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Starbucks Corp. (SBUX)

Deutsche Bank dbAccess Global Consumer Conference - Fireside Chat

CORPORATE PARTICIPANTS

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

OTHER PARTICIPANTS

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

MANAGEMENT DISCUSSION SECTION

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

All right. I guess, we will get started. Hi. I am Lauren Silberman. I'm the equity research analyst here at Deutsche Bank, covering the restaurant sector. I am thrilled to kick off day two of Deutsche Bank's Global Consumer Conference with Starbucks. Pleased to be joined by Starbucks' CFO, Rachel Ruggeri. So Rachel, thanks so much for being here.

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

Well, thank you for having me.

QUESTION AND ANSWER SECTION

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

Q

So Rachel, you've been at Starbucks for more than 20 years. You've seen a lot over your tenure. Can you frame some of the near-term headwinds Starbucks is facing within your longer-term perspective of the business?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

A

Yeah. I mean, as you said, I've been at Starbucks for a long tenure. And what's been consistent over my tenure is that we have always focused on a relationship with our partners and our customers. That's differentiated Starbucks. It gives us a competitive advantage. And those relationships evolve over time. And we, as a company, have to evolve accordingly.

More specifically, following COVID, as an example, we had to strengthen the relationship with our partners. And that was the genesis of our Reinvention Plan. And so we invested meaningfully over the past couple of years to create a more stable environment, so our partners could better serve our customers. And that's led to a new low in terms of turnover. So we've made good progress there.

But more recently, what we're seeing is headwinds related to our customers, particularly occasional customers, largely as it relates to the awareness of what we have and the perception of value. And it's going to take some time to strengthen those relationships, but I'm pretty confident – very confident, actually, that as we continue to focus on relationships, particularly with our partners and our customers, it'll continue to differentiate us as we grow.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

Q

Fabulous. You talked about a little bit of the challenges with the occasional customer. In particular, last quarter, you lowered your guide for US comps flat to down low-single for the fiscal year. You're working through some of the macro as well as the company-specific headwinds. What do you see as the factors that are driving the recent slowdown? What do you see as transitory versus more permanent?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

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Well, as we shared in Q1, we started to see headwinds across really three fronts. And that was with our – the negative impact we were seeing in our business in the Middle East, and that had an impact on our business in the US, particularly with our occasional customer that tends to frequent in the afternoon. And then, of course, we saw a slower-than-expected recovery in China. And we expected those headwinds to persist into Q2, but it persisted even further than what we expected.

And on top of that, we started to see a more cautious consumer environment in the US. And in addition to that, the action plans that we had in place didn't materialize in the way we had expected. And so from that aspect, it's going to take us some time to recover. But we feel encouraged. We believe most of these are transitory in nature, but we do believe it's going to take some time. But we feel encouraged by the progress we're seeing so far with the action plans we've put into place, particularly in the US.

We launched the Summer-Berry Refreshers with Pearls in May. And it resonated well with customers and it drove afternoon growth, which was good to see. We're seeing that our integrated campaign around best offers in the app is driving more customers into our Rewards program. We're seeing growth quarter-over-quarter and year-over-year. And in addition to that, our efficiency efforts are materializing in line with our expectations.

Now it's clear that we're navigating, continuing to navigate a very complex environment with continued volatility in China. But we expected to see some benefit in Q3 from our action plans and in Q4 as well. And that's what we're seeing so far in Q3. And it's helping to counterbalance some of the continued headwinds we're seeing. And it's allowing us to see sequential revenue growth in Q3 and Q4, which is in line with the earnings guidance that we provided.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

Q

Great. So let's talk a little bit more about the action plan. You had mentioned some didn't materialize but you're starting to see a little bit of improvement. So what are the most impactful drivers that you're seeing benefits from with respect to the action plan that you laid out last quarter?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

A

I'd say it's a combination of really three areas. We've talked about we have an opportunity to address the morning daypart by improving the throughput. We have a very busy morning daypart. Almost 50% of our volume comes by 10:00 AM, and that's up a couple of points even from a few years ago. So our morning daypart gets busy and busier. And so as a result of that, we're focused on how we optimize throughput. We're increasing product availability and we're addressing the wait times and MOP.

