



## Starbucks Corporation: Competing in a Global Market



Starbucks Corporation is a Seattle, Washington-based coffee company. It buys, roasts, and sells whole bean specialty coffees and coffee drinks through an international chain of retail outlets. From its beginnings as a seller of packaged, premium specialty coffees, Starbucks has evolved into a firm known for its coffeehouses, where people can purchase beverages and food items as well as packaged whole bean and ground coffee. Starbucks is credited with changing the way Americans—and people around the world—view and consume coffee, and its success has attracted global attention.

Starbucks has consistently been one of the fastest growing companies in the United States. Over a 10-year period starting in 1992, the company's net revenues increased at a compounded annual growth rate of 20 percent, to \$3.3 billion in fiscal 2002. Net earnings have grown at an annual compounded growth rate of 30 percent to \$218 million in fiscal 2002, which is the highest reported net earnings figure in the company's history (see Exhibit 1). As *BusinessWeek* tells it:

On Wall Street, Starbucks is the last great growth story. Its stock, including four splits, has soared more than 2,200 percent over the past decade, surpassing Wal-Mart, General Electric, PepsiCo, Coca-Cola, Microsoft, and IBM in total return. Now at \$21 [September 2002], it is hovering near its all-time high of \$23 in July [2002], before the overall market drop.<sup>1</sup>

To continue this rapid pace of growth, the firm's senior executives are looking to expand internationally. Specifically, they are interested in further expansion in Europe (including the Middle East), Asia Pacific (including Australia and New Zealand), and Latin America. Expanding in these three continents represents both a challenge and an opportunity to Starbucks. While the opportunity of increased revenues from further expansion is readily apparent to the company's top management, what is not clear is how to deal with growing "antiglobalization" sentiment around the world.

This case looks at issues that are arising as Starbucks seeks to dominate specialty coffee markets around the world and explores what changes in strategy might be required.

This case was written by Professors Suresh Kotha and Debra Glassman, both from the University of Washington, Business School, as the basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation. Some of the facts provided in the case have been disguised to protect confidentiality. The case was originally developed for the 2003 Global Business Challenge case competition at the University of Washington Business School. The authors thank the Global Business Center, the University of Washington, and the Starbucks Corp. for their generous support in preparing the case. Copyright © Kotha & Glassman 2003. All rights reserved.

### BACKGROUND

In 1971, three Seattle entrepreneurs—Jerry Baldwin, Zev Siegl, and Gordon Bowker—started selling whole-bean coffee in Seattle's Pike Place Market. They named their store Starbucks, after the first mate in *Moby Dick*.<sup>2</sup> By 1982, the business had grown to five stores, a small roasting facility, and a wholesale business selling coffee to local restaurants. At the same time, Howard Schultz had been working as VP of U.S. operations for Hammarplast, a Swedish housewares company in New York, marketing coffeemakers to a number of retailers, including Starbucks. Through selling to Starbucks, Schultz was introduced to the three founders, who then recruited him to bring marketing savvy to their company. Schultz, 29 and recently married, was eager to leave New York. He joined Starbucks as manager of retail sales and marketing.

A year later, Schultz visited Italy for the first time on a buying trip. He noticed that coffee is an integral part of the culture in Italy; Italians start their day at an espresso bar and later in the day return with their friends. There are 200,000 coffee bars in Italy, and about 1,500 in Milan alone. Schultz believed that, given the chance, Americans would pay good money for a premium cup of coffee and a stylish place to enjoy it. Enthusiastic about his idea, Schultz returned to tell Starbucks' owners of his plan for a national chain of cafes styled on the Italian coffee bar. The owners, however, did not want to be in the restaurant business. Undaunted, Schultz wrote a business plan and began looking for investors. By April 1985 he had opened his first coffee bar, *Il Giornale* (named after the Italian newspaper), where he served Starbucks coffee. Following *Il Giornale's* immediate success, he expanded to three stores. In 1987, the owners of Starbucks agreed to sell the firm to Schultz for \$4 million. The *Il Giornale* coffee bars took on the name of Starbucks.

Convinced that Starbucks would one day be in every neighborhood in America, Schultz focused on growth. At first, the company's losses almost doubled (to \$1.2 million in fiscal 1990), as overhead and operating expenses ballooned with the expansion. Starbucks lost money for three years running, and the stress was hard on Schultz, but he stuck to his conviction not to "sacrifice long-term integrity and values for short-term profit."<sup>3</sup> In 1991 sales shot up 84 percent, and the company turned profitable. In 1992 Schultz took the firm public at \$17 a share.

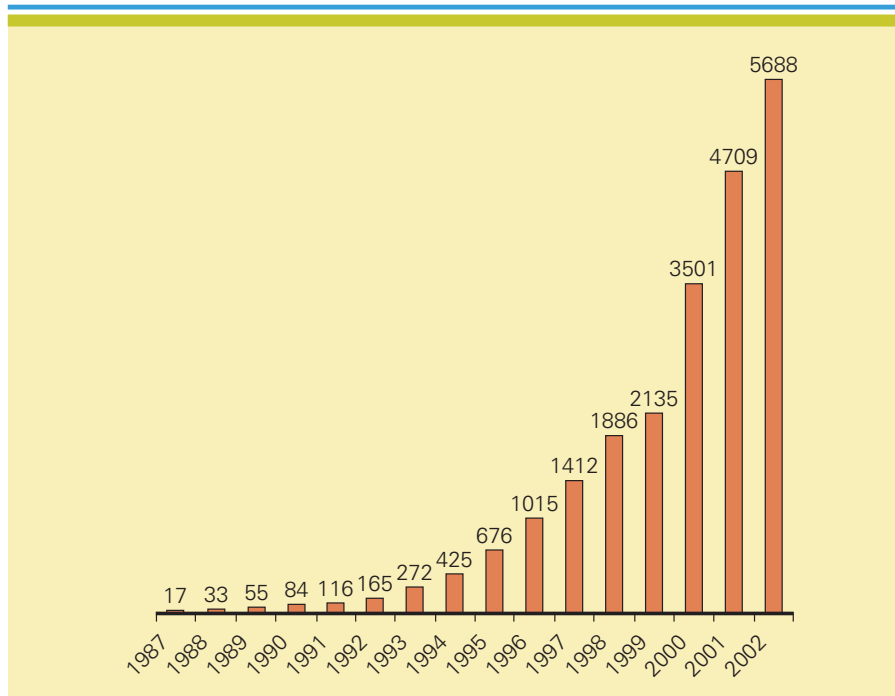
Believing that market share and name recognition are critical to the company's success, Schultz continued to expand the business aggressively. Schultz observes,

As of and for the fiscal year ended (1)	September 29, 2002 (52 Weeks)	September 30, 2001 (52 Weeks)	October 1, 2000 (52 Weeks)	October 3, 1999 (53 Weeks)	September 27, 1998 (52 Weeks)
<b>Results of Operations Data</b>					
<b>Net revenues:</b>					
Retail	\$ 2,792,904	\$ 2,229,594	\$ 1,823,607	\$ 1,423,389	\$ 1,102,574
Specialty	496,004	419,386	354,007	263,439	206,128
Total net revenues	3,288,908	2,648,980	2,177,614	1,686,828	1,308,702
Merger expenses (2)	—	—	—	—	8,930
Operating income	318,725	281,094	212,252	156,711	109,216
Internet-related investment losses	—	2,940	58,792	—	—
Gain on sale of investment	13,361	—	—	—	—
Net earnings	\$ 215,073	\$ 181,210	\$ 94,564	\$ 101,693	\$ 68,372
Net earnings per common share - diluted	\$ 0.54	\$ 0.46	\$ 0.24	\$ 0.27	\$ 0.19
<b>Balance Sheet Data</b>					
Working capital	\$ 310,048	\$ 148,661	\$ 146,568	\$ 135,303	\$ 157,805
Total assets	2,292,736	1,846,519	1,491,546	1,252,514	992,755
Long-term debt (including current portion)	5,786	6,483	7,168	7,691	1,803
Shareholders' equity	1,726,638	1,375,927	1,148,399	961,013	794,297
<b>Store Operating Data</b>					
Percentage change in comparable store sales (3)					
North America	7%	5%	9%	6%	5%
International	(3)%	2%	23%	20%	28%
Consolidated	6%	5%	9%	6%	5%
Systemwide retail store sales (4)	\$ 3,796,000	\$ 2,950,000	\$ 2,250,000	\$ 1,633,000	\$ 1,190,000
Systemwide stores opened during the year: (5)	1,177	1,208	1,003	612	474
Systemwide stores open at year-end:					
Continental North America					
Company-operated stores	3,496	2,971	2,446	2,038	1,622
Licensed stores	1,078	809	530	179	133
International					
Company-operated stores	384	295	173	97	66
Licensed stores	928	634	352	184	65
Total	5,886	4,709	3,501	2,498	1,886

## EXHIBIT 1

### Selected Financial and Store Data (In thousands, except earnings per share and store operating data)

- (1) The company's fiscal year ends on the Sunday closest to September 30. All fiscal years presented include 52 weeks, except fiscal 1999, which includes 53 weeks.
- (2) Merger expenses relate to the business combination with Seattle Coffee Holdings Limited.
- (3) Includes only company-operated stores open 13 months or longer.
- (4) Systemwide retail store sales include sales at company-operated and licensed stores and are believed by management to measure global penetration of Starbucks retail stores.
- (5) Systemwide store openings are reported net of closures.



