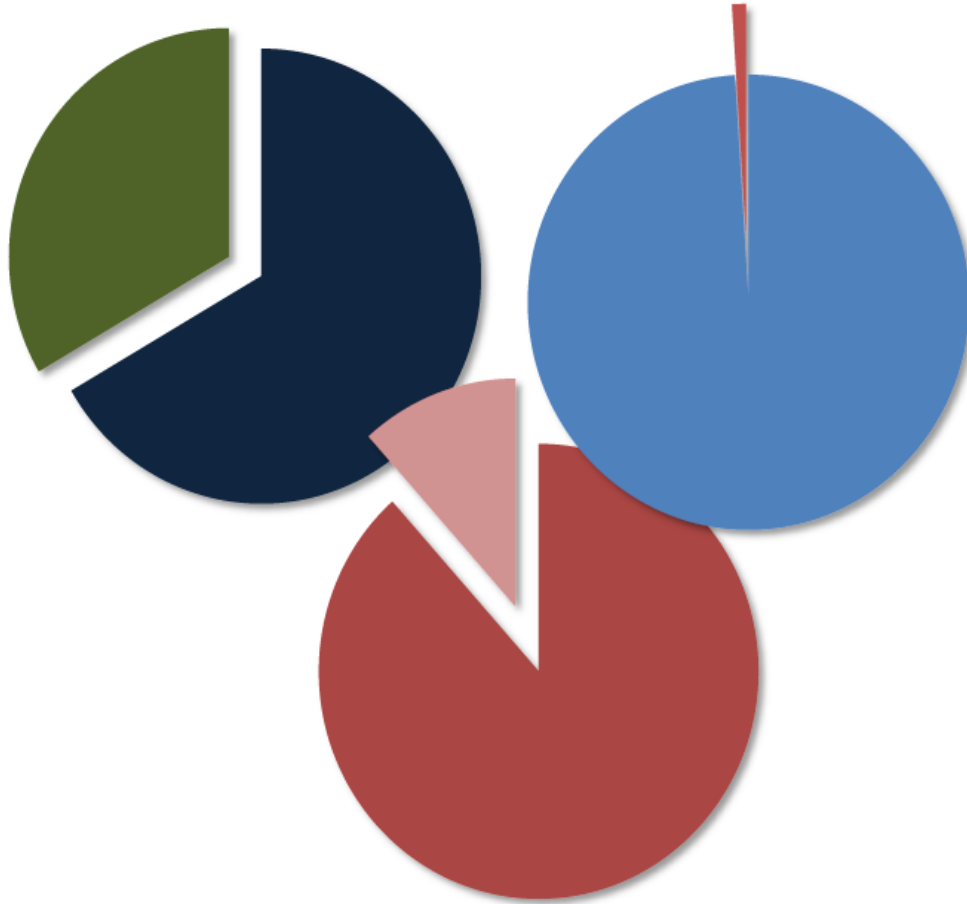


WHY SHOP LOCAL?

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PROCUREMENT MATTERS: THE ECONOMIC IMPACT OF LOCAL SUPPLIERS



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CIVIC ECONOMICS
CREATIVITY · OPPORTUNITY · PROSPERITY

Civic Economics is pleased to present this analysis of the economic impact of office products procurement from a locally-owned supplier compared to procurement from a national supplier with local operations.

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STUDY BACKGROUND

Over the past five years, Civic Economics has developed, applied, and refined a methodology for measuring the true local economic impact of businesses of all sizes. While this expertise has been applied in conventional economic development situations, measuring the impact of a proposed development or policy change, it has also facilitated a unique series of studies comparing the economic impact of local businesses and their chain competitors.

The first application of this methodology evaluated the impact of a publicly subsidized chain retailer of books and music relative to existing local merchants at the same intersection. In that study, known as the Liveable City study of 2002, the local merchants were demonstrated to generate more than three times the local economic activity relative to revenue. A broader study in Chicago, the Andersonville Study of Retail Economics, evaluated comparative impacts across several lines of goods. That study, too, demonstrated that local retailers, restaurants, and service providers generated dramatically greater economic activity than their chain competitors. The firm continues to add to the knowledge base with a comprehensive study underway in Grand Rapids, Michigan which will include retailers, restaurants, and banks.

In each case above, the enhanced economic impact of locally-owned firms was driven by four factors:

1. Labor costs, which directly inject money into the local economy through payments of wages and benefits to local residents;
2. Profits, which remain in the community in proportion to local ownership;
3. Procurement of local goods and services for resale and operations; and
4. Charitable giving, when local firms contribute a greater share of revenue to local causes.

