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Starbucks Corp. (SBUX)

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Analyst, JPMorgan Securities LLC

MANAGEMENT DISCUSSION SECTION

John Ivankoe

Analyst, JPMorgan Securities LLC

Hi. It's John Ivankoe with JPMorgan. Thank you everyone for joining the Starbucks session. Here this morning joining with Starbucks is Pat Grismer, the company's Chief Financial Officer who I believe will start us off with some slides.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

Thank you very much, John. I do appreciate the opportunity to participate in today's session. Before we do get started with our fireside chat, I do want to provide a quick update on our sales recovery in our two lead growth markets, the US and China. So I'm going to first share my screen, so if you'll bear with me, that's set up here. And hopefully, you can see the slides. I will be speaking to these slides that will soon be posted to our Investor Relations website, so I'll lead with our standard cautionary language as I will be making some forward-looking statements.

But starting with the US, you know, our sales recovery is sustained with comp sales improving from minus 14% in July to minus 11% in August, on track to achieve positive comps by the end of our fiscal second quarter in 2021 as we previously outlooked. We've noted at the bottom of the slides some 2-year comps to normalize for some variability in prior year lap. The recovery as you can see is unfolding fairly steadily.

Worth noting that now more than half of our stores in the US have at least limited seating available and we've seen that as we've progressively opened our ordering and sales channels, from drive-thru to entry way pick-up to in-store ordering and seating comps have improved and they're continuing on that path. Looking ahead, we expect three key initiatives will fuel our future recovery in the US: first, the deployment of handheld POS at the drive-thru; second, the roll-out of curbside pick-up where we have convenient parking; and third, today, the launch of Stars for Everyone. We are very pleased with the upward momentum in our US business. But we still have a ways to go to fully recover sales in the US and the overall operating environment remains somewhat uncertain. So prudently we foresee another six months of recovery as previously outlooked, but we're very pleased with our progress thus far and we're very optimistic for the future.

So, moving then to our second lead growth market which is our business in China, you can see that our business there is approaching full sales recovery. We posted flat comps in August up from minus 10% in July. Those numbers include a 4 percentage point benefit from a temporary VAT exemption. So, we've also shown the numbers without that temporary benefit. We are still on track to achieve positive comps excluding the VAT benefit by the end of our fiscal Q1 in 2021 as we previously outlooked.

Like the US, we've noted here at the bottom of the slide, 2-year comps which show a steadier recovery and turned to positive in August. Our future recovery enablers in China include, number one, the accelerated development of our convenience store format Starbucks Now. Number two, increased digital customer engagement which has grown through ongoing improvements to our digital platform including the recent introduction of Starbucks Rewards multi-tier redemption and third ongoing leverage of our digital partnership with Alibaba which includes delivery.

Now, there are some headwinds to our full sales recovery in China and those are continuing lower levels of traffic at travel and transportation hubs as well as city center locations that are impacted by reduced inbound international travel.

So, I'm going to wrap-up my opening remarks with some reminders about some upcoming key dates. We are set to report our fourth quarter and full year earnings on October 29 at which point, we will also provide guidance for fiscal 2021. Now, that will be 53-week fiscal year for Starbucks instead of a normal 52 weeks, as happens every five or six years. We will highlight the impact of the 53rd week, when we do provide guidance. Looking further ahead, we will host our Biennial Investor Day on December 9, which will obviously be conducted virtually.

So, I am going to now stop sharing my screen here, as we've reached the end of the slides. And John, at this stage, really happy to take your questions.

QUESTION AND ANSWER SECTION

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yes. Thank you. Yeah. So the August comp of down 11 in the US, I assume, I can ask you very specific question. How many stores [ph] have or any still closed (00:04:45), and could you tell me again the percentage of stores that have limited [ph] seating, I think you said (00:04:49) half the stores have limited seating?

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

Yeah. So, currently about 3% of our company-owned stores in the US remain closed. Those are concentrated in central business districts and large metropolitan areas and yes, more than about 50% of our stores that are open do have some form of seating.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

And the stores, I guess, they have more than 50% have seating, 57% of your stores have drive-thru. So, I mean, would it be more likely that a drive-thru store would not have its seating open or is that just really – is that – market like California, for example [indiscernible] (00:05:30) of course what I'm going to get at is, does seating mean higher sales performance?

