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CLAREMONT MCKENNA COLLEGE

DOES A CHANGE IN A LOGO AFFECT THE VALUE OF THE BRAND? THE CASE OF STARBUCKS

SUBMITTED TO
PROFESSOR MARC MASSOUD
AND
DEAN GREGORY HESS

BY BRITTANY ISOBE

FOR
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1. Introduction

When the first Starbucks opened in 1971, not even the founders expected that just two decades later, it would become one of the strongest international corporations. Starbucks has experienced unprecedented growth and unfathomable success. The company grew from 17 stores in the company's founding years to approximately 17,000 stores across 55 countries just 40 years later. According to the corporate website, the Starbucks mission is "to inspire and nurture the human spirit – one person, one cup, and one neighborhood at a time".

In order to fulfill their mission statement, Starbucks has to mold their company to align with the ever-changing consumer interests. Starbucks has continued to use its logo as the symbol of change in the company's product base. Over the years, Starbucks's brand name has consistently strengthened and was a determinant factor in the company's unparalleled success. The corporation's first major logo change in 1987 reflected the move away from a main-street coffee shop and into a more modern espresso bar that offered a broader array of products. The company's second major logo change occurred in 1992 when Starbucks had their initial public offering on the NASDAQ stock exchange. Finally, this thesis will examine the impacts of Starbucks most recent logo change in 2011, and will conclude that better accounting methods must be created to quantify the value of a strong brand like Starbucks.

¹ "Year in Review: Fiscal 2011." *Starbucks Global Responsibility Report – Goals and Progress 2011*. Starbucks Corporation. Web. 2 Feb. 2012. http://assets.starbucks.com/assets/goals-progress-report-2011.pdf>.

² Starbucks Corporation. "Our Mission". *Starbucks Home* Page. 28 Feb 2012. Web. http://me.starbucks.com/en-US/ About+Starbucks/Mission+Statement.htm>.

³ Schultz, Howard, and Joanne Gordon. *Onward: How Starbucks fought for its life without losing its soul.* New York, NY: Rodale, 2011. 1-11.

2. A History of the Starbucks Corporation

2.1 The Beginning

The first Starbucks Coffee Tea Spice opened in Seattle's Pike Place Market on March 30, 1971 by three partners: Jerry Baldwin, Zev Siegel, and Gordon Bowker⁴. They were inspired by Alfred Peet (owner of Peet's Coffee and Tea) to sell high-quality coffee beans and expose people to freshly brewed coffee; they learned proper bean-roasting techniques from mentor Alfred Peet.⁵ These three men shared a love of fine coffees, exotic teas, and were driven to form a clientele in Seattle, similar to what had emerged with Peet's in San Francisco.⁶

The name of the company was taken from Moby Dick – the great American Novel that chronicles the adventures of the wandering sailor Ishmael. The first name proposal, Pequod – the name of the whale ship – was rejected by one of the co-founders. As a result, the company was named after the first mate on the Pequod, Starbuck. Starbuck was a thoughtful and intellectual Quaker from Nantucket, but more importantly, Starbuck was a coffee-lover. Since they believed the name evoked the romance of the high seas and seafaring tradition of the early coffee traders, they designed the company's

⁴ "Starbucks Company Timeline." Starbucks Corporation, Jan. 2010. Web. 5 Feb. 2012. http://news.starbucks.com/images/10041/StarbucksCompanyTimeline-JAN2010.pdf.

⁵ Schultz, Howard, and Dori Jones. Yang. *Pour Your Heart into It: How Starbucks Built a Company One Cup at a Time*. New York, NY: Hyperion, 1997. Print.

⁶ Bussing-Burks, Marie. *Starbucks*. Santa Barbara, CA: Greenwood, 2009. 1-9. Print

⁷ Fellner, Kim. Wrestling with Starbucks: Conscience, Capital, Cappuccino. New Brunswick, NJ: Rutgers UP, 2008. 10-14. Print.

logo with a two-tailed siren encircled by the store's name to evoke the romantic mysteriousness of the coffee.⁸

By the early 1980s, the company had four Starbucks stores in Seattle that reported yearly profitable results. When Zev Siegel left the partnership, Jerry Baldwin became the everyday manager and the CEO while Gordon Bowker was still involved as the owner but focused on other interests. In 1981, Hammarplast Vice President and general manager of U.S. operations, Howard Schultz, visited Starbucks in Seattle, after realizing that Starbucks was placing larger orders for a particular drip coffeemaker than retail giant Macy's. When he first entered Starbucks the powerful and pleasant aromas of the coffee beans and the wall displaying the coffee took his breath away. 10 And after his first cup of full-flavored, dark-roasted coffee; he was hooked. Schulz scheduled a meeting with Baldwin and Bowker to talk about Starbucks and was impressed by their knowledge of coffee, commitment to providing high-quality products, and passion for teaching customers about dark-roasted coffees. Starbucks bought the finest Arabica coffees and used meticulous dark-roasting processes to extract the full flavors of the coffees. The company's differentiating feature was top-quality, fresh-roasted, whole-bean coffee. Starbucks wanted to allow its customers to appreciate fine coffee. The brand built customer loyalty cup by cup and relied on word-of-mouth to attract customers. 11

On his trip back to New York, Schultz was determined to work for Starbucks; he was excited by the passion and authenticity of the company. Starbucks was nervous about

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⁸ Fellner, Kim. *Wrestling with Starbucks: Conscience, Capital, Cappuccino*. New Brunswick, NJ: Rutgers UP, 2008. 17-20. Print.

⁹ Schultz, Howard, and Joanne Gordon. *Onward: How Starbucks fought for its life without losing its soul.* New York, NY: Rodale, 2011. 3-7.

¹⁰ Schultz, Howard, and Dori Jones. Yang. *Pour Your Heart into It: How Starbucks Built a Company One Cup at a Time*. New York, NY: Hyperion, 1997. Print.

¹¹ Bussing-Burks, Marie. Starbucks. Santa Barbara, CA: Greenwood, 2009. 9-29. Print

hiring Schultz because he was from New York and did not fully align with the company's principles. He was set on franchising the Starbucks enterprise throughout America. Schultz was so convinced that Starbucks had endless potential that he offered to take a salary cut in exchange for a stake in the company's equity. In the spring of 1982, Schultz pitched his idea of expanding Starbucks to the owners. Baldwin decided to not hire Schulz as the head of marketing because geographic expansion of the company was a risky maneuver and enfranchisement was not part of the company's original vision. Schultz fought back and worked to reverse their decision; the next day, Baldwin called Schultz and notified him that he had become the director of marketing and manager of the retail stores. 13

When Schultz visited Italy, he fell in love with the Italian coffee bars in Milan and was determined to introduce America to the communal traditions of the Italian. He was impressed with the charisma of the baristas, counter workers, the vibrant atmosphere in the espresso bars, and the delicious caffe lattes. Schultz tried to implement his brilliant idea of espresso bars by proposing that Starbucks should serve fresh-brewed coffee, cappuccinos, and espresso in addition to their current products. He believed that recreating the espresso-bar culture in America would give Starbucks a differentiating factor. The market for a meeting place that offered a delicious cup of coffee in a relaxed atmosphere was definitely available. However, Baldwin and Bowker did not approve of Schultz's proposition; they did not want Starbucks to deter from their core purpose of a coffee store. About a year later, Schultz was able to convince Baldwin to build an

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¹² "Starbucks Corporation," *Hoover's Company Profile*, 2002, pg. 1-6.

¹³ Gilbert, Sara. *The Story of Starbucks*. Mankato, MN: Creative Education, 2008. 6-8. Print.

¹⁴ Fellner, Kim. Wrestling with Starbucks: Conscience, Capital, Cappuccino. New Brunswick, NJ: Rutgers UP, 2008. Print.

espresso bar in a Starbucks. In April of 1984, the sixth Starbucks was opened; it was the first Starbucks to serve caffe lattes. After two months had passed, the little 300 square foot espresso bar was serving about 800 customers a day. While the lines for the espresso bar out the door, Baldwin strongly believed the espresso bar was a distraction to Starbucks' core business.¹⁵

Schultz, frustrated with the restrictions from Baldwin and Bowker, left Starbucks to start his own coffee company called II Giornale in 1986, which resembled an Italian coffeehouse. Baldwin ironically, was Schultz's first investor and invested \$150,000 of Starbucks' money into Il Giornale. Bowker was Schultz's part time consultant and Baldwin was the director of the new company. ¹⁶ Schultz worked hard to present his proposition to 242 potential investors, but only 25 investors agreed to pitch in. The other investors believed that coffee was a basic commodity and his business had no comparative advantage; but they were wrong. In April 1986, the first Il Giornale store opened. The store was 700 square feet, full of Italian décor and contained no chairs. At first, customers detested the opera music and Italian menus, but after a few accommodations, the coffee-bar was a hit. After six months, Il Giornale was serving more than 1,000 customers a day and their speedy service proved to be a competitive advantage. Schultz started to open more stores and eventually had three stores whose sales were equal to \$1.5 million per year. ¹⁷ In March 1987, Baldwin and Bowker wanted to sell Starbucks and the entire operation because they were burned out. Schultz immediately seized the opportunity and acquired Starbucks on August 18, 1987 for \$4

¹⁵ Bussing-Burks, Marie. Starbucks. Santa Barbara, CA: Greenwood, 2009. 1-15. Print

¹⁶ Ibid., 17-19.

¹⁷ Ibid., 19-21.

million. This is when Howard Schultz became the President and Chief Executive Officer of Starbucks Corporation. He was determined to turn the coffee roasting establishment into a nationally recognized coffee shop chain.¹⁸

To represent the merger of Starbucks and II Giornale, Schultz had a new logo created. He decided to let go of II Giornale because Starbucks already had an impressive reputation for high quality and established a loyal customer base. ¹⁹ The brown Starbucks logo was replaced by II Giornale's green color. Also the Starbucks stores were remolded from its nautical theme to resemble an Italian Espresso Bar. Starbucks had transformed into an espresso bar that specialized in retail coffee-beans. Schultz was determined to turn Starbucks into a national brand that not only served the highest quality of coffee, but created a "Starbucks Experience." He wanted Starbucks to be people's "third space"; a place of community and a place for well needed alone time. Starbucks became an affordable luxury over the years and the Starbucks Experience was a personal connection that slowly became an affordable necessity. ²⁰

Schultz managed to form strong relationships between the management and employees and was able to spearhead the opening of new stores in Vancouver and Chicago²¹. Surprisingly, Starbucks' entrance in Chicago was not a smooth transition. The first Chicago store opened the same day the market crashed on October 1987. At first the Chicagoans did not appreciate the dark-roasted coffee which resulted in a low customer count in the four Chicago stores. Also, it was costly for the Chicago stores to supply fresh

¹⁸ Gilbert, Sara. *The Story of Starbucks*. Mankato, MN: Creative Education, 2008. Print.

¹⁹ Moore, John. *Tribal Knowledge: Business Wisdom Brewed from the Grounds of Starbucks Corporate Culture*. Chicago, IL: Kaplan Pub., 2006. 65-71. Print.

²⁰ Michelli, Joseph A. *The Starbucks Experience: 5 Principles for Turning Ordinary into Extraordinary*. New York: McGraw-Hill, 2007. 11-15. Print.

²¹ "Our Company." *Starbucks Coffee Company*. Starbucks Corporation. Web. 11 March. 2012. http://www.starbucks.com/about-us/company-information>

coffee to their consumers out of the Seattle warehouses. The Chicago Starbucks stores were not profitable until 1991, due to an increase in prices and customer base. Schultz then decided to expand into Portland and California and increased the count of Starbucks stores to 17. The company decided to open a store in Los Angeles because of the city's trendsetter status and cultural connections to the world. Interestingly enough, The Los Angeles Times named Starbucks coffee the best coffee in America even before the first L.A. store opened.²²

When deciding where to open the next Starbucks store, the executives looked at Starbucks mail-order operation to see where the majority of customers were located. In 1988, Starbucks produced its first catalog to help expand its mail-order business.²³ The sales started to continually increase as the brand name and reputation started to formulate a loyal customer base. In addition to this business opportunity and a total of 33 Starbucks stores, Starbucks offered full health benefits to both their eligible full- and part-time employees. In 1991, Starbucks becomes the first privately owned United States Company to offer a stock option program that also applied to part-time employees.²⁴

2.2 Going Public

It was not until June 1992 that Starbucks released its initial public offering; they had one of the most successful IPOs of the year. In becoming a public company,

²² "Our Company." *Starbucks Coffee Company*. Starbucks Corporation. Web. 11 March. 2012. http://www.starbucks.com/about-us/company-information>

²³ "Starbucks Corporation," Standard & Poor's Corporate Descriptions. April 27, 2002, 1-8.

²⁴ Moore, John. *Tribal Knowledge: Business Wisdom Brewed from the Grounds of Starbucks Corporate Culture*. Chicago, IL: Kaplan Pub., 2006. 3-7. Print.

Starbucks was able to broaden its mission and expand its network of stores. Between 1992 and 1994, the company focused on store expansion across the United States, increasing the number of domestic locations from 165 to 425. Starbucks was very deliberate in identifying top retail sites for potential stores. Comprised of the best real estate team in the coffee-bar industry and developed a sophisticated system that allowed them to identify the best store locations on the most popular city blocks. The company's track record for successful store location was almost flawless; only two sites were closed out of the 1,500 site chosen. Starbucks designed a large city as the "hub" which hosted a team of professionals to aid in the opening for about twenty stores hub during the first two years. Once the stores opened throughout the hub, additional stores were opened in smaller regions and referred to as "spoke" areas. In 1995, the new stores generated about \$700,000 in revenue during their first year. In 1993, Starbucks opened a roasting plant in Kent, Washington and in 1995 they opened a roasting facility in York, Pennsylvania.

Schultz constructed an elaborate six-month opening schedule to ensure that each Starbucks store accurately conveyed the company's image and character. Each store was custom-designed; assuring that no two stores looked exactly alike. Schultz wanted a Starbucks store to represent an authentic coffee experience that paid tribute to the artistry of espresso. The "stores of the future" project team developed four store designs that symbolized the four stages of coffee making: growing, roasting, brewing and aroma.

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²⁵ Simon, Bryant. *Everything but the Coffee: Learning about America from Starbucks*. Berkeley: University of California, 2009. 121-140. Print.

²⁶ Fellner, Kim. Wrestling with Starbucks: Conscience, Capital, Cappuccino. New Brunswick, NJ: Rutgers UP, 2008, Print.

²⁷ Schultz, Howard, and Dori Jones. Yang. *Pour Your Heart into It: How Starbucks Built a Company One Cup at a Time*. New York, NY: Hyperion, 1997. Print.

Each stage had a unique color palate and lighting scheme. ²⁸ By defining each stage as template, store-opening costs were drastically cut and it was ensured that each store evoked the romance of the coffee and displayed the company's passion for the coffee. The project team ensured that the new store locations in areas of high-traffic and highvisibility. When designing the store, the concept of "everything matters" applied. Every little detail had to be exactly right to meet the expectations of the Starbucks brand name; Starbucks was not all about the coffee, but a lifestyle.

The mail-order catalog was now distributed six times a year and included a wider variety of products: coffee, candies, pastries, and coffee-making equipment. Starbucks also created an electric store on the Internet to adapt to the changing consumption patterns.²⁹

Starbucks has capitalized on the company's strong brand name over the years. In 1994, PepsiCo and Starbucks entered a joint venture to mass distribute cold coffee drinks through Pepsi. Starbucks was able to move into more mainstream markets with this joint venture. Previous attempts by other beverage companies to enter the cold coffee market received poor reception from consumers. Starbucks first attempt at producing a cold coffee beverage called Mazagran flopped. While discussing the failures of Mazagran, Schultz had the idea to develop a chilled version of the Starbucks Frappuccino. This proposition excited Pepsi executives because the Frappuccino blended beverage was an extraordinarily popular drink when first introduced in the summer of 1995. The response to the newest Starbucks product was phenomenal. In September 1996, the joint venture

²⁸ Schultz, Howard, and Joanne Gordon. Onward: How Starbucks Fought for Its Life without Losing Its Soul. New York, NY: Rodale, 2011. 106-124. Print.

29 "Starbucks Corporation," Standard & Poor's Corporate Descriptions. April 27, 2002, 1-8.

between Pepsi and Starbucks yielded three bottling facilities to produce the ready-to-drink Frappuccino, which enabled increased distribution. By the end of 1997, the sales of Frappuccinos reached \$125 million and achieved a national supermarket penetration of 80 percent.³⁰

In addition to Starbucks' joint venture with Pepsi, Starbucks partnered with Dreyer's Grand Ice Cream in 1995 to supply coffee extract for Dreyer's new line of coffee ice cream; the new product was sold under the Starbucks brand name. The Starbucks ice creams hit supermarket shelves in April 1996 and by July; Starbucks coffee-flavored ice cream was the top-selling super premium brand in the coffee ice cream segment. In addition to ice cream pints, Starbucks also created frozen Frappuccino ice cream bars. Starbucks entered into other joint ventures with Jim Bean and Kraft. Starbucks' partnership with Jim Bean resulted a Starbucks coffee liqueur and Kraft helped to design a line of specialty coffees strictly for supermarket shelves. In 2001, there were about 18,000 U.S. supermarkets that carried Starbuck's whole bean and ground coffees.³¹

Along with these joint ventures with varying established companies, Starbucks entered licensing agreements in areas where they were previous not able to open store locations. Starbucks' biggest contract with Marriott Host International, allowed Marriott to operate Starbucks retail stores in airports. In 1991, Starbucks opened its first licensed airport store at Seattle's Sea-Teach International Airport; the store was met with

³⁰ Starbucks. 1997 Annual Report. Seattle, WA: Starbucks Corporation, 1997. Starbucks Investor Relations: 1997 Annual Report. 1997. 19 March 1997 http://investor.starbucks.com/phoenix.zhtml?c=99518&p=irol-reportsAnnual

³¹ Starbucks. *1996 Annual Report*. Seattle, WA: Starbucks Corporation, 1996. *Starbucks Investor Relations: 1996 Annual Report*. 1996. 18 March 1996 http://investor.starbucks.com/phoenix.zhtml ?c=99518&p=irol-reportsAnnual

immediate success.³² Starbucks then entered contracts with Aramark Food and Services to place Starbucks on university campuses. Starbucks created specialty sales groups which focused on providing coffee products to restaurants, airlines, hotels, hospital, business offices, and country clubs, further expanding their customer base. Starbucks created an agreement with United Airlines to serve Starbucks coffee on all United flights. To ensure the quality of the coffee and not damage the company's brand name, Starbucks wrote detailed procedures so there would be quality control on the coffee-making procedures. With this new contract, Starbucks became the supplier to the 20 million passengers who flew United Airlines each year. In addition to these contracts, Starbucks arranged to supply an exclusive coffee blend to Nordstrom's that was only available at Nordstrom stores, to manage coffee bars in Barnes & Nobel book stores, and to create coffee shops in some California Wells Fargo banks.³³

After dominating coffee markets in the United States, Starbucks was looking to expand nationally. They created a strategy for international store expansion that paralleled its domestic store expansion. In order to manage the international aspect of the company, a subsidiary was created and referred to as Starbucks Coffee International (SCI). In 1996, Starbucks opened stores in Japan and Singapore which boosted the global store location totals to 1,015. The response to the opening of the first international coffeehouse in Japan was extremely positive. SCI not only focused on only serving high-quality Arabica coffees to international customers, but guaranteed that each new store represented a lifestyle that was committed to Starbuck's mission statement of inspiring

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³² Simon, Bryant. *Everything but the Coffee: Learning about America from Starbucks*. Berkeley: University of California, 2009. 169-175. Print.

