Mark Details

Case Studies #1   15% (8-10 Pages double-spaced)

- Answer the 5 questions of the case, 3 marks will be allocated to each question based on: (1) did you grasp the concept being asked, (2) is your response logical, (3) are you consistent in your viewpoint throughout

CLOSING CASE

Starbucks

In 2006, Starbucks', the ubiquitous coffee retailer, closed a decade of astounding financial performance. Sales had increased from $697 million to $7.8 billion and net profits from $36 million to $540 million. In 2006, Starbucks' was earning a return on invested capital of 25.5%, which was impressive by any measure, and the company was forecasted to continue growing earnings and maintain high profits through to the end of the decade. How did this come about?

Thirty years ago Starbucks was a single store in Seattle's Pike Place Market selling premium roasted coffee. Today it is a global roaster and retailer of coffee with more than 12,000 retail stores, some 3,000 of which are to be found in 40 countries outside the United States. Starbucks Corporation set out on its current course in the 1980s when the company's director of marketing, Howard Schultz, came back from a trip to Italy enchanted with the Italian coffeehouse experience. Schultz, who later became CEO, persuaded the company's owners to experiment with the coffeehouse format—and the Starbucks experience was born.

Schultz's basic insight was that people lacked a "third place" between home and work where they could have their own personal time out, meet with friends, relax, and have a sense of gathering. The business model that evolved out of this was to sell the company's own premium roasted coffee, along with freshly brewed espresso-style coffee beverages, a variety of pastries, coffee accessories, teas, and other products, in a coffeehouse setting. The company devoted, and continues to devote, considerable attention to the design of its stores, so as to create a relaxed, informal and comfortable atmosphere. Underlying this approach was a belief that Starbucks was selling far more than coffee—it was selling an experience. The premium price that Starbucks charged for its coffee reflected this fact.

From the outset, Schultz also focused on providing superior customer service in stores. Reasoning that motivated employees provide the best customer service, Starbucks executives developed employee hiring and training programs that were the best in the restaurant industry. Today, all Starbucks employees are required to attend training classes that teach them not only how to make a good cup of coffee, but also the service oriented values of the company. Beyond this, Starbucks provided progressive compensation policies that gave even part-time employees stock option grants and medical benefits—a very innovative approach in an industry where most employees are part time, earn minimum wage, and have no benefits.

Unlike many restaurant chains, which expanded very rapidly through franchising arrangement once they have established a basic formula that appears to work, Schultz believed that Starbucks needed to own its stores. Although it has experimented with franchising arrangements in some countries, and some situations in the United States such as at airports, the company still prefers to own its own stores wherever possible.

This formula met with spectacular success in the United States, where Starbucks went from obscurity to one of the best known brands in the country in a decade. As it grew, Starbucks found that it was generating an enormous volume of repeat business. Today the average customer comes into a Starbucks' store around 20 times a month. The customers themselves are a fairly well-healed group—their average income is about $80,000.

As the company grew, it started to develop a very sophisticated location strategy. Detailed demographic analysis was used to identify the best locations for Starbuck's stores. The company expanded rapidly to capture as many premium locations as possible before imitators. Astounding many observers, Starbucks would even sometimes locate stores on opposite corners of the same busy street—so that it could capture traffic going different directions down the street.

By 1995 with almost 700 stores across the United States, Starbucks began exploring foreign opportunities. First stop was Japan, where Starbucks proved that the basic value proposition could be applied to a different cultural setting (there are now 600 stores in Japan). Next, Starbucks embarked upon a rapid development strategy in Asia and Europe. By 2001, the magazine *Brandchannel* named Starbucks 1 of the 10 most impactful global brands, a position it has held ever since. But this is only the beginning. In late 2006, with 12,000 stores in operation, the company announced that its long term goal was to have 40,000 stores worldwide. Looking forward, it expects 50% of all new store openings to be outside of the United States.[50]

Case Discussion Questions

1. What functional strategies at Starbucks' help the company to achieve superior financial performance?
2. Identify the resources, capabilities, and distinctive competencies of Starbucks?
3. How do Starbucks' resources, capabilities, and distinctive competencies translate into superior financial performance?
4. Why do you think Starbucks' prefers to own its own stores wherever possible?
5. How secure is Starbucks' competitive advantage? What are the barriers to imitation here?