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

Yes. In drive-thrus more often than not we do have seating available, which is important because there are customers who would prefer not to wait in the very long drive-thru lines, they can come into the store, place their order and collect their order and be on their way or if they like, they can sit and stay where we have limited seating available.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yeah.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

With respect to the drive-thru locations, they're performing really well, they are already comping positively. The cafes that are concentrated in our central business districts, they're continuing to comp negative those that are open, but as I mentioned before a large number of those remain closed. But all of that is reflected in the improving sales comps that I've shared.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

And how do you define CBD or urban obviously have been – I think there could be a lot of – kind of cross definition here, but what percentage of your stores would you define as CBD, which for obvious reasons take the longest to recover, getting full mobility back [ph] subway traffic (00:06:36), other things like that?

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

And the best way to think about it is, as you mentioned before, about 60% of our company-owned stores in the US are drive-thru, the remaining 40% are cafes. Of that 40%, about a third are in central business districts. Not all of those are closed, but a fair percentage are and those represent the 3% of the total company-owned system that remain closed at the moment. But you know what I think is important to highlight is that through the pandemic, we've seen customers change their behavior, so as increasing numbers of our customers are working from home, that's why we have low levels of traffic in central business districts, but we are seeing very significant increases in customer traffic at our suburban drive-thrus. Customers have changed their behaviors. They are eager to re-establish their routines and find some measure of normalcy. They're visiting Starbucks closer to home. They're tending to visit a bit later in the day and they're spending more when they do come. So, as customers have modified their behavior, we've adapted to accommodate them.

John Ivankoe

Analyst, JPMorgan Securities LLC

(

Thank you. You know, so again this is a very quick math. So 60% of your drive-thru stores are positive, 60% of your stores have drive-thrus and that cohort is positive, maybe more specifically. That will suggest something like comps were down somewhere like 25%, maybe more for the non-drive-thru stores. I mean, is that kind of within your expectations at this point [ph] in a recovery and – I am going to use sell tell, but I mean, (00:08:00) lack of better word, is there anything that you can do to kind of pull – basically pull up that lagging cohort that you feel that is within your control that bodes to basically the government – government kind of opening, people just getting back to work?

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

Here's how we think about it. There will be a cohort that will for some period of time be under pressure until the environment normalizes. We don't know when that would be. We're not waiting for that. And so, we are rapidly innovating in order to capture new demand, new occasions that we didn't have before that tie to how customers are currently living their lives, which is why we have moved quickly to open up new channels of distribution at our existing stores, primarily in the suburbs, because there's significant latent demand, there's unmet demand. And so, as we've seen customers change their behavior patterns, we've moved swiftly in order to capitalize on that recognizing that for a cohort of our stores, it may be some time before, you know, we see volumes return to where they were before and we're not waiting around for that.

And then, also as we mentioned back in June, some stores in central business districts that were already lagging in their performance, in the current environment, just aren't going to deliver a level of performance that will warrant maintaining those operations. And so, many of those stores formed part of the roughly 400 stores that we said we would accelerate a closure on in the next 12 to 18 months and that process has started. So, we are rapidly shifting our business in response to shifting customer behavior in the near-term and for the long-term, and of course another important part of that is the rapid innovation around our convenient retail store format, which is the Starbucks pick-up store where we're looking to accelerate the pace of development in the coming year and that will be focused in these urban centers.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yeah. There's a letter that was sent to landlords [indiscernible] (00:09:52) Starbucks is obviously a big tenant. But you're not getting – the walk by traffic [indiscernible] (00:09:59) traffic, what have you, that a lot of stores would have contemplated when you signed those leases. Are you having success in that, that 40% of non-drive – let's just assume that that's the case. The 40% of non drive-thrus or maybe that one-third of CBD and the 40% of kind of getting significant rent reductions.