³³ Fellner, Kim. Wrestling with Starbucks: Conscience, Capital, Cappuccino. New Brunswick, NJ: Rutgers UP, 2008. Print.

the human spirit. Starbucks international expansion was successful because they did not spread themselves too thin; they made sure they developed clout in one area before looking to expand elsewhere. Eventually, however, Starbucks stores opened at such a rapid pace, that the quality of these new stores was becoming increasingly poor.³⁴

In addition to Starbucks global expansion, Starbucks made their first commitment to the community by creating the Starbucks Foundation. At first, the Starbucks Foundation focused on funding U.S. and Canada literacy programs, but it has now evolved into an organization that supports multiple communities through its global efforts. Starbucks wanted to be the company that makes a difference in the world and a company that their customers could be proud to be affiliated with.

After focusing on store expansions between 1995 and 1996, the company returned to an aggressive acquisition strategy. In 1998 Starbucks acquired Tazo, a tea company based in Portland, Oregon. This acquisition allowed Starbucks to diversify its products and adapt to the public's desire for healthy products. Schultz said, "This partnership now positions Starbucks to provide the very highest quality tea and tea-based beverages through all of our channels of distribution. Tazo also brings to Starbucks creativity and focus on tea that will lead us into new and exciting growth opportunities." The CEO of Tazo wanted Tazo to reinvent tea; similar to how Starbucks reinvented coffee. Tazo's product line consists of filter bags for hot teas, ready to drink Tazo tea and juice beverages, and organic Tazo Chai concentrate, which was later combined with Starbucks

³⁴ Simon, Bryant. *Everything but the Coffee: Learning about America from Starbucks*. Berkeley: University of California, 2009. 179-182. Print.

Corporate Social Responsibility FY01 Annual Report," Starbucks Coffee Company, February 2002. 26.
 Schultz, Howard, and Joanne Gordon. Onward: How Starbucks Fought for Its Life without Losing Its Soul. New York, NY: Rodale, 2011. 231-242. Print

Coffee to make the famous Chai Latte. Starbucks hoped to attract a new customer base with this healthier product line. ³⁷

In addition to this acquisition, Starbucks acquired Seattle Coffee Company, which includes Seattle's Best Coffee and Torrefazione Italia coffee brands, in 2003. In the following years, Starbucks acquired Ethos water, Coffee Equipment Company, and the Clover brewing system. The Clover brewer, a hybrid between a French press and vacuum pot, caught Schultz's attention during his visit to an independent coffee shop. Schultz thought the Clover made an excellent cup of brewed coffee and would create an unbeatable partnership with the Pike Place Roast; elevating the consumers' coffee experience. The Clover brewer added a personal touch and a level of theater to every cup of brewed coffee. This acquisition displayed that Starbucks refocused on its core mission: producing high quality coffee.³⁸

In 2000, Schultz, the current CEO of Starbucks, transitioned into the position of chairman so that he could focus on the company's global expansion and less on day-to-day activities.³⁹ Orin Smith, who was the Vice President and CFO in 1990, was promoted to President and Chief Executive Officer in 2000. Starbucks had already opened 3,501 stores across the world and had 525 store locations outside of the United States. As the chairman of Starbucks, Shultz ensured that values of new international partners aligned with the company and that the Starbucks' brand was accurately and consistently displayed all over the world. During his chairmanship, he opened stores in Dubai, Hong

³⁷Corporate Social Responsibility FY01 Annual Report," *Starbucks Coffee Company*, February 2002. 29. ³⁸ "Starbucks Company Timeline." *Starbucks Coffee Company*. Starbucks Corporation, Jan. 2010. Web. 2 Feb. 2012. http://www.starbucks.com/blog/starbucks-receives-green-energy-accolades-from-the-epa/1160>. ³⁹ Company to Social Boundary Company to

³⁶ Corporate Social Responsibility FY01 Annual Report," *Starbucks Coffee Company*, February 2002. 34.

Kong, Saudi Arabia, Australia, Paris, Bahamas, Brazil, Egypt, Ireland, Jordan, Northern Ireland, and Romania. In 2001, Schultz announced that Starbucks was giving full- and part-time "partners "equity in the company to the Japan Starbucks, the first store located outside of the United States and Canada. This offering gave partners a sense of pride in the company and reiterated that Starbucks respected its employees. After all, without the passion and hard work from the partners, the company would not be as successful.⁴⁰

2.3 A New Millenium: Corporate Responsibility

One of Starbuck's important advancements under Smith's leadership was its formal commitment to social responsibility. By the late 1990s, a company's social responsibility was a key factor in determining its leadership in the marketplace. People wanted to buy a product from a company they respected and trusted and public awareness of global issues emerged and affected customers' tastes. The public started to care about the environment and was truly interested in how company's manufactured their products. Between 2000 and 2005, Starbucks committed more than \$47 million to the local communities all around the world to support many efforts; Jumpstart, relief from the September 11 terrorist attacks, 2004 South Asian tsunami, and Hurricane Katrina. 41 The company partnered up with Global Green USA to raise the world's environmental awareness. Also, when Starbucks acquired Ethos Water in 2005, the company agreed to honor Ethos' mission to enhance access to drinkable water for children all over the world.

Ibid.

⁴⁰ "Starbucks Company Timeline." *Starbucks Coffee Company*. Starbucks Corporation, Jan. 2010. Web. 2 Feb. 2012. .

The company has tried to lessen its carbon footprint by using renewable energy and other conservation efforts and reducing water consumption.⁴²

Starbucks took concrete steps to ensure that they were buying ethically sourced premium coffee. In 1999, a partnership was formed with the Conservation International, which focused on promoting sustainable coffee-growing performances. Starbucks also established a licensing agreement with Fairtrade advocates, licensing their coffee as Fairtrade certified in the United States and Canada. ⁴³ The Fairtrade certification strives to enhance the livelihood of small producers by allocating a minimum price and offering them a connection to the global market. Starbucks agreed to "buy one million pounds of Fairtrade certified coffee",44 which resulted in the company being the largest supporter of Fairtrade green coffee beans. In addition to this agreement, Starbucks worked with Conservation International to introduce ethical coffee-sourcing guidelines called C.A.F.E; this ensured that the coffee Starbucks bought was ethically grown and properly traded. All of Starbucks' coffee suppliers had to comply with these guidelines and humanitarian standards. The economy has changed and consumers are more sensitive and demanding; they still want a delicious cup of Joe, but they expect it to support Fairtrade certified coffee, the well-being of employees, and be in a recyclable cup. 45 Starbucks coffee is more than a cup of coffee, it represents the consumer's experience with the coffee and the process that took to make the coffee. This cup of coffee represents trust;

⁴² Bussing-Burks, Marie. *Starbucks*. Santa Barbara, CA: Greenwood, 2009. 31-49. Print

⁴³ Packard, Ben. "Sustainability Practices Presentation," National Recycling Coalition Conference, January 16, 2001

⁴⁴ Schultz, Howard, and Joanne Gordon. *Onward: How Starbucks fought for its life without losing its soul.* New York, NY: Rodale, 2011. 20. ⁴⁵ "Spilling the Beans on the Coffee Trade," *The Fairtrade Foundation*. March 2002. 18 – 21.

successful brands require trust, trust that the company is developing products that have similar values to a model citizen.⁴⁶

After five years had passed, Smith stepped down from CEO and the company's outstanding shares shot up. Smith was succeeded by Jim Donald, who was first integrated into Starbucks in 2002 as the Director of North America operations; he embodied the company's values and effortlessly formed relationship with everyone in the company. Under Donald's leadership, the company penetrated the entertainment industry. The produced Ray Charles's *Genius Loves Company* with Concord Records; this CD won eight Grammy Awards and named Album of the Year. There were a total of 3.25 million copies sold in the United States; about 25 percent of the CDs were sold in the Starbucks retail stores.⁴⁷

The relationship between Donald and Schultz was strained because they did not see eye to eye on the company's future. Donald was focused on growing the company one store at a time, instead of one cup at a time while Shultz noticed cracks in the company's foundation. Starbucks was not providing customers the "Starbucks Experience." They thought that opening more stores would continue to propel the company's success, but they did put in the time and effort required to make them profitable. Schultz recognized that while the store designs were sleek and streamlined, they were missing their souls; as more stores opened, the absence of signature Starbuck's traits became more apparent. Schultz wanted to revitalize the Starbucks Experience. In 2006, Starbucks' success stagnated and the amount customers were spending in stores

⁴⁷ Bussing-Burks, Marie. *Starbucks*. Santa Barbara, CA: Greenwood, 2009. 105-121. Print

⁴⁶ Champniss, Guy, and Vila Fernando. Rodes. *Brand Valued: How Socially Valued Brands Hold the Key to a Sustainable Future and Business Success*. Chichester, West Sussex: Wiley, 2011. 127-28. Print.

decreased. The traffic in stores drastically fell by the summer of 2007 and at the end of that year, Starbucks' stock dropped 42 percent. The Starbucks Experience had diluted and the brand was beginning to saturate.⁴⁸

In addition to the company's unsuccessful rapid expansion, their problems were compounded with the recession. Starbucks' sales were in free fall. With the crumbling economy, consumer tastes and priorities changed; people became cost-conscious and more environmentally and ethically concerned. In addition to these changes, the digital revolution evolved and different types of media emerged. The Internet and social media instantaneously documented a company's every move and required a company to rethink their marketing strategies. The emergence of technological inventions redefined relationships and how people interacted.⁴⁹

By 2008, it looked like the Starbucks empire would topple. However, Schultz, who had stepped down to chairman in 2000, returned to Starbucks as the CEO and overseer of daily operations. Before the 2008 fiscal year annual report was printed, Schultz edited the company's letter to shareholders. He wrote about his new vision for Starbucks and announced that he would be coming back as the President and CEO of Starbucks. Schultz was determined to transform the company by focusing on its original core values. He stated:

"We believe that success is not an entitlement and that it has to be earned every day. We do not embrace the status quo and constantly push for reinvention. This is a consistent long-standing business philosophy to ensure we provide our customers the uplifting experience they have come to expect."

⁴⁸ Michelli, Joseph A. *The Starbucks Experience: 5 Principles for Turning Ordinary into Extraordinary*. New York: McGraw-Hill, 2007. 175-178. Print.

⁴⁹ Simon, Bryant. *Everything but the Coffee: Learning about America from Starbucks*. Berkeley: University of California, 2009. 239-40. Print.

Schultz believed the company had to slow its US growth and to ramp up its international expansion in successful locations like China. Schultz did not like the competition from the up and coming fast-food chains distract him. He knew that behind every cup of Starbucks was the world's highest-quality coffee bean, baristas who had health-care coverage and equity in their company, a company committed to their social responsibility, farmers who were treated ethically, and coffee experts who had indestructible passion for Starbucks coffee. No one in the coffee industry could compete with a cup of Starbucks Coffee and its intangibles.⁵⁰

Shultz first improved the current state of the retail shops in the United States since the US stores comprised of 70 percent of revenues. Starbucks drastically slowed down its pace of store openings and permanently closed underperforming locations. Second, Schultz ignited Starbuck's emotional attachment with its customers since the majority of Starbucks' success came from its intangibles. These intangibles were the company's differentiating factor. Third, Starbucks started making long-term adjustments to its foundation. Starbucks analyzed current operations; reducing costs and improving customer service. Schultz made it clear that he would never take away the employee health-care program and never allow the quality of the coffee to deteriorate. He understood that the way to win over customers was to win over the partners; Schultz had to reignite passion for the coffee and bring back the art of espresso. In 2007, Starbucks was offended when a Consumer Report ⁵¹ stated that Starbucks fell behind McDonalds Coffee in a taste test. Consumers did not like the bold taste of Starbucks coffee; in fact,

⁵⁰ Bussing-Burks, Marie. *Starbucks*. Santa Barbara, CA: Greenwood, 2009. 31-49. Print

⁵¹ Simon, Bryant. *Everything but the Coffee: Learning about America from Starbucks*. Berkeley: University of California, 2009. 239-40. Print.

they referred to Starbucks coffee as "burnt". ⁵² Schultz did not understand why people did not appreciate the deep flavors of the Arabic coffee beans. Although he could not grasp why consumers preferred the taste of diluted coffee, he formed a team of coffee roasting experts in November 2007 to create a new coffee blend. After many different creations, the team finally came up with a balanced blend that was rich in flavor; this unique blend would reach out to a new audience. They named the blend, Pike Place Roast in honor of Starbucks first store. Pike Place Roast reinvented Starbucks' brewed experience with its freshness. The retail stores also reverted back to grinding the coffee beans in the actual stores to intensify the aroma and rebuild the magic of Starbucks. ⁵³

Eight weeks passed and Schultz's three pillar plan had launched into a Transformation Agenda that required seven big moves and one vision: "to become an enduring, great company with one of the most recognized and respected brands in the world, known for inspiring and nurturing the human spirit." To execute this vision, the Transformation Agenda laid out the seven goals and specific tactics to achieve each goal. First, Starbucks needed to become the undisputed coffee authority. Starbucks needed to lead in its core business by incorporating their history into each perfect cup of coffee and constantly reinventing the coffee culture. Second, Starbucks needed to engage and inspire its partners. The partners' passion and enthusiasm for the coffee needed to capture customers and build relationships. Schultz knew that Starbucks most irreplaceable and unique asset was the emotional connections they built with their customers through the

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⁵² Fellner, Kim. *Wrestling with Starbucks: Conscience, Capital, Cappuccino*. New Brunswick, NJ: Rutgers UP, 2008. 4-6. Print.

⁵³ Bussing-Burks, Marie. *Starbucks*. Santa Barbara, CA: Greenwood, 2009. 87-105. Print

⁵⁴ Fellner, Kim. Wrestling with Starbucks: Conscience, Capital, Cappuccino. New Brunswick, NJ: Rutgers UP, 2008. 4-6. Print.

Starbucks Experience. Starbucks was focused on improving partner training and developing meaningful incentive packages for partners. Third, the company needed to reignite its emotional attachment with the customers. The retail stores needed to deliver world-class customer service and put the customers in the center of attention; after all, people did not just come to Starbucks for the coffee, but for the human connection that partners the delicious cup of Joe. 55 Fourth, Starbucks had to focus on global expansionwhile ensuring that each retail store became the soul of the surrounding neighborhood. New global stores would offer local cuisine and support the local causes to gain the trust from the community. Fifth, Starbucks would be a leader in corporate responsibility and have a powerful environmental impact by lowering their carbon footprint. Sixth, Starbucks would produce innovative growth platforms that aligned with their high quality coffee. The company focused only on expanding its brand to goods that complimented its coffee and the shift in customer's preference for healthy goods. The final goal of the Transformation Agenda was to deliver a sustainable economic model because without a profitable business model, none of these other moves would be possible. Starbucks cut costs and constructed a supply chain. The Transformation Agenda and new mission statement was presented at a summit to all of Starbucks' leading partners. The summit was a success and aligned the top global leaders to two important documents: the Transformation Agenda, which stated what needed to happen within the company, and the new mission statement, which reminded partners why this needed to be done.⁵⁶

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⁵⁵ Moore, John. *Tribal Knowledge: Business Wisdom Brewed from the Grounds of Starbucks Corporate Culture*. Chicago, IL: Kaplan Pub., 2006. 64-73. Print.

⁵⁶ Bussing-Burks, Marie. *Starbucks*. Santa Barbara, CA: Greenwood, 2009. 19-31. Print

On February 26, 2008 Starbucks closed all of their stores across the United States; 7,100 doors were locked and a posted note stated, "We are taking time to perfect our espresso. Great espresso requires practice. That's why we're dedicating ourselves to honoring our craft."⁵⁷ This was a risky maneuver and had never been executed by a retailer. While Starbucks lost about \$6 million dollars that day, it was something that needed to be done to improve Starbucks' quality. In order for Starbucks to regain the essence of its company, they needed to focus on the quality of their products, not the quantity of their stores. Schultz stated, "Starbucks has always been about so much more than coffee. But without great coffee, we have no reason to exist."⁵⁸ In addition to restoring the artistry of the coffee, Shultz wanted to instill the love and commitment that Starbucks' partners had to have for the customers to complete the Starbucks Experience.

Shultz also believed a primary component of the success of the Starbucks

Experience results from focusing on employees and customers first. The company refers to employees as "partners", and the employees get a number of benefits including common stock. Schulz has made physical improvements to the store, such as lowering the espresso machines to eliminate the physical barrier between the customer and employees, which fosters a better relationship between baristas and customers. Schulz did not budge when investors pressured him to drop the health-coverage for his employees

⁵⁷ Bussing-Burks, Marie. *Starbucks*. Santa Barbara, CA: Greenwood, 2009. 1-3. Print.