Another factor is, we're looking at driving new demand in the afternoon through product innovation, integrated with marketing, so we can create more awareness and excitement of the offerings we have. The Summer-Berry Refresher launch was an example of that, and it resonated well with customers. And in addition to that, we're focused on demonstrating value to our customers, taking marketing as well as targeted offers to attract and retain new and existing customers into our Rewards program. And as I shared, we're seeing good success along those measures.

Now, as I said, we expect that this will provide some benefit in fiscal year 2024, and we're seeing that. And it's helping to counterbalance some of the headwinds, and it is leading to sequential revenue growth. But, again, it's going to take time to fully recover.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

Q

Great. So let's dig a little bit deeper into value, which is a key area of focus across the restaurant industry, and broadly, across consumer. You talked about increasing a bit more on the focus on value, a bit more personalized value. You're looking to increase that value messaging with both Starbucks Rewards and non-Rewards customers. So how do you assess and view Starbucks' current value proposition and how are you evolving your value strategy and see it going forward?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

A

Well, our brand demonstrates premium value for what it offers. And even in the most recent quarter, we saw that our most loyal customers said that they get value for what they get, and that was continue to be strong. We also have been very measured with our pricing actions. In last quarter, we saw that ticket increased due to pricing, but also as customers traded up to more premium and cold beverages, specifically like the Iced Lavender Matcha Tea Latte, which was a promotional offering.

But on top of that, we actually see that there's still an opportunity as it relates to value perception. And so that's where we've been focused around this integrated approach across product and marketing and very specific offers. More recently, we launched in May the very specific offers for the Rewards program. Every Monday, there's a new and targeted offer.

In addition to that, we're going to open the app for all in July and allow customers to leverage MOP that aren't in the Rewards program. That will give them visibility to the experience that MOP offers. We know with our customers today that when they leverage MOP and they have convenience and they're able to customize, it leads to habituation. So we're encouraged by that opportunity. And we're also focused on the best offers in the app really as a campaign to address customers and show them the value that they get, not only when they download but when they activate and then when they continue to increase frequency and overall spend. And so those are all the ways that we're addressing value. And like I said, we're seeing progress so far but we've got a ways to go, but we're encouraged by what we're seeing.

Lauren Silberman*Analyst, Deutsche Bank Securities, Inc.*

Q

It's great. So pricing across the industry has been elevated over the last few years. Starbucks is priced as a premium product. It always has been, though. As you enhance your value messaging, how are you thinking about your approach to price?

Rachel Marie Ruggeri*Chief Financial Officer and Executive Vice President, Starbucks Corp.*

A

Yeah. When we think about pricing, it's really about ensuring that it's value for what I get. And so our most loyal customers, like I had just said indicate that they get value for what they get. And that's coming from a combination of not only actual price, but the product and the overall marketing and the approach to how we create awareness and excitement.

In Q2, for example, when we saw some of the headwinds with our customers, we did customer intercepts. And what we heard from our customers is they said, in particular, our Gen Z and Millennial customers, who tend to skew younger and more in the afternoon. And what we heard was they want more news, more often and a broader array of offering. And so we're innovating around that, not only through coffee but through innovation in other beverages, textures, functional benefits, flavors.

And we're also innovating around the offers. So we're being more targeted with the offers we have, and we've more recently invested in a revenue management system, in a digital storyboard that will allow us over time to be able to innovate as it relates to dayparts, as it relates to inventory, as it relates to location. And that's going to continue to create the value for our customers that will create a better experience. And we know that all of that pricing and the value for what I get is related to the experience, and that's what we're focused on driving.

Lauren Silberman*Analyst, Deutsche Bank Securities, Inc.*

Q

Great. So you talked about product innovation. Starbucks is ramping up your level of product innovation, particularly in the afternoon. You've done Lavender, Spicy Refreshers, and your first innovation of texture with the boba inspired drink. Can you talk about, one, some of the opportunities that you see with food and beverage innovation; and two, some of these new products, who are you resonating most with?

