Starbucks: A Strategic Change and Management Perspective

Master Thesis

Submitted in partial fulfilment of the requirements

for the degree of a

Master of Science in Management

Reader:	Name of Reader
Submitted by:	Your Name
	Student ID: Your Immatriculation ID
	Degree Program: Your Programme
	Semester of Study Semester
	Address
	ZIP Code and City
	Tel.: Phone Number
	Email: e-mail address
	Date of Submission: Calender date

Table of Contents

List of Figures and Tables

Introduction

Starbucks Coffee Company's success in the coffee business echoed resoundingly across the globe. The company was able to attract many customers despite its overpriced coffee. The coffee-chain managed to draw the attention of investors as well, as they saw in the Starbucks a profitable investment. Starbucks is best known for its overpriced coffee and its excellent stores adorned with comfortable couches and wonderful music. Starbucks marketed itself as the "Third Place" – a place where people can go aside from home and the workplace.

The rapid growth of Starbucks has become a success story in the business world and many people are bewildered by the company's business strategy. Who could have imagined a coffee outlet, selling overpriced coffee with fancy Italian names, can persuade people to buy its products, and can make these people happy? Why are financiers lured into investing in the company? Why do investors put their money in Starbucks stocks? What's in Starbucks that made it very successful in the coffee business, selling its products at grossly high prices and yet been able to attract both the buyers and the investors?

For sure, the speedy success of Starbucks is a mystery in the industry of coffee business. Starbucks' rivals were not able to match the rapid growth of the company. In a span of less than two decades, Starbucks was able to open tens of thousands of stores across the globe. The value of its shares in the stock market also increased rapidly, evidence of its attractiveness to investors.

However, the Starbucks "miracle" ceased to become a miracle. The fast-paced growth that the company experienced had gone to a sudden stop. Starbucks posted a

50% decline in profit by the end of the 2008 fiscal year. The company's stocks fell sharply to $9.44 at the end of 2008, from a high of $38.45 in mid-2007. Currently, the coffee store is undertaking a major organizational retransformation. The company's chief executive officer, James Donald, was sacked and was replaced by its former CEO Howard Schultz.

The company's business model seemed to have lost its magic. The sharp decline in all figures stated above makes it an interesting topic to be analysed. The company's success, which took decades to be achieved, had ceased at such a fast rate. It took only a year to have the success story turn into a disaster.

The company's very own principle of aggressive expansionism seemed to be the reason for its decline. Its expansionism cannibalized the coffee chain's luxurious nature. It lost its sense of exclusivity and high-end characteristics. The company has transformed into a mass marketer selling overpriced coffee to a diverse market segments, wealthy or not. It appears that the Starbucks outlets seem to have become like fast-food chains. The previous posh experience offered by Starbucks has now been challenged by the other food chains such as McDonald's and Dunkin Donuts. Hence a significant portion of Starbucks' customer base has been sliced and shifted to its competitors, who sell the same posh coffees at lower costs.

The company's SRI (socially responsible investments) funds seem to have not been delivering as well. The company has invested heavily in socially responsible activities such as environmental awareness campaigns, educational campaigns, acquisition of organic materials and donations to charitable and non-profit organizations. However, these investments appear to have not contributed to the company's revenue

and profit generations. The company seems to be losing money from these investments.

These circumstances make it interesting to study the Starbucks business model and how the company adopts to these situations. Business analysts are very much interested at the situation that Starbucks is in now. The company's sharp decline is a cause of wonder since Starbucks has been previously seen as a formidable company. This makes the Starbucks a very interesting company to study. Why did Starbucks fell sharply? What happened with its business model? How did it occur? These are the questions that need to be answered.

To answer these issues, Starbucks' business strategies and processes will be examined and its value chain will be evaluated. The company's primary and secondary activities and how these activities produce the company's desired output will be analysed to understand the company's downfall. Based on this study, recommendations for a strategic change will be put forward in an attempt to enhance the company's performance and bring back the magic of the "Starbucks Experience."

Research Methodology

In gathering information and data for this paper, the writer used various materials regarding the company. These include the company's website, online newspapers, magazines and online articles to collect preliminary data regarding the company's background and financial status. The writer also gathered information on online magazine articles and editorials that reflect the opinions and insights of business writers and editors, investors and analysts on the current situation of Starbucks. A major source of information was also taken from Taylor Clark's (2007) book detailing Starbucks'

history. Most of the quotations from Starbucks CEO Howard Schultz in this paper were taken from Mr. Clark's book as a reference to the chief executive's thoughts and opinions.

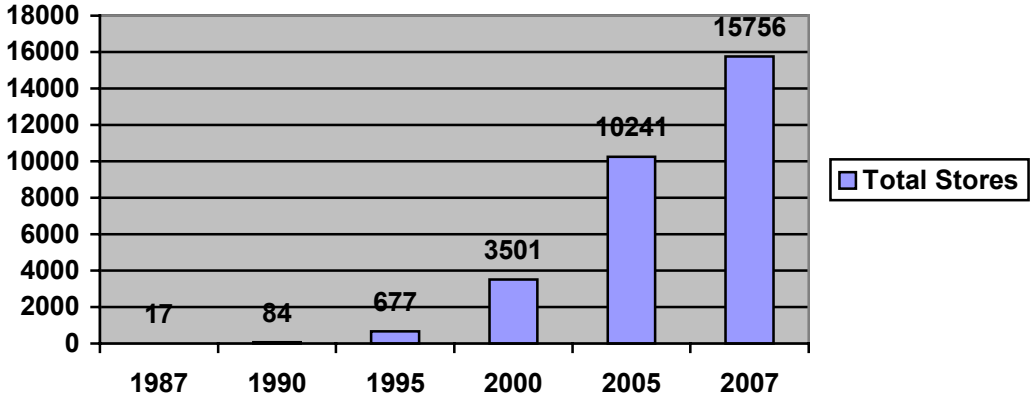
Academic books and journals written by known management, marketing and business academicians and scholars were used as a guide in analysing the current situation of Starbucks. These academic materials were also utilized to provide the basic principles for the recommendations on the need for a strategic change in the management and business operations of Starbucks. An online survey was also conducted to support the findings and conclusions drawn in this paper. The survey was conducted with a primary aim of getting the customer's insights and perceptions toward Starbuck's recent and past activities that include pricing strategy, Fair Trade activities, and other operational and management activities.

Company Background and Overview

Starbucks first opened its store in 1971 at Pike Place Market in Seattle. It was originally called Starbucks Coffee, Tea and Spices. The company first began its operations by providing coffee to restaurants and espresso bars. In the mid-1980s, then director of retail operations and marketing Howard Schultz introduced the idea of a coffeehouse to the company's founders, an idea he derived from his visit in Milan, Italy. Schultz was captivated by the popularity of espresso bars and coffeehouses in Italy, which he then relayed to the company founders. Due to the success of this idea, Schultz later established Il Giornale, which later became the Starbucks Coffee Company when the founders of the original Starbucks Company sold it to him. Since then, the company experienced steady growth.

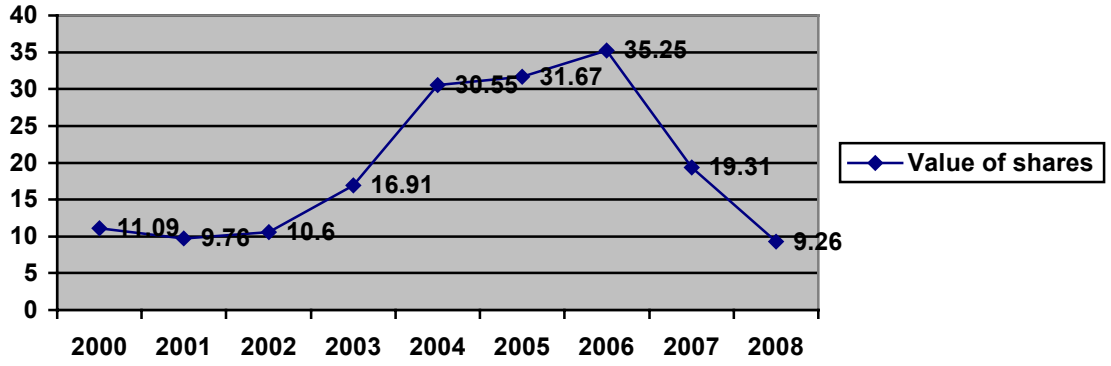
In 1991, the upward growth of Starbucks was beginning to gain ground and by the end of the decade, the company grew significantly. The 1990s was considered as the company's turning point toward becoming a giant company. However, it was at the start of the millennium that the Starbucks "miracle" through the introduction of the "Starbucks Experience" really occurred. The coffee store grew in leaps and bounds since the year 2000. On the first half of this decade, the company aggressively expanded in the domestic and international markets. Starbucks coffee shops began to open by the hundreds every year in the United States. Starbucks outlets have sprouted in almost every urban and suburban area in the U.S (see Figure 1). The coffee chain also started its aggressive expansion in the global market, opening hundreds of stores worldwide every year.

Figure 1 Total number of Starbucks outlets



In the period 2000-2007, the value of the company's stocks also leapt significantly. By the start of the year 2000, the company's stocks were valued at $8 each at the Nasdaq stock trading, then the stocks climbed to its highest at $38.45 in the middle of 2006 (see Figure 2). However, by 2007, the miracle began to dwindle and Starbucks is beginning to lose its magic.

Figure 2 Stock Trading History (2000-2008)



Note: The highest stock value was at $38.45 in May 9, 2006, Source: The New York Times

The Starbucks "magic" was on a large extent spearheaded by the company's core competencies and a strategy of focus and differentiation, which led to the company's success. Foremost among this strategy is the company's focus on a particular segment of the market. Starbucks has established personal relationship with its target customers. Its coffee shops are designed to have a cool, cozy feeling. The feel-good experience that the customers can have at a Starbucks outlet constitutes its strongest appeal to the public. Customers are enticed by the very design of the shop. Every Starbucks coffeehouse exudes a sense of luxury. The coffee outlet is obviously a high-end coffee shop that attracts the young and hip, and even those in the middle age and several elders who can throw in several dollars for a cup of a fancy coffee. At first, the stores attract only the "yuppies" (young professionals). Gradually, Starbucks succeeded in drawing even the executives, young and old, and people from all walks of life. Everybody appears to want to have a share of the "Starbucks experience" even at the price of an expensive coffee. This is where the Starbucks magic began.

