27-Apr-2017

Starbucks Corp. (SBUX)

Q2 2017 Earnings Call
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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon. My name is Julie and I will be your conference operator today. At this time, I'd like to welcome everyone to the Starbucks Coffee Company's Second Quarter Fiscal Year 2017 Earnings Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions]

Thank you. Mr. Shaw, you may begin your conference.

Tom Shaw
Vice President, Investor Relations, Starbucks Corp.

Thanks, Julie, and good afternoon, everyone. This is Tom Shaw, Vice President, Investor Relations at Starbucks Corporation. Thank you for joining us today to discuss our second quarter 2017 results, which will be led by Kevin Johnson, President and CEO; Belinda Wong, EVP and CEO, Starbucks China; Scott Maw, CFO; and Howard Schultz, Executive Chairman. Joining us for Q&A are John Culver, Group President, Global Retail; Matt Ryan, Global Chief Strategy Officer; Adam Brotman, EVP of Global Retail Ops; Kris Engskov, EVP, President of U.S. Retail; and Tony Matta, President, Channel Development.

This conference call will include forward-looking statements, which are subject to various risks and uncertainties that could cause our actual results to differ materially from these statements. Any such statements should be considered in conjunction with cautionary statements in our earnings release and risk factors – risk factor discussions in our filings with the SEC, including our last annual report on Form 10-K. Starbucks assumes no obligation to update any of these forward-looking statements or information. Please refer to the tables at the end of our earnings release and on our website at investor.starbucks.com to find a reconciliation of non-GAAP financial measures referenced in today’s call with their corresponding GAAP measures. This conference call is being webcast, and an archive of the webcast will be available on our website.

With that, I'll turn the call over to Kevin Johnson. Kevin?

Kevin R. Johnson
President and Chief Executive Officer, Starbucks Corp.

Thank you, Tom. Welcome, everyone. Before getting into Starbucks’ Q2 results, I thought I'd comment on a recent Wall Street Journal article noting that more retail stores have closed in the first quarter of calendar year 2017 than closed in all of 2016. And that more retail stores are expected to close in the U.S. this year than closed in any year during the Great Recession that began in 2008. The article illuminated once again the seismic shift in consumer behavior underway and the devastating impact that this sea change in behavior is having on many traditional brick and mortar retailers. Articles like this prompt three very important questions that I've repeatedly asked myself over the years and that I suppose many of you on today’s call have asked as well.
What are the critical, transformative components required to propel a brick and mortar retailer into the future? How do these transformative components relate to Starbucks? And what are the proof points? It is against this backdrop that I decided to open my first earnings call as Starbucks’ CEO by sharing my perspective on what it’s going to take for a brick and mortar retailer to survive in the future, and to explain how in the face of tremendous retail headwinds and cross currents underway, Starbucks continues to produce record financial and operating results quarter after quarter, and open a new class of over 2,000 stores around the world every year that continue to outperform both the immediate prior class and the industry overall, and deliver record AUVs and profit.

Now, Howard understands this intuitively, our senior leadership team has been intimately engaged in the topic. As a company, we have a clear perspective on the answers. The critical transformative components required for any brick and mortar retailer to survive, let alone succeed in the future are an engaging, digital and mobile relationship with customers that is threaded into a branded, immersive, experiential retail destination.

The attributes of the destination will vary. They may include theater, intrigue, or romance. But the common denominator will be the creation of a consumer experience that evokes human emotion and connection. I firmly believe that these are the ingredients that will determine which brick and mortar retailers thrive in the future, and which become victims of the current trend.

The analogy from my years in the tech industry is how companies respond when a new disruptive technology, like cloud computing, for example, emerges. Those who recognize the disruption think long term and innovate for the future are the big winners. Those who don’t, struggle. The retail industry is going through a period of similar profound disruption right before our eyes. These critical components are at the very core of Starbucks’ business and investment strategies. To be sure, many of our investments will yield near term returns; others, longer term returns, but in all cases, they will further solidify Starbucks foundation as we build for future. Starbucks Coffee Company is playing the long game, and we are playing to win globally.

Let me now share with you the evidence of our success in Q2 and why we are so optimistic about the second half of fiscal 2017. I’ll start with four important and very encouraging headlines of today’s call. U.S. comp sales accelerated through the quarter, culminating with a 4% comp in March. U.S. comps are further accelerating into April. Our newest class of retail stores continue to perform at record levels. And our business in China posted accelerating 7% comp sales growth, including 6% transaction growth.