I'm sure, when a landlord says, hey, when you – when Starbucks leaves a street, the value of that street goes down. I mean, our landlords kind of recognizing that and giving you the kind of terms that basically make a marginal decision, one that in fact that you'll stay because they appreciate that you add value to everyone around you.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

Well, John, you're absolutely right. We recognize the strength and the power of our brand and the prominent position that we have in retail. And so, we are seeing success in those conversations with landlords. But it's not necessarily in the way that you might expect or that you've alluded to, that is we're not seeing short-term rent abatement. What we are seeing is more favorable terms for existing locations and importantly for new locations because remember, we're still growing. Even though we're accelerating the closure of stores, we have a very robust new store development program focused on our drive-thru assets largely in the suburbs and we're able to bring to bear the current environment to secure favorable rent terms or lease terms for those new locations as well as for again existing.

So, to give you some examples of the types of concessions we are seeing, we are securing additional parking spots. That's very significant, because, in fact, we see curbside pickup as an important enabler as I mentioned before of our longer term recovery. Already we're in about 800 stores with curbside pick-up. We will more than double that number in the next couple of months. We're also securing early termination rights in our new leases, which is important because circumstances as we've learned can change...

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yeah.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

...and we need to have the flexibility to exit as the situation warrants. And then finally, we're also writing into our current leases and new leases provisions for rent relief in the event of new disruptions comparable to what we've experienced in the last several months. We didn't have that on our leases before.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yeah.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

So, I think we've been able to capitalize on the current environment in a way that is very helpful to our current operations and to our future operations, but not necessarily in the form of rent abatement per se.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Okay. Yes. No, thank you. I want to [ph] re-hit (00:12:20), flipping back and forth my notes, this conversation is great by the way, I mean, I didn't know we were going to be able to get such specific detail. Let's see, sorry about this, so the three initiatives in the US, handheld point-of-sale curbside and Stars for Everyone. So, let's focus first on the handheld point-of-sale. Is that someone that's standing in the drive-thru? Is that – there's an additional person in the store? Explain what that is? And, and how much of a – I mean, of a theoretical throughput enhancer that could, of course, be. And whether, and is that an all-weather type of event, or just kind of like the practical solution across your store base?

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

So, all great questions, John. We are currently in the process of refining our model for handheld POS, so we're currently piloting and refining our model through the testing that we're doing so that we can rapidly deploy this. But absolutely, we expect this to be a game changer for us in drive-thru. Bear in mind, that when Starbucks was first launched as a concept, it was not designed for drive-thru. We added drive-thru as consumers were looking for more convenience. But the fact is that given the profile of our menu with beverages that are handcrafted to customers' individual specifications down to how many pumps of syrup they want, how much ice they want, what kind of milk they want...

John Ivankoe*Analyst, JPMorgan Securities LLC*

Yes.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

...because many customers are pivoting to plant-based milk and we're able to provide that to them, given the complexity of the build, the wait times in the drive-thru line can be long. The other thing we've seen is that with how customers have changed their behavior in this pandemic. As I mentioned before we're seeing tremendous demand at our drive-thrus in the suburbs because people are working from home.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Yeah.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

They're taking a break in the morning, maybe in the afternoon again, they're bringing the family with them. We have a significant increase in the average order size and with that very high ticket growth and you saw that in our third quarter results. We're continuing to see that. We do expect that that will moderate over time but that does put pressure on the drive-thru experience and so we see handheld POS as an opportunity to collect orders sooner in the line, so that we can start the production of those handcrafted beverages and be prepared to fulfill those orders more quickly than we are today. And we know from our experience because we do measure this that when we improve drive-thru time, we reduce balking, we reduce line rejection. So we're better able to capture the demand...

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Right.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

...that is out there. The last thing we want to have happen is someone drive up to Starbucks, see a long line and continue on their way. That's another reason why curbside pick-up is so important because it provides customers another option. I don't want to get in the drive-thru line. I placed my order via my mobile phone.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Right.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

I can conveniently pull into a parking spot that is designated for pick-up.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Right.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

And partners will bring my order out to me. That is working beautifully. That's taking pressure off the drive-thru and it's accommodating more of that customer demand.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Yeah. And ironically I mean, I would think where you have drive-thru is just probably where you can most likely have curbside, so it's like...