⁵⁸ Ibid., 5

⁵⁹ Moore, John. *Tribal Knowledge: Business Wisdom Brewed from the Grounds of Starbucks Corporate Culture*. Chicago, IL: Kaplan Pub., 2006. 131-142. Print.

during the 2008 recession; he stuck to his customer-centric and employee-centric philosophies.⁶⁰

In the retraining process, Schultz held the baristas to higher standards; the baristas became artists and perfected their work. After the training period was over and Starbucks opened back up, it was evident Schultz did the right thing. Customers appreciated the bold move by Starbucks and noticed a difference in the quality of the espressos; Starbucks was finally getting back to its roots with a leader who focused on quality instead of quantity. In the previous years, Starbucks opened about 2,200 new stores every year. But in Schultz's first year back as CEO, he only opened a few stores and closed underperforming stores across the world. The store count from 2008 to 2009, dropped from 16,680 to 16,635 stores.⁶¹

On March 19, 2008 Howard Schultz had to face the shareholders in the annual shareholders meeting. The company's earnings and share price was lower than projected and the stock was down a drastic 40 percent. At this meeting, Schultz presented the Mastrena, a new machine that would improve the quality and consistency of Starbucks coffee. The Mastrena had a built in grinder that freshly ground coffee beans before the espresso shot was poured. He then explained the relationship that Starbucks formed with Conservation International and Starbucks' commitment to protect the farms and farmers and to educate customers about the climate changes. Starbucks espresso beans were "Responsibly Grown. Ethically Traded. Proudly Served." After elaborating on the

⁶⁰ Schultz, Howard, and Joanne Gordon. *Onward: How Starbucks Fought for Its Life without Losing Its Soul*. New York, NY: Rodale, 2011. 159-163. Print.

⁶¹ Ibid., 61-69.

⁶² Ibid.,181-185.

⁶³ Bussing-Burks, Marie. *Starbucks*. Santa Barbara, CA: Greenwood, 2009. 133. Print

company's corporate responsibilities, Schultz announced Starbucks new rewards program. Starbucks would acknowledge their most loyal customers through this Rewards Programs and generate incentives. The card also brought economic relief to the customers who still chose to get coffee at Starbucks instead of a less expensive place. The Rewards card, allowed customers to receive special benefits; most importantly, Starbucks would allow these Rewards Members to customize their beverages for free, picking up the extra costs of soy milk and flavored syrups. Market studies showed the loyal Starbucks customers had a favorite beverage they loved to customize; the customization was a part of the Starbucks Experience and gave each customer an identity. In addition to this Rewards Card, the company presented its new website and first online community, MyStarbucksIdea.com. When the website was launched, more than 7,000 ideas were posted in the first 24 hours. Finally, the Clover Brewing System was revealed as commercial equipment made to replicate a French press. Even with these many promising changes, the company's stock continued to drop. 64

By the end of April 2008, Starbuck's second-quarter earnings were down 28 percent. For the first time in Starbuck's history, the company's net income was negative. No one understood why the company was still not profitable, especially after the huge success of the Pike Place Roast. Starbucks realized that they were not providing their store managers with sufficient incentive and technology to perform at their highest potential.⁶⁵

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⁶⁵ Ibid., 144-147.

⁶⁴ Schultz, Howard, and Joanne Gordon. *Onward: How Starbucks Fought for Its Life without Losing Its Soul.* New York, NY: Rodale, 2011. 319-324. Print.

In July 2008, Starbucks decided to close about 600 underperforming stores in the United States. The irony of the stores being closed was that about 20 percent of these underperforming stores were new stores. It became apparent that "Starbucks thought all they had to do was show up to be successful." Starbucks learned that success is not sustainable through quantity but quality. The only statistic that truly mattered was "one." One cup. One customer. One partner. One experience at a time. 67

With the successful introduction of the Pike Place Roast in April 2008, the public's response to the Rewards Card was not enormous. So Starbucks launched the Rewards Card program in June 2008 and it was an instantaneous success. By July, one million people had a Rewards Card. In addition to the Rewards Card Program, Starbucks launched a value promotion called the Treat Receipt. This allowed customers who made a morning purchase to return any time after two in the afternoon to receive any cold grande beverage for only two dollars. This promotion was launched nationally and reduced the company's afternoon lull. Also, changes in societal trends revealed that consumers were becoming more health conscious. To accommodate these changes, Starbucks launched its version of a smoothie, the Vivanno. However, as Starbucks learned, there was not one product launch that could save Starbucks. On July 29th, Starbucks faced their reality and eliminated 1,000 positions. Starbucks continued to revert back to their core values and focus on creating the Starbucks Experience for their customers. With Schultz back in the driver's seat, Starbucks was finally heading down the right path to success. Within one year, Starbucks' performance finally became profitable in the third quarter of its fiscal

⁶⁶ Bussing-Burks, Marie. Starbucks. Santa Barbara, CA: Greenwood, 2009. 156. Print

⁶⁷ Schultz, Howard, and Joanne Gordon. *Onward: How Starbucks Fought for Its Life without Losing Its Soul*. New York, NY: Rodale, 2011. 157-159. Print.

year, posting a 20-cent profit. 68 The company beat analysts' forecast by five cents. 69

Starbucks became a popular brand on social networking sites such as Facebook and Twitter; and named one of the most engaging brands in social media in 2009. The launch of Starbucks' first online community, My Starbucks Idea in 2008, mystarbucks, Starbucks Card iPhone applications, and Starbucks Card Mobile Payment Starbucks really allowed Starbucks to make an impact in the technological world. My Starbucks Idea spearheaded Starbucks towards transforming into a top Social Equity Brand. 70 Starbucks has always focused on social capital development by building a company on social capital. This innovation encouraged customers to help share the future by proposing future initiatives to help local communities. The Starbucks Card Mobile Application was developed for Blackberry smartphones and iPhones to allow customers to pay with their phones in retail stores. With these new technological innovations, the company increased customers' loyalty, traffic, and brand awareness. Within two years, Starbucks reverted back to its original core values and managed to add more positive aspects to the company. The espresso training increased the quality of the beverages served at Starbucks and the improvement in customer service was apparent. In accordance with the change in the public's tastes, Starbucks has offered tastier and healthier food to its customers. Starbucks did not need any more mending; they finally

⁶⁸ Bussing-Burks, Marie. Starbucks. Santa Barbara, CA: Greenwood, 2009. 297. Print

⁶⁹ Schultz, Howard, and Joanne Gordon. *Onward: How Starbucks Fought for Its Life without Losing Its Soul*. New York, NY: Rodale, 2011. 167-168. Print.

Moore, John. *Tribal Knowledge: Business Wisdom Brewed from the Grounds of Starbucks Corporate Culture*. Chicago, IL: Kaplan Pub., 2006. 142-161. Print.

regained their status as a stable organization and could once again think about the company's expansion.⁷¹

To continue building their brand and helping to make a difference in the world through their corporate responsibility, Starbucks partnered with (RED) to help save lives in Africa and open an East Africa Farmer Support Center in 2009. Starbucks wanted to focus on its core values during its rebuilding stages. In addition to their commitment to corporate responsibility, Starbucks focused on their innovation of coffee products. They introduced VIA Ready Brew Instant Coffee in 2009; these packets were perfect for the busy drinker who only wants to one delicious cup of freshly brewed coffee that captures the perfection excepted from a Starbucks Store. ⁷²

To accommodate the emergence of society's dependence on technology,

Starbucks expanded its digital service for customers in 2010; providing customers with
free unlimited Wi-Fi access and Starbucks Digital Network in the U.S. Stores. Also

Starbucks introduced Starbucks Reserve Coffee; exotic, rare, and exquisite coffees from
across of the worlds. This line of coffee is only offered for a limited time since Starbucks
only packaged the exceptional coffees that would captivate its customers. In addition to
the launch of the Starbucks Reserve Coffee, Starbucks introduced Starbucks Natural
Fusions in 2010. This was the coffee industry's first and only nationally-branded
premium packaged coffee that was naturally flavored with real ingredients, such as

⁷¹ Schultz, Howard, and Joanne Gordon. *Onward: How Starbucks Fought for Its Life without Losing Its Soul*. New York, NY: Rodale, 2011. 203-10. Print.

⁷² Ibid., 320-323.

⁷³ Starbucks. 2010 Annual Report. Seattle, WA: Starbucks Corporation, 2010. Starbucks Investor Relations: 2010 Annual Report. 2010. 22 March 2010. http://investor.starbucks.com/phoenix.zhtml?c=99518&p=irol-reportsAnnual

cinnamon, nutmeg, and vanilla, blended into the coffee. With these new product lines, Starbucks hoped to change the way customers view instant coffee.⁷⁴

In January 2011, Starbucks offered its customers high quality Artisan breakfast sandwiches, which can be purchased for \$2.00 with any Starbucks beverage. These breakfast sandwiches were perfectly crafted with the finest ingredients and perfectly complement a cup of smooth Pike Place Roast Coffee. Six months later, on July 12, 2011, Starbucks launched its selection of premium Bistro Boxes. These on-the-go boxes were launched in stores across the U.S. and in Canada to meet the demands of customers who desired a wholesome and convenient food options to accompany their coffees. These Bistro Boxes were nutritious and less than 500 calories per box. The box contained vegetable fruit and whole grains to satisfy the health conscious consumer. The entrée size bistro boxes were chipotle chicken wraps, sesame noodles, chicken lettuce wraps, and salami and cheese bistro boxes. There were also snack size bistro boxes that contained tuna salad, protein specific meal, chicken and hummus, or cheese and fruit.⁷⁵

2.4 The New Direction

In March of 2011, Starbucks celebrated their 40th year anniversary by introducing its new logo, and new global products. The new logo celebrates the Starbucks Siren and was introduced on March 8th. ⁷⁶ In addition to the new logo, Starbucks launched four new products as a testament that Sawbucks has not deterred away from its core values –

⁷⁴ Bussing-Burks, Marie. *Starbucks*. Santa Barbara, CA: Greenwood, 2009. 215. Print

⁷⁵ Schultz, Howard, and Joanne Gordon. Onward: How Starbucks Fought for Its Life without Losing Its *Soul*. New York, NY: Rodale, 2011. 266-270. Print. ⁷⁶ Ibid., 233-251.

handcrafting premium espresso and coffee: the cocoa cappuccino, Starbucks Tribute Blend, Starbucks VIA Ready Brew Starbucks Tribute Blend, and Starbucks Petites were introduced to the company's menu. The Starbucks Petites was a global food platform that focused on eight delicious sweet treats that are perfect for the little afternoon treat; cake poops, whoopie pies, mini cupcakes, and sweet squares. In addition to these new products and new logo, Starbucks also made a commitment to thriving neighborhoods by announcing the month of April 2011 as the Global Month of Service to celebrate the company's committee to community service.⁷⁷

On March 10, 2011 Starbucks partnered with Green Mountain Coffee Roasters, leaser in single-serve brewing systems and specialty coffee, to form a relationship to market and distribute Starbucks and Tazo tea with the use of K-Cup portion packs that are specific to the GMCR's Keurig Single-Cup brewing system. This new partnership will allow owners of Keurig Single-Cup brewers to drink a perfect cup of Starbucks Coffee or Tazo tea. Starbucks' goal of expanding its presence in the premium single-cup coffee was achieved with this new partnership. This partnership was a win for both companies because Starbucks was able to expand into the single-cup industry and the majority of Starbucks customers did not own a single-cup brewer. Starbucks exceeded their projected goal by shipping more than 100 million K-Cup packs after just launching their product for two months.

⁷⁷ Ibid., 246-251.

⁷⁸ "Starbucks Newsroom: Nearly 30 Million Starbucks® Coffee K-Cup® Portion Packs Hit U.S. Store Shelves This Week." *Starbucks Newsroom.* Starbucks Corporation, 1 Nov. 2011. Web. 18 Feb. 2012. http://news.starbucks.com/article_display.cfm?article_id=582.

⁷⁹ "Starbucks K-Cup Shipment Exceeds 100 Million In Two Months." *VendingMarketWatch*. Cygnus Business Media, 27 Jan. 12. Web. 13 Apr. 2012. http://www.vendingmarketwatch.com/news/10619440/starbucks-k-cupr-shipment-exceeds-100-million-in-two-months.

In 2011, Seattle's Best Coffee launched its first ever integrated advertising campaign. Using the slogan "anywhere great coffee is needed" the company's new mission was obvious. This was the company's first effort attracting a mass audience. Seattle's Best is introducing its bold new approach to premium coffee. During February, they partnered with Delta Air Lines to serve freshly brewed premiums coffee onboard all Delta Flights. Seattle's Best Coffee, acquired by Starbucks, finally started to establish itself in the coffee industry as a company that sold premium coffee. ⁸⁰

In the end of November 2011, Starbucks acquired Evolution Fresh to establish itself in the Health and Wellness Sector. Jimmy Rosenberg, the founder of Naked Juice, also founded Evolution Fresh. Rosenberg decided to enter the premium juice business; Evolution Fresh is one of the few true juicers left in the industry. They still freshly peel and squeeze fresh fruits and vegetables to create their juices. Starbucks plans on using this brand to grow and dominate this industry. Starbucks has expanded their products to attract the more health conscious consumer. Their efforts have been successful with their nutritious on-the-go Bistro Boxes, but Starbucks hopes this acquisition will take the company even further. Starbucks plans to reinvent the \$1.6 billion super-premium juice segment industry to enter the larger \$5 billion Health and Wellness industry. Evolution Fresh is a premium juice product that will become a differentiated brand and experience through this partnership with Starbucks. Evolution Fresh utilizes a new innovative

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⁸⁰ "Starbucks Newsroom: Seattle's Best Coffee Introduces Iced Canned Lattes Nationwide." *Starbucks Newsroom: Home.* Starbucks Coffee Company, 15 Jan. 2011. Web. 17 Mar. 2012. http://news.starbucks.com/article_display.cfm?article_id=492.

⁸¹ Hansberry, Jeff. "Starbucks Announces Acquisition of Evolution Fresh." *Starbucks Coffee Company*. Starbucks Corporation, 10 Nov. 2011. Web. 20 Apr. 2012. http://www.starbucks.com/blog/starbucks-announces-acquisition-of-evolution-fresh/1105?utm_source=facebook>.

technology called High pressure Pasteurization. 82 This technology allows Evolution Fresh to manufacture one of the few "never heated" juices available in the market. This allows for a more fresh tasting and nutritious juice for their consumers since the nutrients in the fruits and vegetables are kept intact during the juicing process. The technology of HPP is Evolution Fresh's differentiating factor in the juice sector and will strongly align with consumers' expectations of Starbucks premium goods and service. Starbucks future seems bright with this acquisition as they start to disperse into different channels and bring Evolution Fresh into Starbucks all over the world, Starbucks will redefine the juice industry with this acquisition. This acquisition also represents Starbucks attempt to accommodate societal trends for a more healthy and wellness concerned society. Howard Schultz states, "Our (Starbucks') intent is to build a national Health and Wellness brand leveraging our scale, resources and premium product expertise. Bringing Evolution Fresh into the Starbucks family marks an important step forward in this pursuit." ⁸³ Starbucks decided to acquire Evolution Fresh because its core values aligned with Starbucks'; both companies believe in premium quality, nutrition and strive for growth. Through this acquisition, Starbucks will have access to the \$1.6 billion super-premium juice market and tap into the \$50 billion Health and Wellness industry.⁸⁴

In addition to their new acquisition with Evolution Fresh, Starbucks also started off the holiday season with their new mobile application, The Starbucks Cup Magic. This new innovative app allows customers to interact with Starbucks characters for the first

⁸² "Starbucks Newsroom: Evolution Fresh Revolutionizes \$3.4 Billion Cold-Crafted Juice Category with the Opening of Its First Store." *Starbucks Newsroom: Home*. Starbucks Corporation, 19 Mar. 2012. Web. 23 Mar. 2012. http://news.starbucks.com/article_display.cfm?article_id=635.

^{83 &}quot;Starbucks Newsroom: Starbucks Acquires Evolution Fresh to Establish National Retail and Grocery Health and Wellness Brand." *Starbucks Newsroom: Home*. Starbucks Coffee Company, 10 Nov. 2011. Web. 11 Mar. 2012. http://starbucks.tekgroup.com/article_display.cfm?article_id=587..

time. A free download of the application allows customer to watch holiday characters to come to life and create merry holiday scenes and bring the Starbucks Experience to life.

Starbucks always manages to embrace the holiday spirit by releasing their delicious menu of seasonal beverages and festive holiday cups.

Starbucks has made quite the global impact and plans to continue its global expansion to the U.K. Starbucks has received strong consumer demand for high-quality espressos on-the-goal and have implemented drive-through programs to meet these needs. Starbucks states to create about 5,000 jobs in the U.K. as it plans to significantly step up its drive-through programs. 85 In addition to the company's global expansion plans, Starbucks started off the New Year with the launch of the Starbucks Blond Roast, a smooth, lighter-bodied coffee, different from its signature dark roast coffees. Starbucks perfected this lighter roast coffee to meet the demands of the 54 million U.S. coffee drinkers who preferred a lighter roast coffee. This light roast coffee opens up Starbucks' consumer market to attract customers who appreciate a milder taste with a gentle finish. Starbucks also revamped their coffee packaging for grocery stores; the packages are now organized by roast- Starbucks Blonde Roast, Starbucks Medium Roast, and Starbucks Dark Roast. 86 This allowed customers to easily find their preferred intensity of coffee. While, Starbucks has launched product lines that do not focus on the full and bold flavors that fueled the passion for this company, their core values of providing premium coffee, no matter what intensity, has not faltered; they launched products with these new

⁸⁵ "Starbucks Newsroom: Starbucks to Create 5,000 Jobs in the U.K." *Starbucks Newsroom: Home*. Starbucks Corporation, 30 Nov. 2011. Web. 24 Jan. 2012.

http://news.starbucks.com/article_display.cfm?article_id=596.

⁸⁶ Schultz, Howard, and Joanne Gordon. *Onward: How Starbucks fought for its life without losing its soul.* New York, NY: Rodale, 2011. 126-135.

intensities to please consumer's desires. Starbucks also created a Blonde Roasted coffee for the K-Cup so that it could capture the forty percent of customers who prefer to drink a lighter roasted coffee.⁸⁷

The solution to fix the afternoon lull was applied in stores in Atlanta and Southern California in 2012. These stores offered their customers time to relax in the evenings by offering wine, beer and premium food on their menus. These premium foods included hot delicious flatbreads and savory snacks. Also, in additional to new menu items, the stores incorporated flexible seating arrangements to accommodate different groups. ⁸⁸

Starbucks has continued to expand its brand into different countries and into different industries, while still remaining their excellence in the places they already dominate. Starbucks has reinvented itself into a company that is built around strong core value and a company that has endless opportunities.

