Starbucks

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Abstract

Despite the financial impact of the recession, Starbucks used leaner operations, improved customer service and discipline to recover. In 2010, Starbucks concentrated on cutting expenditures and improving resource allocation. Such efforts resulted in significant savings and helped recover Starbucks’ financial health. Fiscal years 2011 and 2012 brought global expansion, innovated products, and a customer loyalty program. Starbucks began realizing the benefits of its leaner model. Since 2010, revenues and cash flow increased drastically; earnings-per-share have seen a steady rise. Financial analysis reveals Starbucks’ high liquidity and profitability measures. However, the corporation’s minimal debt and A- credit rating demonstrates its need to re-evaluate capital structure and leverage some debt. Shareholders do not seem too concern with Starbucks capital structure, however, as their stocks have nearly doubled in the last year. Despite a subtle warning for such hasty expansion, experts commend Starbucks on their stability through the sluggish economy and such rapid growth in the last five years.

Starbucks

Everyone knew the economy had hit rock bottom in 2009 when doors started closing. Supply for the beloved morning staple that, not just Americans but, caffeine-addicted consumers worldwide could agree over was suddenly not available at every corner they could turn. Starbucks Corporation had closed 6.5% of stores – a catastrophe worthy of worldwide news and with no hope of a government bailout. Nope, Starbucks knew the company would have to dig out of the hole the old fashion way: improved customer service, leaner operations, leadership, and innovation. Plus, the return of Howard Schultz, prior owner of Starbucks, as CEO could not hurt. So from 2009 to 2010 Starbucks proved that, even in a down economy, with a little discipline a company could exceed financial expectations and have the most profitable year to date.

1. **Financial Statements**

In 2010, Starbucks Corporation had successfully lowered capital expenditures by more than half of previous years. Leaner spending and adjustments in resource utilization gave Starbucks a cost savings of $600M while operating cash flow increased by nearly 25%. Starbucks’ earnings-per-share had increased 60% of that of 2009 and store sales growth rose from -6% to 7% (a 13% increase). Starbucks netted its highest revenue to date of $10.7 billion. Additionally, this year saw many changes in international markets, products, and customer appreciation. Starbucks concentrated on expansion in China where they opened 29 new stores. New products, such as the Verismo coffee machine, were offered contributing to sales growth. And faithful customers were offered a customer loyalty card (Starbucks, 2011).

The following two years only brought more success. The company focused on ethical sourcing and fair-trade products as social conscience is at the core of the Starbucks mission. Operating income and margin both rose over previous years. Operating cash flow also increased in 2011 and 2012 to $1,612 and $1,750 respectively. By 2010, Starbucks’ earnings per share increased 10% to $1.79 and the company hit a record-breaking net revenue of $13.3 billion. Table 1.1 below highlights Starbucks growth over the last three years (Starbucks, 2013).

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| **Table 1.1: Financial Highlights** | | | | |
|  | 2009 | 2010 | 2011 | 2012 |
| Revenue (billions) | $9.8 | $10.7 | $11.7 | $13.3 |
| Operating Income (millions) | $562 | $1,419 | $1,728 | $1,997 |
| Operating Cash flow (millions) | $1,389 | $1,705 | $1,612 | $1,750 |
| Expenditures (millions) | $446 | $441 | $532 | $856 |
| Operating Margin | 5.7% | 13.3% | 14.8% | 15% |
| Sales Growth | -6% | 7% | 8% | 7% |
| EPS | $0.52 | $1.24 | $1.62 | $1.79 |

1. **Financial Ratios**

Today, Starbucks Corporation’s financial health is on track and made a successful recovery from the recession. Leaner operations proved beneficial to both liquidity and profitability. Table 2.1 demonstrates the company’s ability to utilize cash (and equivalents) to pay off its short-term debt. The current ratio shows how Starbucks can nearly double its liabilities with assets. However, in a more stringent measurement, the cash ratio demonstrates how Starbucks has roughly 55% of cash to cover its liabilities. Either way, Starbucks has positioned itself well to incur more liabilities if needed (Starbucks, 2013).