Accelerating comps and strong positive trends in our two largest markets sets up the narrative for FY 2017 as being the year of two halves. We’re quite confident that we’ve turned the corner on U.S. comps, and that given the strength we are seeing in our U.S. business going into the second half and the beverage, food and digital innovation we will be rolling out over the next two quarters, that we will deliver on our mid-single digit comp target for the full year, despite the soft start in the first half. I want to be very transparent with you on our priorities, and explain how they relate to the two most important things for the future, digital relationships with customers, and branded experiential retail that are customer destinations.

Our five priorities are focused on near term, as well as long-term growth. They include: One, continuing to accelerate comp sales and transaction growth in the U.S. Two, driving breakthroughs in food for the lunch day part. Three, enabling long-term growth in China. Four, extending our digital flywheel assets; and five, elevating through the Starbucks Reserve brand. Each of these are powerful drivers of value creation that will once again provide us with outsized current returns while strengthening our business and positioning us to deliver sustained, profitable growth in the future.
Let me start with an overview of our efforts to accelerate U.S. comp sales. We have several initiatives supporting this objective underway, including food and beverage innovation, strengthening and leveraging our digital and marketing capabilities, operational improvements, and improved in-store execution. You will recall that in Q1, we highlighted that 1,200 of our busiest U.S. company operated stores were experiencing 20% or more of their peak transactions coming from Mobile Order & Pay.

The rapid adoption of Mobile Order & Pay and resulting demand increase was causing throughput challenges at peak in these stores. By the end of Q2, approximately 1,800 of our U.S. company operated stores were experiencing 20% or more of peak transactions from Mobile Order & Pay. Steps we have taken since the beginning of the calendar year to increase throughput have enabled to us to better and more efficiently handle increased demand from both Mobile Order & Pay and non-Mobile Order & Pay customers at peak. And we saw measurable progress in peak transaction throughput in Q2, as compared to Q1, in these busiest stores.

As we enter Q3, Mobile Order & Pay continues to be a powerful driver of comp, revenue, and attach. And we are maintaining sharp focus on further increasing throughput. Our action plan includes three ways to unlock growth in all day-parts, and particularly at peak.

Wave one actions have largely been completed and included additional training and reallocation of partner roles to Mobile Order & Pay during peak, testing of additional labor at peak in select stores, implementation of new approaches to order consolidation at the hand-off plane, and new tools and processes to support beverage and food production. These actions alone enabled quantifiable increases in both March and April, and improved the customer experience as evidenced by recent customer service scores.

Wave two actions are now underway and involve the introduction of a new Digital Order Manager, or DOM. And the selective addition of labor in our busiest stores at peak based on the results of the wave one test. The DOM shows up as a tablet-based device that provides baristas with visibility on all incoming orders and enables better tracking and real-time order production management.

It also enables a digital notification to a customer's mobile app when their order is ready, improving many dimensions of the customer experience, both in the app and in the store, while reducing congestion at the hand-off plane. We will be deploying DOM technology to our highest volume stores this quarter. But the DOM does more. As we deployed this high value, low cost technology across our store portfolio, we will create an extremely valuable source of new data insight around operations and customer experience. Data that will enable us to further optimize store operations, increase throughput, and elevate our customer experience.

Wave three actions are being integrated into our existing store development and renovation approach. We are sharpening our focus on the selection and addition of in-store equipment and pursuing improvements in overall store layout and design, all with the goal of delivering a great customer experience and further increasing throughput. The actions we have taken to improve throughput are contributing to the acceleration we are seeing in sequential monthly U.S. comp sales now squarely back in the mid-single digit range.

Looking to the future, this is all about how our digital relationships with customers intersect with experiential retail in our stores. We are confident that we're well on our way to further increasing overall store capacity while delivering enhanced Starbucks experience to our customers.

Moving on to food. At our Investor Day in December, we highlighted the importance of food to our strategic growth agenda and are focused on driving breakthroughs in food for the lunch day-part. In many ways, this is about
elevating experiential retail in Starbucks by providing a new customer offering in a relevant day-part and doing it well.