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⁸⁷ Reuters. "Starbucks to Create 5,000 New UK Jobs in Next 5 Years." *Employment*. Cnbc.com, 01 Dec. 2011. Web. 16 Feb. 2012.

http://www.cnbc.com/id/45504092/Starbucks_to_Create_5_000_New_UK_Jobs_in_Next_5_Years
** "Starbucks Newsroom: Starbucks to Extend Evening Day-Part Concept." ** Starbucks Newsroom: Home. Starbucks Coffee Company, 23 Jan. 2012. Web. 26 Mar. 2012. http://news.starbucks.com/article_id=610
** display.cfm?article_id=610>

3. The "Three P's": Profit, People, Planet

Starbucks's success is derived from its emphasis on exhibiting a strong corporate social responsibility. Corporate Responsibility requires companies to behave ethically and aid in economic improvement and improve the quality of life of the people it touches as well as the entire society. The triple bottom line of: people, planet, profit, can be the determining factor of a company's success and longevity. Starbucks is not about the coffee but about the people; this company emphasizes the importance of putting its customers first. Schultz has always showed that a great business is one with a conscience.⁸⁹

From the very beginning, Starbucks has been dedicated to obtain a balance between profitability and social responsibility. Starbucks "continues to believe that the ultimate way to scale the power of brand is to share the good we do so that Starbucks and everyone we touch – can endure and thrive." Starbucks focuses on five main aspects of corporate responsibility: community, environment, ethical sourcing wellness, and diversity. Starbucks is determined to positively impact the community of every neighborhood where stores are located and the neighborhoods of where the coffee is grown. Starbucks are determined to help communities that they do business with thrive. Organizations like the Starbucks Foundation and Create Jobs for USA allows Starbucks

⁸⁹ Behar, Howard. *It's Not about the Coffee: Leadership Principles from a Life at Starbucks*. London: Penguin, 2009. Print.

⁹⁰ "Being a Responsible Company." *Starbucks Coffee Company*. Starbucks Coffee Company. Web. 11 Feb. 2012. http://www.starbucks.com/responsibility.

to inspire change in communities.⁹¹ In efforts to achieve a balance between the three P's: profit, people, and planet, Starbucks has focused on reducing its carbon footprint. Starbucks has noticed its customers' commitment to the environment and have decided to align itself with their views. Not only does Starbucks believe in the importance of environmental stewardship, but they encourage other companies to operate at the same standards. Starbucks focuses on minimizing its waste of energy and water, building greener stores, and reducing the waste they create. In February 2012, Starbucks was announced as the 7th organization on the Environmental Protection agency's Nation Top 50 ranking; making Starbucks on of the top renewable energy purchasing organizations in the United States. Starbucks is dedicated to offering its customers products that are ethically sourced and of the highest quality; Starbucks prides itself on its responsible purchasing practices that have been invested in the relationships with communities, farmers, and suppliers. Starbucks is also committed to the wellness of its customers; the company supports policies and efforts to improve the overall health of society by providing customers with balanced foods and drinks to its customers. 92

Starbucks incorporates diversity in every aspect of the company; from the partners to products and suppliers. The company is a foundation where diversity is welcomed and highly respected. Starbucks's C.A.F.E. Practice is now been successful for eight years and Starbucks is sourcing an estimated 86 percent of its coffee with a method that improves the company's environmental impact and the overall quality of the coffee

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⁹¹ Schultz, Howard. "Creating and Sustaining Thriving Communities." *Starbucks Coffee Company*. Starbucks Corporation, 3 Oct. 2011. Web. 17 Feb. 2012. http://www.starbucks.com/blog/creating-and-sustaining-thriving-communities/1086>.

⁹² S, Brad. "Starbucks Receives Green Energy Accolades from the EPA." *Starbucks Coffee Company*. Starbucks Corporation, 23 Feb. 2012. Web. 1 Apr. 2012. http://www.starbucks.com/blog/starbucks-receives-green-energy-accolades-from-the-epa/1160>.

itself. Focusing on its environmental stewardship, Starbucks has begun to build 75 percent of the new stores according to the LEED Standard; resulting, in the company being a green building retail industry leader. ⁹³

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⁹³ "Year in Review: Fiscal 2011." *Starbucks Global Responsibility Report – Goals and Progress 2011*. Starbucks Corporation. Web. 2 Feb. 2012. http://assets.starbucks.com/assets/goals-progress-report-2011.pdf>.

4. Accounting For Intangibles

4.1 Accounting Standard Adjustments

There is no simple way to define the term intangibles because it is a very broad term that covers many aspects of a company. Intangible assets are very valuable to firms as they can be critical in businesses long-term success. One of the most important intangibles that a company has is its own brand. Brands should be accounted for on company's financial statements because although it is not a physical asset, it is extremely valuable as its positively affects bottom-line profits of firms like Starbucks and Coca-Cola, Nike, as well as others; companies who have built strong brand recognition, use their brand strength to drive their yearly global sales. Kohler defines intangibles as capital assets having no physical existence and whose value depends on the rights and benefits that possession confers to the owner. 94 In addition, Paton emphasizes that the lack of physical existence with intangible assets makes them affect the enterprise value of the company more than tangible assets.

The Accounting Research Bulletin issued ARB No. 24 *Accounting for Intangible Assets* in December 1944. ⁹⁶ It stated that intangible assets either had a limited life that was determined by law or their nature or did not have a limited life, this included

⁹⁴ Kohler, Eric Louis, William W. Cooper, and Yuji Ijiri. *A Dictionary for Accountants*. Englewood Cliffs, NJ: Prentice-Hall, 1983. 269. Print.

⁹⁵ Paton, William A., and William A. Paton. *Asset Accounting: An Intermediate Course*. New York: Macmillan, 1952. 486-90. Print.

⁹⁶ Massoud, Marc F., and Cecily A. Raiborn. "Accounting for Goodwill: Are We Better Off?" *CBS Interactive*. CBS Interactive Business Network, 01 Aug. 2004. Web. 9 Mar. 2012. http://findarticles.com/p/articles/mi_hb6451/is_2_24/ai_n29004124/pg_6/?tag=content;col1>.

goodwill. The second definition of an intangible was forever with the company until it was apparent that the life of the asset became limited or the item was deemed worthless.⁹⁷

Accounting Research Study No.10 *Accounting for Goodwill*, written in 1968, implied that goodwill should be written off immediately. Critics who supported this argument stated that goodwill was derived from evaluations of earnings or the value of expected earnings; goodwill was not used in the actual earning production process. Therefore, this argument implies that since goodwill's "value has no reliable or continuing relation to costs incurred in its creation, its purchase or its maintenance," the "value" of goodwill was deemed subjective and could contain material fluctuations created by investor's opinions. This perception of goodwill continued for about three years until the changing economy required a new definition of goodwill to be defined. This issued study created a lot of deliberation that finally resulted in the issuing of APB Opinion #16 and #17. 99

The Accounting Principles Board of the American Institute of Certified Public Accountants issued Opinion 16, *Business Combinations*, and Opinion No.17, *Intangible Assets*, in August of 1970. Opinion 16 accounted for business combinations with two methods: the pooling method or the purchase method. The pooling method was only utilized when 12 criteria were met; this method did not identify economically dissimilarly transactions. The results from having two accounting methods decreased the comparability of different companies since the pooling and purchase method accounted

American Institute of CPAs. ARB No. 24: Accounting/or Intangible Assets, New York: AICPA, 1944.
 Catlett, G. and N. Olson. ARS No. 10: Accounting for Goodwill, New York: AICPA, 1968.

⁹⁹ Massoud, Marc F., and Cecily A. Raiborn. "Accounting for Goodwill: Are We Better Off?" *CBS Interactive*. CBS Interactive Business Network, 01 Aug. 2004. Web. 9 Mar. 2012. http://findarticles.com/p/articles/mi_hb6451/is_2_24/ai_n29004124/pg_6/?tag=content;col1>.

for intangibles assets differently. The purchase and pooling method accounted for different methods for similar business combinations. The purchase method recognized all intangibles assets acquired in business combinations, while the pooling method only recognized intangibles assets that had been previously recorded by acquired company. In Opinion 17, the Accounting Public Board indicated that goodwill would only be recognized if the merger was accounted for as a purchase and not as a pooling of interest. 100 This required goodwill to be accounted for on company's balance sheet and be amortized for acquisitions. Though this standard better valued the goodwill for mergers, it did not address the pooling of interest for intangibles; the pooling of interest method allowed for earning manipulation by allowing companies to hide their intangibles. "Dirty pooling" referred to incidents in which management had tried to hide their intangibles through mergers, which allowed them to not recognize goodwill. Management avoided recognizing goodwill because it was amortized and reduced reducing the company's income when recorded on the financial statements. This opinion addresses the issue of accounting for intangible assets acquired by a company. At the end of this opinion, the APB concluded intangible assets acquired by a company should be recorded at the historical cost paid for the assets. A flaw of opinion 17 was it did not clearly address the difficulties of calculating the value of intangible assets that are internally developed. ¹⁰¹

The APB No.17 stated that intangible assets acquired from others, individuals, or companies, must record the cost of acquisition on the balance sheets as intangible assets. Also, these intangible assets must be amortized over the periods of benefits and were not

Andrews, Wesley T. "The Evolution of APB Opinion No. 17. Accounting for Intangible Assets.": A Study of the U.S. Position on Accounting for Goodwill (1981): 37-49. *Http://www.jstor.org*. JSTOR. Web. http://www.jstor.org/stable/40697668>.
 Ibid

allowed to exceed forty years. Amortization is another word for depreciating intangible assets over the assets useful life. Usually these intangible assets are amortized on a straight-line basis; most intangibles are subject to amortization. APB Opinion No. 17 addressed the issue of goodwill amortization by stating that the value resulting from goodwill disappears eventually and this value should be amortized for a maximum of forty years. Another rule under the Opinion No. 17 was that the cost of developing intangible assets that were not specifically identifiable was charged to income when they were incurred. Also, internally developed intangible assets were not recognized as assets on the balance sheet. 102

With the issue of "dirty pooling" and manipulation of the financial statements, the accounting standards for intangibles needed to be updated. In June 2001, APB Opinion No. 16 and Opinion No.17 were superseded by the Statement of Financial Accounting Standards SFAS No. 141, *Business Combinations*, and SFAS No. 142, *Goodwill and Other Intangible Assets*. SFAS No. 141 addressed the accounting methods for business combinations stated in Opinion No. 16; SFAS No. 141 stated that business combination must be accounted for using the purchase method. The introduction of FASB 141 and 142 allowed for more accurate accounting of intangibles for business mergers. This application of SFAS 141 improved financial reporting for business mergers because it allowed companies to better reflect their true underlying economic standing. SFAS 141¹⁰³ presents a more complete financial understanding with its explicit criteria on how companies should recognize their intangibles apart from goodwill. By allowing only one

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¹⁰² Ibid.

¹⁰³ "Summary of Statement No. 141." *FASB: Financial Accounting Standards Board*. Financial Accounting Standards Board, June 2001. Web. 25 March. 2012. http://www.fasb.org/summary/stsum141.shtml.

method of accounting, the purchase method, the comparability and representational faithfulness of the financial statements were improved. SFAS 142 addresses accounting standards for a company's acquired goodwill and other intangibles assets. The SFAS 142 also discloses the accounting requirements and treatments of intangible assets after they are acquired. The effective date of this statement was for the fiscal years beginning after December 31, 2001; any goodwill that was acquired through business after June 30, 2001 shall not be amortized. Statement No. 142 focuses on the financial accounting and reporting for acquired goodwill and other intangible assets. This statement explains how intangible assets that are acquired, individually or grouped in with other assets should be included in the company's financial statements. This Statement focuses on how goodwill and other intangible assets should be accounted for after they are initially recognized in financial statements.

Statement No. 142 needed to be released because analysts and users of the financial statements realized that intangible assets are crucial in determining the important economic resource for many companies. Also, it became apparent that intangible assets are an increasing proportion of the assets that are acquired in various transactions. Also, financial statement users expressed that goodwill amortization expense was not considered useful information when analyzing various investments. The difference between Statement No. 142 and Opinion No. 17, is their dissimilar approach in how company's account for and recognize goodwill and other intangible assets. The Statement requires that goodwill and some intangible assets not be amortized. This

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¹⁰⁴ "Status of Statement No. 142." *FASB: Financial Accounting Standards Board*. Financial Accounting Standards Board, June 2001. Web. 21 Mar. 2012. http://www.fasb.org/st/status/statug142.shtml. ¹⁰⁵ Ibid.

change in accounting standards also applies to company's total assets. Statement No. 142 may cause volatility in companies reported income because impairment losses are likely to occur spontaneously and in fluctuating amounts.

Implementing the new statements drastically improved financial reporting and the quality of financial statements because it allowed the entities that acquire goodwill and other intangible assets to better represent the true underlying value of the intangible assets. With this clearer representation, financial statement users will be able to better comprehend the investments made in intangible assets and the succeeding performance of the investments. Most importantly, the enhanced disclosure on goodwill and intangible assets pertaining to after their acquisition, will give users a better understanding of the expectations and changes in the assets as time passes. Since acquired goodwill and intangibles will be more accurately recorded. By forcing companies to represent the underlying economics of acquired goodwill and intangibles, financial statement users will be able to track the performance of these intangibles assets over time and accurately assess intangibles' future profitability and cash flows

The FASB states that the conclusions in Statement No. 142, are related to the Conceptual Framework since, "the Board concluded that amortization of goodwill was not consistent with the concept of representational faithfulness, as discussed in FASB Concepts Statement No. 2, *Qualitative Characteristics of Accounting Information*. The Board concluded that non-amortization of goodwill coupled with impairment testing *is* consistent with that concept. The appropriate balance of both relevance and reliability and costs and benefits also was central to the Board's conclusion that this Statement will improve financial reporting. This Statement utilizes the guidance in FASB Concepts

Statement No. 7, *Using Cash Flow Information and Present Value in Accounting Measurements*, for estimating the fair values used in testing both goodwill and other intangible assets that are not being amortized for impairment."¹⁰⁶

Under the SFAS No. 142, acquired intangibles assets are recognized based on their fair value. 107 Also, intangible assets that are not specifically identifiable are considered internally developed intangible assets. Internally developed intangible assets are not recognized as an asset on the balance sheet; this rule is the same as what is stated in APB Opinion No. 17. However, the cost of internally developed intangible assets is recognized as an expense when incurred. In addition to this rule, an intangible asset with a finite useful life is amortized over its useful life. The equation used to determine the amount to be amortized is cost minus residual value. However, if the useful life is not limited by legal, economic, or other constricting factors, the useful life is considered indefinite. When determining an intangible assets amortization method, a pattern of economic benefits should be reflected; but, if the pattern of economic benefits cannot be determined, one must use the straight-line amortization method. The rules of SFAS No. 142 state that goodwill should not be amortized and will be tested for impairment on an annual basis. Goodwill will be considered impaired if its fair value is less than the carrying amount. This value must be recorded on the financial statements of the current period. These impairment tests ensure that the asset continues to maintain its stated value. Also, if certain events possibly reduce the goodwill's fair value below its carrying amount, a test of impairment needs to be executed between the annual impairment tests.

¹⁰⁶ "Status of Statement No. 142." *FASB: Financial Accounting Standards Board*. Financial Accounting Standards Board, June 2001. Web. 21 Mar. 2012. http://www.fasb.org/st/status/statpg142.shtml. ¹⁰⁷ Ibid.

Goodwill and intangibles assets were previously viewed as assets with finite lives in Opinion 17; this assumption required that these values be amortized when calculating net income. Also, an arbitrary ceiling was required for the amortization of 40 years in Opinion 17. In contrast, Statement 142 does not assume these assets have finite lives; it treats goodwill and intangible assets as assets with indefinite useful lives, thus the amounts will not be amortized but are required to be annually testes for impairment. If an intangible asset is considered to have a finite useful life, the value will still be amortized throughout its useful life, but there will be no restriction from the arbitrary ceiling.

In addition to this difference stated above, the procedure for measuring goodwill impairment has been modified. Opinion 17 did not provide a clear structure of how to determine and value impairment; this led to inconsistency and poor transferability with the financial statements, resulting in poor decision usefulness. Statement 142 contained explicit directions for testing impairment of goodwill by introducing a two-step test that is done at least annually. This procedure of the two-step test to impair goodwill starts by estimating the fair value of a reporting unit; a reporting unit refers to the asset group when addressing goodwill. In the old two-step proposal; the first step of the test identified a potential impairment of the goodwill while the second step accurately quantified the degree of the impairment. In step 1, the fair value of the reporting unit is compared to the carrying value of the reporting unit; if the carrying amount greater than the fair value, there is a possibility of impairment and step 2 is necessary. In Step 2, if the carrying amount of goodwill is greater than the implied fair value of goodwill, the impairment loss is recognized. If the intangible assets' fair value is greater than its

108 Ibid.

carrying amount the impairment must be recognized. To quantify the amount of impairment loss, the intangible assets carrying amount is subtracted by its fair value. ¹⁰⁹ The SFAS 144 impairment test was usually performed along a SFAS 144 analysis; the SFAS 144 analysis tested for the impairment of intangible and long-lived assets. This test was a two-step test: Step 1 – Recoverability Test and Step 2 – Measurement Test. Step 1 determines if there a possibility for impairment by comparing the carrying value of the asset and its sum of undiscounted cash flows. ¹¹⁰ If the intangible assets undiscounted future cash flows are less than the carrying value, it is determined that the asset is not recoverable, categorized as impaired, and Step 2 must be performed. In Step 2, the calculation of the impairment loss, the impairment loss is valued at the difference between the asset's fair value and the asset's carrying value. ¹¹¹

The new proposal offers a more simplistic method for detecting impairment. The benefit of this new two-step test is that if a company meets certain criteria, the requirement of an annually impairment test for goodwill can be met without an actually remeasurement of the fair value, saving the company a lot of time and money, while still depicting the true economic value of the company to financial statement users.

