Starbucks | Ticker: SBUX| Initiate 1.50% Position **April 2024**

Company Overview

Starbucks Corp. engages in the production, marketing, and retailing of specialty coffee. Starbucks operates 38,587 stores worldwide with 51% company-operated and 49% licensed. U.S. and China account for 61% of the company's global portfolio with 16,466 stores in the U.S. and 6,975 in China. North America has 17,931 stores and International has 20,656. Roughly 85% of operating income comes from North America. The company operates in 86 markets.

Positives

Starbucks is a premier operator in the premium-quality coffee market. The company boasts a strong brand with significant customer loyalty. Starbucks has a robust and growing global presence that is expanding at an impressive rate. Starbucks is forecasting revenue growth between 7%-10% and guidance for earnings per share between 15%-20%.

Digital Transformation:

Starbucks is focusing on strengthening their digital footprint by expanding their Starbucks Rewards Member count. Currently it stands at 34.3 million users (up 13% over the prior year) with a targeted goal of reaching 75 million users in a few years. Their plan for growth is framed around expanding their digital offerings on their app, along with digital only promotions such as "Thurs-Yays!" There are multiple reasons to be excited about this transformation. The promotions bring in customers during off-hours, they allow for easy ordering which helps reduce customer wait times, increases employee efficiency which helps with overall store efficiency. In addition to their loyalty program, Starbucks is embracing technology in other ways to become more efficient. The company recently began rolling out their Siren System Cold Bar (think automated drink station). The company has installed its new Clover Vertica machine in over 600 stores in the United States. This new system helps with order management, reduces waste, and saves time. Technology partnerships are important at Starbucks. The company is partnering with Microsoft and using AI (artificial intelligence) to take product development and personalization to the next level. Starbucks is also partnering with Apple and Amazon to enhance the customer experience.

Expansion:

Starbucks is targeting a store count of 55,000 by 2029 (currently at 38,600). That is an average of 8 new stores per day, all bolstered by further expansion of their digital platforms. Three out of every four new store openings are planned for outside of the U.S. This growth adds to economies of scale internationally, which should increase profitability.

Triple Shot Reinvention with Two Pumps Plan:

While we might not like the name of this transformation, it is difficult to dismiss the potential for value added. This program is targeting more efficiently run stores (use of technology), cost savings of $3 billion, and reinvigorating partner culture (employees). The company recently increased hourly compensation, and coupled with a more efficient store, it creates a better working environment that will likely lower employee attrition and create a better customer experience.

Brand Loyalty:

Starbucks maintains a strong brand loyalty, making their stores a place where people want to visit. The company is offering a better in-store experience, ordering through the app, more personalized purchase suggestions, shorter wait times, electric vehicles charging stations, and free dog treats.

Financial and Management Strength:

Starbucks boasts strong store-level economics. Margins have been expanding in the face of higher wages and inflation, which is a testament to management's actions to increase efficiency. The company has the resources to adapt quickly to changing environments that their competitors might not have.

Negatives & Risks

While we believe that Starbucks has numerous, attractive opportunities in front of them, some come with a few risks. Global expansion might not be as profitable as expected, with cost savings from economies of scale not fully materializing as planned. Continued wage inflation along with the potential of unionization could also present a headwind. This is somewhat mitigated by some of the efficiencies detailed above and automation. Commodity inflation (coffee, dairy) might be difficult to entirely pass through to the customer in the current environment. The company hedges, but that offers only some protection. While we believe Starbucks offers an inexpensive luxury, a slowing economy and weaking consumer will impact sales and profitability.

Dividend Characteristics

Starbucks has an impressive dividend history. The company has 55 consecutive quarters of dividend payments and an impressive dividend growth over that period (20% CAGR). In January, the company raised their dividend 7.5, from $0.53 to $0.57 per share. The company has a 5 year dividend annual growth rate of 11%.

Conclusion

Starbucks Corporation is in a unique position to grow and focus on total shareholder return. Valuation is as cheap (compared to historic levels) as it has ever been while fundamentals are improving (sales, margins). The innovation and efficiencies that their technologies make this a compelling investment.

Current & Historical Valuations

Valuation Matric	Current	5-Year High	5-Year Low	Average	Vs. Industry
Trailing PE	24.5	213.8	16.3	51.5	1
Forward PE	20.9	37.6	16.3	28.1	.9
Price to Cash Flow	15.4	95.5	7.4	29.8	.8
Price to Sales	2.8	6.3	2.2	3.9	.9
Enterprise Value to EBITDA	14.6	38.1	13.5	20.8	.8
Enterprise Value to Sales	3.2	6.1	3.2	4.2	.8
Dividend Yield	2.5	3	1.4	1.9	1.4

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Definitions
PE (Price-to-Earnings Ratio): PE is a financial metric that measures the valuation of a company by comparing its stock price to its earnings per share. It indicates how much investors are willing to pay for each dollar of a company's earnings. Trailing refers to the past 12 months and forward is on expected next 12 months of earnings.

Book Value: Book value is the net asset value of a company, calculated by subtracting its total liabilities from its total assets. It represents the theoretical value of a company's equity if all its assets were sold, and its debts were paid off.

Cash Flow: Cash flow refers to the money that flows in and out of a business. It's the difference between the cash generated from operating activities and the cash used for investing and financing activities. Positive cash flow indicates a healthy financial position.

Enterprise Value to EBITDA (EV/EBITDA): EV/EBITDA is a financial ratio used to assess a company's overall value in relation to its earnings before interest, taxes, depreciation, and amortization (EBITDA). It provides a more comprehensive view of a company's value, accounting for its debt and other financial factors.