

Starbucks sustained during economic crisis

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Abstract

Purpose: The purpose of this paper is to study and understand that how companies compute their financial ratios and use these financial ratios to identify company's financial situation. The company is also compared with the competitor's financial statements to identify current position in markets.

Design/ Methodology: The case study method is used to better understand the company. In this study researchers developed that how company's operations and position is effected by the great economic downfall in overall world's economy. Moreover they discussed that how they are trying to survive in markets to retain their leading position.

Findings: After considering all financial aspects researchers found that the company is no doubt badly effected with the worse economic situations but still they adopted strategies from top to operational level that keep them a right hand to sustain in market as a leader.

Suggestions: Developing advertisement strategies, international price stability, target to all economic classes and all aged persons, and diversify business rather than only beverages or confectionary item related businesses.

Keywords: Economic effects, Aggressive growth, McDonalds, Market leader, Starbucks

1. Introduction

Starbucks is the largest coffee company as the market leader. It is situated in United States, Seattle, Washington. The finest qualities of roasters, coffee are available on Starbucks restaurants. Starbucks is primarily selling coffee but other confectionary items like tea, pastries, sandwiched, beverages and other snacks. Starbucks started its business in 1971 with a small coffee store and now spread over more than twenty thousand locations across the globe. Operations are conducted now more than 150,000 employees all over the world. The company also faces some difficulties in its running during economic downturn but still they have sustained their growth and continue as market leader with the help of its experienced management and in-time successful implementation of strategies. The company's operating performance and market share under its sales can be determined as:

Financial Performance:

(All figures in Millions)

Year	Net sales	Net Earnings	Earnings per Share	Cash dividend
2013	14892.2	8.3	0.01	0.89
2012	13299.5	1383.8	1.83	0.72
2011	11700.4	1245.7	1.66	0.56
2010	10707.4	945.6	1.27	0.36
2009	9774.6	390.8	0.53	0.00

In past years due to economic downturn the company has adopted different capacitive techniques to retain its market position. As they make acquisitions by entering into UK markets. Fair-trade certificates also won by company's products in 2000 (wisegreek.org). "They also labels as Top10 businesses running in UK markets". The company started aggressive growth strategy to enhance its workplaces and operations in the whole world. The major achievements of the company are relationship with CI, initiate programs to empowering young employee, introduction of Starbucks University.

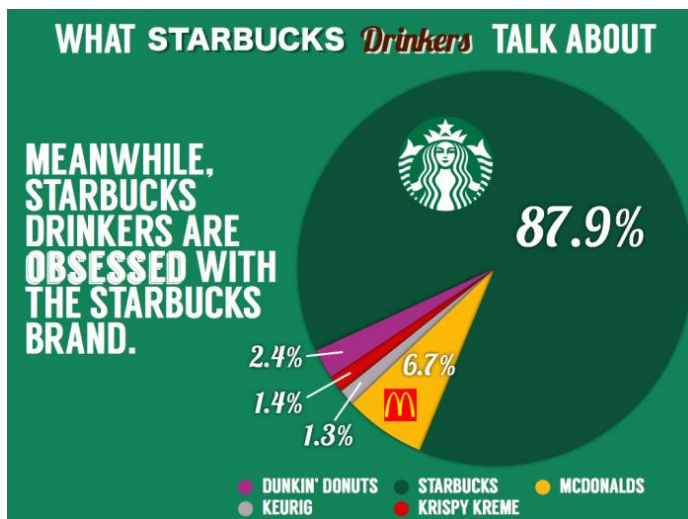
To meet its competitive edge company is focusing on new developments as motivating continuous innovation, additional benefits to face technological advancements such as access to Wi-Fi and downloads facility to its customers and mobile payments. Moreover new breakfast and lunch options are also provided by company.

2. Industry Analysis

2.1 Competitor's aspect:

As the company is the largest entity in its market. It is operating as the market leader so researchers compare the company's operations with its direct competitors. Its major competitors are McDonalds, Dunkin donuts, Yum Brands and Nestle. The major competitor to whom they are directly competes are McDonalds (coffee segment). The market capital is about more than 50 million at present (financials.morningstar.com).