Before the introduction of SFAS 142, came the SFAS 141 *Business*Combinations, which addresses accounting issues for intangibles assets that are acquired in business combinations. While both standards address how intangibles assets should be report, neither of them states how companies should report the intangible assets that are internally developed. This poses the question, what values are hidden in intangible assets

¹⁰⁹ Ibid

¹¹⁰ Wasson, Dick D., and Donald E. Kieso. *Working Papers, Intermediate Accounting, Tenth Edition, Donald E. Kieso, Jerry J. Weygandt, Terry D. Warfield.* New York: Wiley, 2001. 716-31. Print. ¹¹¹ Ibid.

that are internally developed.

As the economy changes, a disparity between company's stockholders equity and market value has become more apparent. As stated in the CPA Journal:

"Recently, many companies' GAAP stockholders' equity per share has been significantly lower than the price per share as traded on stock exchanges... Critics of the current financial reporting model cite the failure to report the value of the certain intangibles assets causes these differences. Those critics say that GAAP must consider the values of these increasingly important, currently unrecognized assets in the financial statements." 112

Critics of the current accounting method defend their argument on the fact that companies' balance sheets should represent the true value company's assets. The entity's true values are not reflected by the financial statements since internally generated intangible assets are not recognized on the financial statements.

To assist in searching for accounting topics, the FASB launched its *FASB*Accounting Standards Codification project in 2007. The purpose of this project was to reorganize all of the relevant GAAP accounting standards into accounting topics that could be found in an online database. The Financial Accounting Standards Board introduced the Accounting Standards Codification, referred to as the FASB ASC in July 2009. 113 "The FASB Accounting Standards Codification® is the source of authoritative generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities." 114 The ASC reorganized all of the U.S. GAAP

Foster, Benjamin P., Robin Fletcher, and William D. Stout. "Valuing Intangible Assets." *NYSSCPA.ORG*. The CPA Journal, 03 Oct. 2003. Web. 13 Mar. 2012. http://www.nysscpa.org/cpajournal/2003/1003/features/f105003.htm.

¹¹³ Cambridge Partners & Associates. "Goodwill Valuations for Financial Reporting under FASB ASC 350." *Fair Value Appraisals for SFAS 142, FAS 142, ASC 350 Goodwill Impairment Valuation Appraisal.* ¹¹⁴ "Intangibles - Goodwill and Other (Topic 350)." *www.fasb/org*. FASB Accounting Standards Update, Sept. 2011. Web. 15 Mar. 2012. http://www.fasb.org/cs/BlobServer?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1175822937733&blobheader=application/pdf.

pronouncements into accounting topics. The U.S. GAAP Codification is structured into eight main topics and nearly 90 subtopics. SFAS 141 fell under FASB ASC 805 – Business Combinations and SFAS 142 fell under Codification Topic 350- Intangibles – Goodwill and Other. Codification Topic 350 was then broken down into subtopics: 350-10 Overall, 350-20 Goodwill, 350-30 General Intangibles other than goodwill, 350-40 Internal-use software, and 350-50 Website Development Costs. 115

In Codification Topic 350-20 Goodwill, goodwill is not amortized and is tested for impairment at the level of a reporting unit. This section discussed the two-step test for impairment, as previously stated in SFAS 142. Also, this Codification Topic states that the Reversal of impairment loss is not allowed. This prevents goodwill from being written up to its previous impairment levels. In Codification Topic 350-30 Intangibles Other Than Goodwill, intangible assets are broken into two categories: intangibles assets with "finite" or "indefinite" useful life. The intangibles assets with a "finite" useful life are amortized over their useful life while "indefinite" intangibles are not amortized. Also, all intangible assets are tested for impairment loss. 116

Under ASC 350, intangibles assets defined with an indefinite life are subject to impairment review testing; some examples of these indefinite life assets are trademarks, trade names and F.C.C licenses. To accurately value these assets, one must turn to ASC 805 to follow the procedures on how to value them. 117 In addition to the release of ASC

¹¹⁵ Ibid.

¹¹⁶ Ibid.

¹¹⁷ Foster, Benjamin P., Robin Fletcher, and William D. Stout. "Valuing Intangible Assets." NYSSCPA.ORG. The CPA Journal, 03 Oct. 2003. Web. 13 Mar. 2012. http://www.nysscpa.org/ cpajournal/2003/1003/features/f105003.htm>.

350, ASC 360, *Intangible and Long-Lived Asset Impairment Testing*, describes the two-step test for intangible and long-lived assets.

Even after all of these accounting standard adjustments and reorganizations, the Board has not addressed the issue of internally developed intangibles. This thesis argues that a standard needs to be implemented in order to represent the company's true economic value and to uphold the integrity of the financial statements.

4.2 GAAP versus IFRS

GAAP and IFRS differ in the way they define and treat intangible assets on their finanical statements; GAAP follows SFAS 142 while IFRS follows IAS 38. Both of these standards use the purhase methods when accouting for business combination and they only mesure goodwill as a residual, only recongizing it in a business combination. Another similarity between U.S. GAAP and IFRS is the acquirer recognizes both the assets and liabitlies at the acquistion date under the fair value. Both standards do no capitalize expenses of intanigbles unless the expenses increase the value of life of the asset. 118

The difference between GAAP and IFRS are apparent in their defintion of an intangible asset, cost and revalution method, procedures for research and devlopement costs, and how to categorize start up costs. SFAS 142 defines intangibles assets as "identifiable non-financial assets that lack physical substance." Under this definiton, assets such as goodwill, research and devlopement, patens, and advertising are classified

¹¹⁸ Wasson, Dick D., and Donald E. Kieso. *Working Papers, Intermediate Accounting, Tenth Edition, Donald E. Kieso, Jerry J. Weygandt, Terry D. Warfield.* New York: Wiley, 2001. 716-31. Print.

as goodwill. While IAS 38 defines intangible assets as "identifiable non-monetary assets that lack physical substance and controlled by an entity." In terms of the cost and revaluation method, GAAP utilizes the cost method and does not allow revaluation of values. In contrast, IFRS does allow revlaution in some cases; resutling in their assets be marked back up to fair value after being written down. In respect to research and devlopment costs, GAAP usually expesses all costs as incurred while the IFRS always exepnses research cost and capitalized devlopment costs if it meets these criteria: intention to complete the intangible, technical feasibility of competing the intangible, aavailability of sufficient resources to complete the development, ability to reliably measure any expenses incurred in the development of the intangible, ability to sell or use the asset, and it generates future economic benefit. And the final difference between GAAP and IFRS is GAAP always expenses start-up costs while IFRS allows the capitalization of start-up costs "if part of goodwill in an acquisition or if it is included in the cost of property, plant, and equipment."

The revaluation model allows the IFRS to use fair value determined by a lively market. Revaluations affect the Other Comprehensive Income and accumulated equity by introducing a new journal entry "revaluation surplus". GAAP never uses the revaluation model to account for intangibles. In terms of how to amortize intangible assets, International Accounting Standard (IAS) No. 22 *Business Combinations* requires that goodwill be amortized generally over a period that does not exceed 20 years. But IAS No. 36 *Impairment of Assets* states, if a useful life can be expressed to exceed 20 years,

¹¹⁹ Foster, Benjamin P., Robin Fletcher, and William D. Stout. "Valuing Intangible Assets." *NYSSCPA.ORG*. The CPA Journal, 03 Oct. 2003. Web. 13 Mar. 2012. http://www.nysscpa.org/cpajournal/2003/1003/features/f105003.htm.

the goodwill will be subjected to an annual impairment test. ¹²⁰ In 2005, there was an Exposure Draft released by the IASB, which is now referred to as the IFRS, stated that the new standard would require goodwill to be accounted for just like in SFAS No. 142.

4.3 Starbucks Financial Statements

Starbucks has endured a tumultuous history but has managed to survive and keep its soul throughout all of its hardships. This company has experienced numerous ups and downs, structural changes, technological innovations, global expansion, and changes in consumer tastes; but throughout all of the adversity, the Starbucks brand has remained strong; always reverting back to its core values and main purpose. In order to understand the effect that Starbucks brand has had on the company we need to look at the accounting standards for intangibles; specifically, the accounting methods for brands. The current accounting model does not include these important intangibles on the company's financial statements. Starbucks is a company with strong brand recognition and it is important to attempt to qualitatively understand the value of the brand and its effect on the overall profitability of the company.

Starbucks has managed to build their brand from within, developing some of the most valuable intangible assets. The company's core value has internally built a brand that thrives off of its intangibles; Starbucks's intangibles allow them to charge a premium for their goods. There are two significant intangibles that have propelled the company's success every year: Goodwill and Trademark. These intangible assets are not reported on

¹²⁰ Waxman, R. N. "Goodwill Convergence." The CPA Journal, October 2001, pp. 18-24.

the company's financial statements. The company's trademark was developed internally over time; it took research, development and advertising to create the infamous Starbucks trademark. Two intangible properties that can never be depreciated are goodwill and trademark. Goodwill can never be depreciated since the useful life of this asset cannot be determined. Section 197 Amortization of Goodwill and Certain Other Intangibles states that the term "Section 197 intangible" means – goodwill and any franchise, trademark, or trade name. 121

The IRS Publication 535, Business Expenses is used for preparing 2010 Returns. The amortization section in Publication 535 states that businesses can generally "amortize the capitalized costs of "Section 197 intangibles" ratably over a 15-year period. You must amortize these costs if you hold the section 197 intangibles in connection with your trade or business or in an activity engaged in for the production of income." Since trademarks are defined as a section 197 intangible, companies generally cannot depreciate the cost of trademarks. However, if the company acquired the trademark after August 10, 1993, they can amortize the cost of the trademark over 15 years.

The company describes their retail goal in their 2007 annual report, "The Company's retail goal is to become the leading retailer and brand of coffee in each of its target markets by selling the finest quality coffee and related products and by providing each customer a unique *Starbucks Experience*. The *Starbucks Experience*, or third place after home and work, is built upon superior customer service as well as clean and well-

¹²¹ IRC Section 197 Amortization of Intangibles and Goodwill." *Accounting, Financial, Tax, and E-Commerce Business Advisors*. Dana S. Beane & Company P.C., 1999. Web. 10 March. 2012. http://www.dsbcpas.com/databases/irc/ircs197.html>.

^{122 &}quot;Publication 535 (2011), Business Expenses." *Internal Revenue Service*. Web. 8 Mar. 2012. http://www.irs.gov/publications/p535/ch08.html.

maintained Company-operated retail stores that reflect the personalities of the communities in which they operate, thereby building a high degree of customer loyalty."¹²³

The new logo featuring the Siren is displayed on the cover of the 2010 annual report. In Schultz's letter to shareholders, he explains the company's blueprint for growth. He states:

"We believe we have the potential to build a portfolio of \$1 billion brands inside and outside our stores using a unique strategy. Sourcing, roasting and serving high-quality coffee will remain our core, but we are also pursuing sustainable, profitable growth with a more diversified, multichannel and multi-brand business model."

The cover of Starbuck's 2011 annual report reflects the company's achievements and innovations of fiscal year 2011 and early fiscal year 2012. Starbucks's fiscal year begins on October and ends at September. The cover emphasizes Starbuck's core value, "We have always believed the way to build a great enduring company is to strike a balance between profitability and a social conscience." It also stated all of the company's accomplishments from that year. Surprisingly, the company did not mention anything about the new logo change. The only mention of an event associated with the revamped logo was the fact that the company "Celebrated 40th Anniversary". In fact, there is no mention of the logo change in the entire annual report; but the new logo was clearly displayed on the first page of the company's 10-K form. Even in Howard Schultz note to shareholders, he does not mention the anything about the new logo. Instead he puts emphasis on

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¹²³ Simon, Bryant. *Everything but the Coffee: Learning about America from Starbucks*. Berkeley: University of California, 2009. 235-46. Print

what was stressed on the cover of the annual report; he states, "I cannot think of a more authentic way to have honored our 40th Anniversary than by living up to our long-held mission of balancing profitability with a social conscience." The company showed a very strong performance during fiscal year 2011. Schultz, commends the company's "unique business model, which continues to leverage our emotional connection to consumers, our global retail footprint, our diversified CPG channel distribution capabilities and ongoing innovation across all areas" for their success.

Schultz mentions the company's acquisition for Evolution Fresh, Inc. in 2011. He refers to this acquisition, "among our most exciting moves in 2011 was our November entrance into the \$1.6 billion super-premium juice segment through the acquisition of Evolution Fresh, Inc., which also represents our intentions to more fully enter the \$50 billion Health and Wellness sector." Schultz has always, "believed that effective innovation is about responding to, predicting and creating customers' needs while staying true to our core values." Starbucks did exactly that type of innovation during 2011 and displayed a spectacular performance.

In the Notes to Shareholders, Schultz explains the difficulty of measuring the company's success. He understands that the company's shareholders value does display the success from fiscal year 2011 as the financial statements have never been this strong

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¹²⁴ Starbucks. 2011 Annual Report. Seattle, WA: Starbucks Corporation, 2011. Starbucks Investor Relations: 2011 Annual Report. 2011. 23 March 2011

http://investor.starbucks.com/phoenix.zhtml?c=99518&p=irol-reportsAnnual

¹²⁵ Ibid.

¹²⁶ Ibid.

¹²⁷ Ibid.

and displayed such high profits. However, Schultz strongly believes that companies need to be evaluated with more well-rounded measurement tactics. He states, "I still believe that shareholder value must be linked to creating value for a company's people, value for its customers and— perhaps now more than ever—value for the communities it serves. Balancing profitability and social conscience is as much a part of Starbucks core as coffee. As we continually ask ourselves how we might use our scale for good, we have answered by proactively addressing environmental issues and supporting our partners' volunteer efforts, among many other things." Starbucks does a lot for the surrounding communities and represents a company that takes on huge corporate responsibilities. In 2011, the company addressed the United States problem of high unemployment by adding approximately 3,700 new jobs to the economy and launched the Create Jobs for USA, which allows Starbucks's customers to donate to this effort. In addition to this effort, Starbucks supports ethical sourcing and puts forth environmental and volunteer efforts. ¹²⁹

Schultz ends his notes to shareholders with, "Starbucks future has never been brighter. Our foundation never more solid. We are remarkably well positioned to pursue our diversified, multichannel, multibrand business model in the year ahead." It is obvious Starbucks is moving towards a future with new channels of distribution and plans on expanding into new markets by introducing new innovations. Starbucks plans on utilizing these opportunities to make an even bigger difference in the world.

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¹²⁸ Ibid.

¹²⁹ Moore, John. *Tribal Knowledge: Business Wisdom Brewed from the Grounds of Starbucks Corporate Culture*. Chicago, IL: Kaplan Pub., 2006. 81-93 Print.

¹³⁰ Starbucks. 2011 Annual Report. Seattle, WA: Starbucks Corporation, 2011. Starbucks Investor Relations: 2011 Annual Report. 2011. 23 March 2011

The company's fiscal year 2011 Financial Statements describe the company's other intangible assets as consisting, "primarily of trademarks with indefinite lives, which are tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. Definite-lived intangible assets, which mainly consist of contract-based patents and copyrights, are amortized over their estimated useful lives, and are tested for impairment when facts and circumstances indicate that the carrying values may not be recoverable. Based on the impairment tests performed, there was no impairment of other intangible assets in fiscal 2011, 2010, and 2009."

The company account for goodwill in accordance with SFAS No. 142.

Starbucks's, "test goodwill for impairment on an annual basis during our third fiscal quarter, or more frequently if circumstances, such as material deterioration in performance or a significant number of store closures, indicate reporting unit carrying values may exceed their fair values. If the carrying amount of goodwill exceeds the implied estimated fair value, an impairment charge to current operations is recorded to reduce the carrying value to the implied estimated fair value. As a part of [their] ongoing operations, [they] may close certain stores within a reporting unit containing goodwill due to underperformance of the store or inability to renew [their] lease, among other reasons. [They] abandon certain assets associated with a closed store including leasehold improvements and other non-transferrable assets. Under GAAP, 49 when a portion of a reporting unit that constitutes a business is to be disposed of, goodwill associated with the business is included in the carrying amount of the business in determining any loss on

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¹³¹ Starbucks. 2011 Annual Report. Seattle, WA: Starbucks Corporation, 2011. Starbucks Investor Relations: 2011 Annual Report. 2011. 23 March 2011

disposal. Our evaluation of whether the portion of a reporting unit being disposed of constitutes a business occurs on the date of abandonment. Although an operating store meets the accounting definition of a business prior to abandonment, it does not constitute a business on the closure date because the remaining assets on that date do not constitute an integrated set of assets that are capable of being conducted and managed for the purpose of providing a return to investors. As a result, when closing individual stores, we do not include goodwill in the calculation of any loss on disposal of the related assets. As noted above, if store closures are indicative of potential impairment of goodwill at the reporting unit level, we perform an evaluation of our reporting unit goodwill when such closures occur. During Fiscal 2011 we recorded no impairment charges and recorded \$1.6 million in fiscal 2010 and \$7.0 million in fiscal 2009." 132

Goodwill and other intangible assets are measured at fair value and measured to see if they should be impaired. Since GAAP requires management to conform to the procedures and make estimates for valuing assets and goodwill impairments when preparing the financial statements. The need to conform to GAAP principles multiplies the difficulties in valuing intangible assets.

Starbucks fiscal year 2011 annual report, Item 1- Business, discusses the company's Patents, Trademarks, Copyrights and Domain Names. It states, "Starbucks owns and has applied to register numerous trademarks and service marks in the US and in many additional countries throughout the world. Some of our trademarks, including Starbucks, the Starbucks logo, Seattle's Best Coffee, Frappuccino, Starbucks VIA and Tazo are of material importance. The duration of trademark registrations varies from

¹³² Starbucks. 2011 Annual Report. Seattle, WA: Starbucks Corporation, 2011. Starbucks Investor Relations: 2011 Annual Report. 2011. 23 March 2011

country to country. However, trademarks are generally valid and may be renewed indefinitely as long as they are in use and/or their registrations are properly maintained. We own numerous copyrights for items such as product packaging, promotional materials, in-store graphics and training materials. We also hold patents on certain products, systems and designs. In addition, Starbucks has registered and maintains numerous Internet domain names, including "Starbucks.com", "Starbucks.net", and "Seattlesbest.com."