## EXHIBIT 2

Starbucks Store  
Locations (As of  
November 2002)

Source: Starbucks Corporation

“There is no secret sauce here. Anyone can do it.” From the beginning, Schultz has professed a strict growth policy. Although many other coffeehouses or espresso bars are franchised, Starbucks owns all of its North American stores outright, with the exception of license agreements in airports. Further, rather than trying to capture all the potential markets as soon as possible, Starbucks goes into a geographic market and tries to completely dominate it before setting its sights on further expansion. Using this strategy, Starbucks has grown from 17 coffee shops in 1987 to 5,688 outlets in 28 countries by the end of fiscal 2002 (see **Exhibit 2**). It also employed over 60,000 individuals, including approximately 50,000 in retail stores at the end of 2002.

Starbucks Corporation is organized into two business units that correspond to the company’s operating segments: North American and International. In 1995, Starbucks Coffee International, a wholly owned subsidiary of Starbucks Coffee Company, was set up to build Starbucks’ businesses outside North America, including opening company-owned, licensed, and joint-venture-based retail stores worldwide.

A recent article in *BusinessWeek* notes:

Starbucks also has a well-seasoned management team. Schultz, 49, stepped down as chief executive in 2000 to become chairman and chief global strategist. Orin Smith, 60, the company’s numbers-cruncher, is now

CEO and in charge of day-to-day operations. The head of North American operations is Howard Behar, 57, a retailing expert who returned last September, two years after retiring. The management trio is known as H<sub>2</sub>O, for Howard, Howard, and Orin.<sup>4</sup>

**Exhibit 3** provides a partial list of Starbucks top management, and **Appendix A** (page 701) provides a timeline and history of Starbucks.

## THE STARBUCKS MODEL

Howard Schultz’s goal is to: “Establish Starbucks as the premier purveyor of the finest coffee in the world while maintaining uncompromising principles as we grow.” The company’s 25-year goal is to “become an enduring, great company with the most recognized and respected brand in the world, known for inspiring and nurturing the human spirit.” The company’s mission statement articulates several guiding principles to measure the appropriateness of the firm’s decisions (see **Exhibit 4** on page 704). In describing Starbucks’ unique approach to competition, *Fortune* notes:

The strategy is simple: Blanket an area completely, even if the stores cannibalize one another’s business. A new store will often capture about 30 percent of the sales of a nearby Starbucks, but the company considers that a good thing: The Starbucks-everywhere approach cuts

### EXHIBIT 3

#### Starbucks Top Management Team

Source: Starbucks Corporation,  
November 2002.

**Howard Schultz** is the founder of the company and has been chairman of the board since its inception in 1985. Mr. Schultz served as chief executive officer from 1985 until June 2000, when he transitioned into the role of chief global strategist. From 1985 to June 1994, Mr. Schultz was also the company's president. From September 1982 to December 1985, Mr. Schultz was the director of Retail Operations and Marketing for Starbucks Coffee Company, a predecessor to the company; and from January 1986 to July 1987, he was the chairman of the board, chief executive officer, and president of Il Giornale Coffee Company, a predecessor to the company.

**Orin C. Smith** joined Starbucks Corporation in 1990 and has served as president and chief executive officer of the company since June 2000. From June 1994 to June 2000, Mr. Smith served as the company's president and chief operating officer. Prior to June 1994, Mr. Smith served as the company's vice president and chief financial officer and later, as its executive vice president and chief financial officer.

**Peter Maslen** joined Starbucks in August 1999 as president, Starbucks Coffee International, Inc. Prior to joining Starbucks, Mr. Maslen served in various executive positions within Asia Pacific and Europe with Mars Inc., PepsiCo, Inc., and Tricon Global Restaurants. From 1992 to 1999, as senior vice president with Tricon, he served as president of its German, Swiss, Austrian, and Central Europe divisions.

**Jim Donald** joined Starbucks in November 2002 as president, Starbucks North America. He is responsible for managing Starbucks North America company-owned and licensed stores, business alliances (food service, grocery, club channels of distribution, joint venture partnerships with Pepsi-Cola Company and Dreyer's Grand Ice Cream) in the United States and Canada, store development, retail systems, administration, and retail partner resources. Mr. Donald brings 32 years of experience in the retail and food industry. Prior to joining Starbucks, he was chairman, president, and chief executive officer at Pathmark Stores, Inc., since 1996. In addition, he has held several senior leadership positions at top-tier retail companies including Safeway, Wal-Mart, and Albertson's.

**Michael Casey** joined Starbucks in August 1995 as senior vice president and chief financial officer, and was promoted to executive vice president, chief financial officer, and chief administrative officer in September 1997. Prior to joining Starbucks, Mr. Casey served as executive vice president and chief financial officer of Family Restaurants, Inc., from its inception in 1986. During his tenure there, he also served as a director from 1986 to 1993, and as president and chief executive officer of its El Torito Restaurants, Inc., subsidiary from 1988 to 1993.

**Eduardo R. (Ted) Garcia** joined Starbucks in April 1995 as senior vice president, Supply Chain Operations, and was promoted to executive vice president, Supply Chain and Coffee Operations, in September 1997. From May 1993 to April 1995, Mr. Garcia was an executive for Gemini Consulting. From January 1990 until May 1993, he was the vice president of Operations Strategy for Grand Metropolitan PLC, Food Sector.

down on delivery and management costs, shortens customer lines at individual stores, and increases foot traffic for all the stores in an area. Last week 20 million people bought a cup of coffee at a Starbucks. A typical customer stops by 18 times a month; no American retailer has a higher frequency of customer visits. Sales have climbed an average of 20 percent a year since the company went public. Even in a down economy, when other retailers have taken a beating, Starbucks store traffic has risen between 6 percent and 8 percent a year. Perhaps even more notable is the fact that Starbucks has managed to generate those kinds of numbers with virtually no marketing, spending just 1 percent of its

annual revenues on advertising. (Retailers usually spend 10 percent or so of revenues on ads.)<sup>5</sup>

*BusinessWeek* adds:

Clustering stores increases total revenue and market share, [CEO] Orin Smith argues, even when individual stores poach on each other's sales. The strategy works, he says, because of Starbucks' size. It is large enough to absorb losses at existing stores as new ones open up, and soon overall sales grow beyond what they would have with just one store. Meanwhile, it's cheaper to deliver to and manage stores located close together. And by clustering, Starbucks can quickly dominate a local market.<sup>6</sup>

## APPENDIX A

### Starbucks Timeline and History

#### 1971

Starbucks opens its first location in Seattle's Pike Place Market.

#### 1982

Howard Schultz joins Starbucks as director of retail operations and marketing. Starbucks begins providing coffee to fine restaurants and espresso bars.

#### 1983

Schultz travels to Italy, where he's impressed with the popularity of espresso bars in Milan. He sees the potential in Seattle to develop a similar coffee bar culture.

#### 1984

Schultz convinces the founders of Starbucks to test the coffee bar concept in a new location in downtown Seattle. This successful experiment is the genesis for a company that Schultz founds in 1985.

#### 1985

Schultz founds Il Giornale, offering brewed coffee and espresso beverages made from Starbucks coffee beans.

#### 1987

With the backing of local investors, Il Giornale acquires Starbucks assets and changes its name to Starbucks Corporation.

Opens in Chicago and Vancouver, B.C.

Starbucks location total = 17

#### 1988

Starbucks introduces mail-order catalog with service to all 50 states.

Starbucks location total = 33

#### 1989

Opens in Portland, Oregon.

Starbucks location total = 55

#### 1990

Starbucks expands headquarters in Seattle and builds a new roasting plant.

Starbucks location total = 84

#### 1991

Establishes a relationship with CARE, the international relief and development organization, and introduces the CARE coffee sampler.

Becomes the first U.S. privately owned company to offer a stock option program that includes part-time employees.

Opens first licensed airport location with HMS Host at Sea-Tac International Airport.

Opens in Los Angeles.

Starbucks location total = 116

#### 1992

Completes initial public offering with common stock being traded on the Nasdaq National Market under the trading symbol "SBUX."

Opens in San Francisco; San Diego; Orange County, California; and Denver.

Starbucks location total = 165

#### 1993

Begins Barnes & Noble, Inc., relationship.

Opens in Washington, D.C.