The Starbucks Miracle

Many people are awed by the speed of the growth of Starbucks. The success of the coffee company in influencing the people's preference in buying coffee is something that could grab the attention of everybody, most especially investors. Starbucks has established a unique image of itself. Thus, it is clear that what the company is selling is not merely its coffee, but its brand image as well. Starbucks founder Howard Schultz said:

> I think we have managed to, with a simple cup of coffee and a very unique experience, enhance the lives of millions of people by creating a sense of community, by bringing people together and recognizing the importance of place in people's lives. In the last few years, I think it's become fairly evident that we're having this effect around the world (cited in Clark 2007a, p. 136).

Indeed, the Starbucks magic did not come from out of nowhere. It is the result of a careful planning and a thorough understanding of the buyer's behaviour, values and preferences. A number of business writers, editors and academicians have attributed the growth of Starbucks to its excellent operations management and marketing strategy.

The company's capabilities on market leadership, superior real estate locations and their supply chain operations allowed Starbucks to stand apart from its competitors and other companies in the coffee industry (Larson 2008). Starbucks managed to offer a place for overworked Americans to hang out and relax; an antidote to an overworked culture and people (Clark 2007b). The firm established the image of its coffeehouses as the "Third Place" – where people can relax, enjoy and experience a luxurious way of sipping coffee. This strategy somehow managed to penetrate the minds of Americans

who are always busy at work and are finding a good place to unwind without getting drunk, and to interact with other people.

The idea of providing a convenient place for the overworked people is, of course, not the almighty answer to the question, “Why did Starbucks succeed in attracting millions of people to buy its grossly overpriced coffee?” Putting up a coffeehouse is just one thing, projecting it as a luxurious place for rest and relaxation is another more difficult thing. It was on the second point that Schultz and his management team concentrated more of their efforts. Image building has been the core of Schultz’s strategy in building his own empire and creating a revolution in the business world. Starbucks invested heavily in improving the company’s brand and creating an image of a cozy coffeehouse where one can enjoy a relaxing and luxurious moment away from the busy and stressful environment of the workplace.

Whilst customers are attracted to Starbucks coffeehouses, stock market investors are also enticed by the company’s continuing growth. The firm has been receiving positive ratings from stock market analysts, its growth seems to be unstoppable and therefore, rate of profitability is high. Analysts have been rating Starbucks’ stocks as “buy” indicating that the company’s stocks are a good investment. One stockholder even said that he purchased Starbucks stocks at $11.40 per share in 2003 and was able to sell these stocks at $27 per share, gaining $15.6 on each shares of stocks (‘Starbucks (SBUX) “Trading Transparency”’ 2007). The primary reason was that the company commands a very strong image and has the ability to continuously grow (cited in Moore 2007). As evidenced by the steady growth in the Starbucks stocks from 2000 to 2007 (see Figure 2 above), the company enjoys a good flow of stock

market investments. Thus, prompting stock investors to buy SBUX stocks, which they can sell later for a higher profit. These are the factors that created the Starbucks miracle. Let us then examine the business strategy employed by Starbucks.

Starbucks' Basic Strategies

Competence-Based Strategy

Prahalad and Hamel (1990) stated that only few companies have proven themselves to be skilful at inventing new markets, quickly entering emerging markets and radically changing the behaviours and preferences of customers in established markets. They added that the decisive task of companies is to create an organization that is capable of infusing products with irresistible functionality or creating products that customer need but have not yet even realized. Starbucks is definitely one of these companies. There is no doubt that the firm was able to introduce products that not only exude luxurious characteristics but also able to create coffee products that made the customers fell they need these coffees.

Starbucks' strategy is one built on developing its core competencies to add value to its products and establish an image of luxury and elegance. Core competencies, as defined by Prahalad and Hamel (1990), are "the collective learning in the organization, especially how to coordinate diverse production skills and integrate multiple streams of technologies" (p. 81). Starbucks' core competencies are evident in its capability to harmonize its expertise in real estate, excellent marketing strategies, management capabilities, operational efficiency and human resource management.

Starbucks' founder Howard Schultz wants to build a company that is truly unique. The famed CEO capitalised on the company's core competencies in order to gain

competitive advantage and strategic competitiveness in the business. Taylor Clark (2007) described Schultz as a maverick businessman who loves to do things his own way and believes that he can achieve the impossible for his company. “This conviction that Starbucks can achieve the unachievable helps explain Schultz’s dismissal of any concerns about resistance to his company’s ubiquity” (Clark 2007, p. 137). Prahalad and Hamel (1990) state that core competence is not only about harmonising streams of technology, it is the organisation of work and the delivery of value as well. In the practice of Starbucks, the company has not only been able to harmonise technology and strategy but has organised its work very well. Schultz said, “I think the art and mystique of Starbucks has been our ability to do that [incorporating romance and theatre into its design] in a company that could be described as a chain” (cited in Clark 2007). Hence, Starbucks’ core competencies are a major source of the company’s competitive advantage in the specialty coffee industry.

Focus Strategy

Having established the competence-based strategy as a major factor in the Starbucks success, we are now to evaluate the company’s other strategies that it implemented or continues to implement to maintain its competitive advantage. According to Porter (1998a), there are three basic strategies a company can use to leverage itself in an industry; these are cost leadership, differentiation and focus. Cost leadership involves the strategy of producing low-cost but high quality products and reducing operational costs at all areas of the firm. Differentiation strategy entails the creation of unique products or services, with the consumers perceiving such products/services to be unique and adding value to it, thereby allowing the firm to put

premium prices on its products/services. The generic strategy of focus, meanwhile, is directed toward a specific segment or section of the consumer, and in combination with either the strategy of differentiation or cost leadership. Starbucks used the generic strategy of focus within its particular target consumer segment, with an emphasis to and in combination with the generic strategy of differentiation (Larson 2008).

Starbucks' target consumer base is composed of the wealthy and educated coffee drinkers who are willing to pay high prices for quality products and customer services (Larson 2008). The firm aims at a very narrow and specific portion of the consumers in the coffee industry. Thus, the company's strategy is focused on this segment and its products and services are especially designed to meet this particular consumer segment's needs or wants. In terms of blending the strategy of differentiation with focus, the Starbucks brand is presented with distinctive characteristics. Its coffees are mixed with other materials, whilst maintaining the credibility of the taste of the Arabica beans. The company uses Italian words in naming its products, which although difficult to pronounce appeared to be attractive to customers. But the most important unique feature of Starbucks is its brand image and reputation, developed through years of image building and marketing capabilities along with a team of managers and staffs who able to deliver first-rate customer service. As summarised by Biff Motley (2007), a marketer himself:

> I began to take note of the details that make Starbucks special. There are the obvious ones, like big, comfortable chairs; soft, well-focused track lighting; well-planned merchandising; and other atmospheric accoutrements. But the real

> differentiators, in my mind, are those details related to the way the place is managed (par. 2).

Hence, the generic strategy of focus has blended effectively with differentiation strategy and the firm mixed them well.

Distribution and Location

Another notable strategy of Starbucks is its admirable real estate management and the location of its coffeehouses. At first, the company's strategy in looking for a good location for its stores was by trial and error (Clark 2007). However, when their experiment in Canada succeeded, where a Starbucks coffeehouse was opened at the other side of the street where another Starbucks coffeehouse was situated, the company went on to open stores either literally a stone's throw away with each other or in close proximity to another Starbucks outlet. This strategy is focused on traffic patterns and demographic criteria (Stone 2008), wherein Starbucks coffeehouses are put on areas where many of its targeted consumers usually go. In every Starbucks location, all the details are carefully planned, like the weather conditions, the customer preferences and behaviours (Larson 2008). These details helped the company choose the location of its stores. So whether their outlets are literally facing each other or not, the company is willing to open these outlets as long as these criteria are studied and planned.

Summary

Having determined the history and background of the company as well as the fundamental strategies used, it can now be said that the Starbucks miracle is not a creation of an imaginary force but a product of years of building competence, strategy, outstanding customer relationship skills and careful planning in choosing store

locations. Hence, the company was able to leverage itself in the specialty coffee industry and reaped huge amounts of profits each year from this business. For the same reason, it was able to attract the affluent sector in society and thus bringing in the fortune to Starbucks out of its high-priced coffees. In this sense, since profits are coming in large quantities, the company also attracted investors when it went public in 1992 and started trading corporate stocks at the Nasdaq stock market.