In the company's annual report, Item A. Risk Factors, the company discusses the risk factor of how their success substantially depends on the value of the Starbucks brand. Starbucks has internally built an excellent global reputation for serving high quality products, a consistent positive consumer experience through the "Starbucks Experience", and through the company's corporate social responsibility efforts. In several studies about global brand, Starbucks brand has been highly rated. In order to continue the company's success internationally, where the Starbucks brand is not as well-known, the company must continue to expand and not deter from their core values in order to grow and leverage the value of the Starbucks brand over varying sales channels. When describing the company's risk factors through expansion, "[Starbucks] brand value is based in part on consumer perceptions on a variety of subjective qualities. Consumer demand for our products and our brand equity could diminish significantly if we or our licensees fail to preserve the quality of our products, are perceived to act in an unethical or socially irresponsible manner or fail to deliver a consistently positive consumer experience in

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¹³³ Starbucks. 2011 Annual Report. Seattle, WA: Starbucks Corporation, 2011. Starbucks Investor Relations: 2011 Annual Report. 2011. 23 March 2011

each of our markets."¹³⁴ Therefore, Starbucks needs to deliberately pick out its new acquisitions of new companies and ensure that the companies that choose to be under the Starbucks brand execute to the level that is expected of Starbucks.

Starbucks's 2011 annual report announced the recent accounting pronouncements applicable to Starbucks. The FASB issued accounting standards to simplify guidance for testing goodwill for impairment on September 15, 2011. This guidance revised the requirements of how companies perform their goodwill impairment assessment and was first approved by the FASB in mid-August 2011. Previously, goodwill impairment occurred when its carrying amount was more than the implied fair value of goodwill. This rule was implemented because "preparers of private company financial statements expressed concerns to the FASB about the recurring cost and complexity of performing the first step of the two-step goodwill impairment test required under Topic 350, Intangibles—Goodwill and Other." The test required a two-step test that occurred at least annually. In the first step of the impairment test, the entity must calculate the reporting unit's fair value and compare it with the reporting unit's carrying amount, including goodwill. If the reporting unit's fair value was less than its carrying amount, the second step of the test needed to be performed to quantify the impairment loss, if there was even any. "The guidance allows companies to perform a qualitative assessment, evaluate relevant events to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount, before calculating the fair value of the

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¹³⁴ Starbucks. 2011 Annual Report. Seattle, WA: Starbucks Corporation, 2011. Starbucks Investor Relations: 2011 Annual Report. 2011. 23 March 2011

¹³⁵ "FASB Issues Accounting Standards Update to Simplify Testing Goodwill for Impairment." *Fasb.org*. Financial Accounting Standards Board, 15 Sept. 2011. Web. 3 Feb. 2012. http://www.fasb.org/cs/Content_C&pagename=FASB/FASBContent_C/NewsPage&cid=1176158924316.
¹³⁶ Ibid.

reporting unit. If entities determine, on the basis of qualitative factors, that the fair value of the reporting unit is more likely than not greater than the carrying amount, a quantitative calculation would not be needed. "137 This reduced the entity's costs and decreased the complexity of calculating impairment tests. "Under the new guidance, an entity may choose to bypass the qualitative assessment for any reporting unit in any period and proceed directly to performing the first step of the two-step test." In addition, this new guidance will broaden the examples of circumstances that a company should consider between annual impairment tests. Starbucks plans to accept and apply this guidance in time for the annual goodwill impairment test. While, this guidance does change the way entities test goodwill impairment, this change will not have a material impact on the financial statements. Since the guidance does not change how an entity calculates an impairment loss for goodwill, it will not affect the information on the financial statements.

Starbucks included line items for "other intangible assets" and "goodwill" in their consolidated financial statements; these line items only account for intangible assets that are acquired. The intangibles assets, such as goodwill and trademarks, that are internally developed are not accounted for on company's financial statements.

When calculating goodwill Starbucks uses a discounted cash flow model. They key assumptions to calculate the company's revenue growth, operating expenses, and discount rate. All of the assumption and estimates are subjective judgments and can are

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¹³⁷ Starbucks. 2011 Annual Report. Seattle, WA: Starbucks Corporation, 2011. Starbucks Investor Relations: 2011 Annual Report. 2011. 23 March 2011

¹³⁸ "FASB Issues Accounting Standards Update to Simplify Testing Goodwill for Impairment." *Fasb.org*. Financial Accounting Standards Board, 15 Sept. 2011. Web. 3 Feb. 2012. http://www.fasb.org/cs/ ContentServer?c=FASBContent_C&pagename=FASB/FASBContent_C/NewsPage&cid=1176158924316>

altered by economic conditions. The calculations for impairment loss are uncertain because they require assumptions to be made by managers. Also it is very difficult to predict future cash flows since they are easily affected by changes in the economy. 139

4.4 Accounting For Brands: The Debate

Accounting methods for brands has been the topic of intense discussion for several years. All of the papers and discussion about these procedures display the importance of accounting for intangible assets in modern companies. Companies in this generation have such strong brand names that the amount of growth and sales received are misconstrued through the financial statements. The issue of accounting for brand was raised during 1985, when there was an increase in takeovers of companies with strong brands. There were huge differences between company's book value of the assets and the price that was paid for the company; resulting in difficulties when calculating goodwill. There have only been accounting standards in place for intangibles that have been bought since the validity of these intangibles is certain; price paid for the company subtracted by the book value of the company, would represent the company's intangibles. Brand names that are internally developed are not recorded on the financial statements because there is doubt for the validity of the estimates. If there is no brand being bought or sold, there is no certainty in estimating how much the market values the brand.

This debate poses a question about the essence of accounting; if financial statements exist to estimate a company's true financial value or is it to only include

¹³⁹ Starbucks. 2011 Annual Report. Seattle, WA: Starbucks Corporation, 2011. Starbucks Investor Relations: 2011 Annual Report. 2011. 23 March 2011

objective data and to only provide users with past and recorded transactions? This debate argues choosing between which decision usefulness elements are more important:

Financial statements that are more valid or more reliable? More subjective or more objective? Containing more present value or historical costs? The later has been chosen in all counties, resulting in only allowing external brands to be recorded; by allowing acquired brands to be recorded at historical cost, the current accounting method respects the fundamental accounting principle. The debate argues is internal brands were recorded on the balance sheet; it would respect the reality principle in exchange for reliability and consistency of the accounting. The best way to measure internal brands are based on future income projects, which are uncertain and subjective and would present heterogeneity in the financial statements. Also, if the value of internally developed brands were noted on the financial statements, the reliability of the statements would increase since the brand value would need to constantly be revalued since its value is derived from a different point of view

To counter this argument, critics who believe the function of accounting should display the commercial expenses of a company, which are accumulated through internally developed intangible assets. The fact is, there needs to be accounting standards to account for internally developed intangibles on the financial statements.

5. The Power of the Brand

5.1 Evolution of the Logo

The power of a brand rests on two major components: the name and the logo. Companies primarily rely on the combination of these two forces to promote their brand. To create a strong brand a company needs to clearly articulate their brand identity, what the brand means to the customer. The phrase Starbucks coffee means excellent coffee to its customers. Starbucks coffee evokes the thought of delicious dark-roasted coffee served in a warm and relaxing environment. A clear brand identity ensures that the business will meet the consumer's expectations. The Starbucks' brand has gone through numerous changes over its forty years, but nothing as transformational as its most recent change. In 2011, Starbucks took a huge risk and decided to take the name "Starbucks Coffee" off of its logo, an indicator that they believe the power of the brand can rest on the logo alone. 140

When Starbucks first started, their logo was an image of a "twin-tailed siren" because of the psychological relation between the passion for fresh roasted coffee, tea, spices and the mythological enchanting character. The Starbucks siren was topless and had a fully visible double fish tail. The material of the logo resembled a brown woodcut with its very visual texture and stated "Starbucks Coffee Tea Spices". "Terry [Heckler] also poured over old marine books until he came up with a logo based on an old sixteenth-century Norse woodcut: a two-tailed

¹⁴⁰ Sauer, Abe. "Starbucks New Logo a Mid-Life Crisis in the Making." *Brandchannel.com.* 5 Jan. 2011. 08 Mar. 2012 http://www.brandchannel.com/home/post/Starbucks-New-Logo-Black-Eye.aspx.

mermaid, or siren, encircled by the store's original name, Starbucks Coffee, Tea, and Spice. That early siren, bare-breasted and Rubenesque, was supposed to be as seductive as coffee itself."¹⁴¹

In the second version, released in 1987, the siren's breasts were covered from her flowing hair but her navel was still visible. The fish tail was cropped slightly and the primary color was changed to green from brown to represent the merger between II Giornale and Starbucks. Il Giornale's logo "reflected the emphasis on speed. The Il Giornale name was inscribed in a green circle that surrounded a head of Mercury, the swift messenger god." ¹⁴² While II Giornale was very successful, Starbucks had more history and a strong foundation to start the new business off, resulting in Schultz deciding to drop Il Giornale and keep Starbucks brand name. "To symbolize the melding of the two companies [Il Giornale and Starbucks] and two cultures, Terry [Heckler] came up with a design that merged the two logos. We kept the Starbucks siren with her starred crown, but made her more contemporary. We dropped the tradition-bound brown, and changed the logo's color to Il Giornale's more affirming green." In addition to these changes, they downplayed the siren's split tail and turned the twin fins into decorations that surrounded the crowned siren. The words "Tea" and "Spice" were removed from the text. Along with the release of the second logo, the company added handcrafted espresso beverages to the menu, influenced by Il Giornale. The third version of the logo was released in 1992 when Starbucks became a publically traded company. The company "asked Terry Heckler to revise our logo: She [Siren] stayed mostly the same but lost her

Schultz, Howard, and Dori Jones. Yang. Pour Your Heart into It: How Starbucks Built a Company One Cup at a Time. New York, NY: Hyperion, 1997. Print.
 Ibid., 108.

navel." This resulted in a more zoomed in image that put more emphasis on the Siren and the vestiges of her fish tails. This logo was a sleeker and more modern logo, representing the current state of society. This logo was iconic, recognizable and resonated with many Starbucks customers. 143

On Wednesday, January 5, 2011, Starbucks unveiled their new logo in preparation for their 40th anniversary. This logo change represented the company's desire to become a company focused on consumer packaged-goods. When Schultz held a webcast meeting with the baristas, he revealed a new simple logo that did include the phrase "Starbucks Coffee." The removal of the phrase would emphasis the company's focus on producing and selling Starbucks-brand products in varying channels that go beyond retail stores. In this webcast, Schultz explained the reasoning for removing the phrase from the logo; he said, "Even though we have been and always will be a coffee company and retailer, it's possible we'll have other products with our name on it and no coffee in it." ¹⁴⁴ By removing the phrase Starbucks Coffee, the brand's transferability increases because the confusion of Coffee being in the brand name, while representing other products is detached. He stated that any new non-coffee products that fall under the Starbucks brand will still adhere to the high standards Starbucks applies to its coffee. Schultz says, "We're not going to put our name on things that dilute the quality of Starbucks." Starbucks has learned from the past; to build a strong brand they must stay true to their core values. In the past, Starbucks has expanded so quickly that they forgot about quality and creating the "Starbucks Experience". Schultz makes it clear that the company plans on developing

¹⁴³ Ibid., 309.

 ¹⁴⁴ Jargon, Julie. "Starbucks Drops Coffee From Logo." *The Wall Street Journal*. 6 Jan. 2011. 8 May 2012
 http://online.wsj.com/article/SB10001424052748704405704576063940765196656.html.
 145 Ibid.

Starbucks non-coffee products and will ensure that the brand is not diluted by products of low quality.

On March 8, 2011, Starbucks marked its 40-year anniversary. To celebrate this accomplishment, Starbucks revealed its new logo that will slowly be implemented throughout stores all across the world. 146 This new logo removed the phrase "Starbucks" Coffee" and merely displayed a green and white image of the two-tailed siren, eliminating the famous black and green background. Many loyal customers despise the new logo, while some really love and accept it. Starbucks acknowledged they anticipated the mixed reaction; the company was sure that this new elegant and simple design would help to transform the Starbucks Experience and increase the transferability of the brand as a whole. They have unleashed the romantic Siren that has represented Starbucks over the last forty years and are hoping that this new logo creates a wave of energy that will inspire customers for the next forty years. Designers believe that the Starbucks siren is a strong logo and it does not need its name "Starbucks Coffee" to clarify. 147 The company felt that they no longer to reinforce the company's name at every chance. Also, the new wordless logo will help the company smoothly transition its expansion into product lines that go beyond coffee and into a vast array of business lines; across domestic and international stores. By removing the word "Coffee" from the name, the company will create a space for their non-coffee products. ¹⁴⁸ Especially since their international market products, such as tea, are confusing to their customers since these products do not have

¹⁴⁶ Schultz, Howard. "A Look at the Future of Starbucks." *Starbucks Coffee Company*. 5 Jan. 2011. 08 Mar. 2012 http://www.starbucks.com/blog/looking-forward-to-starbucks-next-chapter.

¹⁴⁷ Sauer, Abe. "Starbucks New Logo a Mid-Life Crisis in the Making." Brandchannel.com. 5 Jan. 2011. 08 Mar. 2012 http://www.brandchannel.com/home/post/Starbucks-New-Logo-Black-Eye.aspx>.

¹⁴⁸ P, Mike. "Bringing the Siren to Life."" Starbucks Coffee Company. 5 Jan. 2011. 08 Mar. 2012 http://www.starbucks.com/blog/bringing-the-siren-to-life/645.

coffee in them. As Starbucks enters these new product lines, they will maintain their current customer base and simultaneously form new relationships with new customers.

Schultz was aware of the risks of such drastic changes of the Starbucks logo, but he "looked to companies like Nike Inc. and Apple Inc., which had earned the power of consumers to drop their names from their logos. And as Starbucks closely watched the failure of stores like Gap Inc., which launched a new logo in October only to withdraw it after harsh criticism by customers and others." ¹⁴⁹ Companies know that the public does not usually respond well to brand changes. However, Starbucks' believes that their brand is strong enough to be represented by the siren alone, which will ultimately allow customers to identify with the new, more diversified Starbucks. This type of logo recognition has only been accomplished by a few businesses around the world. The new logo pays tribute to Starbucks' heritage, and positions Starbucks for a future of endless opportunities. The world has changed and so has Starbucks. According to Schulz, the new interpretation of the logo preserves the essence of the Starbucks experience. Schulz explains that by revamping the logo, Starbucks' has allowed the siren to come out of her circle and stand alone; this will give the company the flexibility to come out of the confines of a strictly coffee-oriented business and expand into many different areas in the quick-stop, gourmet food industry. 150 The company has stated that no matter what changes Starbucks' goes through, the company will never stray from their core values. Ever since the beginning, from the opening of the first store: Starbucks has always created a unique retail experience by providing a "third place" for its customer between

¹⁴⁹ Sauer, Abe. "Starbucks New Logo a Mid-Life Crisis in the Making." Brandchannel.com. 5 Jan. 2011. 08 Mar. 2012 http://www.brandchannel.com/home/post/Starbucks-New-Logo-Black-Eye.aspx.

¹⁵⁰ Schultz, Howard. "A Look at the Future of Starbucks." *Starbucks Coffee Company*. 5 Jan. 2011. 08 Mar. 2012 http://www.starbucks.com/blog/looking-forward-to-starbucks-next-chapter.

their work place and home. Starbucks creates the Starbucks Experience, making emotional connections between the partners and customers every day. Schultz explains that the siren represents Starbucks' heritage and has represented the company for four decades, reminding the company of its core values and ensuring that the company always remains true to its roots.

In the video, "True to Our Heritage" that is located on Starbucks's website,

Howard Schultz talks about Starbucks new logo change and Starbucks's plan to evolve
the company. Schultz states:

"In March of 2011, we will celebrate the 40th anniversary of our company. There is some symmetry to getting to do this at the same time. This new evolution of the logo does two things that are very important, it embraces and respects our heritage and at the same time evolves us to a point where we feel it is more suitable for the future. It is important to go back in the history, we embraced the siren. So now here we are, the world has changed and Starbucks has changed. The new interpretation of the logo at its core is the exact same essence of the Starbucks experience; the love we have for our coffee, the relationship we have with our partners the connection we build with our customers. We have allowed her to come out of her circle in a way that gives us the freedom and flexibility to think beyond coffee. But make no mistake, we have been, we will continue to be, and we will always be the world's leading purveyor of the highest quality coffee." 151

Schultz describes the company's preparation to mark forty years and the company's plans for the future. He emphasizes that Starbucks will start to expand their company while staying true to their roots and core values. In addition to this video, the company posted numerous articles informing customers about the company's new vision and facts about the Siren. 152

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Schultz, Howard. "A Look at the Future of Starbucks." *Starbucks Coffee Company*. 5 Jan. 2011. 08 Mar.
 2012 http://www.starbucks.com/blog/looking-forward-to-starbucks-next-chapter.
 Ibid.

On the Starbucks website, Schultz posted an article on January 5, 2011 titled "Looking Forward to Starbucks Next Chapter." This article informed customers about Starbucks new direction. Schultz mentions the difference between the original Pike Place store in Seattle, and the newly refurbished Olive Way Store. One store displays the future of Starbucks, while the other honors the company's past; but at the core, both stores are identical as they create a Third Place for Starbucks customers, offer the finest coffees, and build relationships with customers every day. Schultz acknowledges the changes that Starbucks has gone through in the last four decades and mentioned how the Siren has been there from the very beginning. Schultz states, "Starbucks will continue to offer the highest-quality coffee, but we will offer other products as well – and while the integrity, quality and consistency of these products must remain true to who we are, our new brand identity will give us the freedom and flexibility to explore innovations and new channels of distribution that will keep us in step with our current customers and build strong connections with new customers." ¹⁵³ Schultz informs customers that the evolutions will start to take place this Spring.