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

That's right.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

[indiscernible] (00:15:20) and so, it's going to 1,600 stores, curbside [ph] we're going to have (00:15:27) 1,600 stores relatively soon. Do you have [indiscernible] (00:15:31) number...?

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

It will go to about 2,000 John, excuse me.

John Ivankoe

Analyst, JPMorgan Securities LLC

Okay.

Q

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

[ph] It will go to about (00:15:33) 2,000 stores in the coming months here, so...

A

John Ivankoe

Analyst, JPMorgan Securities LLC

Okay.

Q

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

[ph] We are looking at the team (00:15:37), I have to give the team a lot of credit. They're moving very rapidly adapting to customer behaviors, rapidly innovating and deploying with tremendous discipline and urgency.

A

John Ivankoe

Analyst, JPMorgan Securities LLC

Okay. [indiscernible] (00:15:49) 2,000 is a huge accomplishment in such a short amount of time. But how many could have it in your opinion? Have you guys gone through this side-by-side on that?

Q

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

It's early to say. So, in the near-term, we can see our way to 2,000. A lot of it has to do with the real estate and we are...

A

John Ivankoe

Analyst, JPMorgan Securities LLC

Right.

Q

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

...uniquely situated and the viability of having convenient parking spaces.

A

John Ivankoe

Analyst, JPMorgan Securities LLC

Yeah. Yeah, yeah, definitely. Okay. I think handheld I mean, like, again this is my opinion, I wonder, have you studied how Chick-fil-a for example, does handheld? I mean – they don't have just one person doing handheld, they just – it's like, not only can you order, but you can actually pay, and so you can kind of do a lot of other things and they have kind of done that. I don't know how much in their capacity – their drive-thru capacity went up with handheld but you can see it, how much faster it is. I don't know if that's – kind of who you benchmark or if that's fair [indiscernible] (00:16:46).

Q

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

Yeah, John. Our team has gone to school on everybody in the category to learn best practices and rapidly apply them. Of course, we have a very complex technology stack that includes our loyalty program and today we're launching the Stars for Everyone. So...

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Yes.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

...we have to be very careful, thoughtful and deliberate about how we introduce even more complexity within that stack to ensure that we execute with excellence both for our partners as well as our customers.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

And do you think – is Stars for Everyone an enhancement or do you think that's a potential game changer?

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

It is a game changer. That's how I think about it, because as we have researched ways of capitalizing on the enormous success of our Starbucks Rewards program time and again what has surfaced in our consumer research is that the number one point of friction, what prevents customers who love Starbucks from joining the program is the requirement to prepay on a stored value card.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Yeah.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

So with Stars for Everyone, we are removing that barrier. And now, all customers who use their mobile phone to place orders, who register as a member of Starbucks Rewards and register a credit card or a debit card, can pay with that credit card or debit card, not a stored value card, and earn stars. Now, as you would expect, the stars earning rate is lower. So, the current program at the stored value card is two stars per \$1. With Stars for Everyone, it's one star per \$1, but it's a reward nonetheless...

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Yeah.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

...and it provides customers with a way of accessing value that we know is quite important and we do expect as we've observed with Starbucks Rewards previously that when customers make the move and we're able to build that relationship with them and bring to bear our personalized marketing, their frequency increases and their average spend increases. And frankly, what I think is going to happen in the case of Stars for Everyone is that once customers become accustomed to how it facilitates their overall experience, many will choose to migrate up and move to...

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yes.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

...the existing...

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yes. Exactly. When there is like...

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

[indiscernible] (00:18:47) they can earn 2X.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yes. Yeah. Definitely. And so, it still is credit, debit based. It's not – the cash is not an option or did I misunderstand that?

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

I don't know. I believe cash still is an option. So, the way that the app has been designed at the time you place the order, you can select your tender, which would include a registered debit or credit card or you can indicate cash and scan at the registers is how I understand it works.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yeah. Okay. Yes. Again, in that, some [ph] percentage of customers (00:19:21) I see it every day do pay with cash. I mean, have you released, [ph] do you say what that number is (00:19:23), the percentage of your transactions [ph] that are still (00:19:27) currency?