The impact of each factor has varied significantly from one line of goods or services to the next and among individual businesses, but in all cases studied to date, local firms have been found to recirculate substantially larger amounts in all four categories.

Though previous studies focused on retail activities, it became increasingly clear that public and institutional procurement presented a significant area of opportunity if an appropriate case study presented itself. Procurement decisions attract little attention outside of those competing for contracts, but they involve exponentially greater values than the retail trade in goods and services. Large contracts move quantities of goods and services as great as thousands of consumer transactions. However, given the significant differences between contract suppliers

and retail operations, it has been unknown up to now whether local suppliers did, in fact, generate greater local economic impact.

Civic Economics jumped at the opportunity to evaluate the relative economic impacts of Wist Office Products and the contract division of Office Max. The procurement of office supplies and equipment for public and private institutional customers involves vast sums, measured in the hundreds of millions of dollars in Arizona alone. Historically, metropolitan areas have been served by a number of wholesalers of varying sizes and specialties, nearly all of which were locally or regionally based. However, in recent years, large national retailers such as Staples, Office Max, and Office Depot have moved into the contract supply business on a massive scale. In the case of Office Max, these operations are a largely independent business unit called Office Max Contract with a separate distribution network.

In determining the national firm to use for comparison purposes, all three major national retailers with such operations were considered. Office Max Contract was selected for this study because it maintains one of its 52 distribution centers in the Phoenix area. If the comparison were made with a firm with no Arizona warehouse, such as Staples, the differences would be far more pronounced. Indeed, Staples revenue recirculation in Arizona would be comparable to that of any online retailer, limited to delivery services in the local area. In order to provide useful data, then, this study focused instead on the national firm with the greatest local presence.

As a matter of full disclosure, it should be noted that funding for this study was provided by Wist Office Products. However, the scope of work was determined by Civic Economics and included broad requirements for data to be provided by Wist. Moreover, contract terms expressly provide Wist with no right to reject the study or refuse payment based on findings. In an ideal research environment, of course, fully independent funding would support studies of this type. For now, though, Civic Economics works diligently to structure objective and comprehensive analyses.

About Wist

Wist Office Products has been serving Arizona businesses since 1955. As the largest independently owned office supply company in the southwest, Wist offers a solution to reducing the cost of business products while exceeding service expectations. Wist operates its headquarters office and warehouse in Tempe.

Learn more at www.Wist.com.

About Civic Economics

Civic Economics is an economic analysis and strategic planning consultancy with offices in Austin and Chicago. Since establishing the firm in 2002, partners Matt Cunningham and Dan Houston have provided a wide range of services from coast to coast. A particular area of focus has been the economics of regional retail and service provision.

Learn more about the firm at www.CivicEconomics.com.

STUDY GOALS AND METHODOLOGY

The goal of this analysis is to quantify the economic impact of both Wist and Office Max Contract in the state of Arizona as a proportion of revenue. Outcomes will allow procurement officials and policymakers to determine if local preferences are justified.

A Note on Confidentiality

As in all previous studies, Civic Economics promises its private sector clients a great deal of privacy. For all firms, business practices are a matter of great competitive importance. This analysis, for example, required Wist to provide the firm with a great deal of financial information that is closely guarded in business. The worksheet completed by company officials reveals such things as wage rates, profitability, the cost of goods and services, and a range of other, admittedly intrusive items. Due to the sensitivity of such information, data reporting in this document is limited to aggregated values for all categories of revenue and expenses expressed as a share of revenue.

The following section describes in detail the methodology for determining the amount of money Wist Office Products (Wist) and Office Max Contract (Office Max) recirculate in the local economy. As described previously, Office Max does have a physical presence in the Greater Phoenix area as a contract supplier of office supplies. Therefore, the impacts that Office Max have on the local economy would be much greater than that of, for example, Staples which merely delivers products stored, sorted, and administered elsewhere. This is an important distinction to make, as essentially Wist is being compared to the one national chain that keeps the greatest amount of money in the local economy.

Methodology

The methodology to calculate the money kept locally for a contract supplier is very similar to that of a retailer. The four main components used to calculate money kept locally for both local retailers and chains remain the same as our previous reports: labor, profit, procurement, and charity. For each of the categories officials with Wist Office Products completed a survey that was supplemented with a phone interview for further clarification. The text box below describes the process that was undertaken to estimate the results for Office Max. Although our confidentiality agreement with Wist Office Products prevents us from divulging answers to specific questions, the following paragraphs describe the major differences between Wist and Office Max for each category.