Rachel Marie Ruggeri*Chief Financial Officer and Executive Vice President, Starbucks Corp.*

A

It's a little bit what I just spoke about is that we know a section of our customer base is really looking for that new news. And we'll continue to innovate in coffee because coffee is core to who we are. And I think sometimes people forget that Iced Shaken Espresso, for example, is one of our fastest growing categories. And it's coffee forward but it's in a cold platform. So we'll continue to innovate in ice, but we'll innovate in other areas. As you noted, we have a zero to low calorie handcrafted energy coming. We have sugar-free customizations that are coming, as well as a lot of plant-based offerings. That resonates technically with the younger set of customers, particularly that skew more towards the afternoon.

We're also continuing to add new variety to food. We have a new Blueberry Muffin. It's more blueberries, a more elevated muffin, but we've leveraged our scale to ensure we maintain pricing and overall cost factors, which is part of our efficiency efforts. And in addition to that, we've got an egg and pesto mozzarella sandwich. So a lot of variety for customers.

But I think along with the product innovation, we're also looking at innovating around offers because part of the overall experience is not just the product but how we bring customers in and create that excitement with the specific offers. And so we're innovating by having very exclusive SR offers. We're innovating by being more targeted in how we personalize the offer to the customer. And then we've got runway in the future with the investment that I mentioned around revenue management and digital storyboard, so a lot of opportunity there. But currently, that's how we're thinking about really bringing innovation together through both product and offers to create excitement for customers.

Lauren Silberman*Analyst, Deutsche Bank Securities, Inc.*

Q

Can you talk a little bit more about the revenue management strategy and the storyboards that you're doing?

Rachel Marie Ruggeri*Chief Financial Officer and Executive Vice President, Starbucks Corp.*

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Yes.

Lauren Silberman*Analyst, Deutsche Bank Securities, Inc.*

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What exactly is that?

Rachel Marie Ruggeri*Chief Financial Officer and Executive Vice President, Starbucks Corp.*

A

Really what it is, is it's about being able to be more personalized in the experience to our customers. So today, we are able to have a connection with customers that are in our Rewards program. And we know those customers, and we can communicate to those customers. But through an investment in revenue management in the digital storyboards, we're actually able to create a deeper connection.

We're able to leverage technology to be able to be more targeted in knowing more specifically who you are as a customer, what your tastes and preferences are, how do we attract through location offers, through daypart offers, through offers in inventory, and done so in a way that we manage our overall margin so that we're creating offers with maybe food and beverage, but in a way that's accretive to the business.

So it's really a big unlock for us not only in creating a more personalized experience for the customer, but also creating more tangible financial benefits for us as a business.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

Q

Great. Starbucks is one of the most sophisticated, if not the most sophisticated digital ecosystem in restaurants, which might be underappreciated. How much is that helping as you assess some of the headwinds and go addressing them with your consumer base?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

A

Our Rewards program is – it's a competitive advantage for us because we know when customers join the Rewards program, they increase frequency and spend. Even if they're a less frequent customer, their frequency in spend still increases when they join the program. And then, when customers leverage MOP, for example, they're increasing their spend and frequency increases even further, and it leads to more habituation. So it's a really great way for us to create kind of a stickiness with our customers. In addition to that, it's one of our best marketing levers, because we're able to communicate directly with our customers.

And over time, as I mentioned, with the investments we're making in revenue management and digital storyboards will be able to be more personalized in those experiences and offers. But we still have a lot of opportunity when we think about the Rewards program, just in terms of so many of our customers are not even aware of it. So awareness is one of our big opportunities. And that's part of what we're doing with the campaign around best offers that are in the app, but it's really the awareness, it's also the ability to be able to enter the program.

Sometimes it's challenging for customers to download or maybe there's not incentives and so we've more recently provided significant offers to think about customers when they download, to get them to activate, and importantly, to continue to activate so that we retain them. And then, we've got opportunities when we think about creating value with partnerships, for example, like our partnership with Delta and more partnerships to come is further ways to extend the experience that our customers have across a broader base of Rewards programs.