Starbucks location total = 272

*Continued*

## APPENDIX A

### Starbucks Timeline and History—*continued*

#### 1994

Awarded ITT/Sheraton (now Starwood Hotel) account.  
Opens in Minneapolis; Boston; New York; Atlanta; Dallas; and Houston.  
Starbucks location total = 425

#### 1995

Based on an extremely popular in-house music program, Starbucks begins selling compact discs.  
Awarded United Airlines account.  
Begins serving Frappuccino® blended beverages, a line of low-fat, creamy, iced coffee beverages.  
Forms alliance with Canadian bookstore Chapters Inc.  
Starbucks Coffee International forms joint venture with SAZABY Inc., to develop Starbucks coffeehouses in Japan.  
Opens in Philadelphia; Pittsburgh; Las Vegas; Cincinnati; Baltimore; San Antonio; and Austin, Texas.  
Starbucks location total = 676

#### 1996

Starbucks Coffee International opens locations in Japan, Hawaii, and Singapore.  
Awarded Westin (now Starwood Hotel) account.  
Starbucks and Dreyer's Grand Ice Cream, Inc., introduce Starbucks® Ice Cream and Starbucks Ice Cream bars. Starbucks Ice Cream quickly becomes the number one brand of coffee ice cream in the U.S.  
North American Coffee Partnership (Starbucks and Pepsi-Cola Company business venture) begins selling a bottled version of Starbucks Frappuccino® blended beverage.  
Opens in Rhode Island; Idaho; North Carolina; Arizona; Utah; and Ontario, Canada.  
Starbucks location total = 1,015

#### 1997

Starbucks Coffee International opens locations in the Philippines.  
Awarded Canadian Airlines account.  
Forms alliance with eight companies to enable the gift of more than 320,000 new books for children through the All Books for Children first annual book drive.  
Establishes The Starbucks Foundation, benefiting local literacy programs in communities where Starbucks has coffeehouses.  
Opens in Florida, Michigan, and Wisconsin.  
Starbucks location total = 1,412

#### 1998

Starbucks Coffee International opens locations in Taiwan, Thailand, New Zealand, and Malaysia.  
Introduces Tiazzì® blended juice tea, a refreshing mixture of tea, fruit juice, and ice.  
Acquires Seattle Coffee Company in the United Kingdom with more than 60 retail locations.  
Acquires Pasqua Inc., a San Francisco-based coffee retailer.  
Forms Urban Coffee Opportunities, a joint venture with Earvin "Magic" Johnson's Johnson Development Corp., to develop Starbucks Coffee locations in underserved, urban neighborhoods throughout the U.S.  
Signs a licensing agreement with Kraft Foods Inc. to extend the Starbucks brand into grocery channels across the U.S.  
Launches Starbucks.com.  
Opens two new coffeehouse concepts, Cafe Starbucks in Seattle and Circadia® Coffee House in San Francisco.  
Opens in New Orleans; St. Louis; Kansas City, Missouri; and Portland, Maine.  
Starbucks location total = 1,886

*Continued*

## APPENDIX A

### Starbucks Timeline and History—*continued*

#### 1999

Starbucks Coffee International opens locations in China, Kuwait, Korea, and Lebanon.  
Acquires Tazo®, a Portland, Oregon-based tea company.  
Partners with Conservation International to promote environmentally sound methods of growing coffee.  
Introduces Shade Grown Mexico Coffee.  
Acquires Hear Music, a San Francisco-based music company.  
Enters agreement with Albertson's, Inc., to open more than 100 Starbucks locations in their supermarkets in the year 2000.  
Opens in Memphis and Nashville, Tennessee; and Saskatchewan, Canada.  
Starbucks location total = 2,135

#### 2000

Enters into licensing agreement with TransFair USA to market and sell Fair Trade Certified<sup>SM</sup> coffee.  
Introduces a Commitment to Origins<sup>TM</sup> coffee category that includes shade grown, organic, and Fair Trade Certified selections.  
Expands contribution to Conservation International to establish conservation efforts in five new sites.  
Enters agreement with Host Marriott International to open locations in select properties.  
Starbucks Coffee International opens in Dubai, Hong Kong, Shanghai, Qatar, Bahrain, Saudi Arabia, and Australia.  
Starbucks current location total = 3,501

#### 2001

Introduces coffee sourcing guidelines developed in partnership with The Center for Environmental Leadership in Business, a division of Conservation International.  
Commits to the purchase of one million pounds of Fair Trade Certified<sup>SM</sup> coffee.  
Offers \$1 million in financial support to coffee farmers through Calvert Community Investments.  
Begins to offer high-speed wireless Internet access in stores.  
The Starbucks Foundation awards more than 450 grants totaling \$4.2 million to literacy, schools, and community-based organizations across North America.  
Begins offering the Starbucks Card, a stored value card for customers to use and reload.  
Enters agreement with Hyatt Hotels Corp.  
Starbucks Coffee Japan introduces a stock option program for eligible full- and part-time partners and successfully implements IPO.  
Starbucks and international business partners seed Starbucks Cares Fund with \$1.2 million contribution to benefit September 11th Fund. Customers and partners contribute more than \$1.4 million to Starbucks Cares.  
Starbucks opens 300th location in Japan and celebrates fifth year of business in Japan.  
Starbucks Coffee International opens in Switzerland, Israel, and Austria.  
Starbucks location total = 4,709

#### 2002

Signs memorandum of understanding with Fairtrade Labelling Organizations International (FLO) that enables the company to enter into licensing agreements with national Fair Trade organizations to sell Fair Trade Certified<sup>SM</sup> coffee in the countries where Starbucks does business.  
Publishes its first Corporate Social Responsibility Annual Report.  
Celebrates 10-year anniversary of Starbucks IPO.  
Introduces Starbucks DoubleShot<sup>TM</sup> to the ready-to-drink coffee category.  
Signs licensing agreement with TransFair Canada to bring Fair Trade Certified<sup>SM</sup> coffee to more than 270 retail locations in Canada.  
Starbucks Coffee International opens in Oman, Indonesia, Germany, and Spain.  
Current location total = 5,688

## EXHIBIT 4

### Starbucks Mission Statements and Guiding Principles

#### Mission Statement

*Establish Starbucks as the premier purveyor of the finest coffee in the world while maintaining our uncompromising principles while we grow.*

The following six guiding principles will help us measure the appropriateness of our decisions:

- Provide a great work environment and treat each other with respect and dignity.
- Embrace diversity as an essential component in the way we do business.
- Apply the highest standards of excellence to the purchasing, roasting, and fresh delivery of our coffee.
- Develop enthusiastically satisfied customers all of the time.
- Contribute positively to our communities and our environment.
- Recognize that profitability is essential to our future success.

#### Environmental Mission Statement

*Starbucks is committed to a role of environmental leadership in all facets of our business.*

We fulfill this mission by a commitment to:

- Understanding of environmental issues and sharing information with our partners.
- Developing innovative and flexible solutions to bring about change.
- Striving to buy, sell, and use environmentally friendly products.
- Recognizing that fiscal responsibility is essential to our environmental future.
- Instilling environmental responsibility as a corporate value.
- Measuring and monitoring our progress for each project.
- Encouraging all partners to share in our mission.

And Schultz points out:

The market is much larger than we originally thought. . . . In most cases local competitors benefit from our arrival because of the expansion of the marketplace. Our strategy is never to eliminate or hurt the competition. We never under-price our coffee and it's clear that we position ourselves so as not to undercut the pricing structure in the marketplace.

Schultz observes that the company is still in its early days of growth worldwide. "We are opening three or four stores every day," he notes. "We feel strongly that the driver of the equity of the brand is directly linked to the retail experience we create in our stores. Our commitment to the growth of the company is significant and will continue to be based on the long-term growth potential of our retail format."

#### Securing the Finest Raw Materials

Starbucks' coffee quality begins with the purchase of high-quality *arabica* coffee beans. Although many Americans were raised on a commodity-like coffee made from lower quality *robusta* beans (or arabica beans mixed with less-expensive filler beans), Starbucks coffee is strictly *arabica*, and the company ensures that only the highest quality beans are used. Dave Olsen, the company's then senior vice president and then chief coffee procurer,

scoured mountain trails in Indonesia, Kenya, Guatemala, and elsewhere in search of Starbucks' premium bean. His standards were demanding, and he conducted exacting experiments in order to get the proper balance of flavor, body, and acidity.

From the company's inception, it has worked on developing relationships with the countries from which it buys coffee beans. Traditionally, Europeans and Japanese bought most of the premium coffee beans. Olsen sometimes had to convince coffee growers to sell to Starbucks—especially since American coffee buyers are notorious purchasers of the "dregs" of the coffee beans. In 1992 Starbucks set a new precedent by outbidding European buyers for the exclusive Narino Supremo Bean crop.<sup>7</sup> Starbucks collaborated with a mill in the tiny town of Pasto, located on the side of the Volcano Galero. There they set up a special operation to single out the particular Narino Supremo bean, and Starbucks guaranteed to purchase the entire yield. This enabled Starbucks to be the exclusive purveyor of Narino Supremo, purportedly one of the best coffees in the world.<sup>8</sup>

#### Vertical Integration

Roasting the coffee bean is close to an art form at Starbucks. Starbucks currently operates multiple roasting and distribution facilities. Roasters are promoted from



within the company and trained for over a year, and it is considered quite an honor to be chosen. The coffee is roasted in a powerful gas-fired drum roaster for 12 to 15 minutes while roasters use sight, smell, hearing, and computers to judge when beans are perfectly done. The color of the beans is even tested in an Agtron blood-cell analyzer, with the whole batch being discarded if the sample is not deemed perfect.