Estimating Results for Office Max

Because Office Max is a publicly traded company, they provide a great deal of information both in annual reports to shareholders and required filings with the Securities Exchange Commission. Office Max's Contract division covers most of what would be called a contract supply division. Office Max Contract operated 52 distribution centers during 2006 and provided exact revenues and information used to estimate the amount of income that was spent on labor. However, these values included a number of retail stores that operated outside the United States. To remove those retail activities from the total, Civic Economics assumed foreign Office Max retail outlets operated the same as retail operations in the United States and subtracted these from the Office Max Contract results. This provided a clear picture of the supply operation. This is important due to the fact that a retail operation generally spends far more on labor as a percentage of revenue than a contract supply operation does. This adjustment allowed for an apples-to-apples comparison.

Labor

In previous studies, local businesses were found to spend a larger percentage of revenue on labor and this was no exception. Wist provides greater employment wages and benefits through two channels. The first is that the entire management and administrative operation is employed by Wist and located in their Tempe headquarters. While Office Max may have a small locally based management team, most of the management team is located in Naperville, Illinois at their headquarters. Another major advantage is that the customer service and sales force for Wist are all located in the Phoenix area. Office Max operates six regional call centers throughout the country. An order placed from central Phoenix for delivery to the region may well be serviced by sales and administrative personnel in Columbus, Ohio, who, of course, spend their paychecks outside Arizona. Civic Economics made no attempt to compare wage and benefit rates on an hourly or per employee basis, only total wages and benefits paid locally.

Profit

The profits earned by Wist remain in the Phoenix area. Whether these profits are used by the firm's owners to buy retail goods or real estate, give to preferred causes, or even rest in a savings account, it is a good bet that this money resides somewhere in the community and gets recirculated as it is spent or invested. Office Max, as a publicly held corporation, distributes profits to investors throughout the world. Of course, some of these investors are located in the Phoenix region, but that represents an incalculably small portion of the total profit.

Local Procurement of Services

Wist Office Products also has an advantage over Office Max when it comes to retaining Phoenix-based companies to provide administrative services that Wist does not do internally. These include such expenditures as accounting, legal, and marketing work. Wist also has a budget for marketing in local media outlets. Office Max, as a national chain, needs not contract for such services in each market area. Rather, these services are provided in-house or contracted for through corporate headquarters in the Chicago area.

Charity

Even though this represents a small dollar advantage for Wist Office Products relative to Office Max, they are proud of their contributions to a wide range of local causes during the past year. As with other locally-owned businesses, Wist's owners and managers are invested in the community and are thus more likely to donate to these types of causes in their community.

Preliminary Findings

When taking these factors into account the results are striking. Wist Office Products recirculates 18.96% of their revenue in the local economy whereas Office Max Contract recirculates only 11.56%. Wist, based on these figures, produces 64% greater local economic impact per dollar of revenue than Office Max.

However, these values tell only part of the story, as demonstrated below.

Extended Analysis

In prior retail impact analyses, Civic Economics has identified only one instance in which a local firm made substantial purchases of local goods for resale: a record store in Austin, Texas with a substantial in-store catalog of independent local artists sold on consignment. Wist presents an even more dramatic example of extended local impact through reliance on additional Phoenix area operations in its supply chain.

Local Suppliers of Goods

Of the total amount Wist expends on the procurement of goods for resale, over 10% goes through locally-owned suppliers based in the Phoenix area. To estimate the additional economic impact of this spending, Civic Economics assumed that these local suppliers operate

very much like Wist itself, recirculating the same proportion of revenue locally through labor, profit, procurement, and charity.