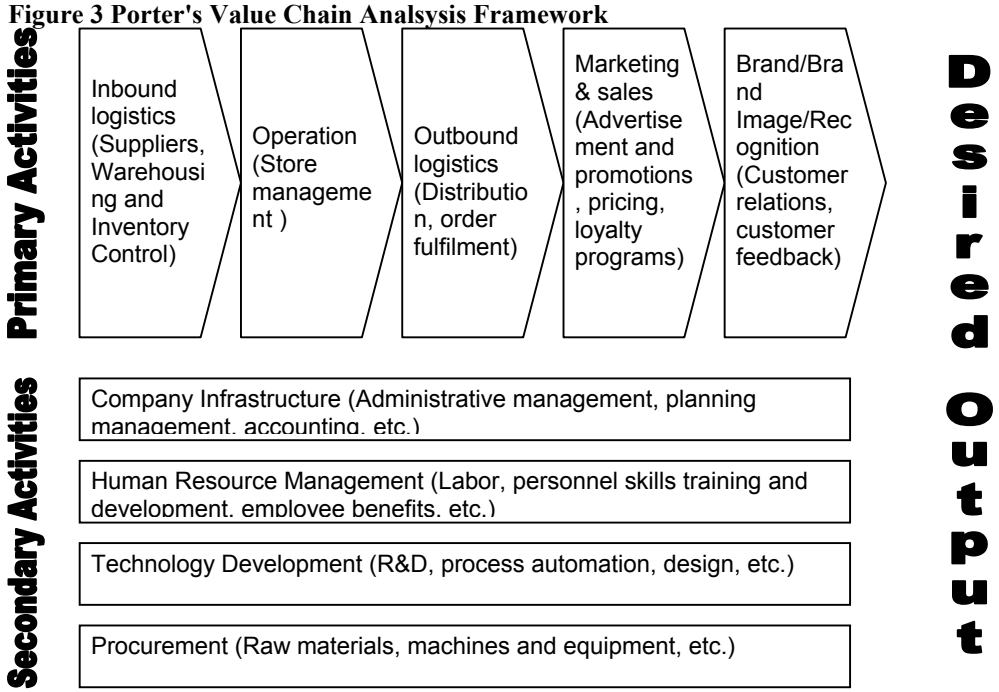
The Starbucks Value Chain Analysis

Michael Porter (1998b) states that acquiring competitive advantage can be done through an analysis of the company's value chain. A firm's value chain is "a system of interdependent activities which are connected by linkages" (p. 78). The value chain is embedded in the company's larger streams of activities, which are connected in linkages when one activity affects the effectiveness or costs of the other activities. Companies can attain competitive advantage when the value chain is optimised by co-ordinating these activities to create value for its products or services that exceeds the costs of performing the value activities (Porter 1998b). In other words, a company can create additional value for its products or services (and increase the prices of the same) without necessarily increasing the amount or costs of producing such products or services, and the customers are willing to pay for the added value.

A company's value chain system can be classified into two categories; (1) the primary activities, where it involves the physical creation of the products, marketing and delivery system, and after sale service and support activities; and (2) the secondary activities, wherein company infrastructure and inputs allow the primary activities to take place (Porter 1998b). When these activities are already defined, the value chain system

can be analysed in order to aid in the development of a strategic goal and gain competitive advantage or, in our case, to understand the current downfall in the Starbucks business model (see Figure 4 below).

Figure 3 Porter's Value Chain Analsysis Framework



Starbucks' value chain system, in the beginning, created additional value on its products, which the customers are willing to pay for. Hence, the firm is not reluctant to charge above-market prices for its products. In fact, its customers are not looking for the prices of the coffee but they are seeking for the quality of the products and brand image that the company offers. Let us then examine the Starbucks value chain and how it contributed to the company's current downfall.

According to Porter (1998b, p.80), every value activity has both physical and information-processing component. The physical component involves all the physical activities, which include individual or group tasks, processing the products, marketing and advertising, delivery and supply chain and continuing after sales service. The

information-processing component encompasses the steps required to capture, manipulate and channel the data necessary to perform the activity.

In the Starbucks value chain system, its primary activities include raw materials (coffee beans) procurement from suppliers, storing the coffees to keep it fresh, and an inventory system to maintain stocks and distribution to all outlets whilst maintaining the freshness of the beans. It also includes the management of stores/coffeehouses, marketing and promotional activities, sales and delivery and customer service/customer relations. These activities belong to the primary activity in the value chain in that it involves the creation of the product, selling, marketing and distributing the product to the consumers, and ensuring the continuing relationship with customers and consumers through service activities such as installation of equipment in stores/coffeehouses, repair and upgrading of these equipments and managing inventory to ensure continuous supply of the materials (coffee beans). All of these involve the physical activities that are necessary to perform in creating and selling its products to consumers and enhancing its brand image/ reputation.

The secondary activities, on the other hand, include the firm infrastructure to support these activities. These are corporate management functions (i.e. management or administrative planning), accounting and legal work. Also included in the secondary activities are human resource management (such as personnel skills development and training), determination of employee salaries, benefits and other emoluments, technological development (research and development activities, design, automated processing system, etc.) These are secondary activities that are necessary to support the primary activities and to provide inputs and services to manufacture the products.

For a company to achieve or maintain competitive advantage and add value to its products or brand, it is necessary to link these activities and optimise the company's value adding activities. These different activities require good co-ordination in order for the linkages between these activities to be managed properly. Careful management of these linkages are powerful sources for competitive advantage because it allows the company to resolve trade-offs across organisational lines and processes, which are difficult to do for most companies (Porter 1998b). If a company can resolve these trade-offs as a result of good organisational inter-activity co-ordination, it is likely to achieve advantage over its rivals as it permeates even outside of the organisation, in the form of excellent procurement management system, the creation of either a low-cost product or a high-priced commodity but with better quality over competitor products, etc. Hence, the company's product or brand is perceived by consumers to be of higher standards and quality and thus creating added value to it. The company can then maximise its pricing strategy for its products or brand.

In the case of Starbucks, as earlier stated, its value activities were at first effective in that the co-ordination between its primary and secondary activities are carefully managed, resulting in the creation of added value to its brand or products. Its inbound and outbound logistics activities, operations, marketing and service activities are supported with a good corporate management planning, human resource management, technological development, and procurement activities. For example, the setting up of stores is well planned. Each location is carefully studied, taking consideration of even minute and seemingly irrelevant details such as traffic flow, density of people and demographic characteristics of an area, and careful selection of

personnel to be deployed in each outlet (Clark 2007). These are done to support the primary activities that aim to deliver good quality coffee products to consumers. In the primary activity component, suppliers are cautiously selected, the distribution of coffee beans to each outlet is carefully planned to maintain freshness, and each store are designed to exude an ambience of luxury and comfort for its consumers (Clark 2007). Hence, creating the “Starbucks Miracle” that made the company a leader in the specialty coffee industry for almost two decades.

However, at present, the company is experiencing a downtrend in major areas. In 2008, the company registered over 50% decrease in operating income from the previous year. In terms of revenue, the company also registered only a 10% increase in the previous year, compared to an average of around 22% from the 2003-2007 fiscal years (Annual Report 2008). This decline translates into a significant reduction in the company/brand recognition. It can also be attributed in the company’s current value chain activities.

As Porter emphasised, to gain strategic competitiveness, a firm must optimise its value chain activities. Linkages between the value activities must be created, and maintained, in order to create a competitive edge over rivals. In the Starbucks business model, gaps in the value chain activities occurred in the recent years. The link between its physical activities and information-processing component were not improved and maintained in the long run. There is no continuation of the co-ordination between these activities in order to optimise the value chain. An example is the rapid expansion in several locations across the United States. The company failed to maintain the link between the physical activity of opening coffeehouses and maintaining the company’s

brand image of luxury and exclusivity. A co-ordination or balance between store operation and design was not maintained. The company rapidly expanded by opening an average of three stores a day, which resulted in the downgrading of the "Starbucks experience" that its customers have been looking for (Velta 2008). In fact, the customers have not seen any noticeable improvements in their experience since last year (see Appendix). Analyst Andrew Barish also commented that Starbucks' operations have "'slipped' and longer lines, more complexity and less-than-stellar-looking assets could be causing a modest decrease in sales in this challenging consumer environment" (cited in Moore 2007). As a result, Starbucks' strategic competitiveness is slowly disintegrating and its rivals are eating up some of its customer base (Rushe 2006).

Another gap in the Starbucks value chain is the management's failure to give attention to strategic marketing. In the context of the value chain, non-coordination between two activities can result into the non-creation or diminution of value to the product or brand/image. In this respect, the Starbucks management's failure to set a marketing strategy has also impacted on the company's recent downfall. There is no noticeable strategic marketing plan for Starbucks. In fact in its operational expenses, marketing receives little in the way of budgeting (Clark 2007). This oversight is now affecting the company's brand image/recognition. With very little money to spend on marketing, which is an integral part of any business, and little or no attention has been given to strategic marketing, the company cannot expect to sustain its leadership in the longer period.

Bradley (2003) states that, “marketing is strategically concerned with the direction and scope of the long-term activities performed by the organisation to obtain a competitive edge” (p. 1). Indeed, strategic marketing activities can create additional value to an organisation’s product or brand in that it sets direction to the organisation’s relationship with its customers. Without a strategic marketing plan, a company cannot create more value to its products or sustain its competitiveness in the long run. As such, Starbucks’ strategic leadership and competitiveness is now being challenged by its rivals who are more experienced in marketing such as Dunkin’ Donuts and McDonald’s.

Online Survey on Starbucks

An online survey was conducted in an aim to know what the customers are thinking about Starbucks and to collate their ideas and opinions regarding the activities of Starbucks in recent months. The survey covered questions about pricing strategy, the effects of the current global economic crisis to their coffee consumption, or more specifically, coffee consumption at a Starbucks outlet. There are 100 respondents to the survey, mostly from North America and Europe, the largest of which were from the United States, whilst a substantial portion also of the respondents was from Asia (the Philippines). Only few respondents from South America took part in the survey.

Two hypotheses are formulated for the survey:

Hypothesis 1: To show that Starbucks customers are looking for quality over the prices of its coffees.

Hypothesis 2: To show that Starbucks did not make any significant improvement in the previous year in terms of enhancing the “Starbucks experience.”

Majority (69%) of the respondents are College/University graduates or students, followed by postgraduate degree holders or students (23%). Forty percent (40%) of the respondents are earning less than $10,000 and an equal number of them have an income of between $10,000 and $25,000. Only two respondents have never been to a Starbucks outlet, whilst 56% have been going to Starbucks at least once a month. Coffee is the desired Starbucks product by most of the respondents (85%). The respondents' reasons in going to a Starbucks coffeehouse vary from socialising with friends (31% said this is most likely the reason for their visit to a Starbucks outlet) to going on to study (44% said this is the least likely reason they go to Starbucks).

With regard to Hypothesis 1, a large majority of the respondents (78%) said the quality of the coffee is more important to them than the price of the product. Whilst they think that coffees in Starbucks are overpriced (79% of the respondents), majority of the respondents (78%) are still willing to visit Starbucks more often if the prices of the coffees are lowered. Majority are still willing to pay an extra $0.50 for a cup of coffee if the product was green or environmentally friendly. Sixty-seven percent (67%) of the respondents also said that the current economic crisis did not affect their coffee drinking habits and purchasing.