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

I don't know that we've released that before, John.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Okay. Yeah. I know. But it's not a small number. I mean – and that person by definition couldn't have a card before, because that's, at least you have – you have it on the phone. Okay and...

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

John, what I would say is that the overriding insight underpinning continued enhancements to our Starbucks Rewards loyalty program whether in the US or in China is flexibility because, remember last year...

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Yes.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

...we introduced multi-tier redemption here in the US. We launched that at the start of the summer in China and that provides customers so much more flexibility in terms of...

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Yeah.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

...how they can earn and use their rewards, and that has contributed to increased spend with our Rewards members. The other thing I want to highlight, because I know that this question came up, in fact I think you may have asked the question on our last earnings call is in relation to our 90-day active Rewards members and we...

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Yes.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

...did see over the course of the pandemic that number come down, it had been, I think at 18.7 million at the beginning of the pandemic. And then at the end of our third quarter, it dropped down to I think 16 million – just over 16 million.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Yeah. We have the tables [indiscernible] (00:20:38).

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

Yeah. So at the end of August it was back above 18 million. So very quickly...

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Okay.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

...as we've re-opened for businesses, as we have opened new channels of distribution, we've been able to rebuild our 90-day active Starbucks Rewards member base, and we expect that upward momentum to continue now with a new catalyst Stars for Everyone.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yeah, interesting. And in terms of communicating these changes, a couple of things; Starbucks uses some traditional media, I mean, your marketing spend over the course of 25 years has gone up and you've obviously had a lot of benefit from that [ph] going up Starbucks, didn't use to – even be on television (00:21:13) now obviously it is. What is kind of your attitude towards traditional and digital media and – or are you taking, this is basically an opportunity to kind of rethink all of our marketing spend and make every dollar be re-earned, if you will?

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

Well I think our marketing team does an extraordinary job of ensuring that our money is spent as efficiently as possible and of course it is the strength of our Starbucks Rewards loyalty program that provides us with the opportunity to be I would say more efficient than a lot of others within our category. That and our brand stature, our brand naturally attracts a lot of attention, a lot of promotions through various channels when we have new news around new product launches or new program launches like Stars for Everyone that attracts a lot of media attention. And that's why [indiscernible] (00:22:06)...

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yeah.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

...when you look at the construct of our P&L, our marketing spend was about 1% whereas others in the category are in the mid-single digits and we see the opportunity to continue to realize efficiencies, not only for our loyalty program-oriented marketing, which includes the personalized marketing that we do as we build these relationships with our customers, but also through social media and traditional media, we have an opportunity to continue to revisit our programs to ensure that those marketing dollars are spent as efficiently as possible. But we are not backing away; in other words, we're not looking to spend less, we're looking to continue to spend what we feel is a healthy amount of marketing and to make sure that that is spent in the most effective and efficient way possible.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Thank you for that. Before just in that 30 seconds we have before the call, you kind of, pointed out that you're wearing a Pumpkin Spice Latte sweater and [indiscernible] (00:22:57-00:23:02), how important are new products and a pumpkin spice something, is it a gift that's continuing to give. Just the time to launch new products, how important is it for food, obviously the impossible sandwich that you have; Starbucks is very much of a new news product driven brand many brands have significantly cut back their menu offerings. I think you've only added. So just talk about the importance of new products and the place within that in an environment that still is very changed and difficult to operate?

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

Yeah. Well, I think for Starbucks, new product innovation continues to be very important to how we create excitement for both new and existing customers to drive visitation. But at the same time, there is no substitute for the return of the fan favorite. So yes, I am wearing my pumpkin-colored sweater today in honor of the fall, the fact that this is Pumpkin Spice season and how excited I am about our relaunch at the end of August of our Pumpkin Spice Latte and my own personal favorite, the Pumpkin Cream Cold Brew.

I think it just goes to show you that in the current environment, customers are looking for a taste of something familiar, something that helps them feel that they return to a sense of normalcy. And that's what Starbucks, as a brand, represents for many customers. And that's what a product like Pumpkin Spice represents for so many of our customers as well. And so, we could not be more delighted with how we're able to leverage these significant assets that are unique to Starbucks in ways that help to continue our recovery and underpin our optimism around full recovery of the business.