Those are all ways to create the value that bring more and more customers into the program, which benefits the customers, but it also benefits us as a business.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

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Great. You have, I think, 33 million 90-day active Rewards members. It's more than doubled over the last five years. What's the runway for growth in that program? How do you see that?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

A

I mean, when you think about – we've talked about we have over 75 million customers, occasional customer – or customers that come to us on a weekly basis. And so when you look at that universe of customers that know Starbucks, there's a significant opportunity across that customer base, which is what we're really focused on right now with our variety of efforts around product and marketing and integrated campaigns to create the value that we have across the customer base.

One big opportunity we have is as we unlock the app for all in July, as an example, we know we've had a long-standing barrier in terms of creating awareness with our customers that are not in the Rewards program. And so as we unlock the app for all and allow customers to leverage MOP outside of the Rewards program through guest checkout, through maps, through social media, it exposes them to not only the value that's in the program, but it gives them the experience that we know customers love with MOP. And we see that as an opportunity to drive approximately \$1 billion over the next three years as we open that program.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

Q

Wow. So mobile order and pay, for those that don't know, represents north of 30% of US transactions, particularly impressive. It's just limited to Rewards members. A few years ago, you unlocked the Rewards program to offer any form of payment rather than requiring customers to pre-load money. So what did you see in terms of reward membership growth once you made that change a few years ago? And how do you compare that to your expectations in terms of unlocking MOP?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

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Yeah. So in Q4 of 2020, we launched Stars for Everyone, and that was really targeted at many of our customers find entering the Rewards program had barriers. There are friction points. And one of the friction points was customers didn't want to have to preload a stored value card. And so we allowed them to pay as you go. And that actually almost doubled our membership in the time period since we've launched. So really a significant benefit for us.

And when we look at opening the app for all, it's another barrier that we're removing for customers by exposing them to the benefits that MOP offers. We know that when customers today have that convenience that comes with MOP and they're able to customize their drinks, that there is an increased habituation. So we see a lot of opportunity and that's where we've identified that we believe there'll be approximately \$1 billion that we're able to drive in net incremental revenue over the next three years.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

Q

Wow. One of the areas of focus that you've talked about is throughput, and particularly, opportunities at that morning daypart where you have so much to your business. What are some of the changes that you're making to unlock capacity at that morning daypart?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

A

Well, I would say, even in this last quarter, we were very encouraged by the progress we were seeing around the ability to unlock capacity in the morning daypart. Because over the past couple of years, we've invested meaningfully in the business over \$1 billion a year on wages, on training, on new equipment. And that's helped us

to make incremental improvements in how we are able to address the speed of service and reduce wait times. But it's been like a second of an improvement, which is actually meaningful.

As we look forward to what we call Siren Craft System, it's really the ability to be able to make a step change improvement. I mean, we're talking closer to, say, 10 to 20 seconds in what we see in our test stores. Now, as we scale that, that may change some, but we see a big opportunity. And it's really about how we address just through process. No capital required, but just through process improvements how we address bottlenecks within the busiest day part, which is our peak. And we see an opportunity to be able to optimize the way we build our beverages, we see an opportunity to optimize the way we position our partners and optimize the way we sequence our orders. And that is the unlock that drives that meaningful improvement in wait time and increases the speed of service.

And what we find is partners love it so far, which is really good, so it's a greater experience for the partners, and it's going to create a better experience for the customer. So we're encouraged by the opportunity that we see there.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

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Great. Are you still in test mode with that and how are you thinking about the timing?

[indiscernible] (00:20:20)

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

A

Well, actually, we'll have it fully rolled out by the end of this year. And like I said, there's no capital involved, which is what allows us to roll it out pretty quickly. I mean, we didn't even have this a year ago. So this is relatively new. It was an unlock as Laxman brought in the Toyota experts to really look at process improvement. And so we're able to roll it out pretty quickly. But I think the important part is we won't to see the benefits immediately because there is a significant change management. And that can't be underestimated.

So, for example, because our turnover is at a new low, which is great, that means partners are very seasoned in terms of how they prepare beverages, how they manage the peak daypart. So they're going to have to relearn how they build beverages. They're going to have to relearn how they position at peak. They're going to have to relearn how they sequence the ordering. So there's a change management involved. But we believe we'll start to see the benefits even as early as next year as we get through all of this change management.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

Q

What do you think are the factors that are supporting these very low turnover levels at the partner level?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

A

I really do believe that it's just a combination of the very focused and deliberate investments we made listening to our partners, but making the investments that they cared about and in response to what they asked for. So as we came out of COVID, we had a lot of opportunity, as I said, to strengthen those relationships. And we invested meaningfully in wages. So I know our partners earn between \$15 to \$23 with the average being around \$17.50 or

so. And you think about federal minimum wage is \$7.25, and then you have an opportunity for another \$10 just in benefits.