Starbucks drinkers as compare to its customers are shown as figure below:



(Source: Socialmediatoday.com)

2.2 Market aspect:

However they are continuously facing difficulties these are due to change in external factors such as market conditions, economic conditions and change in government regulations. These challenges are: financial downturn in America which is badly affected over all business

sectors in the country. Starbucks had to close its a large number of stores in USA due to such crisis in 2008. According to forbs.com, Moreover on one corner the company is focusing on aggressive growth strategy in China but on the other hand they are also facing climate changes and strongly positioned tea markets in India etc (businessinsider.com). The company has added almost total estimated 338 million to the UK economy. As per the recent research round about total consumption of coffee cups in world is 2.25 billion. The production process takes place in developing countries up to 90% whereas industrialized economies survey shows more consumption of coffee. There was about 22.1 gallon of coffee per capita consumption in US for the period of 2000. From which 4% of sales was helped to get higher by visiting new customers in Starbucks. It is expected that china will be the second largest market for coffee consumption in 2015 of Starbucks by their aggressive growth strategies.

3. Financial Ratio Analysis

year	G.P Star buc ks	N.P Star buc ks	RO E Star buc ks	ROI Star bucks	Invent ory turnov er Starbu cks	Avg. Colle ction perio d Starb ucks	Asse t turn over Star buc ks	Curr ent asset Starb ucks	Liqui d asset Starb ucks	Debt to equity Starb ucks	Interes t covera ge Star bucks
2004	20.1	7.40	17.15	17.11	0.90	41.58	1.75	1.76	1.01	0.34	17.96
2005	22.0	7.76	21.60	20.34	1.30	38.49	1.86	1.52	0.76	0.31	19.33
2006	21.3	7.25	26.13	21.27	1.04	37.52	1.96	0.79	0.35	0.99	20.44
2007	23.3	7.15	29.91	20.77	1.00	36.75	1.93	0.79	0.34	1.34	19.32
2008	19.2	3.04	13.21	7.64	0.98	33.63	1.89	0.80	0.29	1.28	17.60
2009	55.7	4.00	14.12	9.89	0.90	32.55	1.74	1.29	0.59	0.83	15.30
201	57.9	8.83	28.1	23.64	1.28	37.33	1.79	1.55	0.98	0.74	44.95

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2011	57.7	10.6	30.9	26.70	1.13	33.95	1.70	1.83	1.17	0.68	55.39
		5	1								
2012	56.3	10.4	29.5	25.71	0.94	30.49	1.71	1.90	1.14	0.61	63.97
		0	1								

(Source: Starbucks.com)

The company of Starbucks here is the market leader in its industry which covers the largest part of market share in coffee industry. Here researchers compare the company's financial performance with its competitors. As they discussed Starbucks's major competitors are McDonalds, Dunkin donuts, nestle and others. Here we select McDonalds for the comparison of Starbucks.

Gross profits of both companies are fluctuating over the years however in recent years Starbucks is more stable for the increasing gross profits ratios whereas the McDonalds is showing fluctuation at every next year or a couple of years. In the case of net profits Starbucks is largely fluctuating over the years. However after a stable situation the company in 2013 got a large decline in net profit ratios of the company. However in the case of its competitors researchers find McDonald more stable in this ratio. However in 2013 it also leads McDonald's towards the decreased trend. Return on equity of Starbucks increases over the year but a sudden decline in 2008, 2009 and in last 2013. However its competitors McDonalds's return on equity is suddenly decreased in 2007 then increasing in next years. but in 2013 it is also decreased. As researchers talk about return of investment both companies are showing fluctuations in results on each next year or a couple of years. The fluctuation of Starbucks fluctuating ratios there may be reasons such as increased stores in each month. But in the great economic fall in UAE all industry declined significantly. Starbucks's strategies to make aggressive growth made its profits stable to some extent (wordpress.com).

Activity ratios are used to measure the efficiency of operations in overall business or industry. Here the inventory turnover ratios of the Starbucks showing increasing in start but a decline in 2008, 2009 were recorded. The preceding years are also showing increase turnover over the years. However McDonalds's inventory turnover is stably increasing over the years but in recent years in shows a decline. Average collection period of Starbucks and McDonald's decreasing almost over the years. it means that both companies are able to recover its debt sooner in comparison. Assets turn over explains that how much our assets are efficient to increase our sales. Starbucks asset turnover was increased in start but in subsequent years it was decreasing over each year but as compare to its competitor McDonald's is decreased, increased over the next years but in recent couple of years it again decreased.

The reason for decreasing trends of Starbucks may be that current assets are not more efficient to generate sales. Or other inefficient operations of company are also caused of decline.