In the company's 2011 annual report, Schultz describes in his note to shareholders the future of the company:

"In 2011, we continued to evolve into a truly dynamic global organization, offering a portfolio of products to serve customers in our retail stores, at home, at work, on the go and online. Coffee remains our core and continues to drive our global business, and last year we launched fantastic

¹⁵³ Schultz, Howard. "Looking Forward to Starbucks Next Chapter." *Starbucks Coffee Company*. 5 Jan. 2011. 08 Mar. 2012 http://www.starbucks.com/blog/looking-forward-to-starbucks-next-chapter.

new products while dramatically improving the ways in which those products reach customers."¹⁵⁴

Schultz expresses Starbucks plan for the future of the company and address the company's change in direction. In addition to this new blueprint, Schultz address Starbucks 40th anniversary. He informs shareholders that this day will celebrate the honor the company's past and celebrate the company's future. When mentioning the logo change in his letter, he states, "This year, we will roll out our elegant new brand identity with an evolved logo that embraces our history while granting us more freedom and flexibility to think beyond coffee and even beyond our stores. A great deal of thought went into creating the new design, and we believe it sets the stage for our next chapter." Schultz is very candid about the company's past difficulties and utilizes them better the company's future.

In reference to the company's trademarks, the financial statements describe the accounting for patents, trademarks, copyrights and domain names. Starbucks owns numerous trademarks throughout the world. Generally, these trademarks are renewable as long as they are in use and properly maintained.

5.2 Brand's Elements

The Starbucks brand does a good job in meeting all of the six elements for brand success: memorability, meaningfulness, likability, transferability, adaptability, and

¹⁵⁴ Starbucks. 2011 Annual Report. Seattle, WA: Starbucks Corporation, 2011. Starbucks Investor Relations: 2011 Annual Report. 2011. 23 March 2011. http://investor.starbucks.com/phoenix.zhtml?c=99518&p=irol-reportsAnnual

¹⁵⁵ Starbucks. 2010 Annual Report. Seattle, WA: Starbucks Corporation, 2010. Starbucks Investor Relations: 2010 Annual Report. 2010. 22 March 2010.

protectability. The brand is memorable because of the recognizability component. In terms of their brand likability, their name is strong, but their logo is a little weak, the likeability of both combined is what stays in consumers' minds. Starbucks has excelled in creating an experience for customers, who have turned into brand advocates themselves. Starbucks' has consistently changed their logo to stay modern and appealing, while introducing new programs to compete with upcoming trends.

The adaptability of the brand name has proven strong with its entrance into the realm of social media. In terms of meaningfulness, it is important that brand elements correlate with the product category. While the Starbucks name is strong, the siren logo is not as correlated with the product base as one would think. The siren does not immediately make people think of coffee, but perhaps this is exactly what Starbucks' was striving for. Howard Schulz said, "We were never in the coffee business serving people, we were in the people business serving coffee." As Starbucks expands and moves into other product lines, the vagueness of the logo may be exactly what it needs to rely on. Starbucks has made a conscious effort to improve the transferability of the brand. They have dropped the word "coffee" from their name, allowing them to brand other products like tea, merchandise, music and more.

With an increase in the brand name's transferability, Starbucks need to increase its brand names protection to ensure that competitors outside of the coffee market do not manipulate the Starbucks name to sell other products.

It is important to remember that a logo is a big factor to a company's brand name and identity. Modifying the company's logo parallels giving the company plastic surgery;

¹⁵⁶ Behar, Howard. *It's Not about the Coffee: Leadership Principles from a Life at Starbucks*. London: Penguin, 2009. Print.

too much modification can cause the customers to not recognize the brand anymore and diminish its strong brand name. There are appropriate time and reasons to modify a company's logo; but it is an important decision that needs to be thoroughly thought out and executed. Companies may feel the need to modify their logo if their logo does not accurately represent the new direction the company may take or has already implemented, the logo is simply outdated, or the logo has to be rebranded to recover from a disaster.

Starbucks' logo change is reasonable because it represents their mission for expansion into other product lines and sales methods to start new distribution channels. Either way, the issue is not about whether the company's logo was positively or negatively received by the customers, but whether this logo change can evoke passion and capture the attention of customers.

The new logo focuses on bringing the siren to life. On January 5, 2011, Starbucks's senior creative manager, Mike Peck, released a statement on the Starbucks Website titled, "Bringing the Siren to Life". ¹⁵⁷ In this article, he mentions that when Starbucks executives first heard about the possibility of modifying the Starbucks identity, there were endless possibilities and suggestions. This project took a long time and many people contributed to the design and launch of the new logo. He stated, "From the start, we wanted to recognize and honor the important equities of the iconic Starbucks logo. So we broke down the four main parts of the mark – color, shape, typeface and the Siren. After hundreds of explorations, we found the answer in simplicity. Removing the words from the mark, bringing in the green, and taking the Siren out of her ring. For forty years

¹⁵⁷ P, Mike. "Bringing the Siren to Life." *Starbucks Coffee Company*. 5 Jan. 2011. 08 Mar. 2012 http://www.starbucks.com/blog/bringing-the-siren-to-life/645.

she's represented coffee, and now she is the star." ¹⁵⁸ The idea of simplicity and removing the infamous Siren from her ring would make her the star she truly is.

Starbucks and its infamous Siren were finally free to go beyond the world of coffee and expand into different product lines and opportunities.

Peck, also informs consumers about the improvements in design technology that have really enhanced the new Starbucks logo. In his article, he states, "The 20-year old logo was built in the early days of AutoTrace and it showed – points everywhere. We improved composition, brought in more sophisticated stroke width and spacing and a smoother line flow. When it came to her – the Siren – we enhanced her form in subtle ways, smoothing her hair, refining her facial features, weighting the scales on her tail to bring the focus to her face. "¹⁵⁹ With access to improved technology, the designers were able to improve the composition and overall appeal of the logo.

Also, with the assistance of Lippincott, an amazing branding firm, the siren's hair was smoothed and her facial features were enhanced. Also, the scales of her tails were less noticeable to emphasize the beauty in her face. This logo is a bold statement that expresses the company's energy and bright future. Dropping the name from the logo suggests Starbucks believes the success of the company can rest on the power of the siren alone. ¹⁶⁰

The Starbucks Global Creative teams worked with Lippincott to rebrand the company not just enhance the quality of the logo. "The design development is only part

160 Ibid.

¹⁵⁸P, Mike. "Bringing the Siren to Life." *Starbucks Coffee Company*. 5 Jan. 2011. 08 Mar. 2012 http://www.starbucks.com/blog/bringing-the-siren-to-life/645.

¹⁵⁹ Ibid.

of a brand revitalization program." 161 Starbucks and Lippincott strived to refresh the Starbucks brand and signal the company's return to success. When Starbucks asked Lippincott for their assistance, Starbucks had already spent months analyzing the market and conducting a brand audit. The bold decision to free the Siren was idea that as chosen since; as Jeffery Fields, Vice President of global creative group states, "Starbucks was founded on the idea of people serving coffee. People have always come first. And today, the value of the personal connections has become much more meaningful than product or beverage." Therefore, the only choice was to liberate the Siren and allowing the customers to make a personal connection with the Siren and the Starbucks brand. Starbucks expressed to Lippincott that they wanted to bring a global perspective to the company's identity; they wanted guidance on how to develop a global implementation tactic, how to define brand elements. Mike Peck, senior design manager of Starbucks's global creative group, stated, "We never set out to change our logo; we set out to evolve the brand. Our goal was to have the Starbucks identity first and foremost express the brand and the evolved sensibilities. We need a mark that could stand on par with the updates to the business, stores, and product portfolio." ¹⁶² In *The New Strategic Brand* Management, the authors state rejuvenating a brand is "based on an updating of the overall offer of the bran while staying true to part of it identity." ¹⁶³ A company who wishes to evolve and revive their brand focuses on a different growth market. A new

¹⁶¹ Abbot, R., Birdsall, C. and Murphy, B. (2011), Branding Inside Out and Outside In. Design Management Review, 22: 26–33. http://onlinelibrary.wiley.com/doi/10.1111/j.1948-7169.2011.00137.x/full ¹⁶² Ibid

¹⁶³ Schultz, Howard, and Joanne Gordon. *Onward: How Starbucks Fought for Its Life without Losing Its Soul*. New York, NY: Rodale, 2011. 238-246. Print.

brand must be relevant to the new market." Lippincott was crucial in demonstrating what the brand elements looked like on actual products; this resulted in Avenir as the primary font, making Centennial secondary. In addition to this change in typeface, Starbucks departed from its nautical-themed patterns and stressed signature Starbucks's cues derived from the Siren. Lippincott also provided important service work; with Lippincott's successful rebranding for other global brands, Lippincott gave Starbuck's the confidence to make such a bold move. Not only did Lippincott improve the new logo, they revitalized and repositioned the brand through their efforts in managing the company's execution and brand rollout. Starbucks strived to reposition their brand and have it represent the idea of evolution.

However, some are concerned that the siren is not strong enough to stand alone. A better move may have been to just drop the word "Coffee" from the logo so that the logo would be more transferable and help to make the company's expansion into other product lines more successful. Since new customers will not really understand what the new logo represents, having the words Starbucks incorporated into the logo would have made the company's transferability more successful. Branding experts feel that dropping "Starbucks Coffee" will only confuse consumers who would not know that this siren symbolizes Starbucks, especially since the Siren does not have any obvious relation to coffee. However, some argue that because Starbucks has become synonymous with coffee, it does make sense to remove the word Starbucks along with the word coffee from the logo.

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¹⁶⁴ Simon, Bryant. *Everything but the Coffee: Learning about America from Starbucks*. Berkeley: University of California, 2009. 245. Print.

¹⁶⁵ Jargon, Julie. "Starbucks Drops Coffee From Logo." *The Wall Street Journal*. 6 Jan. 2011. 8 May 2012 http://online.wsj.com/article/SB10001424052748704405704576063940765196656.html.

Recently, one company has successfully removed the product name from its brand: Apple Computers. It is important to compare the removal of the word "Computer" from Apple's brand to the removal of "Starbucks Coffee". On January 9th, 2007, Steve Jobs made the announcement that "Computers" would be dropped from the company's name since the company has expanded into product sectors other than just personal computers. Apple successfully developed the Mac, iPod, iPhones, and AppleTV, only one of which was related to computers. And its logo, the apple, was immediately recognizable whether or not it was accompanied by the brand name: "Apple Computers." ¹⁶⁶ The difference between these two rebranding situations is when the point of rebranding took place. Apple had evolved enough to show that it was a company that represented more than computers; it was a brand that associated with the highest-level of cutting edge technology, sleek designs, and easy-to-use products. Whereas Apple rebranded after the completion of their successful product expansion, Starbucks has decided to drop "Starbucks Coffee" in hopes of using the rebranding to transition into new product industries. In addition, some critics note that Apple did not drop the entirety of their brand name because the apple logo is the company's name, but the power of Starbucks now solely rests on the siren, which does not directly connote coffee.

¹⁶⁶ Sauer, Abe. "Starbucks New Logo a Mid-Life Crisis in the Making." Brandchannel.com. 5 Jan. 2011. 08 Mar. 2012 http://www.brandchannel.com/home/post/Starbucks-New-Logo-Black-Eye.aspx.

6. Valuing Brands

6.1 BrandZ

In an article titled, "Tracking the Value of the World's Major Brand" several top companies ran annual brand valuations. These brand values were measured by the cash flows each company created. There are two components to determining the future of brands: art and science. Mathematical formulas and skilled forecasting, which determines a company's reputation and valuation of the brand will be three years from now, determine these brand valuations. BrandZ Top 100 brand is a major brand rating that bases its data on "the published, extensive results of over 650,000 people who were quizzed across thirty-one countries, comparing over 23,000 brands." ¹⁶⁷ BrandZ analyzes consumer data to determine the value of brands. According to BrandZ, "Brand value is the financial value of a brand defined as the sum of all earnings that a brand is expected to generate." ¹⁶⁸ In the 2009 BrandZ Top 100 Full Report, Starbucks brand value dropped 40 percent. Customers were not willing to pay a premium for their good there were producing; Starbucks destroyed their brand value through its overexpansion of stores. 169 BrandZ used an equation to measure the companies brand values: intangibles corporate earnings multiplied by brand contribution and multiplied by brand multiple. The intangible company earnings were derived from Bloomberg's Datamonitor and Millward Brown Optimor's additional research. Company's brand contribution is the portion of

167 2009 BrandZ Top 100 Most Power Brands. Rep. Millward Brown, 2009. Web. 5 Mar. 2012.

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http://www.brandz.com/upload/brandz-report-2009-complete-report%281%29.pdf Thid

¹⁶⁹ Ibid.

intangible earnings that is determined solely by the brand; this number was based on customer loyalty data located in the BrandZ database. The last calculation, brand multiple, is a projection of the brand value according to market valuations, risk factors, and potential for growth; brand momentum represent the company's potential for short-term growth.

The BrandZ Top 100 Most Valuable Global Brands report is commissioned by WPP and undertaken by Millward Brown Optimor, the experts in branding valuations. BrandZ is the only brand ranking system to include consumer data when calculating brand values. In the sixth annual report, David Roth, CEO of WPP, states, "Brand plays an important – and measurable – role... The value of the BrandZ Top 100 Most Valuable Global Brands increased 64 percent since 2006." All of these strong brands have experienced a tumultuous economy, but they were resilient during these times because their strong brands protected them and allowed them to be resourceful through product innovation and close customer relationships. In BrandZ 2010 report, Joanna Seddon, CEO of Millward Brown Optimor, states, "companies with strong brands, such as Starbucks and Samsung, have the ability to recover faster from difficulties." ¹⁷¹ Especially in this uncertain economy, a strong brand is important because customers are more diligent when deciding where to spend their dollars. According to BrandZ data, which contains on the largest databases in the world, "On average worldwide, only 7 percent of consumers buy on price alone, down from the 20 percent ten years ago. In contrast, 81

¹⁷⁰ 2011 BrandZ Top 100 Most Power Brands. Rep. Millward Brown, 2011. Web. 5 Mar. 2012. http://c3232792.r92.cf0.rackcdn.com/WPP_BrandZ_2011.pdf

¹⁷¹ 2010 *BrandZ Top 100 Most Power Brands*. Rep. Millward Brown, 2010. Web. 5 Mar. 2012. http://www.wpp.com/NR/rdonlyres/65F2F519-0A74-423C-ADC7-DC7B0FCE7E5C/0/brandz_top100_2010.pdf.

percent regard brand as an important consideration."¹⁷² Brand is a very valuable asset as it significantly contributes to a company's earnings. A brand comprises of a company's reputation and the trust the company builds with its customers.¹⁷³ As stated in the 2010 BrandZ report, customers turned to "familiar and trusted brands that delivered on their promises provided an element of certainty in a turbulent time. Many brands maintained and grew their value, even when selling at a premium price."¹⁷⁴ Also, in addition to the shift in consumer attitude from philanthropy to responsibility, consumers are concerned with whether or not what they are buying was made responsibly.

6.2 Starbucks Brand Valuation

Ever since BrandZ released its first Top 100 Global Brand ranking in 2006,
Starbucks has appeared at the top of the ranking. Starbucks first appeared as the 48th Top
Most Valuable Global Brand valued at \$11,077,000. Starbucks was ranked 6th in the Top
10 Brands with Highest Brand Momentum and ranked the second in fast food. ¹⁷⁵ In
2007, Starbucks held its position in the fast food sector and improved its overall ranking
to the 35th Top Most Valuable Global Brand valued at \$16,057,000. Starbucks increased
its ranking to the 4th Top 10 Brands with Highest Brand Momentum and had a positive

¹⁷² 2011 BrandZ Top 100 Most Power Brands. Rep. Millward Brown, 2011. Web. 5 Mar. 2012. http://c3232792.r92.cf0.rackcdn.com/WPP BrandZ 2011.pdf>

Moore, John. *Tribal Knowledge: Business Wisdom Brewed from the Grounds of Starbucks Corporate Culture*. Chicago, IL: Kaplan Pub., 2006. 23-27. Print.

¹⁷⁴ 2010 *BrandZ Top 100 Most Power Brands*. Rep. Millward Brown, 2010. Web. 5 Mar. 2012. http://www.wpp.com/NR/rdonlyres/65F2F519-0A74-423C-ADC7DC7B0FCE7E5C/0/brandz top100 2010.pdf>.

¹⁷⁵ 2006 BrandZ Top 100 Most Power Brands. Rep. Millward Brown, 2006. Web. 5 Mar. 2012. http://www.brandz.com/upload/2006_BrandZ_Ranking_Report.pdf>.

change in brand name value of 45 percent. ¹⁷⁶ In 2008, the company's internal problems became apparent and were reflected in their brand value. The company dropped down to 56th Top Most Valuable Global Brand and was valued at \$12,011,000. It was completely removed as one of the Top Brands with the Highest Momentum chart, but still maintained its ranking as second in the fast food sector. The brand reported a negative 25 percent change in the value of the brand name. ¹⁷⁷ In 2009, Starbucks was ranked the 89th Top Most Valuable Global Brand and was valued at \$7,260,000. Starbucks entered the coffee sector into the 6th position; resulting in a brand value of \$848,000, a 2 percent change in brand value and high number in brand contribution. Since customers view Starbucks as a luxury brand, the consumers have a strong bond with the brand. Unfortunately Starbucks did not see similar results in the fast food sector. Starbucks dropped down to fourth in the fast food sector; reporting \$6,413,000 brand value and a 43 percent decrease in brand value. Starbucks was able to maintain its overall position on the Top Most Valuable Global Brands ranking due to its ability to stay relevant. Starbucks launched its instant coffee line to follow the trend of consumers who were trading down from one category into another category: replace coffee from coffee houses with quality coffee that is prepared at home. 178

In 2010, the efforts from CEO Howard Schultz were apparent. Starbucks focused on reinventing their brand and adjusted the different consumer spending habits caused by the recession. Starbucks lowered prices on simple coffee drinks and charged a higher

¹⁷⁶ 2007 *BrandZ Top 100 Most Power Brands*. Rep. Millward Brown, 2007. Web. 5 Mar. 2012. http://www.brandz.com/upload/BrandZ 2007 Ranking Report.pdf >.

¹⁷⁷ 2008 *BrandZ Top 100 Most Power Brands*. Rep. Millward Brown, 2008. Web. 5 Mar. 2012. http://www.brandz.com/upload/BrandZ 2008 Ranking Report.pdf >.