So there's a lot of opportunity there around wage. We've done a lot of work around staffing and scheduling to increase the number of hours per partner. So not only they're getting a higher wage but they're getting closer to the hours they need. We still have progress to make there, but we've made good improvements, and that's helping with engagement. And so that's helping with overall compensation.

And in addition to that, we've put new equipment into the operating environment, we've put new processes and practices in place and it's helped create a greater efficiency. And all of that's leading to a new low in terms of turnover. And the good news is we still have a lot of opportunity and a lot of improvements still to make. So we're encouraged by the progress so far, but we're not nearly done.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

Q

You're making a lot of process improvements and that's to come at the same time also bringing in new product innovation into the business. How are you balancing, limiting added complexity?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

A

Yeah. It's a great question because we know customers are looking for new news and a broader offering. And we're definitely ramping up – our product innovation team is being much more agile in terms of the product pipeline and we're really ramping up in terms of a lot of different new and innovative offerings across beverage and food. But we're trying to do the innovation with partners in mind. And that means sometimes it may be existing ingredients or it may be a function of a product that really resonates with the partners, so that there's pull and engagement for it. But when it's existing ingredients, it allows us to create the news, but it doesn't create added complexity to the partners. But I think as we're continuing to innovate both across beverage and food, what continues to be incredibly important is the work we're doing around throughput improvements.

So what I talked about with the Siren Craft System, as an example, because all of those are ways for us to create a better environment for our partners to serve the customers. And we know that personalization and customization is incredibly important to our customers, so too is the new news. And so we have to create the environment for our partners to serve that.

And so while it's important to be thinking about how we think about our product innovation and how it resonates with the partners, it's equally as important to think about how we create the environment to be able to receive that demand.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

Q

Great. Personalization and customization has been a theme in terms of what's driven some of the outperformance over the last few years. Do you see continued opportunities for personalization and customization? I think a majority of your beverages are currently customized.

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

A

Yes. I mean, personalization, I would say, is really a competitive advantage of Starbucks. So many people I meet have a very specific drink. I mean, we just met a woman yesterday that shared a drink that – I was like, wow, I'd have to write that down. But what it creates is it creates an experience for the customer and creates a stickiness. It's hard to make that at home and it gives a reason to come back to Starbucks.

So we are very deliberate in how we innovate, so that we're creating opportunities for customers to personalize things like the cold foams. Some of them are premium beverages. Those are opportunities for customers to be able to customize in ways that meet their tastes and preferences. And as long as we create the environment so that partners can service that customization, that balance is really incredibly important.

And then, when you think about our Rewards program, our Rewards program offers us even more opportunity to personalize not only across the offer space that I already spoke about, but in terms of the way we approach customers with opportunities. Maybe part of our new revenue management and digital storyboards is you can see that if a customer used to come in the afternoon maybe you provide some benefit for them to come in the afternoon, and maybe it's through a beverage or maybe it's through an offer, but you're personalizing the experience and the opportunity even further, so that collectively we continue to strengthen that experience. And that's really a competitive advantage.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.



Great. Cold beverage is interesting in particular. I think it's anywhere from 60% to 80% of your US business, depending on the quarter. It's always just a surprising figure. Do you see this high cold beverage mix translating to a more resilient business than the past because it's more difficult to replicate Shaken Espresso than a Hot Drip Coffee? I guess, on the other side of it, is Hot Drip Coffee, a more habitual occasion, so how do you just look at that?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.



Yeah. I think it's really important to have the balance. We have seen the growth in cold and that's really where the customer is going. And so we innovate towards cold with coffee and non-coffee beverages. And absolutely a lot of those innovations in those cold beverages are more difficult to make at home. But I think when you think about Starbucks and really who we are at the core, we are a coffee company. And we should always be first choice as it relates to coffee. And so we've been innovating around the Clover Vertica, and that will be rolled out to nearly 60% of our stores by the end of the year. And it's a way for us to continue to elevate the coffee experience.