Let me put the size of the Starbucks lunch opportunity into perspective for you. You may recall that we first began delivering significant growth in our food program several years ago when we up-leveled the quality and appeal of our bakery case with particular emphasis around breakfast sandwich innovation following the acquisition of La Boulange. Our strategic focus on the bakery case and breakfast sandwiches has paid off and is contributing to sales.

In fact, in Q2, food represented 21% of our U.S. revenue and contributed 2 points of comp. We have demonstrated that by focusing on a specific day-part, we can create new customer occasions that add to the branded experience and become long-term drivers of growth. That is precisely what we are doing by up-leveling our lunch offering with the new fresh food concept we call Mercado.

We launched Mercado in over 100 Starbucks stores in Chicago earlier this month. And though still in the early days, we are extremely encouraged by the customer response to Mercado. So much so that we are accelerating plans to deploy Mercado to a second market over the next two quarters. We view Mercado as an opportunity to provide our customers with a fresh, healthy and delicious lunch menu that we believe has the potential to drive increased traffic and attach, and ultimately help us achieve our long-term goal of 1 points to 2 points of U.S. comp growth from food once deployed across a significant portion of the Starbucks platform.

We are very excited about our strategy and the opportunity to enable long-term growth in China, a country we first entered 18 years ago. Our business in China has never been stronger, nor have our aspirations ever been greater. We continue to open a new store in China roughly every 15 hours, a rate of new store growth that is likely to continue for decades to come.

Increasing customer engagement and accelerating strength in Starbucks business in China once again demonstrates the global power of the Starbucks brand. Given the strength of our China business and the size of the opportunity, I've invited Belinda Wong, CEO of Starbucks China to join us on today's call from Shanghai to share insights into how we are continuing to drive our business in this very important growth market.

Belinda, thank you for getting up so early, and welcome.

Belinda Wong
Chief Executive Officer, Starbucks China

Thank you. Thank you, Kevin. Good afternoon, everyone. I'm very pleased to report that partner and customer enthusiasm for the Starbucks brand and the momentum in Starbucks China business have never been greater. Comps in Q2 accelerated to 7%, driven by a 6% increase in transactions. We saw growth in all categories and day-parts. Beverage, food and digital innovation are laser-focused on operational excellence, and targeted brand investments are attracting new customers into our stores and bringing existing customers in more often.

Last December, we launched a strategic partnership with Tencent, including offering Tencent's popular WeChat Pay as a digital payment option in all of our stores. In its first quarter, WeChat Pay has already reached a remarkable 29% of tender, and has elevated the Starbucks experience for both customers and partners through its convenience and fast transaction speed.

Following on that success in February this year, we've launched social gifting to unprecedented customer demand, partner excitement and social media interest. In only the first seven weeks after launch, over 1.2 million
gifts were sent and over half have been redeemed by recipients in our stores. Our innovative new social gifting platform, we call it Say it with Starbucks, is not only encouraging everyday simple acts of kindness and connection, it is also bringing new customers into our stores to trial and enjoy the Starbucks experience. This is a great opportunity to further build new and authentic customer connections. We're only in the very early stages of social gifting in China and the growth opportunity ahead is enormous.

We opened five new cities in Q2 and entered Q3 with 2,628 stores across 127 cities. Once again, our newest class of stores are delivering record transactions, AUVs and profits. We're also creating new Starbucks locations beyond our retail stores. In Q1, we launched Bottled Frappuccino, a new ready-to-drink beverage tailor-made to local customer taste preferences, and it is already available through more than 30,000 points of distribution. Since launch, we've tripled our RTD business and added 5 points of market share compared to Q2 last year. And we have many exciting new CPG products in the pipeline, including a delicious tea-based Frappuccino.

Howard experienced Starbucks’ accelerating momentum in China firsthand on a milestone trip he made to Beijing two weeks ago when we also held our fifth Annual Meeting of partners and families. At the meeting, we respectfully announced a new breakthrough partner benefit, critical illness insurance to parents of our partners, a benefit that is giving great joy to our partners and over 10,000 of their parents. I am so proud that we’re setting a new precedent in China by helping our partners better take care of their aging parents. Our partners are our family, and it is important for us to also take care of our extended family. This is deeply rooted in our Chinese culture and values. We will continue to invest in our people and are committed to remaining one of the most admired brands and an employer of choice in China.