### The Starbucks Experience

According to Schultz, “We’re not just selling a cup of coffee, we are providing an experience.” In order to create American coffee enthusiasts with the dedication of their Italian counterparts, Starbucks provides a seductive atmosphere in which to imbibe. Its stores are distinctive and sleek, yet comfortable. Though the sizes of the stores and their formats vary, most are modeled after the Italian coffee bars where regulars sit and drink espresso with their friends.

Starbucks stores tend to be located in high-traffic locations such as malls, busy street corners, and even grocery stores. They are well lighted and feature plenty of light cherry wood and artwork. The people who prepare the coffee are referred to as “baristas,” Italian for bartender. Jazz or opera music plays softly in the background. The stores range from 200 to 4,000 square feet, with new units tending to range from 1,500 to 1,700 square feet. In 2003, the average cost of opening a new store (including equipment, inventory and leasehold improvements) is in the neighborhood of \$350,000; a “flagship” store costs much more.

### Building a Unique Culture

While Starbucks enforces almost fanatical standards about coffee quality and service, the policy at Starbucks toward employees is laid-back and supportive. They are encouraged to think of themselves as partners in the business. Schultz believes that happy employees are the key to competitiveness and growth.

We can’t achieve our strategic objectives without a workforce of people who are immersed in the same commitment as management. Our only sustainable advantage is the quality of our workforce. We’re building a national retail company by creating pride in—and stake in—the outcome of our labor.<sup>9</sup>

On a practical level, Starbucks promotes an empowered employee culture through generous benefits programs, an employee stock ownership plan, and thorough employee training. Each employee must have at least 24 hours of training. Classes cover everything from coffee history to a seven-hour workshop called “Brewing the Perfect Cup at Home.” This workshop is one of five classes that all employees must complete during their first six weeks with the company. Reports *Fortune*:

It’s silly, soft-headed stuff, though basically, of course, it’s true. Maybe some of it sinks in. Starbucks is a smashing success, thanks in large part to the people who come out of these therapy-like training programs. Annual barista turnover at the company is 60 percent compared with 140 percent for hourly workers in the fast-food business.<sup>10</sup>

Starbucks offers its benefits package to both part-time and full-time employees. The package includes medical, dental, vision, and short-term disability insurance, as well as paid vacation, paid holidays, mental health/chemical dependency benefits, an employee assistance program, a 401k savings plan and a stock option plan. They also offer dependent coverage that includes same-sex partners.<sup>11</sup> Schultz believes that without these benefits, people do not feel financially or spiritually tied to their jobs. He argues that stock options and the complete benefits package increase employee loyalty and encourage attentive service to the customer.<sup>12</sup>

Employee turnover is also discouraged by Starbucks’ stock option plan known as the Bean Stock Plan. Implemented in August of 1991, the plan made Starbucks the only private company to offer stock options unilaterally to all employees.

Starbucks’ concern for employee welfare extends beyond its retail outlets to coffee producers. The company’s guidelines call for overseas suppliers to pay wages and benefits that “address the basic needs of workers and their families” and to allow child labor only when it does not interrupt required education.<sup>13</sup> This move has set a precedent for other importers of agricultural commodities.

### Leveraging the Brand

**Multiple Channels of Distribution.** Besides its stand-alone stores, Starbucks has set up cafes and carts in hospitals, banks, office buildings, supermarkets, and shopping centers. Other distribution agreements have included office coffee suppliers, hotels, and airlines. Office coffee is a large segment of the coffee market. Associated Services (an office coffee supplier) provides Starbucks coffee exclusively to thousands of businesses round the United States. Starbucks has deals with airlines, such as an agreement with United Airlines to provide Starbucks coffee to United’s nearly 75 million passengers a year. Starbucks, through a licensing agreement with Kraft Foods Inc., offers its coffee in grocery stores across the United States.

**Brand Extensions.** In 1995, Starbucks launched a line of packaged and prepared teas in response to growing demand for tea-houses and packaged tea. Tea is a highly profitable beverage for restaurants to sell, costing only 2 cents to 4 cents a cup to produce.<sup>14</sup> As its tea line became increasingly popular, in January 1999 it acquired Tazo, a Portland, Oregon-based tea company.

Starbucks coffee is also making its way onto grocery shelves via a carefully planned series of joint ventures.<sup>15</sup> An agreement with PepsiCo Inc. brought a bottled version of Starbucks Frappuccino (a cold, sweetened coffee drink) to store shelves in August of 1996. In another 50–50 partnership, Dreyer’s Grand Ice Cream Inc. distributes seven quart-products and two bar-products of Starbucks coffee ice cream.

Other partnerships by the company are designed to form new product associations with coffee. For instance, the company’s music subsidiary, Hear Music, regularly releases CDs, some in collaboration with major record labels, that are then sold through Starbucks retail stores.

While Starbucks is the largest and best known of the coffeehouse chains and its presence is very apparent in metropolitan areas, the firm’s estimates indicate that only a small percentage (about 7 percent) of the U.S. population has tried its products. Through distribution agreements and the new product partnerships, Starbucks hopes to capture more of the U.S. market.

## INTERNATIONAL EXPANSION

For many years analysts have observed that the U.S. coffee-bar market may be reaching saturation. They point to market consolidation, as bigger players snap up some of the smaller coffee bar competitors.<sup>16</sup> Further, they note that Starbucks’ store base is also maturing, leading to a slowdown in the growth of unit volume and firm profitability. In response, some argue, Starbucks has turned its attention to foreign markets for continued growth. For instance *BusinessWeek* notes:

To duplicate the staggering returns of its first decade, Starbucks has no choice but to export its concept aggressively. Indeed, some analysts give Starbucks only two years at most before it saturates the U.S. market. The chain now [in August 2002] operates 1,200 international outlets, from Beijing to Bristol. That leaves plenty of room to grow. Indeed, about 400 of its planned 1,200 new stores this year will be built overseas, representing a 35 percent increase in its foreign base. Starbucks expects to double the number of its stores worldwide, to 10,000 in three years.<sup>17</sup>

However, of the predicted three or four stores that will open each day, the majority will continue to be in the United States.

### Early Expansion

In 1995, the firm established a subsidiary called Starbucks Coffee International Inc. At that time, the subsidiary consisted of 12 managers located in Seattle. Today, this subsidiary is led by Australian expatriate Peter Maslen and is staffed with about 180 experienced multinational and multilingual managers located in Seattle and three regional offices around the world. This

group is responsible for all Starbucks business development outside North America, including developing new businesses, financing and planning stores, managing operations and logistics, merchandising, and training and developing Starbucks’ international managers.

Starbucks’ first non-North American store was opened in 1996 in Tokyo. In reflecting on this early step in internationalizing the chain, Schultz notes:

Two years prior to opening up in Japan, we hired this blue-chip consulting firm to guide us to succeed here. Basically, they said we would not succeed in Japan. There were a number of things they told us to change. [They said] we had to have smoking, but that was a nonstarter for us. They also said no Japanese would ever lose face by drinking from a cup in the street. And third, they said that given the [high] rent, stores couldn’t be larger than 500 square feet . . . Well, our no-smoking policy made us an oasis in Japan. As for our to-go business, you can’t walk down a street in Tokyo today and not see someone holding a cup of Starbucks coffee. And our store size in Japan is identical to our store size in the U.S., about 1,200 to 1,500 square feet. It just shows the power of believing in what you do. And also that Starbucks is as relevant in Tokyo, Madrid, or Berlin as it is in Seattle.<sup>18</sup>

### The Starbucks Way

According to *U.S. News & World Report*:

When venturing overseas, there is a Starbucks way. The company finds local business partners in most foreign markets . . . It tests each country with a handful of stores in trendy districts, using experienced Starbucks managers. It sends local baristas to Seattle for 13 weeks of training. Then it starts opening stores by the dozen. Its coffee lineup doesn’t vary, but Starbucks does adapt its food to local tastes. In Britain, it won an award for its mince pie. In Asia, Starbucks offers curry puffs and meat buns. The company also fits its interior décor to the local architecture, especially in historic buildings. “We don’t stamp these things out cookie-cutter style,” says Peter Maslen, president of Starbucks Coffee International.<sup>19</sup>

Although Starbucks is committed to owning its North American stores, it has sought partners for much of its overseas expansion. As Kathy Lindemann, SVP of Operations for Starbucks International, describes it:

Our approach to international expansion is to focus on the *partnership first, country second*. We rely on the local connection to get everything up and working. The key is finding the right local partners to negotiate local regulations and other issues. We look for partners who share our values, culture, and goals about community development. We are primarily interested in partners who can guide us through the process of starting up in a foreign location. We look for firms with: (1) similar philosophy to ours in terms of shared

values, corporate citizenship, and commitment to be in the business for the long haul, (2) multi-unit restaurant experience, (3) financial resources to expand the Starbucks concept rapidly to prevent imitators, (4) strong real estate experience with knowledge about how to pick prime real estate locations, (5) knowledge of the retail market, and (6) the availability of the people to commit to our project.