Current assets of the Starbucks was increasing in start but in sudden it was declined for three years but after this they also retained their current position stable in next years. However the competitors McDonald's were fluctuating in current ratio over each next or couple of years. researchers see no significant change of Starbucks and McDonald's current asset ratio as compare to liquid assets. As sufficient to liquid asset ratio is also enable to meet current debt as well as its inventory.

This ratio shows the support of debt to attain the assets of the company. Here the ratio in case of Starbucks is fluctuating at each interval. But in comparison to McDonalds's debt to equity ratio this is increasing over the years till 2008 and then started to reduce over the next years. As they talk about the total capitalization ratio shows that how much part of debt in overall capitalization of the company. The Starbucks here again is fluctuating in all discussed years. However the interest coverage ratio of the company show either company's profit before interest and taxes are sufficient to meet the company's interest expenses over the relevant years. Here both companies Starbucks and McDonald's are fluctuating with a little year in each year and in comparison of both companies.

FINANCIAL RATIO COMPARISON

Ratios	Starbucks	McDonalds
Gross Profit	56.3	39.2
Net Profit	10.40	20.00
Return on Equity	29.00	37.00
Return on Investment	25.71	18.33
Inventory Turnover	0.95	208.95
Average Collection Period	30.49	20.34
Asset Turnover	1.71	0.81
Current Asset	1.90	1.45
Liquid Asset	1.41	1.19
Debt to Equity	0.61	1.15
Interest Coverage	63.97	16.64

4. Dupont System Of Financial Analysis

A DuPont analysis of Starbucks and its competitor McDonalds is shown in the table below.

$$\text{ROA} = \text{NPM} \times \text{TAT}$$

	Starbucks	McDonalds
Return on Assets	18	16
=	=	=
Net Profit Margin	10.40	19.82
X	X	X
Total Assets Turnover	1.71	0.81

$$\text{ROE} = \text{NPM} \times \text{TAT} \times \text{A/E}$$

	Starbucks	McDonalds
Return on Equity	29	37
=	=	=
Net Profit Margin	10.40	19.82
X	X	X
Total Assets Turnover	1.71	0.81
X	X	X
Assets / Equity	1.61	2.31

The company here shows that the competitor's return on shareholder's equity is greater than Starbucks. Here the net profit margin and leverage portion are the indicators to reduce the return on equity. Because both net profit is less and leverage is also lesser than competitor. However the usage of total asset is absolutely showing an upper trend than competitors.

The reduce on net profit is reasoned by enhancing operating expenses because of opening new stores and growth strategies. However usage of assets are more efficient can show that they are effectively managing their resources and properly utilizing for each growth to make it sustain.

4.1 Short Term Liquidity Management:

Here the Starbucks is on favourable condition with the quick ratio of 1.41 whereas the competitor is having 1.19 quick asset ratio. And it indicates the solid situation of Starbucks for the payment of its short term debt as compare to MacDonald's. Current ratio with 1.90 is also increasing trend as compare to other. It indicates the inventory was also taken efficiently and utilized effectively. This efficiency in current assets ratio almost continuous for many preceding years that means that company has sustain and consistently enjoying its liquidity position. Little decrease in ratio was observed is some years but on the whole it was consistent. A glance of current assets are given below here of Starbucks.

ITEMS YEARS	cash and cash equivalent	short term investments available for sale	short term investments for trading securities	account receivables	Inventories	prepaid expense	deferred income tax net
2004	299.1	329.1	24.8	131	422.7	71.3	81.2
2005	200.9	128.9	20.2	114.4	343	55.2	61.5
2006	312.6	87.5	53.5	224.3	636.2	126.9	88.8
2007	281.3	83.8	73.6	287.9	691.7	148.8	129.4
2008	269.8	3	49.5	329.5	692.8	169.2	234.2
2009	599.8	21.5	44.8	271	664.9	147.2	286.6
2010	1164	236.5	49.2	302.7	543.3	156.5	304.2
2011	1148.1	855	47.6	386.5	965.8	161.5	230.4
2012	1188.6	848.4		485.9	1241.5	196.5	238.7

(Sources: Starbucks.com)

Total current liabilities are given below for Starbucks:

ITEMS YEARS	accounts payable	accrued compensation and relaxed costs	accrued occupancy costs	accrued taxes	other accrued expenses	deferred revenue	current portionof long termdebt	TOTAL CURRENT LIABILITIES
2004	191.6	208.9	65.9	63	122.3	121.4	0.74	773.8
2005	169	152.6	56.2	54.9	101.8	73.5	0.72	608.7
2006	340.9	289	54.9	94	700	232	0.8	1935.6
2007	390.8	292.4	74.6	92.5	160.3	296.9	0.8	2155.6
2008	324.9	253.6	136.1	76.1	164.4	368.4	0.9	2189.7
2009	267.1	307.5	188.1	127.8	147.3	388.7	0.2	1581
2010	282.6	400	173.2	100.2	262.8	414.1		1779.1
2011	540	364.4	148.3	109.2	319	449.3		2075.8
2012	398.1				1133.8	510.2		2209.8

(Sources: Starbucks.com)

4.2 Capital Structure & Debt Management:

Starbucks shows a decrease of debt to equity ratio for the recent years (2007 to 2012). Company's long term debts and shareholder equity is given below tables:

ITEMS YEARS	deferred income tax net	long term debt	OTHER LONG TERM LIABILITIES
2004	46.7	3.6	8.1
2005	33.2	4.4	1.1
2006		2	262.9

2007	550.1	354.1
2008	549.6	442.4
2009	549.3	400.8
2010	549.4	375.1
2011	549.5	347.8
2012	549.6	345.3

(Sources: Starbucks.com)

The reason has been shown in table that long term liabilities of the company is decreasing over the recent years. This situation may be cause an attractiveness for the lenders because their credit risk has been reduced over the years.

Increase in total shareholder equity may create a possible chances for investments and attractiveness for the lenders and marketers as well. It shows that if company need funds, they can generate it form inner sources rather than borrowing for short or long term loans. This may also cause a reduction in interest payable for the company.

4.3 Profitability:

There is continuous increase in sales of company form previous last years (2004 to 2012). On the other side of cost of sales has also been increased. Operating expenses are also increasing over the years that ultimately reduced net profits of the company in early years but later in recent years it is also increased with a decreasing trend consistently.

5. Discussion

The above mentioned details related to company shows all financial aspects of the Starbucks that how they are continuously focusing on business strategies to remain as market leader in such a diverse and competitive market scenarios. However they are facing some difficulties for this challenge. First of all economic recession period in all over the country has significantly affected the company's operations. Even in 2008 they have to shut down hundreds of their stores in only in US. A large number of close stores effected company's strategic design for policies they divert towards aggressive growth policies in all countries especially in eastern countries.

China was on the first preference of company for implementation of such growth but with the passage of time they expanded towards India but not succeed remarkably because of strong positioning of tea markets and tea lovers. Moreover the lower per capita income became a hurdle for the company to grow because of its higher priced and higher quality products.

In addition to this they also have a hurdle due to warm and hot climates all around the eastern Asian countries.

But still company is growing its stores and operations. They are making acquisitions, joint ventures to get entrance in new markets and after getting strong positioning they develop their own stores for their products and services with improved quality and efficient staff.

6. Conclusion

In past years due to economic downturn the Starbucks has adopted different techniques to retain its market position. As they make acquisitions by entering into UK markets. Fair-trade certificates also won by company's products in 2000. "They also labels as Top10 businesses running in UK markets". The company started aggressive growth strategy to enhance its workplaces and operations in the whole world. To meet its competitive edge company is focusing on new developments as motivating continuous innovation, additional benefits to face technological advancements such as access to Wi-Fi and downloads facility to its customers and mobile payments at stores.

However they are continuously facing difficulties these are due to change in external factors such as market conditions, economic conditions and change in government regulations. These challenges are: financial downturn in America which is badly affected over all business sectors in the country. Starbucks had to close it's a large number of stores in USA due to such crisis in 2008. Researchers select McDonalds for the comparison of Starbucks. Gross profits of both companies are fluctuating over the years however in recent years Starbucks is more stable for the increasing gross profits ratios whereas the McDonalds is showing fluctuation at every next year or a couple of years. In the case of net profits Starbucks is largely fluctuating over the years.

As researchers talk about return of investment both companies are showing fluctuations in results on each nest year or a couple of years. The fluctuation of Starbucks fluctuating ratios there may be reasons such as increased stores in each month. But in the great economic fall in UAE all industry declined significantly. Starbucks's strategies to make aggressive growth made its profits stable to some extent.