Starbucks is building a different kind of company in China, a truly one-of-a-kind company, and we're doing it one cup at a time. And with the opening of our Shanghai Roastery in December, we will further elevate the brand and introduce our Shanghai customers and visitors from all across China and Asia-Pacific to an immersive ultra-premium coffee-forward experience currently available only one other place in the world – Seattle.

We will continue to put our customers and partners at the heart of everything we do and to share our success. By doing so, we will continue to grow and to win, and to win with partners' pride in China now and in the future.

Thank you.

Now I'll pass the call back to Kevin. Kevin?

Kevin R. Johnson  
President and Chief Executive Officer, Starbucks Corp.

Thank you, Belinda. As you can see, extending the digital flywheel is a powerful asset that is driving deep customer engagement and growth around the world. And we are very pleased with the results our digital flywheel made to our business in Q2. This is one of the two critical transformative elements for brick-and-mortar retailers of the future. A year ago, we made the strategic decision to transform our rewards program from a frequency-based to a spend-based program. Following this transition, we have seen solid growth in customer membership.

We entered Q3 with 13.3 million active Starbucks Reward members in the U.S., up 11% year-on-year, and with 36% of total tender coming from Starbucks Rewards members. If you include sales from unregistered gift cards, a meaningful 44% of all transactions in the quarter were prepaid on our proprietary Starbucks payment platform.

The program change positioned us well for investments in the next wave of priorities. One to one personalization, the ability for customers to earn stars outside of Starbucks stores, and additional social gifting partnerships around the world modeled after our phenomenally successful partnership with Tencent. The personalized Star
Dashes and suggested selling are examples of how we are using personalization to provide a relevant customer experience and to increase engagement.

Starbucks rewards spend per member accelerated through the quarter as both average transaction frequency and average ticket size grew for active members. This past quarter, we saw 8% growth, the highest growth rate in average spend per active rewards member over a prior year ever, reflecting both increased ticket and transaction frequency. We have line of sight to additional digital features that will drive sales growth in the quarters and years ahead, and you will see us continue to invest to extend our digit reach to more customers in new ways that are accretive to the Starbucks brand experience and that leverage our over 26,000 stores around the world.

Finally, we are investing to elevate both our brand and our customer experience around coffee through our roasteries and the Starbucks Reserve brand. Starbucks Reserve is at the center of our innovation strategy around branded, experiential retail customer destinations. Complementing our first roastery in Seattle are additional roasteries now under construction in Shanghai, New York, Milan, and Tokyo. And a sixth in Chicago, announced only yesterday, will be underway soon.

We continue to extend and solidify our global leadership around all things coffee. Our investment in roasteries and Reserve stores not only enable a world-class, ultra-premium, coffee-forward experience in flagship locations around the globe, it also establishes a core innovation center second to none that will feed innovation throughout our global fleet of Starbucks stores.

As I said earlier, the retail industry is going through a period of disruption right before our eyes. We believe in the two transformative elements that will continue to propel Starbucks into the future, and we are allocating resources thoughtfully. As our second half U.S. comps and revenue growth accelerate, there are two priorities that will require modest increase in investment. First, we continue to see a rapid and significant return on investment by accelerating features of our digital flywheel. We have a strong roadmap of features to drive top-line growth, and accelerating those features will require incremental investment in second half. These are the right investments for our business and they will provide outsized returns. Second, we are investing against our long-term strategy to elevate the Starbucks brand through the design, construction, and introduction of five additional iconic ultra-premium Roasteries.

As Belinda noted, our second Roastery in Shanghai will be opening later this year complimented by Starbucks Reserve stores around the world and the introduction of food inside Roasteries and Reserve stores through our partnership with Italian artisanal baker, Princi. Each of these is a smart, strategic investment [ph] that will pay dividends long into the future. (24:57)

Finally, while the Teavana brand continues to be highly accretive to our tea business in Starbucks stores and is now being further leveraged with the introduction of Teavana branded ready-to-drink tea sold into CPG channels, many of our mall-based Teavana stores are continuing to have a negative impact on our overall result. We have launched a review process and intend to take clear action to improve the performance of our Teavana mall store portfolio.