In an international joint venture, it is the partner that chooses store sites. These are submitted for approval to Starbucks, but the partner does all the preparatory and selection work. Cyndie Horwat, VP for international assets development systems & infrastructure, explains how a Starbucks market entry plan starts with brand building, which then facilitates rapid further expansion in a country:

When first entering a market, we're looking for different things in the first one to three years than later on. During these early years, we're building our brand. Our stores are the biggest source of advertising, since we do not do a lot of separate advertising. So we have a higher investment in stores in the first three years. About 60 to 70 percent of stores opened in these first three years are our high brand-builders.

Adds Horwat:

First, we look for extremely visible sites in well-trafficked areas and focus on three major factors: demographics, branding potential, and financials. Second we categorize sites on an A to D scale. "A" sites are "signature" sites that are qualitatively superior to all other sites within the trade area [an area within which Starbucks chooses to locate one store]. We rarely take a "C" or "D" store.<sup>20</sup> Third, we ask our international Market Business Unit<sup>21</sup> (MBU) to send in the "site" submittal package with quantitative and qualitative measures, such as how the site meets Starbucks' established criteria and the partner's agreed-upon criteria. This package is reviewed by a number of functional units—operations, finance, and real estate—within the International Group. Fourth, we move into the design phase, which is done in Seattle using information provided by the partner. Next we negotiate the lease with the landlord and initiate the construction when the appropriate permits are obtained. Finally, we turn over the store to operations. The whole process takes about 13 to 16 weeks from start to finish.

### Establishing Starbucks as a Global Brand

Based on the success in Japan and other locations, Schultz's goal is for Starbucks to have a ubiquitous image as one of the most respected brands in the world. He notes:

Whenever we see the reception we're getting in markets in places such as China, the Philippines, Malaysia, the U.K., and most recently Spain and

Germany, we recognize that the growth potential for the company [overseas] is very significant. We want to accelerate that growth, maintain our leadership position, and, ultimately, become one of the most respected brands in the world.<sup>22</sup>

Since its early foray into the Japanese market, the pace of international expansion has picked up significantly. In 1998, Starbucks acquired Seattle Coffee Company in the United Kingdom, a chain with more than 38 retail locations. That same year, it opened stores in Taiwan, Thailand, New Zealand, and Malaysia. In 1999, Starbucks opened in China (Beijing), Kuwait, South Korea, and Lebanon. In 2000, it entered another seven markets (China-Hong Kong and Shanghai, Dubai, Australia, Qatar, Saudi Arabia, and Bahrain). It added three markets in 2001 (Switzerland, Israel, and Austria). Last year, another nine markets were opened (Oman, Spain, Indonesia, Germany, Southern China-Macau and Shenzhen, Mexico, Puerto Rico, and Greece). **Exhibit 5** highlights the growth of international stores, and **Exhibit 6** provides the list of countries where Starbucks has a presence.

Schultz says that this expansion is only beginning and confidently predicts more to come:

Ten years ago, we had 125 stores and 2,000 employees. Today we have 62,000 people working in 30 countries outside of North America, serving approximately 22 million customers a week. Our core customer is coming in about 18 times a month. With the majority of adults around the world drinking two cups of coffee a day and with Starbucks having less than 7 percent share of total coffee consumption in the U.S. and less than 1 percent worldwide, these are the early days for the growth and development of the company. We've got a model that has been well tested from market to market.

Starbucks is well on its way to becoming a global brand. According to *BusinessWeek*:

[T]he Starbucks name and image connect with millions of consumers around the globe. It was one of the fastest-growing brands in a *BusinessWeek* survey of the top 100 global brands published August 5 [2002]. At a time when one corporate star after another has crashed to earth, brought down by revelations of earnings misstatements, executive greed, or worse, Starbucks hasn't faltered.<sup>23</sup>

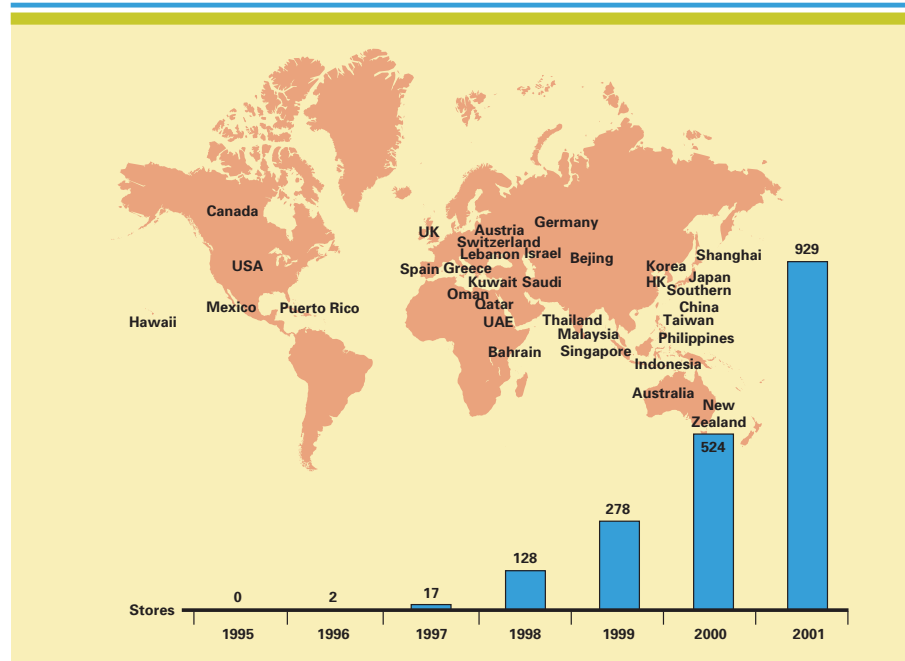
But becoming a global company is not without risks. As *BusinessWeek* points out,

Global expansion poses huge risks for Starbucks. For one thing, it makes less money on each overseas store because most of them are operated with local partners. While that makes it easier to start up on foreign turf, it reduces the company's share of the profits to only 20 percent to 50 percent.<sup>24</sup>

**EXHIBIT 5**

Growth of International Stores, 1996–2002

Source: Starbucks International Group.



**EXHIBIT 6**

Licensed Starbucks International Stores (as of September 2002)

These figures do not include company-operated stores.

Source: Starbucks 10K report.

Asia-Pacific	Europe/Middle East/ Africa	Latin America
Japan	United Arab Emirates	Hawaii
Taiwan	Saudi Arabia	Mexico
China	Kuwait	Puerto Rico
South Korea	Switzerland	
Philippines	Lebanon	
New Zealand	Israel	
Singapore	Austria	
Malaysia	Spain	
Indonesia	Germany	
	Qatar	
	Bahrain	
	Greece	
	Oman	
<b>Total</b>	<b>783</b>	<b>32</b>

Product sales to, and royalty and license fee revenues from, licensed international retail stores accounted for approximately 17% of specialty revenues in fiscal 2002

In addition, the firm is becoming a target for antiglobalization activists around the world.

**PERILS OF GLOBALIZATION**

As Starbucks establishes a global presence, its growing ubiquity has not gone unnoticed by antiglobalization activists. A clear manifestation of this came in November

1999, as tens of thousands of protesters took to the streets of downtown Seattle when the World Trade Organization (WTO) held its third Ministerial conference there. Although nongovernmental organizations (NGOs) and activists had gathered to oppose the WTO, some activists deliberately targeted multinationals like Starbucks, Nike, and McDonald's.<sup>25</sup> A small, but vocal, percentage of these protesters garnered international press coverage by com-

mitting acts of vandalism against carefully chosen targets. As a report in *BusinessWeek* recalls:

Protesters flooded Seattle's streets, and among their targets was Starbucks, a symbol, to them, of free-market capitalism run amok, another multinational out to blanket the earth. Amid the crowds of protesters and riot police were black-masked anarchists who trashed the store, leaving its windows smashed and its tasteful green-and-white decor smelling of tear gas instead of espresso.<sup>26</sup>

Recalling this incident against his firm Schultz says: "It's hurtful. I think people are ill-informed. It's very difficult to protest against a can of Coke, a bottle of Pepsi, or a can of Folgers. Starbucks is both a ubiquitous brand and a place where you can go and break a window. You can't break a can of Coke."

Antiglobalization protesters target recognizable global brands because they are convenient symbols. The following excerpt from "The Ruckus Society's Action Planning Manual and Media Manual"<sup>27</sup> illustrates the close ties between global brands and the principles of direct action against them:

First, [we] use direct action to reduce the issues to symbols. These symbols must be carefully chosen for their utility in illustrating a conflict: an oil company versus an indigenous community, a government policy versus the public interest. Then we work to place these symbols in the public eye, in order to identify the evildoer, detail the wrongdoing and, if possible, point to a more responsible option.