Regarding Hypothesis 2, the respondents felt that there are no significant improvements in the Starbucks outlets since last year. Ninety percent (90%) of the respondents said they did not notice any improvement since 2008. However, 38% of the online respondents said that Starbucks is slightly better than its competitors, 25% responded that Starbucks is of higher quality and 26% rated Starbucks as having the same quality with other coffeehouses. Only 11% rated Starbucks with having slightly

worse or worse quality than its rivals. Among the competitors, Gloria Jean's has been chosen by 29% of the respondents to prefer over or instead of Starbucks and 16% said they would rather go to the local vendor in their area.

The survey shows two things; (1) that Starbucks' competitiveness is waning as evidenced by the responses that there is no significant improvement in their experiences from going to a Starbucks coffeehouse; and (2) that there is only a small difference between those saying that the quality of the coffee in Starbucks is higher or slightly higher than the other coffeehouses and those that responded saying it is of the same quality with the other coffee stores. The survey implies that Starbucks' overpriced coffee can be a disadvantage in the longer term if the company does not significantly improve its value chain to create a perception that its prices are worth the value that the customers get and pay for in its coffee.

The Need for Strategic Change

Since the 1950s, management guru Peter Drucker already recognised the need for strategic thinking in management. The legendary expert in the field of management said:

> In particular the new technology demands that management create markets. Management can no longer be satisfied with the market as it exists, it can no longer see in selling an attempt to find a purchaser for whatever it is that the business produces. It must create customers and markets by conscious and systematic work (Drucker 1954, p. 371).

Managers need to be strategic in their perspective in order to cope up with the ever changing business and market environment. Strategic management is the conscious

and continuous effort of creating new customers and markets. This is a result of the competition between and among business organisations. Thus, organisations must conform to this condition by implementing strategic change within the organisation.

Organisations change and they also compete against other organisations for the same resources, competencies and customers (Drejer 2002). Business organisations must change to stay alive and remain in the business (Abrahamson 2000). Every organisation must accept this reality even if they seem to be the leader in the particular industry they are engaged in. For instance, Starbucks have been the industry leader in the specialty coffee for more than a decade now. However, the reality is that Starbucks is not the only organisation in this industry and there are other organisations that compete with the company for the same market and resources, and there are still others who are willing to enter the fray and compete against Starbucks and the others who are already in the specialty coffee sector.

Strategic change is therefore necessary for Starbucks to maintain its leadership in the specialty coffee industry. The change needed would be for the long term with a strategic perspective and not only for a short-term period. In order to do this, the company may need to reform or revise its current practices and business models and realign its resources to what is needed by the market. The change process is, in its actuality, a series of phases that usually require a considerable length of time (Kotter 2007). Strategic change requires effective leadership. Good management of change will require the formulation of strategies that recognise the needs of those who implement the change, wherein the leader makes clear the objectives and goals of the change to the staff and the latter will work with the former in making the change successful

(Humphries & Senden 2000). Through this method, strategic change will be effectively implemented and the strategic objectives will be achieved.

However, implementing strategic change will not be easy, especially in a large and established organisation such as Starbucks. A globally diverse company like Starbucks can experience difficulties in implementing changes to its established business practices. Leaders of companies such as the case in study can face a dilemma or dilemmas in handling strategic organisational changes. Differences abound among individuals and groups within the organisation. These differences can be a barrier to the successful implementation of organisational changes. Hence, managers or leaders of Starbucks must be skilful in dealing with this situation and they must also be skilful in dealing with differences within the organisation (Davidson 2003). The leaders of such organisation must win the approval of their members to the proposed organisational transformation (Duck 1993). But before going any further, let us first make an analysis of the internal and external conditions affecting Starbucks today using Porter's Five Forces Model and the SWOT analysis framework.

Porter Five Forces Analysis

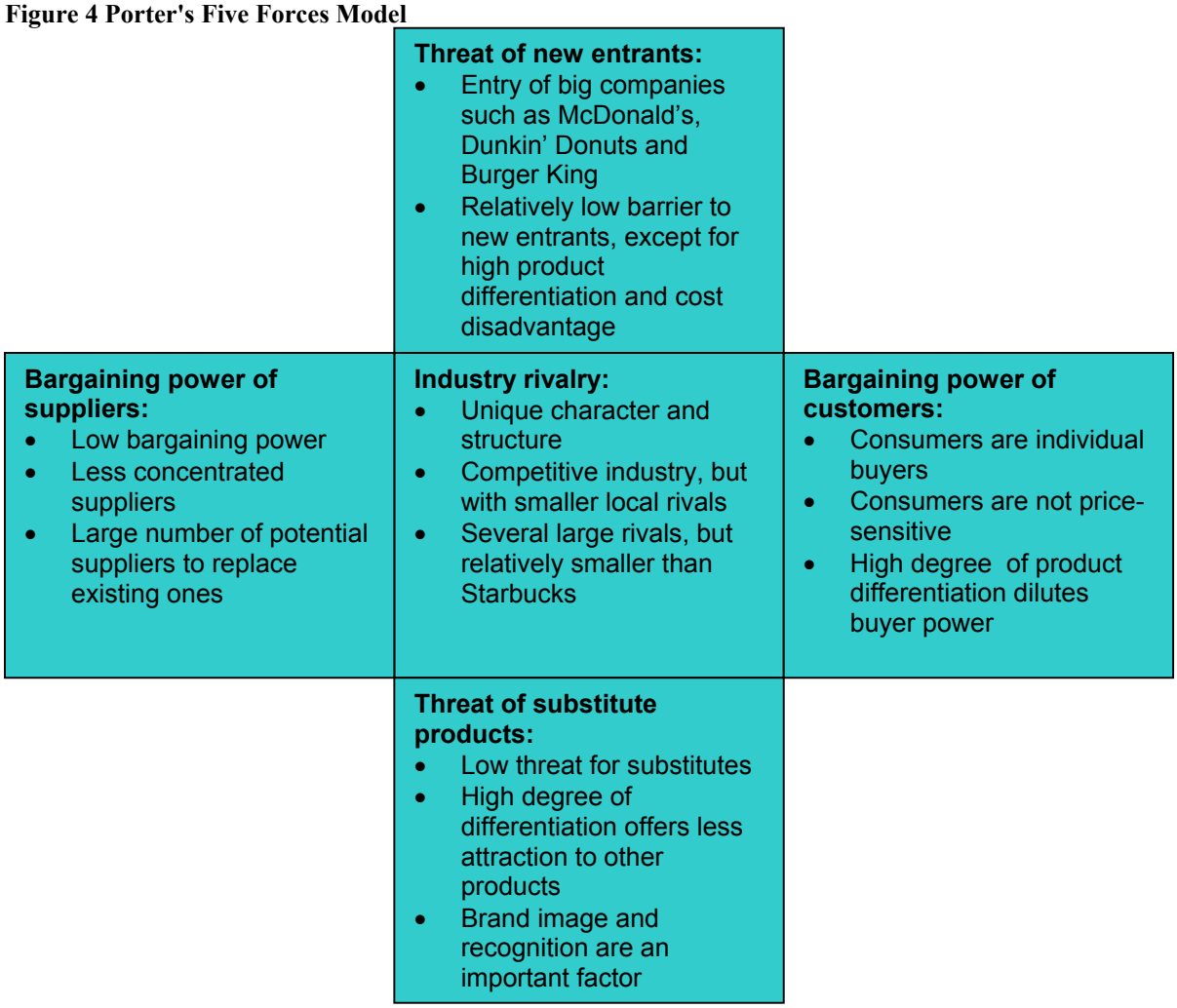
Using the Porter Five Forces model, we shall analyse the competitive environment that is surrounding the company today in order to formulate strategies to undertake changes in the Starbucks business model. Michael Porter (1998b) states, "Every industry has an underlying structure, or a set of fundamental economic and technical characteristics, that give rise to these competitive forces" (p. 23). These forces are industry competition/rivalry, threat of new entrants, threat of substitute products, bargaining power of suppliers and bargaining power of buyers. These five forces shape

and influence the strategies of companies. The Porter Five Forces analysis presents a clear view of the external conditions and the contending forces within a specific business industry. It also allows strategists to create a strategy in order to gain competitive advantage or sustain the same for a longer period of time. Porter added that, “Knowledge of these underlying sources of competitive pressure provides the groundwork for a strategic agenda or action” (Porter 1998b, p. 22). Hence it is important to make this analysis in order to have an overview of the industry and the underlying forces that put pressure on the company and understand the objective condition facing the Starbucks Coffee Company. The Porter Five Forces analysis on Starbucks is summarised in the diagram below (Figure 3).

Industry Competition

The greatest among the five forces is perhaps industry rivalry. It has the biggest potential to influence the competitiveness of the industry and in turn the rate of profit for companies. Although the collective strength of the five forces determines the ultimate profit potential for an industry (Porter 1998b, p. 21), industry rivalry is the deciding factor for the determination of such profit rate. If competition within the industry is mild, or there are only few competitors, the rate of profit is generally higher, but if the competition is intense, companies cannot expect to earn “spectacular returns on investment” (Porter 1998b).

Figure 4 Porter's Five Forces Model



The coffee industry has a structure or characteristics that are difficult to define or to set a boundary from which it can be differentiated with other industries (Larson 2008). Although it can be easily recognised from a single commodity, which is the coffee bean, the coffee industry's characteristics are unique in that its scope is much larger than what it appears to be. The coffee industry can be divided into two categories, the production-based segment and the retail-based segment. For purposes of this paper, the production-based segment will be confined to those companies and individuals who plant and grow coffee beans, whilst the retail-based segment is confined to the specialty coffee sector, wherein the coffee beans are sold to consumers directly, either in the

coffeehouses or in retails stores, department stores and supermarkets. It is on the latter segment that the focus of this analysis will be given.

In 1987, when the company was bought and formed by Michael Schultz, Starbucks faces competition against other small coffeehouse chains across Seattle. In the entire United States, a number of coffeehouses are established. Most of these coffeehouses are small and medium sized and they are owned by individuals or families. Today, although there are several companies that compete against Starbucks, these competitors were relatively smaller and most often are concentrated only in a certain area or region. In the coffeehouse sector, Starbucks' competitors are Second Cup, Gloria Jean's, Coffee People and other similar coffeehouse chains, which are now either situated in a specific state or are expanding or planning to expand their domestic and international operations. Gloria Jean's for example, started its international expansion in the 1990s when the Starbucks stores overseas are already numbering by the hundreds. Among these direct competitors, it appears that Gloria Jean's is the primary competitor for Starbucks, as evidenced in an online survey conducted (see Appendix).