I did want to come back quickly to the numbers because I have them now here in front of me. At the end of – this is for Starbucks Rewards. At the end of our fiscal Q2, we were at 19.4 million 90-day actives in the US. At the end of Q3, that had dropped to 16.3 million. And at the end of August, we were at 18.7 million. So, not quite to the 19.4 million pre-pandemic, but you can see how quickly our Starbucks Rewards customers have come back and we're seeing healthy numbers of 90-day actives. And like I said, today's launch of Stars for Everyone is going to take that to a new level and we could not be more excited about that.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Any markets that have been reopened the longest, Georgia North Florida and what have you, Tennessee, for example, are these markets performing significantly ahead from the markets that like a Michigan that's still been relatively slow? I mean, what kind of a [indiscernible] (00:25:39) understand the CBDs, let's – we can kind of talk outside of that, but are the markets that've been open the longest performing the best I mean because the markets that have been open the longest, the consumers have a lot more choice and people are acting "more normally" and aren't necessarily in the drive-thru line with 20 other cars [indiscernible] (00:25:57) a lot of things. So, I think it'd be kind of an interesting dynamic to understand.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

Yeah. John, so here's how I would talk about it. We have the ability to dial up and dial back our operations, based on prevailing conditions in every one of the markets where we operate and we have seen through this pandemic in places like California, Texas and Florida where there were flare-ups...

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Yeah.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

...in the beginning or middle of the summer where measures were taken that reduced traffic, we dialed back our operating protocols. But then, as conditions improved, we dialed back up and what I mean by dialing up and dialing back is what I mentioned by way of these progressive orders of sales.

So, from drive-thru to entryway pick-up, to curbside, to in-store ordering, sit and stay and as we make our way across that spectrum regardless of the market, we see sales improve because we're able to accommodate more customers for the type of experience they're looking to have.

So, it's more a function of what those prevailing conditions are, they can go up and down and importantly, we have a new level of resilience that allows us to dial up and dial back our operations as needed. And that choppiness and performance across the markets is embedded in the numbers that I shared in terms of how we progressed from July to August and as I mentioned, the positive momentum continues.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Q

Yeah. Very interesting. Obviously, labor is the biggest cost. At the store level, you were mentioning dialing up and dialing down based on various factors that you mentioned. Has the labor model changed in anyway at Starbucks, obviously you've been very focused on, at one point your drive-thru only, you couldn't even come into a store, so obviously that's a very different labor model than being able to come into store, and where it's different labor model that having a café model where people are sitting down. So how do you anticipate the labor model potentially permanently changing? And should we see for example labor hours be lower on a given level of sales based on some learnings that you've had from COVID, how significant could that be in your business?

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

A

Not significant on the labor side, and it's not to say that we aren't continuing to find ways to be more efficient, we're continuing to automate tasks where we can. We're continuing to apply best practices to improve the efficiency of our operations, as I mentioned before we're looking for unlocked capacity of the drive-thrus, but through the pandemic we've had to add labor in areas like cleaning, and with the rollout of curbside pickup or handheld POS, that adds more labor to the store. But it's being done very smartly in a way that ensures we get a return on that investment.

But given the complexity of our menu that goes with offering hand-crafted beverages that are customized to the specifications of each and every customer, we don't have the ability like, I think some others in our category who are looking at opportunities to simplify and rationalize their menu because they can. We offer personalization, which drives a lot of menu complexity that is a source of competitive advantage because we're the only one who can do it at scale backed by a loyalty program that keeps people coming back once they've found their favorites.

So we're not going to walk away from that. We do expect that we'll get back to our pre-COVID efficiency overall, so we will find some efficiency opportunities, those will be offset with new investments around opening up some of

these channels as I mentioned, but also our commitment to our partners for the long term and continuing to invest in their development and in their growth, and we are planning for investments like that in fiscal 2021.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Do you need to get back to previous ADs (sic) [AUVs], even higher ADs (sic) [AUVs] to get back to previous store level profitability?

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

Yes, we do.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Okay.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

We do so that's why, John, what we said on the Q3 call was that – and I'll just focus on the US business for a minute, but of course we have a whole global business...