Financial ratios showing complicated analysis for both companies. Here Starbucks results showing that company has more operating costs in each year. Inventory is more efficiently utilizing for the period in each year and more equity with lesser long term liabilities shows an attractive overview for the company's financial leverage to invest and lending more. Risks to reduce operations are covered by using aggressive growth policy in US as well as Asian countries.

7. Recommendations

Starbucks can increase market share of the non-coffee drinker if they have begun by introducing an extension of a product line targeted to this segment. Starbucks launched the summer drinks as like their competitors. Starbucks also launched our products in Asian countries like India with better strategies. Starbucks needs to expand its current international

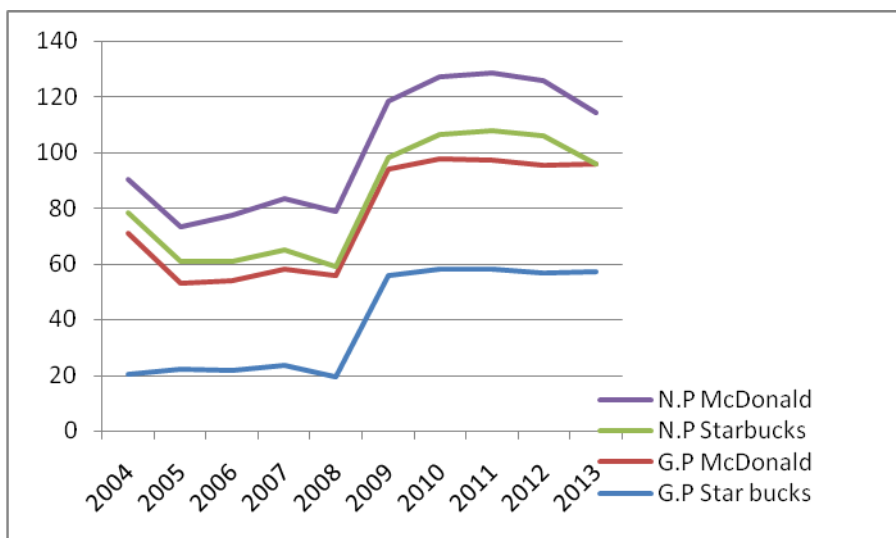
markets in order to diversify its income base. Another suggestion is to focus on quality of products and their service. In addition to this Starbucks could better succeed as a company is by diversifying its product base and offering more economical pricing for customers.

Starbucks creating a big diversity of food and beverages so that the Starbucks coffee shops become a real restaurant snack place, not only just a coffee shop. Develop other light roast coffees that will bring in customers that normally avoid Starbucks because of the “bitter taste” Of the coffee.

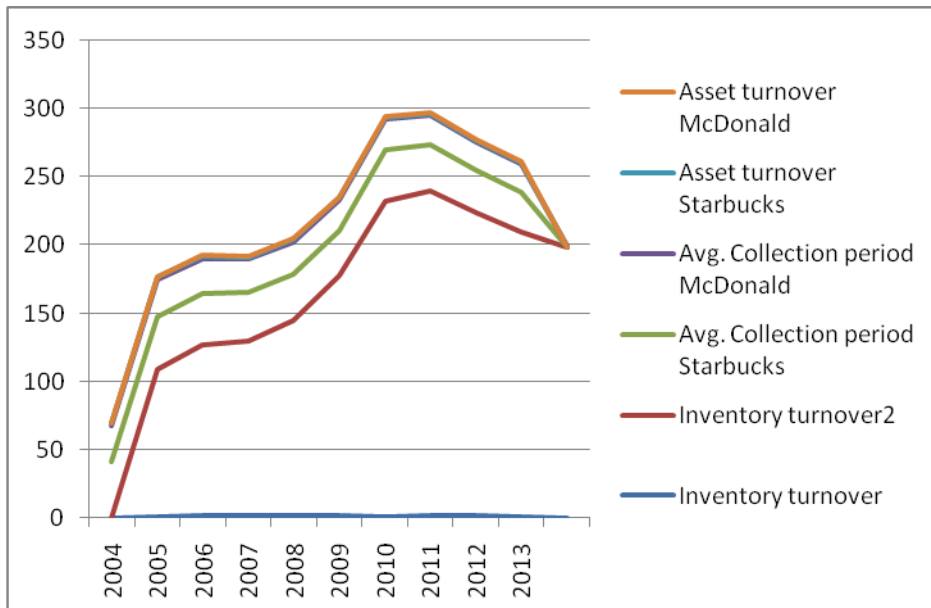
Starbucks may focus on differentiation strategy. Starbucks needs to communicate with its customers now. Starbucks also needs to create new customers and new markets to prevent the saturation of its current market segment.