The company is also engaged in the consumer products segment selling bottled coffee drinks, whole grain coffee beans or ready-to-drink coffees in packs, and other similar product descriptions. In the consumer products segment, the company's noted and biggest rivals include Procter & Gamble, Nestle and Kraft. The latter companies have been in the packaged coffee sector for a significantly longer period, in fact they have been in this business for more than a century, than Starbucks, which started to enter this sector only a few years ago with the formation of its Global Consumer

Products Group segment. Apart from the two large consumer product companies, the Starbucks products also face competition with substitute products such as soft drinks, energy drinks, and other non-alcoholic beverages.

The specialty coffee industry competition is, however, not price-based unlike the other industries. In this particular industry, consumption of coffee is not dependent on the price of the product or commodity but on the differentiation between each product and several value adding variables such as the quality of customer services, brand, brand recognition or image of the company. Hence, the specialty coffee industry is not sensitive to price adjustments or movements.

Threat of New Entrants

The entry of new players in an industry can bring the competition into new, higher levels. New entrants, most especially large ones, bring new capacity, the desire to gain market share and often substantial resources that could cause a shake-up or a rearrangement of the current competitive positions of companies within the industry (Porter 1998). In order to protect the players'/companies' positions in the industry, they have to set up high barriers for new entrants. These barriers include economies of scale, product differentiation, capital requirements, cost disadvantages independent of size, access to distribution channels and government policy (Porter 1998). Major players often force new entrants to come in at a cost disadvantage by compelling the latter to spend or invest large amounts of money on production, research and development, marketing, distribution channels, financial resources and all aspects of the business.

The specialty coffee industry today is undoubtedly dominated by Starbucks, having no equal or larger company in size that competes directly against the company. However, the industry is open to all potential rivals, especially to large companies engaged in the consumer products and retail chain business. For example, the new entrants in the coffeehouse business today are McDonald's and Dunkin' Donuts and Burger King, three large companies which are challenging Starbucks' dominance in the industry. These new entrants can equal Starbucks capabilities in the aspects of distribution channels, marketing and other areas. They have the capacity to bring new resources that can cause a shake-up in the industry, but not yet enough to topple Starbucks from its current dominant position. With the three big companies' entrance into the specialty coffee retailing segment, Starbucks' position is definitely shaken.

Despite the openness of the specialty coffee segment to new entrants, barriers to the successful entry of new players appears to be tall. First, product differentiation in the industry is high. Specialty coffees are so differentiated in appearance, presentation, taste and even in image. Brand recognition is especially important for consumers, along with excellent customer service and the overall ambience of the coffeehouse. These barriers were successfully established by Starbucks long before McDonald's or Dunkin' Donuts decided to venture in this industry.

Favourable access to raw materials is also an important barrier in this industry. Starbucks have exclusive access to quality coffee beans from several suppliers around the world. The beans Starbucks bought from its suppliers follow the Fair Trade criteria established in the industry. This characteristic is simply costly for Starbucks competitors since they have to assure their customers that the coffee they serve is made from the

finest coffee beans similar to Starbucks'. On this aspect, cost disadvantage will be experienced by the new entrants, such as McDonald's and Dunkin' Donuts. However, at present, McDonald's, Dunkin' Donuts and other potential rivals are still targeting the lower end of the market, leaving the high-end bracket who are still attracted to Starbucks. However, these new entrants are now shaking up the industry, pressuring Starbucks to cut its price to maintain its rate of investment as the coffeehouse chain's market share is now being eaten up by the rivals.

Threat of Substitute Products

Substitute products, as explained by Porter (1998), are those products that come from other industries and can pose as a trade-off for products in the underlying industry. In the specialty coffee industry, substitute products can be those non-alcoholic beverages such as tea, soft drinks, fruit juices and energy drinks and other caffeinated drinks. These are sources of substitute products which the consumers can purchase in place of coffee. However, the only true direct substitute for specialty coffee is the basic coffee, but the basic coffee is considered to be a substantially lower quality than specialty and as such does not present threat to specialty coffee.

On the other hand, whilst there are several potential substitutes, a cup of specialty coffee is still what consumers prefer to purchase. Product differentiation and brand image plays an important role in this industry. The specialty coffee products are different in many aspects from the substitutes. Coffeehouses offer not only a cup of coffee but the experience of sipping the specialty coffee on a luxurious ambience, such as what Starbucks is offering. Soft drinks companies and non-alcoholic beverage producers are on a mass marketing, selling their products in retail stores, supermarkets

and department stores. Coffeehouses, on the other hand, offer an exclusive place for its consumers to enjoy their coffee. Hence, the threat of substitute products is not significant or is not considered a major force in the specialty coffee business.

Buyer's Bargaining Power

Customers are a powerful force in an industry. They can pressure the companies to cut down their prices, demand better services from the company and can pit one company against another (Porter 1998). In other words, customers can influence the rise and fall of rate of profits in a particular industry. According to Porter, buyers or a buyer group become powerful if:

- They are concentrated or purchases in large volumes.
- The products they purchase in an industry are undifferentiated or standard.
- The products they purchase form a component of their own products or a significant fraction of its cost.
- They are of low income levels which create incentive to lower their purchase costs.
- The industry's products are unimportant to the buyers' quality of services or products.
- The buyer does not benefit from the product.
- They pose a credible threat of integrating backward to make the industry's product.

These powers can be acquired by the consumers if they act as a group. However, in the specialty coffee industry, the largest fraction of buyers is the individual consumers, and they do not act in unison (Larson 2008). In the specialty coffee

industry, individual consumers compose the largest purchasers of the product and these buyers tend to be less concerned with the price of the product (Larson 2008). This decreases their bargaining power further. Product differentiation in this industry is so high that consumers tend to look more for the quality of services and the image of the brand than the price of the product or where did the product's raw materials come from, or what is the price of the raw materials, etc. hence, the bargaining power of the buyers are low.

Bargaining Power of Suppliers

Similar with the buyers, suppliers can also exert influence on the players in an industry. Suppliers can gain bargaining power and can be potential threat to industry players in terms of industry profits. They have the ability to increase or decrease the quality of products in a particular industry (Porter 1998). Michael Porter also outlined the major sources of bargaining power of suppliers. The author said a supplier group is powerful if:

- It is dominated by a few companies and is more concentrated than the industry it sells to.
- Its product is unique or at least differentiated, or if it has built up switching costs.
- It is not obliged to contend with other products for sale to the industry.
- It poses a credible threat of integrating forward into the industry's businesses.
- The industry is not an important customer for the supplier group.

Again, similar to the buyers' situation, the bargaining power of suppliers can only be increased if they act in unison and they are highly concentrated. However, in the specialty coffee industry, suppliers generally have less bargaining power due to the

number of coffee farms and plantations spread across several continents, namely Latin America, the Pacific Rim and East Africa (Larson 2008). Whilst there is only one variety of coffee needed for the industry, Arabica, there are however practically thousands of plantations and individual coffee growers growing this particular type of coffee bean, giving the coffeehouse companies more choices to replace existing suppliers should the latter demand higher prices for their coffee beans. Hence, the suppliers are diverse and spread and the industry players exert more influence and get a larger share of the profits of the industry over the suppliers.

To sum up the five forces analysis, it can be concluded that the specialty coffee industry today is generally attractive and highly competitive. Despite the monopoly of Starbucks in the past two decades, a number of small, individual and family-owned coffeehouses have sprouted. The buyers and suppliers have less bargaining power and the threat of substitute products is insignificant. Thus, the rate of profit in the industry is highly concentrated upon the major industry players, particularly to Starbucks. However, with the entry of new players such as fast-food chain giants McDonald's and Dunkin' Donuts, Starbucks' dominance in the specialty coffee industry is being threatened.

SWOT Analysis

After determining the external forces and conditions surrounding the company, an analysis of the internal organisational characteristics and external factors are necessary in order to have a clearer view of the Starbucks organisation's capabilities and position in the industry. An evaluation of the organisation's strengths and weaknesses as well as the opportunities and threats facing it will help in determining the

company's future actions and strategic changes. Table 1 shows a summary of the SWOT analysis on Starbucks.

Strengths

Starbucks' primary strength is its impeccable brand reputation and image. The company is known to deliver high quality products and customer service. Despite its overly priced cup of coffee, brewed using high quality Arabica beans, most of its customers keep coming back to the store to feel the "Starbucks experience" the company has promised to its customers. Thus, the price of its coffee is not the issue but the quality of service the company gives to its customers. As one of its patrons have stated, "The coffee is unique and tasty, but it is not the only reason I like to visit each day. The place has energy and it is well run" (Motley 2007).

Apart from its strong brand, Starbucks also have access to high quality resources and raw materials. Its Arabica beans are derived exclusively from coffee plantations and a percentage of its raw materials are Fair Trade certified. The company also has advantageous access to distribution channels as its stores ad coffeehouses are located in strategic areas, with several stores almost a stone's throw away or are literally facing each other on both sides of the street. Starbucks is also known to treat its employees well, paying its staff with above-market salaries and wages.

Weaknesses

One of the weaknesses of Starbucks is its grossly overpriced coffees. Whilst the company targets the affluent executives, young and old, as its primary market, the current economic conditions make the customers become sensitive to prices of commodities and products (Velta 2008). The frequency of customer visits may be

reduced due to the current economic situation. Hence, Starbucks' current price strategy may seem to be out of place and needs to be changed. Apart from the pricing strategy, the Starbucks coffeehouses' image as luxurious "Third Place" seems to be vanishing. With stores literally facing each other, the lush experience the customers wanted appears to be diminishing (Velta 2008). It is increasingly becoming like a fast-food chain, only the prices of its products are much higher.