NOTES

1. The concept of consumer surplus is an important one in economics. For a more detailed exposition see D. Besanko, D. Dranove, and M. Shanley, *Economics of Strategy* (New York: John Wiley & Sons, 1996).
2. However, $P = V$ only in the special case where the company has a perfect monopoly, and where it can charge each customer a unique price that reflects the value of the product to that customer (i.e., where perfect price discrimination is possible). More generally, except in the limiting case of perfect price discrimination even a monopolist will see most consumers capture some of the value of a product in the form of a consumer surplus.
3. This point is central to the work of Michael Porter. See M. E. Porter, *Competitive Advantage* (New York: Free Press, 1985). See also Chapter 4 in P. Ghemawat, *Commitment: The Dynamic of Strategy* (New York: Free Press, 1991).
4. Harbour Consulting, "Productivity Gap Among North American Auto Makers Narrows in Harbour Report 2006," *Harbour Consulting Press Release*, July 1, 2006.
5. M. E. Porter, *Competitive Strategy* (New York: Free Press, 1980).
6. This approach goes back to the pioneering work by K. Lancaster, *Consumer Demand: A New Approach* (New York: Columbia University Press, 1971).
7. D. Garvin, "Competing on the Eight Dimensions of Quality," *Harvard Business Review,* November–December 1987, 101–119; P. Kotler, *Marketing Management* (Millennium ed.) (Upper Saddle River, N.j.: Prentice-Hall, 2000).
8. J.D. Power Asia Pacific 2010 Malaysia Initial Quality StudySM (IQS), October 29, 2010, http://businesscenter.jdpower.com/news/pressrelease.aspx?ID=2010208 (accessed January 6, 2011); and "Proton Bomb," *The Economist,* May 8, 2004, 77.
9. C. K. Prahalad and M. S. Krishnan, "The New Meaning of Quality in the Information Age," *Harvard Business Review,* September–October 1999, 109–118.
10. See D. Garvin, "What Does Product Quality Really Mean," *Sloan Management Review,* Fall 1984, 26, 25–44; P. B. Crosby, *Quality is Free* (New York: Mentor, 1980); and A. Gabor, *The Man Who Discovered Quality* (New York: Times Books, 1990).
11. M. Cusumano, *The Japanese Automobile Industry* (Cambridge, Mass.: Harvard University Press, 1989); and S. Spear and H. K. Bowen, "Decoding the DNA of the Toyota Production System," *Harvard Business Review*, September–October 1999, 96–108.
12. W. Chan Kim and R. Mauborgne, "Value Innovation: The Strategic Logic of High Growth," *Harvard Business Review*, January–February 1997, 102–115.
13. G. Stalk and T. M. Hout, *Competing Against Time* (New York: Free Press, 1990).
14. Ibid.
15. M. E. Porter, *Competitive Advantage*.
16. H. Luft, J. Bunker, and A.C. Enthoven, "Should Operations Be Regionalized?" *New England Journal of Medicine* 301 (1979): 1364–1369.
17. S. Chambers and R. Johnston, "Experience Curves in Services," *International Journal of Operations and Production Management* 20 (2000): 842–860.
18. Source: G. P. Pisano, R. M. J. Bohmer, and A. C. Edmondson, "Organizational Differences in Rates of Learning: Evidence from the Adoption of Minimally Invasive Cardiac Surgery," *Management Science* 47 (2001): 752–768.
19. See P. L. Nemetz and L. W. Fry, "Flexible Manufacturing Organizations: Implications for Strategy Formulation," *Academy of Management Review* 13 (1988): 627–638; N. Greenwood, *Implementing Flexible Manufacturing Systems* (New York: Halstead Press, 1986); J. P. Womack, D. T. Jones, and D. Roos, *The Machine That Changed the World* (New York: Rawson Associates, 1990); and R. Parthasarthy and S. P. Seith, "The Impact of Flexible Automation on Business