The message that activists want to communicate focuses on the overseas activities of corporations. They accuse multinationals of paying less than a living wage to workers in the Third World, of engaging in labor and environmental practices that would be outlawed in their home countries, of driving local competitors out of business, and of furthering "cultural imperialism." As one Global Trade Watch field organizer describes it:

The rules by which trade is governed need to have more to do with the interests of citizens than with the back pockets and cash wads of a couple corporate CEOs. And we want to make sure that there is a balance consideration. Obviously people are always going to be concerned with their profits—it's business, we understand that, we accept that. But we think that needs to be balanced with concern for the rights of workers, basic human rights, [and] protecting the environment.<sup>28</sup>

Critics further accuse international organizations like the WTO, World Bank, and IMF of promoting corporate globalization by supporting trade liberalization, by promoting export-based economic development, and by facilitating foreign direct investment. According to an organization that bills itself as *Mobilization for Global Justice*:

Most of the world's most impoverished countries have suffered under IMF/World Bank programs for two decades: they've seen debt levels rise, unemployment skyrocket, poverty increase, and environments devastated. Urged to export, they focus on cash crops like coffee instead of food for their own people, and allow foreign governments to build sweatshops—which also puts pressure on jobs in the U.S.<sup>29</sup>

When Starbucks opened its first store in Mexico in September 2002, it chose a site in the Sheraton Hotel on Reforma Boulevard in Mexico City. This was Starbucks' first store in Latin America and its first in an "origin country," i.e., a coffee-producing country. An article on the Organic Consumers Association Web site describes Starbucks' Mexican flagship store:

The new Starbucks on Reforma features soft lighting and an aromatic ambiance. . . . Behind the counter, well-groomed employees whip out the signature Frappuccinos and lattes. Indeed, the only jarring note is the 36 pesos (\$3.60) the young woman at the register wants for a double latte, 10 times the price Indian farmers are getting for a pound of their product in Chiapas, Oaxaca, and other coffee-rich states of southern Mexico. . . . There is no starker contrast in the economics of coffee these days than between the cushy comforts and gourmet blends of the Starbucks "Experiencia" and the grim, daily existence of 360,000 mostly Indian coffee farmers who work small plots carved from the jungle mountains of southern Mexico.<sup>30</sup>

Multinational corporations and their supporters respond that the effects of—and solutions for—globalization are more complicated than the critics contend. They note that multinationals create jobs, pay better prices and wages than domestic firms, and conform to *local* labor and environmental regulations.

The skeptics are right to be disturbed by sweatshops, child labour, bonded labour, and the other gross abuses that go on in many poor countries (and in the darkest corners of rich ones, too). But what makes people vulnerable to these practices is poverty. . . . The more thoroughly these companies [multinationals] penetrate the markets of the third world, the faster they introduce their capital and working practices, the sooner poverty will retreat and the harder it will be for such abuses to persist.<sup>31</sup>

Moreover, multinationals argue, they have responded to the criticism of profit-driven behavior by developing corporate codes of conduct, corporate social responsibility programs, and partnerships with nongovernmental organizations.<sup>32</sup> They point out, however, that they are in a no-win situation vis-à-vis their critics, because they can always be criticized for not doing enough.

Starbucks has found that global concerns often get mixed up with and intertwined with local issues. Even the mere act of opening a Starbucks retail store in a

neighborhood can result in local activism and community “push-back” against the Starbucks brand. For example, when Starbucks opened a store in Cambridge, Massachusetts, in 1998, picketers carrying signs that read, “Don’t Let Corporate Greed Destroy Our Neighborhood,” greeted it. A lawyer who helps communities keep national chains out, says: “It’s part of the growing tension in the world between the mass-market economy and people’s desire to retain self-control and some local culture. . . . If you’ve got a beef with Starbucks, you’ve got a beef with capitalism.”<sup>33</sup>

Starbucks has faced a variety of “community push-back” situations around the world. Soon Beng Yeap, one of Starbucks’ International brand reputation managers, notes: “This [community push-back] is a live issue and Starbucks manages each push-back incident case-by-case. In some markets [we] have gone in and in some [we] have pulled out.” He cites two recent examples, one in London, where Starbucks decided to withdraw its efforts to open a store after local activists actively campaigned against the firm, and the other in Beijing, where the firm opened a store in a historic district, and, following subsequent and significant adverse comment reported in local and international media, decided to stay put.

### Primrose Hill and Starbucks’ Decision to Withdraw

In 2002 Starbucks made plans to open a store in Primrose Hill, a London suburb. Located in northwest London, Primrose Hill is a well-known historical and picturesque area comprised of a public park, a shopping “village” area, and attractive Victorian residential housing. Residents of Primrose Hill—many of whom are writers, photographers, actors, and musicians—take great pride in the area and are protective of their local environment, acting to ensure that no chain stores operate in the area.<sup>34</sup>

In early 2002, Starbucks selected Primrose Hill as a potential site for a store, and in April 2002 submitted an application to the local council. When this information was published in the local papers, it received considerable negative feedback from the residents, in particular from the Primrose Hill Conservation Area Advisory Committee. This committee claimed that litter, noise, and disruption from deliveries to Starbucks’ store in Primrose Hill would ruin the village ambience and contribute to the “homogenization of the high street.” The opposition surprised Starbucks because Primrose Hill residents, associations (including the Primrose Hill Conservation Area Advisory Committee), and businesses had been contacted as part of consultation period for the potential site. Although the objections to Starbucks’ entry focused on local planning issues, there was an antiglobalization element as well. One critic was quoted

as saying that Starbucks was “renowned for not paying proper money to coffee growers.”<sup>35</sup>

In response to the critics, Starbucks offered to arrange meetings between the planning committee, local councilors, and its representatives to discuss the issue and hear their concerns. Despite Starbucks’ efforts, no meeting offers were accepted and minimal responses were received.

In the meantime, the Primrose Hill Conservation Area Advisory Committee began to campaign strongly against Starbucks. They collected more than 1,300 letters of objection, which they then presented to the local council. Many celebrities, such as the actor Jude Law, National Theatre director Nicholas Hytner, broadcaster Joan Bakewell, singer Neneh Cherry, author Jeanette Winterson, and artist Patrick Caulfield, lent their support by opposing the Starbucks application. Media coverage that was initially local became national when celebrities became involved. According to Horwat:

Primrose Hill was an “A” site. A very affluent neighborhood, little or no competition, and we knew it would be a winner. Everyone [at Starbucks International] loved it. The real estate people, the finance people, and others signed off on the deal. Opposition came only when city council was about to approve [our application]. The opposition claimed that our entry would raise rents in the community. So we went back to city council to argue our case. But activists brought in movie stars and got local and national media attention.

In early June 2002, when it was apparent that Starbucks was not welcome in Primrose Hill, the company decided against opening the store. Reflecting on their decision to withdraw, Horwat explains:

We care about the views of the communities of which we are a part. We try to have our stores be part of a community. We had hoped to make a positive contribution for people to get together in Primrose Hill. If the community does not welcome us, it’s not someplace we want to be.

Adds Soon Beng Yeap:

You have to understand the bigger picture in the U.K. to appreciate what was going on locally at that time—Starbucks was seen as an American chain coming into the British market and the British media tend to be very cynical. The specialty coffee market was becoming crowded and extremely competitive with several other chains such as Café Nero, Coffee Republic, and Costa Coffee making a strong push for market share. The Starbucks team reviewed all the factors involved as well as listened carefully to the community concerns. At the end of the day, we decided to withdraw our application.

### Beijing and Starbucks' Decision to Stay

Starbucks opened its first outlet in Beijing in January 1999 and has over 100 stores in the country today. However, Starbucks touched a nationalist nerve in 2000 when it opened a small coffee shop in Beijing's Forbidden City.<sup>36</sup> In highlighting this particular store, *The New York Times* noted:

If ever there was an emblem of the extremes to which globalization has reached, this is it: mass-market American coffee culture in China's most hallowed historic place. Even a McDonald's in the Kremlin would not come as close. Starbucks opened its Forbidden City shop a month ago [September 2000] with a signature menu board advertising the usual Americano and decaf latte coffee and a glass display case filled with fresh glazed donuts, cinnamon rings, and banana walnut muffins.