When you put all of this together, we remain focused on the critical transformative elements that will propel Starbucks into the future while maintaining a sharp focus on near-term value creation for our shareholders. These priorities are linked directly to the strategy we presented at the December Investor Day, and I believe will prove to be drivers of meaningful increases in shareholder value, both near and long term.
Following Scott’s comments on the financials, I’ve asked Howard to share a few thoughts before we transition to Q&A. And with that, I’ll turn the call over to Scott. Scott?

Scott Harlan Maw  
Executive Vice President and Chief Financial Officer, Starbucks Corp.

Thank you, Kevin, and good afternoon, everyone. As Kevin shared, Starbucks once again posted record quarterly revenues, operating income and EPS in Q2. Our business accelerated through the quarter and with the momentum we are seeing and the beverage, food and digital innovation we will be introducing, we are confident in the further acceleration through the second half of the year. Now at the midpoint of our fiscal year, we are better able to assess how our year-to-date performance, our investment plans, and overall macro factors will impact our full year expectations.

Before getting into our fiscal 2017 outlook, I'd like to provide color on our second quarter performance. Consolidated revenues in the second quarter grew 6% to $5.3 billion. The largest contributor to revenue growth came from the 2,240 net new stores we opened over the past 12 months followed by 3% global comp growth, comprised of a 4% increase in average ticket and a 1% decline in traffic that after a 1% adjustment for transaction splitting, nets to flat traffic.

Consolidated operating income in Q2 increased 8% year-over-year to $935 million, despite two points of impact resulting from recording certain prior period revenue adjustments in our channel development segment and one point of negative impact from foreign currency translation. Consolidated operating margin totaled 17.7% in Q2 on a GAAP basis and 17.9% on a non-GAAP basis, up 30 basis points year-over-year.

Margin improvement in Q2 was driven primarily by sales leverage, partially offset by higher partner investments in the Americas. Both GAAP and non-GAAP EPS in Q2 grew 15% over prior year to $0.45 per share. Both measures are inclusive of a favorable $40 million impact in other income related to a gain on the sale of our investment in Square, Inc., our previous payment processor. Noteworthy is that the below the line gain on Square was largely offset by the $21 million impact of certain out-of-period accounting adjustments in channel development, as well as asset impairments related to our Teavana mall stores. I will discuss both of these items further in a few minutes.

I’ll now take you through our Q2 operating performance by segment. America’s revenue in Q2 grew 8% year-over-year to $3.7 billion, driven primarily by 952 net new store openings over the past 12 months and 3% comp growth. America’s delivered strong operating income of $826 million in Q2. Operating margin declined 130 basis points in the quarter to 22.2%, primarily due to increased investments in our U.S. store partners and higher cost of goods sold resulting from very strong food sales partially offset by sales leverage. Expanding a bit on food, we saw two points of comp from food in Q2, the most in four quarters driven entirely by attach. In fact, food attach in Q2 was the highest since we rolled out La Boulange three years ago. We saw continued momentum in our morning bakery and breakfast sandwich platforms, and strong positive customer response to our recently introduced Sous Vide egg bites.

There were several contributors to the additional one point of Americas comp in Q2, the largest being continued success of our iced beverage platform with double digit growth across each of our espresso, coffee, Teavana tea, and Starbucks refreshers. And we are launching Frappuccino happy hour next week, with far more operational focus compared to last year, new beverage offerings, and the significant tailwind and customer excitement provided by the incredible Instagrammable success of last week’s Unicorn Frappuccino. As we moved into summer, we will be launching revamped Easter boxes with an increased focus on protein and new Teavana iced teas.
Let's move on to China/Asia-Pacific. Our CAP segment once again delivered a very strong quarter in Q2, with revenues up 13% over prior year to $769 million, driven by incremental revenues from over 1,000 net new store openings over the past 12 months and 3% comp sales growth. In addition to the accelerating momentum and continued strong performance from China that Belinda highlighted, Japan also delivered a very solid quarter, despite the adverse timing impact of a large annual New Year promotion that benefited Q1 rather than Q2 this year.

Adjusted for this timing, CAP comps would have been a positive 4%. We're very pleased with our new store performance in CAP, and are seeing accelerating sales of Teavana branded teas in Starbucks stores across the region. Teavana is now available in all CAP markets with both Japan and China recording an over 40% increase in tea sales. Noteworthy is that we are creating momentum in our food program in Japan, aided by the success of recently launched pudding products and scones.