I mean, that's what we're known for as a company. And when you think about the new system, the Clover Vertica system, it allows choice so there's – and what we hear from customers, they want convenience, they want choice, and this offers both convenience and choice. You have six different options, including a decaf all day. It's very quick, it's a great cup of coffee. And so it's an opportunity for us to be able to leverage our innovation and our knowhow to continue to elevate the coffee experience. And so I think it's really important to have that balance.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.



Great. So you're rolling out the Clover Vertica, and then you also have other elements that are within the Siren System. How much of that Siren System do you need to roll out in full versus what types of equipment can you roll out piecemeal?

Rachel Marie Ruggeri*Chief Financial Officer and Executive Vice President, Starbucks Corp.*

A

There's definitely pieces of the Siren System that we leverage today, things like the Nugget Ice, for example, which is better for our cold beverages and our blended beverages. And that's rolling out to more stores outside of – our full Siren System equipment is rolling out through renovations and new stores. But there's a lot of pieces, things like the Nugget Ice, things like the way we look at warming food or the way that we're looking at some of the components like Clover Vertica, some of the Cold-Pressed Espresso that's coming. Those are ways to be able to continue the innovation across the stores that don't have the full suite of equipment.

But I think what's important is coupling that now is this new opportunity we have with Siren Craft, which when we look at that, that allows us to create even further opportunity in terms of how we address the bottlenecks, how we increase throughput that isn't necessarily dependent on the Siren equipment. The Siren equipment is a great solve for many of our bottlenecks and our growth in the future. But I think the balance of the two is giving us a lot of opportunity.

Lauren Silberman*Analyst, Deutsche Bank Securities, Inc.*

Q

Great. Let's shift over to China. And China has been a challenging market broadly over the past few years. And within the restaurant industry, we certainly see an increasing competitive headwinds, a more cautious, value-centric consumer. Can you talk about your latest views on what you're seeing in the market near-term and just how you're feeling about your brand positioning in China?

Rachel Marie Ruggeri*Chief Financial Officer and Executive Vice President, Starbucks Corp.*

A

Well, I mean, China is definitely an increasingly competitive environment. And you see that with aggressive store openings, you see that with aggressive promotional offerings. But you are seeing – start to see a little bit of an industry shakeout. The good news is that, this is driving coffee consumption. And so coffee consumption is still in its early stages, and it's going to eventually get larger and there's going to be a natural tiering in the overall market.

And when we look at our business, we're well-positioned to continue to grow over the long term by strengthening the premium positioning that we have. And when you think about the tiering, we're well set with the capabilities and the core competencies that we've built over many, many years to be able to amplify our position in this space as the market shakes out. And so we see a long-term opportunity based on this premium positioning. Today, we still are the number one choice for the Chinese consumer in terms of away-from-home coffee and freshly made beverages, which gives us a leadership position. So we believe that we have an opportunity to continue to differentiate and can continue to leverage our competitive advantages as we grow for the long term.

Lauren Silberman*Analyst, Deutsche Bank Securities, Inc.*

Q

Starbucks really helped to, I guess, start the real coffee market in China. And I think over your history there, you've seen market shakeouts.

Rachel Marie Ruggeri*Chief Financial Officer and Executive Vice President, Starbucks Corp.*

A

Yeah.

Lauren Silberman*Analyst, Deutsche Bank Securities, Inc.*

Q

So can you just talk a little bit about what you've seen over time? There's been competitors that have come and gone.

Rachel Marie Ruggeri*Chief Financial Officer and Executive Vice President, Starbucks Corp.*

A

There's definitely been an evolution in the overall coffee market, in the coffee industry. But our core positioning and our core values really hasn't changed. What we create is an elevated coffee experience, and we create value across all of our stakeholders as we grow sustainably. And that's incredibly important. And while you are seeing increasing competition in China, particularly, in the ways that I spoke about, we continue to have a strong brand. We continue to have a very loyal base of customers. And importantly, we're seeing that our business is profitable.