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| **Table 2.1: Liquidity Measurements** | | |
|  | 2011 | 2012 |
| Current Ratio | 1.83 | 1.9 |
| Quick Ratio | 1.17 | 1.14 |
| Cash Ratio | .55 | .54 |

Table 2.2 represents the profitability of the company. An increasing profit margin is a direct result of the new processes Starbucks put into place after 2009. Its focus on lowering expenditures drove the profit margin to 14.8%. Both the return-on-assets (ROA) and the return-on-equity (ROE) demonstrate how well the company is using assets and equity to perform on their investments. Experts suggest that ROE ratios in the 15-20% range represent attractive investments. Starbucks’ nearly 34% ROE in 2012 would certainly prove worthy (Starbucks, 2013).

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| **Table 2.2: Profitability Indicators** | | |
|  | 2011 | 2012 |
| Net Profit Margin | 13.3% | 14.8% |
| Return on Assets | 19.28% | 21.03% |
| Return on Equity | 32.4% | 33.8% |

Starbucks Corporation current debt standings are demonstrated in Table 2.3. The debt ratio is a measurement of how dependent Starbucks is on borrowed funds. While this appears high, operational liabilities (those day-to-day accounts payable) included in “total liabilities” may offset a true account for the company’s reliance on debt. Such accrued liabilities for Starbucks include occupancy costs, employee compensation, taxes, and dividends payable and make up 37% of total liabilities in 2012 and 32% in 2011. Like the debt ratio, Starbucks high debt-equity ratio may also be dramatized by operational liabilities (Starbucks, 2013).

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| **Table 2.3: Debt Ratios** | | |
|  | 2011 | 2012 |
| Debt Ratio\* | 40.4% | 37.8% |
| Debt-Equity Ratio\* | 67.8% | 60.8% |
| \*Accrued Liabilities | 32% | 37% |
| \*accrued liabilities as a percentage of total liabilities | | |

Efficiency ratios measure how well companies manage assets and inventory. Table 2.4 represents Starbucks’ asset turn over and inventory turnover. In 2011, Starbucks each dollar of assets produced $1.83 in sales; 2012 brought in slightly less with $1.81 in sales. It is, however, Starbucks’ inventory turnover that may bring unexpected results in the food-and-beverage industry. The corporation’s inventory turnover ratio was 21.54 and 13.77 in 2011 and 2012 respectively. For the food and beverage industry, these ratios may be on the higher end.

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| **Table 2.4: Efficiency Ratios** | | |
|  | 2011 | 2012 |
| Asset Turn Over | 1.83 | 1.81 |
| Inventory Turnover | 21.54 | 13.77 |

1. **Trend Analysis**

A central aspect of Starbucks’ business model relates to ethical sourcing, fair trade agreements, and fair labor of suppliers. Thus, when evaluating the trend analysis of the company, it is important to also weigh that such financial performance measures were accomplished while maintaining this social conscience. Since going public at $21 per share in 1992, Starbucks has only had minor fluctuations in stock price. This remained true until November of 2008 when stock prices plummeted to less than $9 per stock. The 2009 year showed only minimum improvements and reflected the struggle of the company. However, since 2011, Starbucks Corporation’s stock price has seen a steady increase reaching as high as $80 per share this week, nearly double the price of this time last year. Quarterly dividends, amongst other operational changes, may be a contributing factor to the stock’s growth. (Yahoo Finance, 2013) Figure 3.1 depicts the change in (closing) stock price from June 2008 until Sept 2013.

Figure 3.1

Starbucks’ financial statements keep getting shinier. The company continues to grow, earnings increase, and it has cash flow coming out of its ears. So, when Standard and Poor’s gave Starbucks Corporation an A- credit rating, it should make other corporations in the industry envious. However, Starbucks understands the meaning of its current position and its direct comparison to the positive improvements of their financials. Chief Financial Officer, Troy Alstead (2013), confesses, ““We’ve long recognized that there’s opportunity with an extremely conservative balance sheet to bring a bit of debt on.” Of the eleven other comparable companies in the industry (per the S&P 500), Starbucks has the lowest amount of debt. (Farzad, 2013)With room to leverage, Starbucks may have opportunities for growth in the near future. Amongst all of Starbucks’ changes, assessing capital structure may be the next to come.