Starbucks, for its part, had taken extraordinary care to ensure that its presence was unobtrusive. To avoid ruining the atmosphere of the Forbidden City, the signs and brand images were placed inside for this store. This small store (barely a closet according to some reports) had only two small tables and few chairs. It was located on the edge of the Forbidden City, among 50 other retailers, including some selling souvenirs and trinkets. Despite such a low-key presence, this store ignited controversy. Dozens of Chinese newspapers reported on reactions to the shop. According to one such report in the *People's Daily*:

The reason for the uproar is due to the cafe's location: the Forbidden City, the world's largest imperial palace. . . . First constructed in 1406, the Forbidden City is China's best-preserved ancient architecture encircled by a rampart of three kilometers. The cafe, named Starbucks, is situated in the southeastern corner of the Hall of Preserving Harmony (Baohedian), one of the three most impressive buildings on the palace ground. The hall used to be the venue to hold feasts by emperors and nobles of ethnic groups on New Year's Eve of China's lunar calendar. . . . Debates over the mini-cafe took place first on Web. A survey by Sina.com showed that over 70 percent of nearly 60,000 people surveyed were opposed to the cafe's entry into the Forbidden City, the main reason being the damaging effects to Chinese cultural heritage and its atmosphere.<sup>37</sup>

The administrators of the Forbidden Palace and other government officials took note of the controversy but were supportive of Starbucks. Chen, a spokesperson for the Forbidden City Museum, maintained that allowing Starbucks into the Forbidden City was part of their efforts to improve services in the area. Moreover, Chen added: "The reaction has been very intense. Some people say this is a gem of Chinese culture and that foreign

brands should not be allowed in. . . . We can't give up eating for the fear of choking."<sup>38</sup>

According to Horwat:

The Forbidden City location was a "C" site at best. But definitely not a "D" site, because there was still the benefit of brand presence. But the government said, "We think you should come in," and it was difficult to say no. There was no local community, only tourists.

Following the flurry of articles in the Chinese media, CNN began to run news clips of this story in the United States. Watching this unfold in the U.S. media, some senior managers at Starbucks became alarmed at the negative publicity. According to Soon Beng Yeap:

The immediate reaction was to "close the store!" due to the relentless negative coverage generated by the international media. After serious discussion among the senior executives, we felt as guests in a foreign country, we should be respectful of our hosts—the Forbidden City officials—who invited us to be there in the first place. We decided to not pull out because it was the international media that stirred up the whole controversy. Unlike the Primrose Hill case, there was no real local community "push-back." It was all media-driven. A few reporters got hold of the story and ran with it, all citing the same survey by Sina.com. We were very disappointed by the negative media coverage, which created a false sense of "cultural imperialism" about our intentions in opening the store, especially when we worked very hard to be culturally sensitive and listen to the local community.

The controversy has since died down, as a recent report (February 2003) in *The Straits Times* (Singapore) indicates:

[Today] if anything, the tourists were more upset than the Beijing residents about the presence of Starbucks in the Forbidden City, complaining that it was out of place in a historical site. . . . Asked what were the hottest issues of the day for ordinary citizens, taxi driver Liu Zhiming said: 'Cars, apartments, and making money. What else?'<sup>39</sup>

### ENTERING RIO DE JANEIRO, BRAZIL

Peter Maslen, president of Starbucks International, hurriedly convened a meeting of his key executives in Starbucks International, including Julio Gutierrez, his president for Latin America. Starbucks' entry into Brazil was in jeopardy because certain activists opposing Starbucks' presence in the country were gaining momentum.

Brazil is the largest coffee-producing country in the world, and this was Starbucks' second foray into Latin America (after Mexico). The company chose not to seek a joint-venture partner to enter Brazil. Since many copycat chains had sprung up in Rio de Janeiro, some

**FIGURE 1**

Map of the Ipanema Area, Rio de Janeiro, Brazil

Source: www.ipanema.com



imitating Starbucks to the last detail, Maslen felt that his team had to move quickly before any particular group established itself as the premier chain. After several years of work by Julio’s Latin America team, no suitable joint-venture partner had been identified, and Maslen was considering establishing a 100 percent Starbucks owned MBU (as it had already done in the U.K., Australia, and Thailand).

The business development group, with Gutierrez’s team, had picked a site in the Ipanema area of Rio de Janeiro. They proposed that a flagship store be opened on this neighborhood’s main commercial street—Rua Visconde de Pirajá (see **Figure 1** above). Many of Rio’s most traditional boutiques started in Ipanema, later to be exported to the malls and other parts of town. Many world-renowned brands such as Cartier, Louis Vuitton, and Polo Ralph Lauren had stores on the Rua Visconde de Pirajá. It is often said that news in Ipanema makes headlines all over Brazil.

Starbucks had also chosen other sites, four to be specific, where the company could open stores immediately following the opening of the flagship Ipanema store. One of these stores was to be located in the posh neighborhood of Barra de Tijuca; another was slated for Leblon, and two others for shopping malls located in affluent residential neighborhoods in the city. The real estate group was ready to sign the lease with the agents of the Ipanema property owner, but was awaiting a formal response from the city council members.

The business development group, led by Troy Alstead, SVP of finance and business development at Starbucks

International, was confident that the Ipanema location was an “A” category site. “The demographics of this area are just right for a flagship store. They are affluent, young, and love American brands.” The business development group’s financial projections indicated that the Ipanema Starbucks store would be profitable in a short time, and Alstead believed that this was a conservative figure. Further, he pointed out:

Based on the company’s experiences of opening flagship stores in similar, high-traffic posh neighborhoods in other cities around the world—our store in Ginza, Japan, comes to mind—we believe the Ipanema store would be viable for Starbucks. We estimate meeting store level ROI targets in aggregate for the first five stores within two years.

**Exhibit 7** provides the finance group’s forecast for the Ipanema and the other four stores in Brazil for the first five years of operations.

But Maslen had some concerns. He was troubled by reports of rising levels of violence and street crime in Rio and São Paulo. In response to this growing violence, some of the most fashionable retailers were relocating themselves in shopping malls. He also questioned whether the timing for Starbucks was off. Current world events had generated anti-American feeling in many countries.

Following the standard practice, Starbucks had been working with the local chamber of commerce since January 2003, and with the local city council for the required permits. The members of the city council and



<b>Projected P&amp;L for Ipanema Store (US \$)</b>					
	<b>Year 1</b>	<b>Year 2</b>	<b>Year 3</b>	<b>Year 4</b>	<b>Year 5</b>
Net Sales [1]	<b>\$1,000,000</b>	<b>\$1,100,000</b>	<b>\$1,210,000</b>	<b>\$1,270,500</b>	<b>\$1,334,025</b>
Cost of Goods Sold [2]	\$350,000	\$330,000	\$326,700	\$343,035	\$360,187
Gross Profit	<b>\$650,000</b>	<b>\$770,000</b>	<b>\$883,300</b>	<b>\$927,465</b>	<b>\$973,838</b>
Staff Costs	\$200,000	\$225,000	\$250,000	250,000	250,000
Marketing [3]	\$75,000	\$50,000	\$50,000	50,000	50,000
Other Costs	\$75,000	\$100,000	\$125,000	125,000	125,000
Occupancy Costs	\$175,000	\$175,000	\$175,000	175,000	175,000
Total Costs	\$525,000	\$550,000	\$600,000	\$600,000	\$600,000
Operating Cash Flow	<b>\$125,000</b>	<b>\$220,000</b>	<b>\$283,300</b>	<b>\$327,465</b>	<b>\$373,838</b>
Depreciation [4]	\$54,200	\$54,200	\$54,200	\$54,200	\$54,200
Store Pre-Tax Profit	<b>\$70,800</b>	<b>\$165,800</b>	<b>\$229,100</b>	<b>\$273,265</b>	<b>\$319,638</b>
Construction Costs [5]	\$400,000				
Key Money [6]	\$1,000,000				
<b>Projected P&amp;L for a "Typical" Store in Locations Outside the Ipanema Area (US \$)*</b>					
	<b>Year 1</b>	<b>Year 2</b>	<b>Year 3</b>	<b>Year 4</b>	<b>Year 5</b>
Net Sales [1]	<b>\$625,000</b>	<b>\$650,000</b>	<b>\$700,000</b>	<b>\$735,000</b>	<b>\$771,750</b>
Cost of Goods Sold [2]	\$218,750	\$195,000	\$189,000	\$198,450	\$208,373
Gross Profit	<b>\$406,250</b>	<b>\$455,000</b>	<b>\$511,000</b>	<b>\$536,550</b>	<b>\$563,378</b>
Staff Costs	\$100,000	\$115,000	\$135,000	\$135,000	\$135,000
Marketing [3]	\$45,000	\$30,000	\$30,000	\$30,000	\$30,000
Other Costs	\$60,000	\$75,000	\$75,000	\$75,000	\$75,000
Occupancy Costs	\$70,000	\$70,000	\$70,000	\$70,000	\$70,000
Operating Cash Flow	<b>\$131,250</b>	<b>\$165,000</b>	<b>\$201,000</b>	<b>\$226,550</b>	<b>\$253,378</b>
Depreciation [4]	\$25,000	\$25,000	\$25,000	\$25,000	\$25,000
Store Pre-Tax Profit	<b>\$106,250</b>	<b>\$140,000</b>	<b>\$176,000</b>	<b>\$201,550</b>	<b>\$228,378</b>
Construction Costs [5]	\$215,000				
Key Money [6]	\$400,000				

## EXHIBIT 7

### Financial Analysis for the First 5 Brazilian Stores

\*Starbucks intends to open 4 such stores in Rio, in addition to the one in Ipanema.