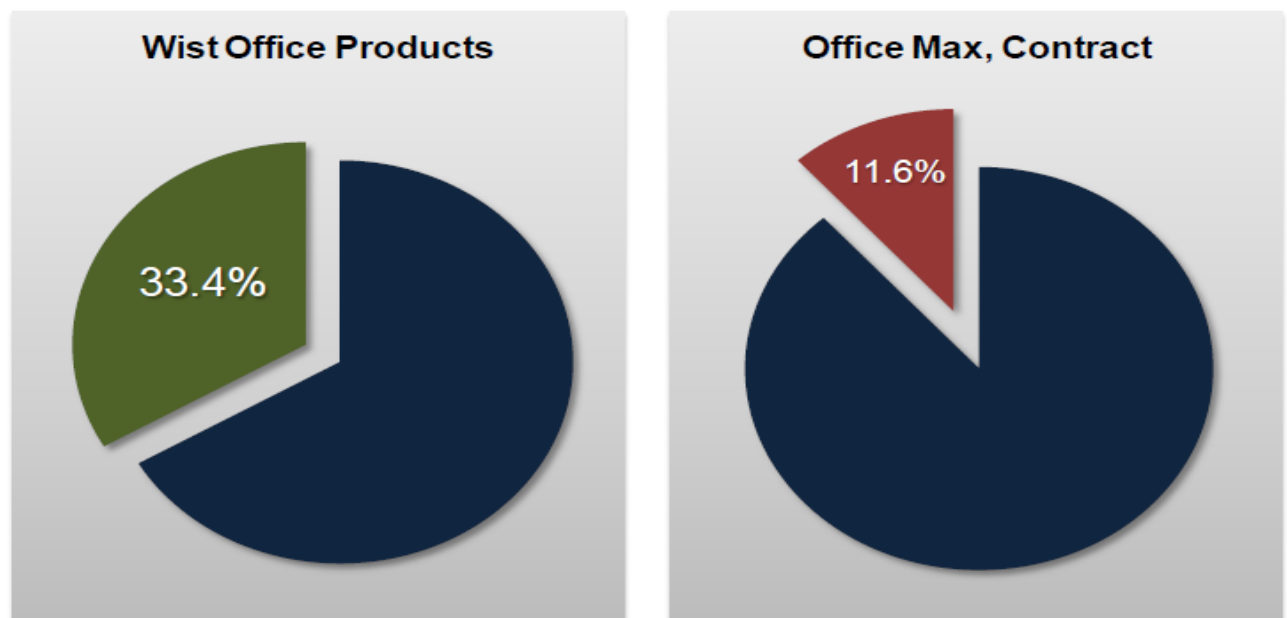
Local Wholesale Distribution Center

Of the total amount Wist spends on the procurement of goods for resale, over half goes through the local distribution center of a national supplier specializing in service to independent office supply firms. To estimate the additional economic impact of this spending, Civic Economics assumed that this distribution center operates very much like Office Max Contract, recirculating the same proportion of revenue locally.

FINDINGS

Incorporating the enhanced economic activity driven by Wist's heavily local supply chain provides a complete and accurate accounting of the local recirculation of money by the two firms: Of total revenue at Wist, 33.4% remains in the local economy. Of total revenue at Office Max Contract, only 11.6% remains.

Percentage of Revenue Recirculated Locally



SOURCE: Civic Economics, Wist Office Products financial survey, Office Max Annual Reports 2005, 2006

IMPLICATIONS

While this study might be used simply to praise Wist and similarly situated local suppliers of other lines of goods or in other communities, Civic Economics believes that it provides a strong economic rationale for reevaluating procurement policies and screening bidders with an eye toward enhancing the local or regional economy at no additional cost to the purchaser.

Procurement Policy

Conventional procurement policy focuses on price and service considerations alone, and the data provided for this analysis indicates that Wist is highly competitive, if not superior, on both fronts. However, these findings suggest that firms and institutions with long-term investments in a given community might benefit from giving additional consideration to the enhanced economic impact of truly local firms.

Private Sector

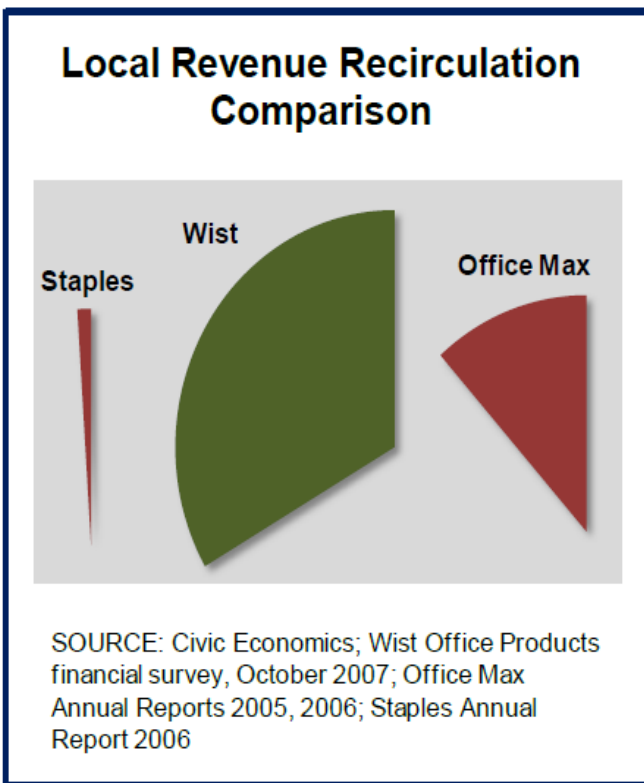
In the private sector, large businesses and institutions are substantial purchasers of office products as well as countless other lines of goods. In all cases, price and service are paramount considerations. In addition, however, those same establishments generally recognize that their long-term health is closely tied to the health of the community in which they operate. This is true of for-profit firms such as banks, manufacturers, retailers, and service providers as well as non-profit institutions such as hospitals and educational institutions.