¹⁷⁸ 2009 BrandZ Top 100 Most Power Brands. Rep. Millward Brown, 2009. Web. 5 Mar. 2012. http://www.brandz.com/upload/brandz-report-2009-complete-report%281%29.pdf

premium for extravagant drinks. They also adjusted to changes in consumer tastes by offering healthier options on their menu. Schultz,' closure on many underperforming stores managed to strengthen the brand and stop the brand's dilution caused by overexpansion. Starbucks positively utilized the growth and power of social media by authentically using it while staying in tune with the brand core values. The Starbucks Facebook site is followed by 6 million fans and the brand's leadership is apparent with the Starbucks iPhone app that allows users to check their Starbucks card and receive varying benefits. In fact, some test markets, the app allows customers to use their mobile phones to pay for their purchases. With these efforts, Starbucks increased its ranking to the 85th Top Most Valuable Global Brand and was valued at \$8,490 million and bumped its fast food ranking up to third. Starbucks also bumped up its rankings in the coffee Starbucks to 5th with a 17 percent increase in brand value, reporting a \$988,000 brand value. Starbucks coffee is sold as a premium brand in supermarkets; during the recession, Starbucks sold value packs to increase its competiveness. "Although the value of the coffee category declined overall, the renewal of the Starbucks brand resulted in a 17 percent rise in value." ¹⁷⁹ This was caused by the company's strong brand name and the connection that Starbucks has with its customers.

In 2011, Starbucks finally posted a positive growth in their brand value on the BrandZ Top 100 Most Valuable Global Brands ranking; ranked 72nd with a brand value of \$11,901,000 and a 40 percent growth in brand value. The brand reinventions that were implemented by Howard Schultz, two years ago were displayed. Starbucks was brand

¹⁷⁹ 2010 *BrandZ Top 100 Most Power Brands*. Rep. Millward Brown, 2010. Web. 5 Mar. 2012. http://www.wpp.com/NR/rdonlyres/65F2F519-0A74-423C-ADC7DC7B0FCE7E5C/0/brandz_top100_2010.pdf.

new and their strength of brand name was apparent as customers did most of the advertising for the company. During 2011, Starbucks launched their breakfast line, revised pricing and a revamped Starbucks Experience. The snacks contributed to the sales of fast-food brands; Starbucks was able to successfully add a \$1.50 price point for coffee while still charging a premium for their more intricate drinks. Even with these prices, Starbucks saw growth in traffic and profits. BrandZ removed the coffee sector from their 2011 report since the coffee sector seemed to have merged with the fast food sector as more fast food chains started to serve coffee drinks. It can be assumed that Starbucks would have jumped up since in the coffee sector with their successful single serve K-cups. Please refer to *Table 1* for the BrandZ Comparison of Starbucks from 2006 to 2011.

Even with all of the internal problems Starbucks has dealt with over the year, the company still remained to hold onto its strong brand name. With the revamping of the brand and the entire company, the Starbucks brand name is starting to become more highly valued; reporting a positive trend in brand value. By looking at lists such as BrandZ, financial users are able to see how much company's brand names affect the entity as a whole.

¹⁸⁰ 2011 BrandZ Top 100 Most Power Brands. Rep. Millward Brown, 2011. Web. 5 Mar. 2012. http://c3232792.r92.cf0.rackcdn.com/WPP_BrandZ_2011.pdf

7. Estimating Starbucks's True Value

7.1 DCF of Starbucks

Financial statements strive to reflect a company's current book value. By comparing a company's shareholders equity, determined by the numbers stated on their financial statements, to the company's market value, the value of intangible assets can be estimated. Theoretically, the market should be pricing in a company's intangibles such as brand name and the company trademark. Because of this, performing a DCF of the company to obtain the value of the firm's share price based solely on the firm's cash flow generating ability and comparing this valuation to Starbuck's current trading price should reflect, at least in part, the value the market places on the firm's intangibles.

According to NASDAQ, as of March 9, 2011, Starbucks has a current share price of \$51.84. 181 Using a discounted cash flow analysis to value Starbucks Company using the time value of money, I calculated an implied share price of Starbucks based on the information presented in the 2011 consolidated financial statements. The DCF of Starbucks was projected over five years: 2011 to 2016. Using the assumption of a growth rate of 8.6%, I predicted the company's future cash flows over five years.

Using the company's financial statements, I was able to calculate the company's revenue growth rate. This calculation only took into account the revenue for years 2010 and 2011 because the company actually experienced a negative revenue growth rate between 2008 and 2009, resulting in the company to reevaluate their current situation.

¹⁸¹ SBUX: Profile for Starbucks Corporation. (n.d.) Retrieved February 19, 2012, from http://www.nasdaq.com/symbol/sbux/after-hours

The average of 2010 and 2011's growth rate is 9.4%. I increased this growth rate to 9.57% so that my enterprise value of the company would mirror the enterprise value of \$37.33 billion posted on March 11, 2012 by Yahoo! Finance. 182

To calculate the company's discount rate I calculated the company's Weighted Average Cost of Capital (WACC). There were two components of capital needed to be calculated: cost of debt and equity. Cost of debt was calculated by taking the percentage of yield-to-maturity on long-term debt and multiplying it by the tax shield, or one minus the tax rate¹⁸³. To determine Starbuck's tax shield, I gathered information from the company's annual report. Starbucks annual report 2011 stated, "Income taxes for the fiscal year ended 2011 resulted in an effective tax rate of 31.1% compared to 34% for fiscal 2010. 184 The effective tax rate of fiscal 2012 is expected to be approximately 33%." So I used 31.1% as the tax rate when calculating the earnings before interest and taxes for year 2011 and projected a 33% tax rate for the following years. This resulted in a 1.58% for cost of debt. To account for the company's cost of equity, I used the Capital Asset Pricing Model. This model states that equity shareholders require a minimum rate of return that is equal to the return from a risk-free investment in addition to a return for bearing additional risk. This extra risk is referred to as the "equity risk premium". The equation I used to calculate Starbucks's cost of equity was the WAAC formula:

$$Re = Rf + B * (Rm - Rf)$$

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¹⁸² SBUX: Profile for Starbucks Corporation. (n.d.) Retrieved February 19, 2012, from http://finance.yahoo.com/g/ks?s=SBUX+Key+Statistics

¹⁸³ Wasson, Dick D., and Donald E. Kieso. *Working Papers, Intermediate Accounting, Tenth Edition, Donald E. Kieso, Jerry J. Weygandt, Terry D. Warfield.* New York: Wiley, 2001.561-572. Print. ¹⁸⁴ Starbucks. *2011 Annual Report.* Seattle, WA: Starbucks Corporation, 2011. *Starbucks Investor Relations: 2011 Annual Report.* 2011. 23 March 2011 http://investor.starbucks.com/phoenix.zhtml?c=99518&p=irol-reportsAnnual

The cost of equity obtained from the CAPM equation was 12.96%, using the total equity value represented by Starbucks's outstanding shares.¹⁸⁵

Then I determined the Starbucks's capital structure by determining the proportion that debt and equity capital contribute to the entirety of the enterprise. Finally, I weighted the cost of the different capital by the proportion that each aspect contributes to the entire capital structure. By plugging all of these elements into the WACC equation, I concluded with a WACC of 11.7%. This discount rate was applied to the terminal value of the free cash flows I projected in my DCF analysis.

To conclude my DCF of Starbucks, I divided my equity value for Starbucks by the number of outstanding shares, resulting in an implied share price of \$44.05. Yahoo! Finance quoted the current share price for Starbucks at \$51.84 on March 12, 2012; which reveals there is a \$7.79 per share premium on Starbucks stock. Please refer to *Table 3* to see the results from the Starbucks DCF Analysis. The market holds Starbucks at a premium according to the discounted cash flow method; I attribute much of this to Starbuck's strong brand. Also, Schultz states in his letter to Shareholders,

"One way to measure our incredible success this year is certainly the shareholder value we have built. Our balance sheet has never been stronger and our profits never higher. However, I strongly believe that today's times require that companies be evaluated by more well-rounded measures. I still believe that shareholder value must be linked to creating value for a company's people, value for its customers and—perhaps now more than ever—value for the communities it serves. Balancing profitability and social conscience is as much a part of Starbucks core as coffee. As we continually ask ourselves how we might use our scale for good, we have answered by proactively addressing environmental issues

http://finance.yahoo.com/q/ks?s=SBUX+Key+Statistics

Wasson, Dick D., and Donald E. Kieso. Working Papers, Intermediate Accounting, Tenth Edition,
 Donald E. Kieso, Jerry J. Weygandt, Terry D. Warfield. New York: Wiley, 2001.561-572. Print.
 SBUX: Profile for Starbucks Corporation. (n.d.) Retrieved February 19, 2012, from

and supporting our partners' volunteer efforts, among many other things." ¹⁸⁷

He emphasizes that Starbucks is more than a coffee company; it is a company that its customers can be proud of, a business that is making a difference in communities and the entire world. All of these aspects are reason why Starbucks's shares are traded at a premium. There are many facets that Starbucks has internally generated and are not accounted for on the company's financial statements. The Starbucks brand, logo, and experience add an undeniable component to the company's value.

The DCF results show that there material information that is not accounted for on Starbucks's financial statements. The market value quotes Starbucks's stock at a premium; this concludes that the true value of the company is not accurately represented by the data presented in the company's financial statements. It is important to mention that although the company's financial statements meet all of the generally accepted accounting principles, they do not meet their core purpose: to display a company's true value to its users.

7.2 Sensitivity Analysis of Starbucks DCF

A Discounted Cash Flow Sensitivity Analysis is applied to the previous Starbucks DCF. This exhibits how the price per share premium changes as the growth rate assumption varies. A DCF Sensitivity Analysis usually attempts to quantify how the implied share price varies during different market conditions. An appropriate sensitivity

http://investor.starbucks.com/phoenix.zhtml?c=99518&p=irol-reportsAnnual

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¹⁸⁷ Starbucks. 2011 Annual Report. Seattle, WA: Starbucks Corporation, 2011. Starbucks Investor Relations: 2011 Annual Report. 2011. 23 March 2011

test time frame to apply to Starbucks is the 2008 recession. My hypothesis is that when stress testing Starbucks during 2008, the DCF analysis will still reveal a per share premium because of the effect that the Starbucks brand has on the company; even in times of distress, the brand name will carry the company.

To perform the analysis, I obtained Starbucks growth rate after the fiscal year 2008. The growth rate Starbucks experienced for fiscal year 2008 to 2009 was -6.75%. I obtained this number from a basic revenue growth calculation. When I applied the -6.75% growth rate to the DCF Sensitivity Analysis, keeping all other factors constant, the implied share price was approximately \$9.54. To obtain the per share premium for this time frame, I took an average of the 2008 monthly share prices from Yahoo Finance, which yielded a market share price of approximately \$18.00¹⁸⁸. The difference between the DCF implied share price and the 2008 market price yields a per share premium of \$8.46, confirming my hypothesis. Please refer to *Table 5* to see the results from the Starbucks DCF Sensitive Analysis. As displayed by these results, Starbucks was carried through the recession in part because of the strength of their brand. This sensitivity analysis strengthens my argument that an accounting standard for internally developed intangibles must be implemented.

¹⁸⁸ SBUX: Profile for Starbucks Corporation. (n.d.) Retrieved February 19, 2012, from http://finance.yahoo.com/q/ks?s=SBUX+Key+Statistics

8. Conclusion

Starbucks is more than a coffee company; it has built itself around core values that emphasize the importance of customer relations and providing customers with the Starbucks Experience. This connection is what has allowed the company to serve its customers at such a high premium for a long time. It is apparent that the company's financial statements do not reflect the true value of a company and that there are no adequate accounting standards for account for intangibles, especially for all that encompasses a company's brand. Financial statement users need to be wary of the limitations of financial statement reporting in terms of internally intangible assets.

Companies and analysts need to resort to other valuation methods to get a clear picture of a company's true value. Financial statement users must use other valuation techniques such as DCFs and rely on companies like BrandZ to help them understand company's brand values.

The addition of SFAS142 definitely assisted in how company's record intangibles on the balance sheet when intangible assets are acquired, but it still neglected to address the issue of accounting for internally generated intangible assets. Internally generated intangibles need to be included in the financial statements to paint a clear picture of a company's value; especially if users believe the purpose of the financial statements is to reflect the true value of a company. Many powerful companies have already succeeded and monopolized their industries, and are now focusing on broadening their product lines and transitioning into other sectors. This study has revealed a company's brand can truly impact the value of the company; so we must develop accounting standards that can

accurately reflect the value of the company. Theoretically, the market value of a company accurately reflects a company's true value, but a company's book value needs to be updated with procedures that account for intangible assets.

Starbucks removal of "Starbucks Coffee" represents a huge risk that the company is willing to take, in hopes for an even bigger reward. Starbucks is a company that heavily depends on its reputation and brand to generate revenues. Its brand change displays that the company believes its brand name is strong and has the power to redefine the company. The company is relying on its brand name to drive its introduction into new products a success. In response to the company's book value Schultz stated, "I strongly believe that today's times require that companies be evaluated by more well-rounded measures." The effect of a company's brand has an impact on company's revenues; we need to discover a method to quantify values that these brand changes are having. By monitoring the success of Starbucks new logo and its launch into new product industries, the power of Siren will be tested.

Appendix of Tables and Figures

Table 1 – BrandZ Comparison of Starbucks from 2006-2011

BrandZ	BrandZ - Top 100 Most Valuable Global Brands	0 Most V	'aluable	Global	Brands	
Year	<u>2006</u>	2007	2008	2009	2010	2011
Most Valuable Global Brand - Ranking	48	35	56	68	85	72
Brand Value	\$11,077,000	\$16,057,000	\$12,011,000	\$7,260,000	\$8,490,000	\$11,901,000
Top 20 Risers	I	ı	ı	ı	ı	11
Top 10 Brands with Highest Brand Momentum	9	4	N/A	N/A	Removed	Removed
Fast Food Sector - Ranking	2	2	2	4	8	3
Fast Food Sector - Value	\$11,077,000	\$11,077,000 \$16,057,000	\$12,011,000 \$6,413,000 \$7,502,000 \$11,901,000	\$6,413,000	\$7,502,000	\$11,901,000
Brand Name Value	N/A	45%	-25%	-43%	17%	40%
Coffee Sector - Ranking	ı	ı	ı	9	5	Removed
Coffee Sector - Value	ı	ı	ı	\$ 848,000	\$ 848,000 \$ 988,000	Removed

Table 2 – Starbucks DCF Test

Starbucks-DCF	(ii	(in \$millions)										
Year		2010		2011	2012	2012 2013 2014 2015 2016	2014	2015	7	916		
Time				0	1	2	3	4		5		
EBIT	\$	1,437 \$		1,079	\$1,080	1,079 \$1,080 \$ 1,081 \$1,081 \$1,082 \$ 1,083	\$ 1,081	\$1,082	\$	1,083		
Depreciation	↔	2,355	↔	2,417	\$2,648	2,417 \$2,648 \$ 2,901 \$3,179 \$3,483 \$ 3,816	\$3,179	\$3,483	↔	3,816		
Capex	↔	441	↔	532	\$ 583	532 \$ 583 \$ 639 \$ 700 \$ 767 \$	\$ 700	\$ 767	↔	840		
Change in NWC	↔	<i>LLL</i> 100 100 100 100 100 100 100 100 100 10	↔	1,719	\$1,884	1,719 \$1,884 \$ 2,064 \$2,261 \$2,478 \$ 2,715	\$2,261	\$2,478	\$	2,715		
Growth Rate Assumption		9.57%								ι.	Termin	Terminal Value
Free Cash Flows			↔	1,245	\$1,261	1,245 \$1,261 \$ 1,279 \$1,299 \$1,321 \$ 1,344	\$ 1,299	\$1,321	⇔		∨	69,354
Discount Rate		11.69%										
Enterprise Value		\$37,310				Discount F	Discount Rate & WACC	CC				
Equity Value		\$33,189			Cost	Cost of Equity		12.960%				
Shares Outstanding		753.4			Total	Total Equity		\$4,387.30				
Implied Share Price		\$44.05			Cost	Cost of Debt		1.58%				
Current Share Price		\$51.84			Yield-To-M	Yield-To-Maturity		2.36%				
			_		Total Debt	Debt		\$549.50				
Per Share Premium		\$7.79			Mark	Market Value		\$4,936.80				
					E/1/			200 00				

Table 3 – Starbucks DCF Results

Starbucks DCF - Results (in	\$millions)
WAAC Assumption	11.69%
Implied Share Price	\$44.05
Current Share Price	\$51.84
Per Share Premium	\$7.79

Table 4 – Starbucks Sensitivity Test

STATUMERS DEF SEIIS	ILIVILY	Allalysis	E CE	nillions)								Te
Year 2010 2011		2010	•	2011	2012	2012 2013 2014 2015 2016	2014	2015	2016			est
Time				0	1	2	3	4		2		
EBIT	S	1,437	s	1,053	\$1,054	\$ 1,055	\$1,055	\$1,056	\$ 1,057	_		
Depreciation	S	2,355	8	2,417	\$2,489	2,355 \$ 2,417 \$2,489 \$ 2,564 \$2,641 \$2,720 \$ 2,801	\$2,641	\$2,720	\$ 2,801	_		
Capex	S	441	8	532	\$ 548	\$ 564	\$ 581	\$ 599	\$ 617	_		
Change in NWC	S	716	8	1,719	\$1,771	\$ 1,824	\$1,879	\$1,935	\$ 1,993	~		
Growth Rate Assumption		-6.75%								Ĭ	Terminal Value	<u>e</u>
Free Cash Flows			8	1,219	\$1,224	1,219 \$1,224 \$ 1,230 \$1,236 \$1,242 \$ 1,248	\$1,236	\$1,242	\$ 1,248	~	6,3	6,312
Discount Rate		11.69%										
Enterprise Value		\$7,737										
Equity Value		\$7,188										
Shares Outstanding		753.4										
Implied Share Price		\$9.54										
Current Share Price		\$18.00										
Per Share Premium		\$8.46										

 $Table\ 5-Starbucks\ DCF\ Sensitivity\ Analysis\ Results$

Starbucks Sensitivity	Test
Growth Rate	-6.75%
Market Price - FY 08 Average	\$18.00
Implied Share Price	\$9.54
Per Share Premium	\$8.46

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