1. Net sales are projected to grow at 10% for years 1 and 2, and at 5% thereafter.
2. Due to increases in efficiency, the cost of goods sold is estimated at 35% for year 1, 30% for year 2, and 27% thereafter.
3. Marketing costs are higher for year 1.
4. Straight-line 10-year depreciation for construction and equipment costs.
5. These represent initial design and construction costs.
6. Monies paid to the landlord to secure the site.

local chamber of commerce were positive about granting Starbucks permission to begin construction. While the formal voting had yet to be undertaken, it looked certain that, barring anything unusual, permission would be granted.

But nongovernmental organizations like the Organic Consumers Association and Global Exchange were mobilizing faster than expected to oppose Starbucks' entry into Brazil. They found out about Starbucks' intent to enter Brazil when the Ipanema district

chamber of commerce newsletter proudly announced that, “We are extremely pleased to welcome Starbucks into the fashionable district of Ipanema. By opening a store in our neighborhood, they will join other global brands and help enhance further our district’s image as *the* place to be in Rio.”

The NGOs were recruiting local activists and had informed Starbucks that they would oppose its entry into Brazil by petitioning the local council to reject its application. They also threatened to start picketing in front of the store once construction was initiated. The “brand” group at Starbucks was concerned about the turn of events. Soon Beng elaborated:

People in Latin America know the brand because of their proximity to the U.S. Potential partners are always contacting us about coming in. Before we go into a place like Brazil, what is the due diligence we have to do? It’s an origin country for us [i.e., coffee-producing country]. It’s a very vocal place, and there is a love-hate relationship with the United States. Finance people always want to say yes to a store when the numbers look good. Today some in Starbucks, at least in our group, say that maintaining and protecting our strong “brand” reputation is equally important. Others counter: if our brand is strong then why worry about it? This is a discussion we have here every day in the company. While the “push-back” is not totally unexpected, it is hard to gauge to the severity of the situation and its likely impact on our brand.

Maslen asked Alstead’s business development group to work with Gutierrez’s Latin American team to estimate how the picketing in front of the store might impact the financial projections his group had prepared. Their answer:

Our financial estimates for the Ipanema store are based on comparables from other flagship stores in locations similar to Rio in other parts of the world. Our financial models are sensitive to the demographics of the area. We project that demand could fall from 5 to 25 percent, because of people picketing in front of the store. We acknowledge it is much harder to guess what the impact on our entire system in Brazil might be as we open new stores. It all depends upon the type of media coverage the activists are able to muster and the issues the media choose to highlight.

Volunteered Soon Beng:

The tide of public opinion is unpredictable. We review each “push-back” incident the best we can, and we have a reasonable track record of predicting outcomes. But, every time we walk into a potential site somewhere in the world, we potentially face this [“push-back”]. It would be great to have a foolproof tool or system to help us evaluate these sorts of issues and make the appropriate decisions.

Maslen had to leave Seattle to attend an important meeting in Europe the following day. He called together his key managers and said,

Look, we’ve experienced a variety of “push-backs” and protests before. What lessons have we learned? We’ve been deciding whether to go into sites or pull out on a case-by-case basis. If we’re going to grow to 25,000 stores, we cannot keep taking an ad-hoc approach. We need a systematic method to respond to push-back—to decide whether we stay with a site or pull out. I want you to come up with a way to help me decide whether to go into Rio at all. And it’s got to be a system or decision process that would work equally well in London or Beijing or anyplace else that we want to open. Let’s meet again when I get back to town in a couple days.

The managers of Starbucks International had their work cut out for them. But they looked forward to tackling the issues raised.

## Notes

1. “Planet Starbucks,” *BusinessWeek*, September 9, 2002, pp. 100–10.
2. According to *BusinessWeek* (September 9, 2002, p. 103), “The name came about when the original owners looked to Seattle history for inspiration and chose the moniker of an old mining camp: Starbo. Further refinement led to Starbucks, after the first mate in *Moby Dick*, which they felt evoked the seafaring romance of the early coffee traders (hence the mermaid logo).”
3. *Success*, April 1993.
4. “Planet Starbucks.”
5. “Mr. Coffee,” *Fortune*, March 30, 2003.
6. “Planet Starbucks,” p. 103.
7. This Colombian coffee bean crop is very small and grows only in the high regions of the Cordillera mountain range. For years, the Narino beans were guarded zealously by Western Europeans, who prized their colorful and complex flavor. It was usually used for upgrading blends. Starbucks was determined to make them available for the first time as a pure varietal. This required breaking Western Europe’s monopoly over the beans by convincing the Colombian growers that it intended to use “the best beans for a higher purpose.”
8. *The Canada Newswire*, March 1, 1993.
9. *Inc.*, January 1993.
10. *Fortune*, December 9, 1996.
11. The decision to offer benefits even to part-time employees (who represent roughly two-thirds of Starbucks 10,000 employees) has gained a great deal of

- attention in the press. According to a Hewitt Associates L.L.C. survey of more than 500 employers, only 25 percent of employers offer medical coverage to employees working less than 20 hours a week. It was difficult to get insurers to sign Starbucks up since they did not understand why Starbucks would want to cover part-timers.
12. *Inc.*, January 1993.
  13. *The Wall Street Journal*, October 23, 1995.
  14. *Nations Restaurant News*, July 10, 1995.
  15. The Specialty Coffee Association of America notes that supermarkets account for over 60 percent of all coffee sold in the Americas, followed by gourmet stores (14 percent), mass market (11 percent), mail order (8 percent), and other.
  16. *The Washington Post*, August 1, 1995.
  17. "Planet Starbucks," p. 102. However, Schultz firmly believes that Starbucks' growth is far from saturation both in the United States and overseas: "We have less than 7 percent of the coffee-consuming opportunities in North America. People are still drinking bad coffee."
  18. "Online Extra: Q&A with Starbucks Howard Schultz," *BusinessWeek*, September 9, 2002.
  19. *U.S. News & World Report*, February 19, 2001.
  20. The difference between an "A" store and a "D" store can be substantial. A "D" store is expected to have about 50–60 percent lower sales. Starbucks classifies a store as "A" if the store location is the focal point of the area, has great visibility, has readily available parking, has excellent access to and from the site, cannot be outpositioned by competitors, and fits with Starbucks' desire to build a distinctive image.
  21. Starbucks' international businesses are typically joint ventures in which Starbucks holds various levels of equity (ranging from 5 percent to 100 percent). These ventures are referred to as Market Business Units (MBU). Regardless of the level of equity Starbucks holds, it supports all of its MBUs in an "ownership blind" manner by providing all MBUs with the same level of support.
  22. "Online Extra: Q&A with Starbucks Howard Schultz."
  23. "Planet Starbucks," p. 102
  24. *Ibid.*
  25. The protesters claim that international organizations like the WTO and International Monetary Fund (IMF) are tools of multinational corporations. Since Seattle, violent protests have been the norm at events such as the annual meetings of the IMF and World Bank, G-8 summits, and the World Economic Forum.
  26. "Planet Starbucks."
  27. The Ruckus Society Web site, [http://ruckus.org/man/action\\_planning.html](http://ruckus.org/man/action_planning.html) (site visited 3/14/03).
  28. Interview with Alesha Daughtrey, Global Trade Watch field organizer, August 17, 2000; archived in the WTO History Project, University of Washington Center for Labor Studies, <http://depts.washington.edu/wtohist/Interviews/Interviews.htm>.
  29. From the Web site of Mobilization for Global Justice, <http://sept.globalizethis.org> (site visited 3/14/03).
  30. John Ross, "The Unloving Cup," December 12, 2002, Organic Consumers Association Web site, [www.organicconsumers.org/starbucks](http://www.organicconsumers.org/starbucks).
  31. "Grinding the Poor," *The Economist*, November 6, 1997.
  32. For example, Starbucks' *Commitment to Origins*<sup>TM</sup> is a four-part Corporate Social Responsibility program that includes offering Fair Trade Certified<sup>SM</sup> coffee, organic certified coffee, Farm Direct (single-origin coffees purchased directly from the farmer), and Conservation coffees (emphasizing shade-grown in partnership with the NGO Conservation International). See [www.starbucks.com/aboutus/cto\\_coffees.asp](http://www.starbucks.com/aboutus/cto_coffees.asp).
  33. Edward McMahon, quoted in "Brewing a Tempest in a Coffee Cup," *Christian Science Monitor*, February 25, 1998.
  34. This desire for protection dates back to 1841 when the residents actively campaigned against the area being opened up to the general public. Such actions discouraged further building developments, thus enabling the residents to retain the look and feel of their neighborhood.
  35. From "Stars V Starbucks: Not a Bean for the Coffee Shop Giant," *Independent on Sunday* (London), June 2, 2002.
  36. "Coffee with Your Tea?" *The Economist*, October 4, 2001.
  37. "Starbucks Cafe in Forbidden City under Fire," *Friday*, November 24, 2000.
  38. Quoted in "Globalization Put as Starbucks into the Forbidden City in Beijing," *The New York Times*, November 25, 2000.
  39. "Capitalism Runs Amok," *The Straits Times*, February 16, 2003.