So that creates a resiliency, which is incredibly important as you think about the shakeout. And so I think as long as we continue to focus on that elevated positioning, which we will do particularly as we play in the premium, I think there's opportunity for us to continue to differentiate ourselves even over the long term as the market continues to evolve.

Lauren Silberman*Analyst, Deutsche Bank Securities, Inc.*

Q

Great. And despite some of the headwinds, you're still generating extremely strong unit economics in China. So can you talk a little bit about that and just what gives you the confidence in the long-term opportunity within the market?

Rachel Marie Ruggeri*Chief Financial Officer and Executive Vice President, Starbucks Corp.*

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Yeah. Just in China?

Lauren Silberman*Analyst, Deutsche Bank Securities, Inc.*

Q

In China, yeah.

Rachel Marie Ruggeri*Chief Financial Officer and Executive Vice President, Starbucks Corp.*

A

Yeah. Really, what gives us the confidence is truly the store unit economics. So our new stores continue to be a very attractive investment. We continue to have very strong cash-on-cash returns, and they're incremental. Our new stores are incremental to the overall business. And we continue to see a lot of whitespace. So when we take the economics and we couple it with the whitespace opportunity, that's what gives us confidence. But I think what's really important at that, when we grow, we're not looking at counts. We're really looking at the economics and ensuring that we have the economics we need to continue to grow the business over the long term. And as long as we have that, then it gives us further confidence to continue to grow.

Lauren Silberman*Analyst, Deutsche Bank Securities, Inc.*

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Great. Let's talk a little bit more about the unit growth. Starbucks is one of the largest restaurant companies in the world, almost 40,000 stores globally. Last year, you grew about 6.5%, among the strongest across global large

cap restaurants. You're targeting about 7% unit growth longer term. What gives you that confidence in the global unit growth algorithm? What are you seeing in the US and China and in some of your international markets?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

A

Well, the comment I made about China really extends to even our broader portfolio is we still see very strong unit economics in our new stores, even in the US where it might seem that having over 16,000 stores – actually 16,600 when you look across company-operated and licensed. It's hard to believe that you still see those kind of strong returns, but we do. We see very attractive returns. We see over 40% cash-on-cash returns. And as a result of that, it gives us a lot of confidence to continue to grow.

And the important part is we see that these new store economics, not only are they strong, but they add incrementality to the overall business. And part of that is because we leverage AI technology to be able to determine where do we have opportunities from an overall trade area and how do we increase the overall capacity in the trade area as we open a new store. And that allows us to have a stronger portfolio overall.

When I look at the portfolio across the globe, we have a very strong and profitable portfolio. And that's driven a lot by the technology that we leverage to open stores. But we also have a very disciplined process every quarter where we review the overall unit economics to determine that we're seeing the strength that we need so that the portfolio remains strong.

When you look at that and you couple with the whitespace opportunity that we see in the US and across the globe, all of that gives us confidence to continue to open new stores as part of one of the drivers of our growth over the long term.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

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Great. So in the US, specifically, growing about a 4% per year, particularly impressive just given the 16,000-plus units. Why is that the right number? Where are you growing within the US? What type of formats?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

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We look at it as the right number because we look at the overall market holding capacity. And within that, then we leverage, like I said, our technology to be able to determine how are we going to be able to increase the overall trade area as we open a new store. And when you look at the opportunity, the opportunity is largely in more suburban and more rural areas. You see a lot of opportunity in the south. You see a lot of opportunity in some of the middle part of the United States. So lots of opportunities as you think about overall growth.

There's still opportunities even as we look at metro areas in terms of leveraging purpose-built design for our store, so maybe it's a pickup store, or it's a smaller store format in ways to be able to meet our customers where they are, but we're increasingly seeing more and more customers in these more suburban and more rural areas. And that's why we've shifted our overall strategy. But I think leveraging design principles to be able to accommodate different markets and different segments, this purpose-built design, we've got an opportunity to grow, but I would say the broader growth is really in some of these middle of America, southern parts of the United States.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

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Great. Sometimes underappreciated, but almost 40% of Starbucks locations are outside of the US and China. Given we're in Paris, and we were talking before, it's some of the most beautiful restaurant Starbucks stores I've ever seen out here, just take a moment to touch upon how the rest of the international portfolio is performing.

