pricing is transparent and comparison shopping is easy. Grainger reacted by introducing 'web pricing' which stopped the volume decline. The company has scaled down the number of stores and ramped up distribution centers to grow their e-commerce business. They are making a multi-year commitment to beat the competition by lowering prices and maintaining their excellent service record. They believe their operating margin will decline in 2017 and 2018, but begin to grow again in 2019. Last year, Grainger's e-commerce sales increased to 60% of total revenue, and management expects that figure to reach as high as 80% by 2022. Given the company's outstanding relations with its customers and the valuable services it provides it doesn't have to be the cheapest to stay alive. While a lot of retailers are currently fighting declining sales and struggling to get rid of their inventories, the company's top line is actually rising each year, while the inventory stays virtually unchanged. Demand for Grainger's products is still strong. Expect high volatility ahead but GWW is the epitome of the selective contrarian buy for me. If you believe its business will not be totally commoditized by Amazon this is a stock you should definitely own. I foresee an annualized total rate of return between 9-12% in the overly conservative scenarios I examined. (Disclosure: I own GWW stock in my personal portfolio.)

Key Data

Price	Dividend Yield	FCF Yield (TTM)	Shareholder Yield (TTM)	FCF Payout %	EPS payout %	ROIC
170.35$	3.0%	7.1%	10.0%	42.1%	56.4%	12.5%