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

I know, we are flying but we have so much to cover. I know.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

So speaking of the US business, we said that we would recover sales, meaning we would turn positive by the end of our fiscal second quarter. And that margin recovery would lag by a couple of quarters.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yes.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

That's one of the reasons I mentioned, which is that we're investing in new areas and new channels to open up sales and we're making new investments in partners, environmental sustainability, technology, all of the things that are important to our brand that differentiate us from the competition. We have never been shy about diluting margin in order to unlock long-term growth and that continues to be how we think about the business.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yes. Understood. So, let's shift to China, I don't know how you guys were so close, even back in January, February to kind of like predict the recoverability in China comps, I don't know if there's a little bit of luck or just

absolute genius in terms of you getting so close to flat by the end of the fiscal year. It's about – that was a very hard target to come as close to, as you did so, obviously, congratulations there.

[indiscernible] (00:30:56)

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

I'll offer just a bit of insight on that. At the time, we put together that projection; it was based on what we experienced with SARS nearly 20 years ago. So, we did have experience in market with a decent number of stores that gave us some visibility to how the market might evolve and eventually recover in response to a major disruption like a pandemic.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

And in your YUM experience, in your China experience probably couldn't have hurt that, I mean you probably had an acute understanding of that customer and how they can kind of get back and what have you. Anyway, amazingly well guided, so what's the opportunity from here? So, excluding that China is down 4% in August, the trend is, let me see if I wrote that down correctly – I mean, the trend is obviously improving significantly.

When did these numbers kind of [ph] become definitively (00:31:45) positive and I want to talk about the state of competition. I mean, obviously cost is, kind of, in the market, Luckin, I don't know if you want to talk about directly, it's like this was like the big threat to you that obviously wasn't what it was supposed to be. So, there is obviously some things that – how has the competitive environment changed in China and does this actually open or expand or widen your market opportunity relative to what you would've thought even 12 months ago based on what you've achieved?

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

Let's first talk about the Starbucks business in China and then we'll talk about competition. We could not be more pleased with how our business has recovered in China from a comp sales perspective, but then also importantly in terms of how quickly the team was able to reinvigorate our new store development program. After...

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yeah.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

...putting new store development on hold for a period of six weeks or so, they very rapidly ramped back up and so we do expect to open more than 500 units this fiscal year, which is quite a monumental achievement. And as I mentioned before, the team is not only opening units with speed, but they're doing it with innovation, with new formats including Starbucks Now and other innovative designs that continue to capture the interest of Chinese customers and we're using that as a vehicle to not only drive traffic with existing customers, but to welcome new customers to the brand because as we open new stores, we're not doing it just in existing cities, but we're entering new cities and so we're using our development program as a platform to broaden the reach of the Starbucks brand in the world's fastest growing consumer market, so we could not be more pleased with how well

positioned we are and how well the team is executing locally in terms of recovering comp sales and driving new unit development.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

And could you give us an update? I mean, I know 80% of transactions are actually consumed on-premise in China. I mean that was a tough obstacle, could you remind us what percentage of your stores are at full capacity, whether it's just in number of seats or the number of operating hours; and if that 80% is still holding true?

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

Well, John, I think the important thing – and I know you're aware of this because you've studied the market for years. China is a dynamic market. It is by no means a static market. And so, as COVID has impacted the market, customers have changed. They've changed their behaviors. They have sought out experiences that are contactless. They were already very digitally savvy. They're leaning increasingly into those digital platforms. And we are evolving our offering to meet their demand. So, contactless is number one.

Number two is convenience, which speaks to, again, the slight pivot in our development program, continuing to open core stores with the beautiful seating areas to satisfy that type of occasion, but being there in a different format to satisfy a different occasion sometimes for the same customer, but oftentimes, a new customer. And so, I think it is more about the fact that the market is dynamic, it is changing in response to COVID. And we are changing as a business in response to those new customer behaviors and preferences. Digital being, I would say, the most important thing.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yeah. So, maybe 80% of transactions are no longer consumed on premise. You didn't give me a number, but I would assume that number is lower, that is less...