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

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Yeah. I think it's important to remember that even in Q2 where we had such a challenging quarter, our international segment, when you exclude China, had revenue growth and comp growth. And that was fueled by double-digit system sales that we saw in our Latin America and Caribbean business. It was fueled by continued revenue growth in Asia Pacific, despite the headwinds we're seeing in Malaysia and Indonesia. And Japan, which is our third largest market, also had double-digit revenue growth. So it speaks to the resiliency and the diversity of our broader portfolio.

And what's important is these stores also have strong unit economics. And they provide incrementality to the business. And so when you look at the store population outside of US and China, you're looking at about 15,000 stores. I mean, that's about a 6% growth year-over-year, and we still see a lot of opportunity. We just opened our 400th store in India, our 600th store in Indonesia and our 1,900th store in Korea. So that gives us a lot of confidence that we'll be able to achieve the 55,000 stores by 2030. But I couch all of that by saying that it always comes down to unit economics first and foremost. And then, with that, we have the opportunity continue to grow.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

Q

Great. Let's talk a little bit about the margin side. You've made significant progress in expanding margins. You've outlined an impressive \$4 billion in cost savings over the next four years. Where are you unlocking these efficiencies? And then, where do you see them show up in the P&L, supply chain, G&A, et cetera?

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

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So we're incredibly pleased with the progress we have around our efficiency efforts and it reinforces our triple shot strategy. So over the past year, we've seen about 200 basis points of margin expansion through both in-store efficiencies and out-of-store efficiencies. In-store efficiencies show up in store operating expense and out-of-store efficiencies show up in product and distribution costs.

And when we look at our in-store efficiencies, that's been the work we've done around creating a more stable environment in our stores. So the investments we've made in staffing and scheduling, the investments we've made in training and overall equipment improvements. That's allowed us to have to hire less partners because turnover is low, we hire less partners so that leads to favorability in benefits, favorability in training costs, and that shows up in our store operating expense.

We've also made improvements in waste. By the way, we merchandise our offerings as well as leveraging automated inventory. And then that's allowed us to create waste improvements. And then, in addition to that, we've been focused out of the store on things like sourcing and manufacturing and distribution.

And again, that shows up in our product and distribution costs. And an example of sourcing is we've looked at some of our bakery offerings. And while we're focused on quality, we leverage our scale to be able to get better pricing. And that's allowing us to create not only tangible financial benefits, but it's allowing us to still continue with the quality offering we have.

I think what's important about all of this efficiency focus, though, is not only is it leading to real tangible financial benefits and margin expansion, but it's also allowing us to unlock investment capability to be able to reinvest back into our business. And then, on top of that, it's allowing us to create a resiliency in the business, so that our earnings growth is coming from a combination of revenue growth, as well as margin expansion. And while we still have an opportunity as it relates to the revenue growth, we're encouraged by what we're seeing in terms of our ability to leverage efficiencies to drive margin expansion.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

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Great. With just about a minute left, Rachel, I'll turn over to you if there's one, two things that you want to leave investors with.

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

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Sure. Well, I would say first and foremost, I mean, we are clearly navigating a very complex and dynamic environment and as we've shared with our most recent earnings guidance, we're encouraged by the action plans we have in place, but it's going to take time for our action plans to materialize. But when I look at the long-term proposition of Starbucks and the fact that we are building for the long term, we've been a company in business for many years, we have a lot of long-term opportunity ahead of us, and we've built foundational benefits and competitive advantages over many years.

We have a strong brand, we have a portfolio of highly profitable stores, we have an increasing capability around digital, as well as around convenience. And importantly, we have a relationship with our partners and our customers that's unlike any other in the industry. And as long as we continue to invest in these competitive advantages and focus on these competitive advantages, I see the long-term opportunity for Starbucks is truly limitless.

Lauren Silberman

Analyst, Deutsche Bank Securities, Inc.

Fabulous. Rachel, thank you so much for being here.

Rachel Marie Ruggeri

Chief Financial Officer and Executive Vice President, Starbucks Corp.

Thank you. I Appreciate it.

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