Opportunities

Despite the current economic turmoil, there are some opportunities that are available for Starbucks to grow. Its venture on consumer products seems to be doing well than its other segments, US domestic segment and international segment. In its 2009 Second Quarter Report, the company increased its operating income to six percent despite a two percent drop of revenue, compared to the same period the previous year. Its other segments have significantly higher decreases in revenues and profit. This means that the company can capitalise more on the global consumer products segment whilst recovering from the other two business segments.

The international market is also showing a good promise for Starbucks. The economies of the emerging markets are growing at a rapid pace. The company can capitalise on this growth by aggressively expanding into these countries. Using its fundamental strategies indicated in the previous sections and the recommendations at the end of this paper, the firm can increase its revenue and profit by penetrating into the emerging markets.

Threats

The entry of two large companies and their fast rise in the specialty coffee presents the most credible threat to Starbucks' dominance. McDonald's and Dunkin' Donuts are formidable opponents to Starbucks. These two companies have the capability to match the Starbucks' distribution channels and marketing activities. The two fast-food chains can equal Starbucks in terms of financial resources. Starbucks still faces the same old criticisms about its overpriced coffee. Hence, its image is being threatened, especially now that the economy is not getting better.

The current global economic crisis also poses a danger to Starbucks. As reflected in the company's financial reports, its revenue and profit are going down due to the bleak economic condition. The company's shares of stocks are also not doing well in the stock market trading, primarily due to its low income and revenue. The economic crisis is pounding on the company's profitability.

Table 1 Starbucks SWOT Analysis

Strengths • Good Brand reputation and image • Access to quality raw materials • Favourable access to distribution channels • Pays its staff well	**Weaknesses** • Grossly overpriced coffee • Image as a high-end coffeehouse is diminishing
Opportunities • Global consumer products segment is doing well • International market is showing a good promise	**Threats** • Entry of new competitors • Economic crisis

As can be seen from the table, Starbucks' strengths far outweigh its weaknesses. The company's weaknesses are more concentrated on the company's pricing strategy.

However, it can be seen that its reputation as a luxurious coffeehouse is diminishing, but that can be remedied by implementing a new strategy, which will be discussed later in this paper. Whilst there are a few opportunities so far, the company can still capitalise on its strengths to outweigh the threats posed by new competitors and the global economic crisis.

Summary

The Porter Five Forces analysis and the SWOT matrix shows that apart from the basic strategies used by Starbucks, the external environmental conditions and the internal characteristics of the Starbucks organisation present a favourable condition for growth. The only notable threat is the competition brought by the entry of new competitors. Porter has already acknowledged that intense rivalry in a specific industry will definitely bring down the rate of profit for the companies or industry players (1998b). Hence, Starbucks profit has declined in the previous year due the growing intensity of competition in the industry. Apart from the competitors, the economic crisis aggravated the situation, making the customers spend less or reduce the number of times they visit a Starbucks outlet, thereby making store sales in Starbucks outlets decrease.

Nonetheless, through its years of experience and brand reputation, Starbucks is still the dominant player in the specialty coffee sector. Thus, the company can use this position to leverage itself and put pressure onto its competitors. But the question is, and despite its still being the dominant player in this industry, “Why is Starbucks failing now?” What happened with its business strategy? These questions have already been answered in the value chain analysis performed earlier. Therefore, what is needed is

the formulation of strategies to implement a strategic change in the company's business model and processes.

Recommended Strategies and Actions

Having determined the causes of Starbucks' current downfall, it is necessary to formulate a plan to address these issues. Strategic change cannot be achieved without specifying which actions are to be undertaken. Since the major issues were already identified, strategies for the remedy of these issues need to be formulated. Proctor (2000) states, "Strategy is a plan that integrates an organisation's major goals, policies, decisions and sequences of actions into a cohesive whole" (p. 1). Thus, based on the above evaluations, the following recommendations are put forward.

Formulate Strategic Marketing

Strategic marketing is an important factor in any business. As discovered above, the company's failure to draw a marketing plan created a gap in its value chain, which has caused a significant deterioration in the company's brand image/reputation. The company needs to have a direction in the marketing arena to further improve its image and brand recognition. Marketing is concerned not only about promotional advertisement activities. Marketing planning is a process by which organisations attempt to understand the market conditions and the needs and preferences of the customers whilst taking into consideration other organisations who are also competing in the market (Bradley 2003). It involves satisfying the customer's wants and needs and managing relationships with stakeholders (Proctor 2000). Drucker (1954) also emphasised that a business has only two functions, one of which is marketing and the other is innovation. The aim of marketing is to create new customers and to

communicate with all of its stakeholders (customers, shareholders and employees). A company cannot effectively implement any activity if no communication with all its stakeholders was made. This is the role of marketing.

In the case of Starbucks, it has made little regards to marketing, as evidenced by its small portion of budgetary allotment for the said value-creating activity. It appears that the company relies on its strong operational capabilities more in such a way that marketing has been put into the sideline. Although this may have worked before, the changing market conditions warrant that the company should start focusing as well in strategic marketing. Competitive advantage can be gained and sustained with the help of marketing. Proctor (2000) argued that competitive advantage should be market-led. Drucker (1954) stated that marketing is the distinguishing, unique function of a business. Thus, Starbucks must focus a substantial amount of resources into improving its marketing activities.

To gain competitive advantage, an organisation must first define its strategy. One of the authorities in the creation of strategy to achieve competitive advantage is Michael Porter. The author defined strategy as, “the creation of a unique and valuable position, involving a different set of activities” (Porter 1998b, p. 55). Marketing strategy, therefore, is the formulation of a different set of activities that aims to create a unique and valuable position in the market. The strategy includes the creation of a plan to identify market conditions and to identify which segment of the market the company will focus on. Strategic objectives must also be set that will serve as a guide in the implementation of the marketing strategy.

It has been identified above that Starbucks employs a generic strategy of focus with an emphasis on differentiation. This strategy, however, may now need to be revisited and adjusted. Starbucks needs to communicate with its customers now. Starbucks also needs to create new customers and new markets to prevent the saturation of its current market segment. Its marketing objective should be focused on creating new markets and, if necessary, new products or product line to accommodate new customers. The company may create new products that will have an appeal to the lower segment of the market, a segment which the company has not yet fully tapped. Its pricing strategy, therefore, may vary accordingly with the creation of these new products that aims at generating new customers in the lower end of the market.

The firm's current marketing communications and customer relationship management practices also need to be changed. As evidenced in the online survey, the customers are not feeling any substantial improvement in Starbucks. If ever there are improvements that the company has been doing in the previous years, these changes have not been effectively communicated to its customers. These improvements in stores or customer service/relationships must be communicated with its customers to make them aware that Starbucks is improving itself to maintain the "Starbucks experience" that its customers have been wanting for in the company.

On the aspect of exclusivity, the company also needs to enhance its current image of luxury. Although it has been recommended above that the firm has to create new customers, or market new segments, this will not necessarily have an adverse effect to its brand reputation. What the company needs to do is to create a system of exclusive membership with rewards or privileges for its frequent customers, especially

the high end segment of the market and the students which have been the company's traditional customers. Privileges and rewards exclusive only to customers, whether individually or by group, who apply for regular membership in the company can be formulated such as unlimited free Wifi access and/or free coffees or other products once a week. The company can also create a function room in each outlet that the exclusive card-bearing members can use. These privileges may help enhance the company's image and reputation of exclusivity. Apart from that, the fees that will be collected from the annual registration dues of the members can add up to the company's profit.

Enhance Operations Management

Aside from improving its marketing capabilities, Starbucks also needs to improve its store operations management. Operational effectiveness means the performance of similar activities better than the competitors perform them (Porter 1998b). However, operational effectiveness alone is not sufficient to gain or sustain competitive advantage. Porter (1998b) states that a company can outperform its rivals if it delivers greater value to customers or create comparable value at a lower cost, or the company should do both. It has also been identified above that the company's value chain has gaps involving its operations. The company is into rapid expansion of stores, however, the quality of its service or its brand's reputation has been sacrificed, resulting into its relegation or into being perceived as similar to a fast-food chain rather than a luxury coffee outlet. Starbucks has not been able to create greater value whilst offering overpriced coffee.

Thus, the company needs to improve its store operations management by enhancing the appearance of each outlet. The company may also need to improve its

customer service further and make these improvements known to the customers, as indicated earlier. The addition or improvement of store equipments and ornaments will provide a new look to the outlets. The addition of a function room, as indicated above, for its exclusive card-bearing members will enhance even more the experience of exclusivity and luxury of each Starbucks coffeehouse.

Also noteworthy in the online survey is the attention given by customers to Starbucks being an environment-friendly store. Therefore, the company must improve this standing by becoming more environmentally friendly. It also has to give emphasis on buying Fair Trade materials since this practice appeals to its customers. The firm must therefore align its resources to these improvements in order to sustain its current position in the market and attract more customers, and gain competitive advantage and strategic competitiveness.

Improve Stock Market Standing

To improve its stock market trading, Starbucks has to show that the company is a profitable business. This can only be done if the company will continue to show that it has a sustainable command of its brand/image reputation and recognition. The company has to significantly stop the current downtrend in sales and profit. But in order to do this, the company must initiate and implement changes within the organisation, as recommended above.

Stock market analysts are closely monitoring the Starbucks shares' performance and profitability. Hence, the company must enhance its reputation by showing significant and substantial improvement in its marketing and operational activities to show that the company is in command of its future and that it can maintain its current

leadership in the specialty coffee industry. Apart from that, the company can also show that it has the capability to venture into new markets. This way, analysts will not hesitate in giving a high rating to the company, and investors will not be reluctant at putting their money into the Starbucks stocks.

Strategic Leadership Improvement

Above all the changes that Starbucks needs, its leadership must be changed. Not that the managers will be removed but their capabilities, skills and attitudes must be improved. No organisational transformation will be complete if the leaders are not receptive of change. Organisational change can be done only if the correct processes are implemented and the leaders have been at the forefront of these activities.