These private sector customers are in a prime position to benefit from the economic benefit of procuring goods from locally owned firms. Without legal and bureaucratic hurdles to overcome, policy change for the good of the community is easily achieved. Moreover, such a change can be expected to produce goodwill in the community.

Public Sector

Even more than in the private sector, public sector institutions are in a prime position to capture benefits from the enhanced economic activity associated with local suppliers. Additional dollars recirculating in the local economy generate taxable transactions, employ local citizens, and promote the economic vitality of the community. This is true for the State and its institutions, and for counties, municipalities, and other political subdivisions.

For example, assume a single government entity in the State of Arizona purchases \$5 Million worth of widgets each year. If that contract were made through Office Max Contract, only \$580,000 would remain in the state of Arizona at the end of the year. If the same contract were made through Wist or a similarly situated local supplier, an additional \$1 Million would find its way to the people of Arizona. Finally, by contrast, were that contract made through Staples, only nominal amounts would remain in state.



Civic Economics understands that there may be bureaucratic and legal hurdles to overcome in promoting local procurement preferences. Given the vast sums at stake, however, a policy change is clearly justified by the economic benefits that will accrue to the people of Arizona. In the meantime, it is likely that purchasing agents of the state and its subdivisions can, without any policy change whatsoever, begin recognizing the highly competitive local suppliers that exist in numerous lines of goods. Truly open bidding is the simplest first step toward reform and the economic activity it can generate.

Degrees of Locality: True Locals, Paper Locals, and Others

In studying the office products market for this analysis, Civic Economics came to understand that there are, indeed, degrees of locality.

Wist Office Products is a solid example of the *true local* supplier. The company maintains all operations in the Phoenix area, including warehouse, distribution, and administration. All Wist employees reside in the region. All Wist property resides locally. All Wist owners reside in the region. And all Wist charitable contributions are made in the region. At the conclusion of a given transaction, nearly 35% of associated revenue remains in the local economy.

Office Max Contract and its national chain competitors, though, highlight another degree of locality. While Office Max maintains a warehouse and small staff in the region, Staples maintains only a small sales force in the area. Of the revenues that pass through the local distribution center of Office Max, 11.6% will remain in the local economy after a given transaction concludes. The same contract through Staples yields only the most nominal local economic activity associated with some portion of one day for a delivery driver and vehicle.

However, recent years have seen an increase in the *paper local* supplier. These firms will have a local owner and a local address and may even qualify under one or more disadvantaged business programs for public procurement. The false local, though, maintains no warehouse or distribution operation and only the most minimal administrative organization. In reality, these firms are merely agents for national suppliers. Transactions originated through these firms are administered and satisfied by the larger, non-local supplier with only a commission or other fee paid to the local shell. Fortunately, procurement officials will be able to identify these false local suppliers with even a most cursory review.

CONCLUSION

Researchers, including Civic Economics, have in recent years developed a better understanding of the economics of local retail and service provision. The premise that locally-owned and operated businesses generate greater local economic activity than their chain counterparts has become widely understood and accepted. In communities across the nation and abroad, public policy has adapted to this reality through a variety of planning and zoning tools.

Even more widespread is the consumer-driven “buy local” movement. In the Phoenix area, Local First Arizona is among the leaders in this movement, with hundreds of participating businesses and supportive individuals uniting behind a marketing campaign to allow concerned citizens to support those firms that make Phoenix special.

Despite the widespread consensus that local retail firms promote strong local economies, there has been little research into the economics of local contract procurement even as national firms have entered every market in America. Prior to this study, neither Civic Economics nor any other research organization could put a dollar value to the impact of traditional local suppliers like Wist.

Now, with the release of this study, the answer is clear. Local suppliers generate dramatically greater economic activity than their chain competitors. In the case at hand, using the most locally invested of the national chain suppliers, one with a sizeable physical presence in the Phoenix area, the local firm generates nearly three times the economic impact.

Civic Economics thanks Wist for their willingness to share sensitive and proprietary business data in furtherance of this research, and looks forward to joining the conversation this study will promote in the coming months and years.

For further information about this study and to download a copy this report and charts, please visit:

www.CivicEconomics.com/procurement