1. **Other Relevant Assessments**

After experiencing financial loss in 2009, Starbucks began seriously analyzing its long-term investment decisions. While the U.S. was struggling, the company saw attractive investments in other countries, specifically in China. At the beginning of the year, there were over 3,000 Starbucks in China with another 600 planned throughout 2013. Today, Starbucks stores are located in 62 countries with plans for rapid global expansion in the coming years (Loeb, 2013) (maybe it will be structured with a little debt!)

In 2010, Howard Schultz announced goals for a new Starbucks experience improving on customer service and rewarding faithful consumers. First, the Starbucks Reward Card was introduced that earns increasingly higher level of benefits. The card offers birthday perks, discounts, free refills, and free food. In 2011, the Starbucks Reward Card was owned by over 3.6 million coffee drinkers. Additionally, the company is answering the call of over 40% of thirsty pallets by offering a new, lighter blend of coffee: Blonde roast. Finally, Starbucks Corporation introduced an elite coffee machine for the consumer’s home: the Verismo System. In 2012, Starbucks shipped almost 500 million single-cup packs to loyal consumers. For companies that might want to cut corners on customer service when finances are struggling might want to review the business model of Starbucks. The direct correlation is reflected in increasing sales and revenue growth.

1. **Expert Opinions**

In a recent article in *Money Magazine*, Taylor Tepper reviews the current financial standings of Starbucks in relation to competitors Dunkin’ and McDonalds. Tepper commends Starbucks for rebelling against a slow economy and recovering from it struggles in 2009. He also compares Starbucks’ annual earnings growth rate of 18.1% to that of Dunkin’ Brands with 16.1% and McDonald’s with 9.5%. In his own words, Tepper explains its strategy, “Starbucks is the world's only premium coffee superpower, and its basic business--selling expensive cups of joe and even pricier espresso drinks through nearly 18,900 stores worldwide--is as robust as its earthy Sumatra roast.” And Starbucks global expansion has just begun. Tepper worries that, after failed ice cream and even an attempted music label, Starbucks may be trying to grow too fast. But, at any rate, Starbucks has the cash, $1.7 billion to be exact, to move quickly (Tepper, 2013).

Experts suggest that Starbucks Corporation has two revenue streams on which to focus. The first is product diversification in the United States. Recently Starbucks acquired San Franciscan bakery, La Boulange, to offer a new line of pastries. The $100 million investment offers significant confidence of Starbucks management. Currently, only 33% of Starbucks orders consist of food products; thus the company hopes for growth. The second earnings stream is in Starbucks’ global expansion. Over the next two years, Starbucks sees a massive opportunity for growth in China, Asian-Pacific regions, and in the Americas (Seeking Alpha, 2013).

In a 2012 article on the *Daily Finance*, Rick Munarriz highlights Starbucks latest endeavors. As previously mentioned, Starbucks’ global expansion will be a massive financial feat. However, this expert outlines the benefits of Starbucks’ newest brand: Teavana. For tea lovers everywhere, or at least near the 300-planned openings, consumers will soon be able to purchase premium tea drinks in an upscale store concept. Munarriz (2012) confirms the common expert opinion when he states, “There's a lot on Starbucks' plate, but it's exactly where the company wants to be. It's hard to imagine that this is the same company that was closing down stores just a couple of years ago. But some brews just take time” (Munarriz, 2012).

**Conclusion**

Recovering from a sluggish economy is a financial endeavor; many businesses in the food and beverage industry failed to survive. Starbucks Corporation, however, took an old-fashion approach. Cutting out expenditures, conserving resources, and improving customer service all proved beneficial to the company. Today, revenues, earnings-per-share, and cash flow are at record highs. Shareholders are satisfied as their investments have nearly doubled in the last year. Plus, dividends are paid quarterly keeping them from wandering off. With global expansion, new brands, and innovative products released, experts think Starbucks might have its plate full. However, Starbucks has room to leverage and money to grow.

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