Leading organisational/strategic change is not an easy task for managers or leaders of a company. There have been efforts that failed because of oversight by the leaders. Whilst Starbucks leaders seem to have not failed, it is necessary that its leaders should know exactly what to avoid in executing changes in the organisation. Kotter (2007) identified eight major mistakes committed by organisations. These are the following:

- Not establishing a great enough sense of urgency;
- Not creating a powerful enough guiding coalition;
- Lacking a vision;
- Undercommunicating the vision by a factor of ten;
- Not removing obstacles to the new vision;
- Not systematically planning for, and creating, short-term wins;
- Declaring victory too soon; and

- Not anchoring changes in the corporation's culture.

Leaders of Starbucks should avoid the above mistakes. Over-performing or underperforming the above points may also lead to failure. Hence, in implementing the recommended changes, the leaders must do what is exactly needed, that is implementing the plans as they are formulated.

Although in some instances, learning from a transformative experience known as crucibles are effective in creating a leader (Bennis & Thomas 2002), such occurrences are rare. It is therefore more relevant to create a leader through training and development. A level 5 leader is one that has the highest capabilities in the leadership hierarchy (Collins 2005). Level 5 leaders are not born, they are created. What is needed to be a level 5 leader is a great amount of political will and a sensible characteristic of humility (Collins 2005). These characteristic may be necessarily possessed by the leaders of Starbucks in order to effectively implement changes in the organisation and persuade the entire membership into action.

Manz, Bastien and Hostager (1991) in their study stated that executive leaders can adopt a framework of bi-cycle model to engage the members of the organisation into the strategic change process. The first cycle involves the participative cycle, wherein the leaders seek employee inputs and participation whilst promoting employee development and self-direction. The second cycle, the transactional cycle, connotes that incentives for contributing will be facilitated through a process of exchange in which participants complied with the adapted vision in exchange for various benefits. The bi-cycle model can be employed, along with a strong political will by the leaders. In the

Starbucks organisation, this might be effective in implementing the above recommended changes.

However, leaders need not do all the tasks. There is a need of balancing the organisational change plan and the actions needed to implement such plan. Duck (1993) puts forward a system of delegating tasks into a team. A “team” model of organisational change will be needed to perform the organisational transformation. The leaders may form a team that will be tasked to implement the changes. The team must also balance its tasks by carefully selecting which information will be given to all the members of the organisation and which are to be withheld until actual implementation so as to prevent others, who are reluctant to changes, from creating steps that would impede the implementation of the strategic changes. As stated by Davison (2003), in every organisation, especially large ones, there are always differences between the members, whether it is difference in opinion, perspective or action. As such, a skilful leader must have the ability to leverage with these differences.

The above-stated characteristics or traits of leaders must be possessed by the current leadership of Starbucks. The recommended changes in the organisation’s business process and models are not easy. These recommendations entail a radical change in the organisation will require the entire membership to act. Thus, the leaders of the company should be at the forefront of this transformation. They need to have the characteristics needed of a leader, as described above, in order to make the organisational change effective.

Conclusion

Strategic change is the call of the day for Starbucks. Perhaps, this is the time that the company will need to revisit its existing business models, practices and strategies to know whether these models still conform to the conditions of the market. The company has been in the business for two decades, and undoubtedly has been the industry leader for almost the same length of time. However, since market conditions change as evidenced by the current events and continuing globalisation of markets, the company may need to reform its strategy.

Starbucks may have already saturated its current market or its strategy may have been going into a different direction, one that is going away from the objective market situation. As such, the company has to implement a strategic change. Its management practices may need to be revised. As Drucker (1954, p.37) said, “It is the customer that determines what a business is.” In this sense, Starbucks should identify what the customer wants, what they need and what they prefer, not the other way around.

In the course of its practice in the previous years, Starbucks seems to be content in expansion alone, not communicating with the customers to know what their preferences have been. It must be emphasised that customers’ needs and preferences are always changing. Hence market conditions also change. In this context, Starbucks failed to keep up with the changing customer behaviour and market conditions. Thus, in the last several months, Starbucks’ performance is going on a downtrend. It is imperative that the causes of this downtrend must be identified and remedies must be put in place.

The remedies, however, need to be long-term, not only short-term. Whilst short-term actions are needed to address tactical changes, it is more important to set a strategic goal, or if necessary, revise the current strategic goal to conform to the realities in today's business environment and the future of the business. Thus, it was recommended that Starbucks should focus on marketing, while enhancing its operational effectiveness. Marketing has been the missing component in the Starbucks practice in recent years. It is therefore significant to put emphasis on this area.

Apart from that, the company's leadership must be transformed as well. It has been recommended that the organisation's leadership should adopt some behaviour, traits or skills that are necessary to implement successful changes in the organisation. Several practices and principles have been described in this paper to serve as a guide or reference in the leadership practices of Starbucks executives and managers. These principles have been set as a product of studies of academicians and practitioners in the field of management, marketing and other areas of business. It is highly recommended that Starbucks should implement these changes within the organisation in order to maintain its current standing in the industry and achieve strategic competitiveness.

Bibliography

Abrahamson, E. 2000, 'Change Without Pain', *Harvard Business Review*, Reprint, July-August.

Bennis, W. and Thomas R. 2002, 'Crucibles of Leadership', *Harvard Business Review*, Reprint, September 2002.

Betz, F. 2001, *Executive Strategy: Strategic Management and Information Technology*, John Wiley & Sons, New York.

Bradley, F. 2003, *Strategic Marketing: In the Customer Driven Organization*, Wiley, Chichester, England.

Braganza, A. 2001, *Radical Process Change: A Best Practice Blueprint*, John Wiley & Sons, New York.

Clark, T. 2007, *Starbucked: A Double Tall Tale of Caffeine, Commerce and Culture*, Little, Brown and Company, New York.

Collins, J. 2005, 'Level 5 Leadership: The Triumph of Humility and Fierce Resolve', *Harvard Business Review*, Reprint, July-August.

Davidson, M. 2003, 'The Path to Leveraging Difference: Seeing, Understanding and Valuing Difference', *Paper Presented to the Darden Graduate School of Business Administration*, University of Virginia Darden School Foundation, Charlottesville, VA.

Drejer, A. 2002, *Strategic Management and Core Competencies: Theory and Application*, Quorum Books, Westport, CT.

Drucker P. 1954, *The Practice of Management*, Harper & Row, New York.

Duck, J. D. 1993, 'Managing Change: The Art of Balancing', *Harvard Business Review*,

Reprint, November-December.

Humphries, E. and Senden, B. 2000, 'Leadership and Change: A Dialogue of Theory and Practice', *Australian Journal of Early Childhood*, vol. 25, no. 1. p. 26.

Kotter, J. 2007, 'Leading Change: Why Transformation Efforts Fail', *Harvard Business Review*, January.

Larson, R. 2008, 'Starbucks a Strategic Analysis: Past Decisions Future Options', *Brown University Economics Department*, Providence, RI.

Manz, C., Bastien, D. and Hostager, T. 1991, 'Executive Leadership During Organizational Change: A Bi-Cycle Model', *Human Resource Planning*, vol. 14, no. 4. p. 275+.

Moore, A. 2007, 'Starbucks Cut to Sell on Slow Growth, Higher Costs', *Market Watch* [Online] Available at: http://www.marketwatch.com/story/starbucks-downgraded-to-sell-shares-slip?siteid=yhoof [Accessed on March 20, 2009].

Motley, L.B. 2007, 'Learning About Customer Satisfaction from Starbucks', *ABA Bank Marketing*, December, p. 43.

O'Rourke, P.J. 2007, 'Venti Capitalists', *New York Times* [Online] Available at: http://www.nytimes.com/2007/12/16/books/review/O-Rourke-t.html?_r=1&scp=1&sq=starbucked&st=nyt&oref=slogin [Accessed February 12, 2009].

Prahalad, C.K. and Hamel, G. 1990, 'The Core Competence of the Corporation', *Harvard Business Review*, May-June.

Proctor, T. 2000, *Strategic Marketing: An Introduction*, Routledge, London.

Porter, M. 1998a, *Competitive Strategy: Techniques for Analyzing Industries and*

Competitors, The Free Press, New York.

--- 1998b, *On Competition*, Harvard Business School Publishing, Boston, MA.

Rushe, D. 2006, 'Coffee Rivals Give Starbucks a Wake-up Call', *Times Online* [Online] Available at: http://business.timesonline.co.uk/tol/business/industry_sectors/retailing/article673462.ece [Accessed March 20, 2009].

Starbucks Corporation 2008, 'Annual Report Fiscal 2008', *Starbucks website*, [Online] Available at: http://www.starbucks.com [Accessed on March 20, 2009].

'Starbucks (SBUX) "Trading Transparency"' 2007, *Stock Picks Bob's Advice* [Online] Available at: <A href="http://search.ebscohost.com/login.aspx?direct=true&db=tsh&AN=26848639&site=ehost-live">Starbucks (SBUX) "Trading Transparency".</A> [Accessed on March 20, 2009].