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

It is less.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

What percentage of your stores are, kind of, at full capacity now? Is that number approaching 100 in China? I think it was 70, if I remember correctly.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

What I would say, John, is that we are far from full capacity because remember the business in China is different from the US. It isn't concentrated in the morning daypart as it has been in the US. It's more spread across the...

[indiscernible] (00:35:20)

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Meaning, seating and hours, I mean, have seating and hours been returned, I think it was at 70% of your stores before we're at previous seating and previous hours. So, not utilization, but that may – I didn't ask the question correctly.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

I'm sorry. I think we have about one stores that – or 1% of our stores that are currently closed. Those that are open are substantially, meaning more than 80%, back to normal seating. So, we are operating at that full capacity.

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

And it is remarkable. I mean, it's like being in a parallel universe to see – China that can be 80% of stores have full seating. And yet, in the US, we're talking about 50 and even the stores that do have capacity are not like they were before. What can we learn from China, in the US and when – I mean, [indiscernible] (00:36:18) sounds like, I mean you have a very specific understanding about this virus.

When can that be the US, in your opinion and can the US consumer follow basically the pattern? And what is a much more dense country? [indiscernible] (00:36:34) ironically enough, I mean, there's a lot of confusing things about how China has recovered so much. And we're still kind of not the [indiscernible] (00:36:43) but we still haven't made the improvements as so many other countries have.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

Yeah. I think it's fair to say that we won't see customers return entirely to their routines until there is a vaccine. We're not waiting for that. And so, what we've recognized is that we have needed to rapidly adapt our operating protocols to make our partners feel safe and secure to come into work and to make our customers feel safe and secure to come see us. And they are coming back. So, I think what we're seeing is that people are feeling more comfortable because appropriate precautions have been taken to ensure the safety and cleanliness of the experience that we offer.

And it just demonstrates how customers are yearning for that taste of normalcy that comes with a Pumpkin Spice Latte [indiscernible] (00:37:27), right, and we need to be there in support of the communities because we're an important...

John Ivankoe

Analyst, JPMorgan Securities LLC

Q

Yeah.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

A

...we see ourselves as being an important part of that healing process.

John Ivankoe*Analyst, JPMorgan Securities LLC*

And perhaps, as unfortunately we're somehow calling on 40 minutes. Can we talk about the organization, how Starbucks is actually a strong organization, how it can take advantage of new market share, I mean where the state of investments have been in technology infrastructure, in people, just like what you cut, what you've maintained in, and how just – speaking in terms of the organization and some of the changes that you made around [ph] silo (00:38:02) and I think some of the changes that Kevin made were under rated by the market in terms of how significant they were, kind of how you perceive Starbucks in 2021 and 2022 versus maybe the organization that you joined?

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

Yeah. Well, there's no doubt that some of the strategic initiatives you mentioned have been instrumental to the, I would say the turnaround of the business prior to the onset of COVID, but those same changes organizationally have been instrumental to the strength of our recovery.

And so what I would highlight is that through this transformation over the last two years, again leading up to COVID, we've become a much more focused company, a much more disciplined company, a company with a higher level of organizational agility that has enabled us to innovate more rapidly and now with the improvements we've made to our operations with COVID, we're a more resilient company.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Yeah.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

And so, all of those things were very deliberate over the last couple of years on top of the specific business initiatives to drive different results was sort of a transformation of the company that has now given us new capability and I think a new mindset that is demonstrated through how rapidly and smartly we've been able to recover our business and underpins the optimism we have for the future.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Excellent. Thank you so much. It's great to see you. Look forward to seeing you soon. I wish we could meet in December 9th in person but I guess that's just not possible.

Patrick J. Grismer*Executive Vice President & Chief Financial Officer, Starbucks Corp.*

It'll be virtual.

John Ivankoe*Analyst, JPMorgan Securities LLC*

Yeah. I'll make sure I have five coffees during that meeting. But okay, talk to you soon and thank you for that detailed update, and we'll talk in a couple of weeks. Thank you.

Patrick J. Grismer

Executive Vice President & Chief Financial Officer, Starbucks Corp.

Thanks so much John. Take care. Bye-bye.

John Ivankoe

Analyst, JPMorgan Securities LLC

Take care. Thank you.

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