8. Graphic View Of Financial Performance

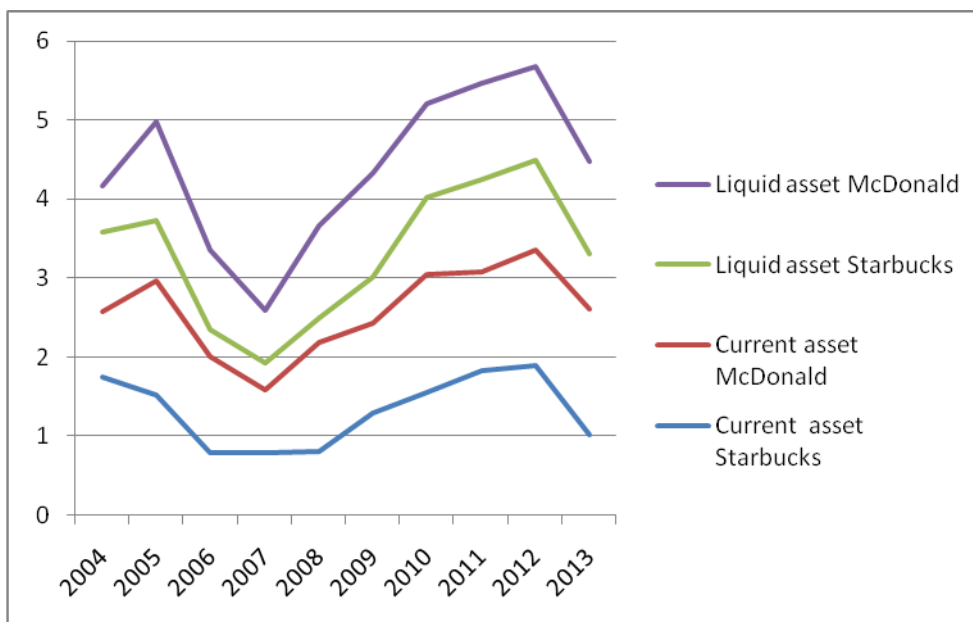
a. Profitability Analysis:



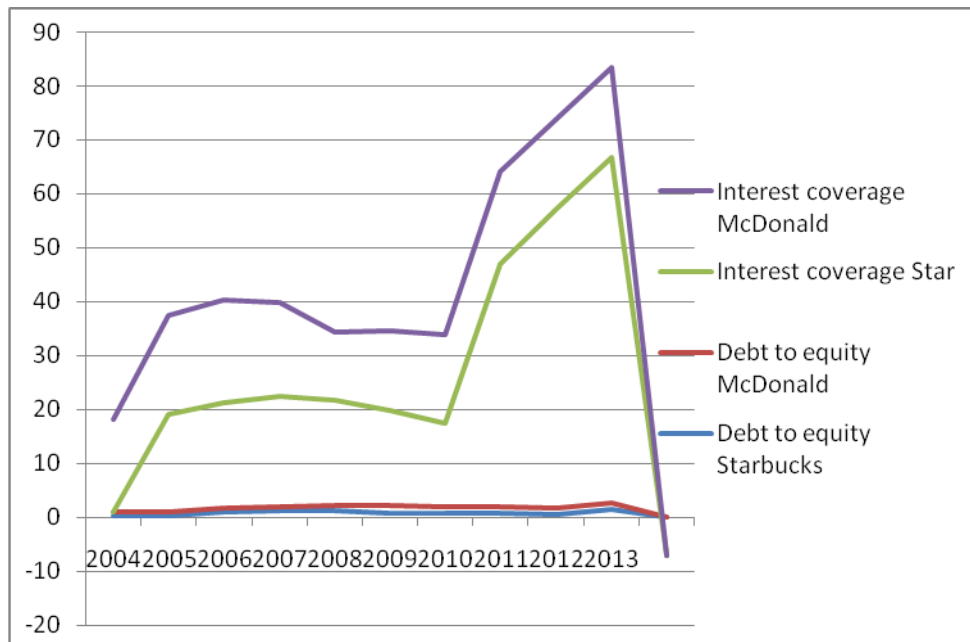
8.2 Activity Analysis:



8.3 Liquidity Analysis



8.4 Financial Leverage Analysis:



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