Starbucks website (www.starbucks.com)

Stone, B. 2008, 'Original Team Tries to Revive Starbucks', *New York Times*, [Online] Available at: http://www.nytimes.com/2008/10/30/business/30starbucks.html?_r=1 [Accessed February 12, 2009]

Velta, M. 2008, 'How to Reenergize Starbucks', *BusinessWeek* [Online] Available at: http://www.businessweek.com/innovate/content/feb2008/id20080220_372003.htm [Accessed February 12, 2009]

Appendix

Figure 5 Perception on Prices of Starbucks Products

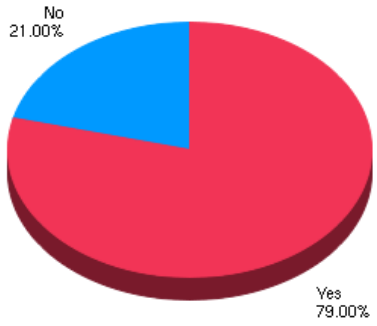


Figure 6 Perception of Starbucks' Fair Trade Policy

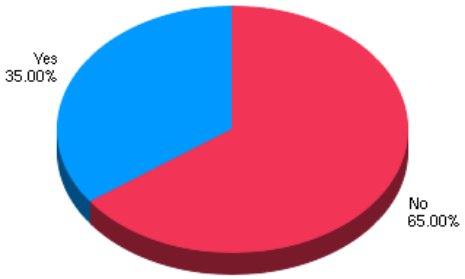


Figure 7 Starbucks Customer's Competitor Preference

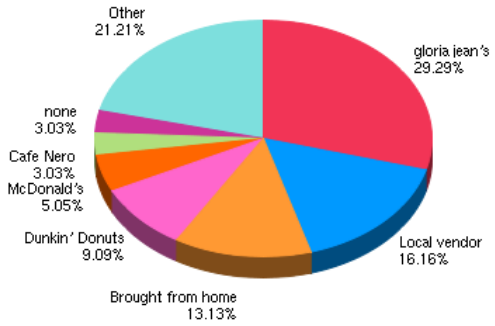


Figure 8 Perception on Starbucks being "Green"

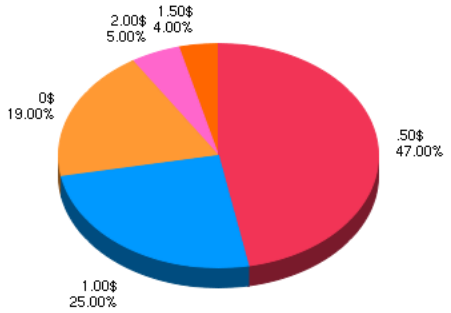


Figure 9 Comparison of Quality with Starbucks Competitors

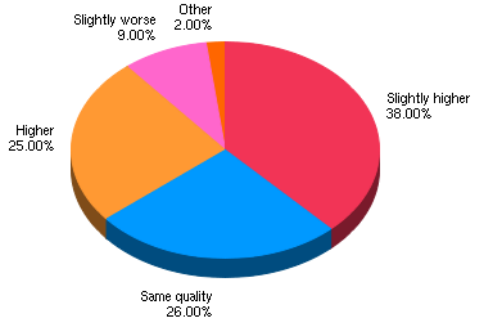


Figure 10 Educational Attainment of Survey Respondents

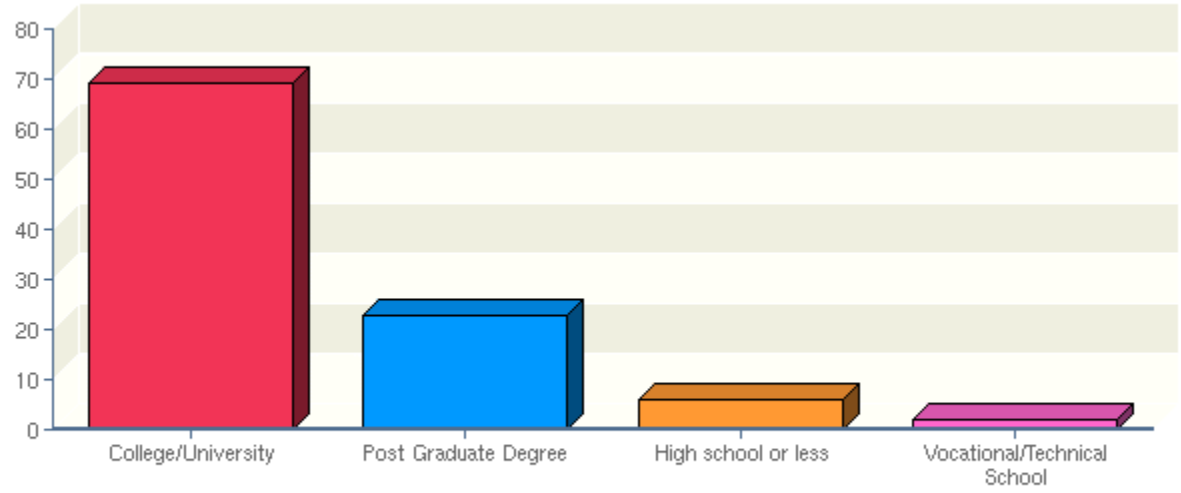


Figure 11 Income Bracket of Survey Respondents

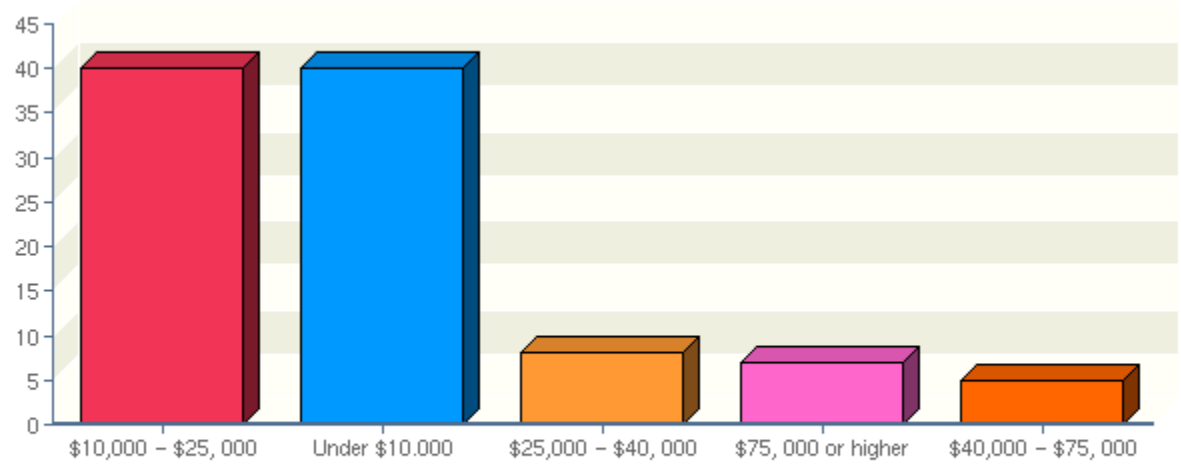


Figure 12 Respondents' Choice of Products When Visiting Starbucks

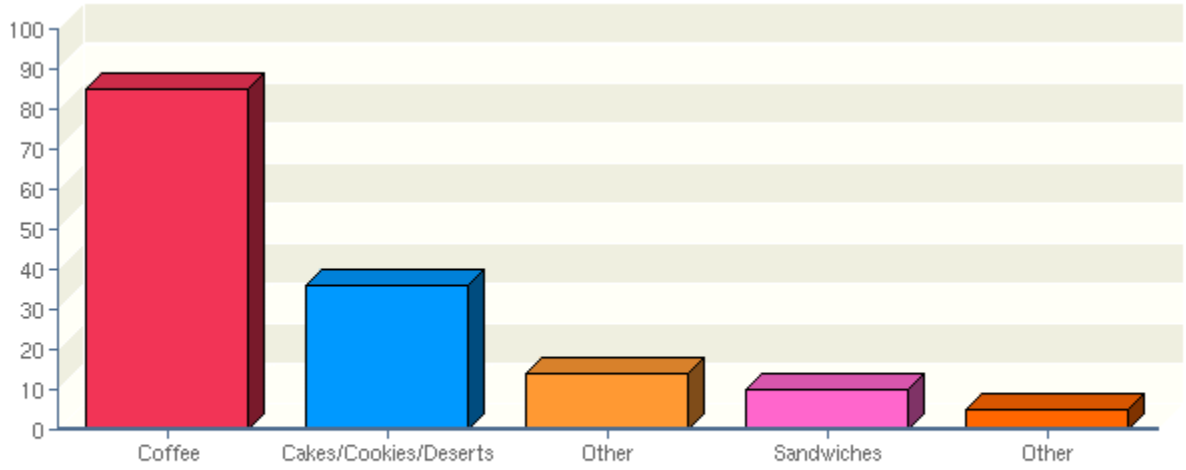


Figure 13 Frequency of Visits to Starbucks

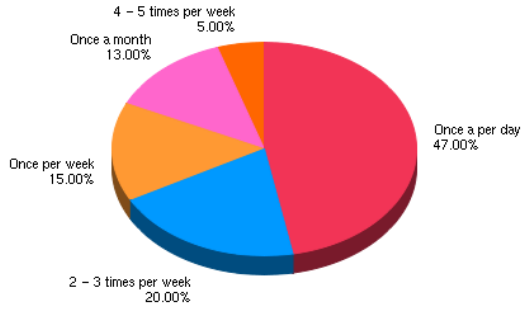


Figure 14 Percentage of Respondents Who Visited Starbucks

Figure 15 Duration of Visits to Starbucks

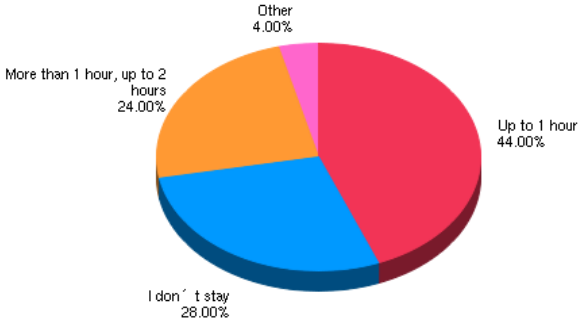


Figure 16 Respondents' Perception on Improvements in Starbucks

Figure 17 Ratio of Coffee Purchased and Made at Home

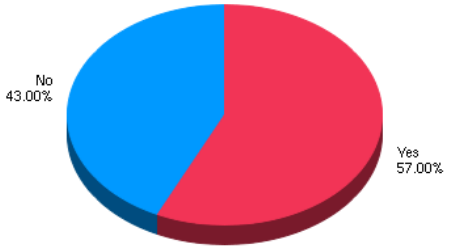


Figure 18 Percentage of Starbucks Customers Affected by the Economic Crisis

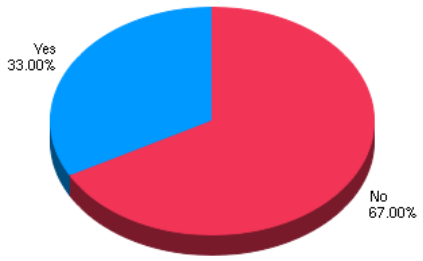


Figure 19 Percentage of Those who Will Purchase Starbucks Coffee at a Lowered Price