Elsewhere in CAP, our licensed joint venture markets including East China and South Korea continue to make meaningful contributions to CAP's strong performance in Q2 as evidenced by a 35% increase in income from joint ventures. CAP's operating income on a GAAP basis grew a strong 36% over prior year to $176 million, with 380 basis points of margin expansion to 22.9%, the segment's highest Q2 margin since we made the Japan acquisition three years ago. On a non-GAAP basis, CAP's operating income increased by 33% to $190 million and operating margin expanded by 370 basis points to 24.7%. Contributing to CAP's margin expansion was the transition to a value-added tax structure in China and sales leverage.

Let's turn to EMEA. Our strategy of repositioning our EMEA portfolio to a predominantly licensed model continues to drive margin expansion in the segment to a quarterly record of 12% in Q2, a 170 basis point increase over prior year. Of EMEA's nearly 2,800 total store count at the end of Q2, 82% were licensed up from 72% in the prior year.

Total revenue in EMEA were $232 million in Q2, a 14% decline versus prior year. However, when normalized for the 20% impact of the transfer of our Germany business to a licensed partner, other portfolio shifts and foreign exchange, EMEA revenue grew 6%, driven by incremental revenues from over 300 net new stores added in the last 12 months. While reported comps in EMEA declined by 1% in Q2, overall system comps increased by 3%. Our system sales and adjusted revenue figures reflect the strength of the Starbucks brand in a region that continues to be significantly challenged and adversely impacted by economic and geopolitical uncertainty.

Let's turn to channel development. As previously noted, we expected seasonality, particularly given the timing of the Easter holiday, to negatively impact Q2 revenue growth in our channel development segment. However, we also recorded an unfavorable revenue and operating income adjustment in Q2, primarily related to certain revenue deductions from prior quarters. This one-time adjustment impacted Q2 revenues by approximately $21 million and operating income by a similar amount, and was the principle reason behind flat segment revenue growth for the period. Excluding the adjustment, channel development revenue growth was approximately 5% and was in line with our expectations. Despite the adjustment, our domestic channel development business remains very strong and we gained approximate one point of market share in each of the K-Cup and Roast and Ground categories for the seventh consecutive quarter. We grew our K-Cup business by 4% during Q2, compared to zero growth for the K-Cup category overall, and now have an approximate 16% share of K-Cups.

Within ready-to-drink our NACP partnership also gained share driven by our core Doubleshot and Frappuccino beverages. We began shipping Teavana ready-to-drink teas through our partnership with Anheuser-Busch InBev in February, with all four flavors already ranking in the top ten in the premium single serve ready-to-drink tea category in our active markets.
On the international front we continue to grow our distribution of Starbucks Nespresso compatible capsules in the UK and France. Since launching the Nespresso compatible program last September, we have already shipped over 20 million units. In the UK, we have achieved 14% share and a number three market position. Channel development's operating income grew 6% in Q2 to $194 million and the segment delivered a 250 basis point improvement in operating margin to 42%.

I'm going to spend a few minutes discussing our Teavana results and in particular the mall stores which are a major component of our all other segment. We currently operate approximately 350 Teavana mall stores and as Kevin mentioned over the last several years many mall based retailers have been adversely impacted by reduced foot traffic, resulting from the accelerating shift of consumer behavior away from brick and mortar retail and changes in consumer retail activity overall. Because Starbucks is a customer destination, profitability in our Starbucks mall store has largely been unaffected. But our Teavana mall stores have not been immune with many reporting negative comps and operating losses for some time.

Since acquisition we've invested in new store designs and improved merchandising, but the rate of the decline coming through last holiday and into Q2 is worse than we had forecast and we are expecting further declines at a number of at-risk Teavana mall stores. Since the Teavana acquisition, we have recorded impairment charges and closed mall stores from time to time, but given these recent performance challenges, we recorded a larger impairment charge in Q2 related to certain of these assets.

This impairment charge was the primary driver of the 12% increase in the all-other segment's store operating expenses. We are currently evaluating strategic options for the at-risk portion of the Teavana mall store portfolio and will update you over the coming quarters as we set our course of action. It is important to note that we do have a meaningful subset of profitable Teavana mall stores.

As a reminder, strategic reviews are not a new practice for us, and typically result in a stronger portfolio and increased profits in the long term as most recently evidenced by significantly improved performance in our EMEA portfolio. Our Teavana branded teas and handcrafted beverages in core Starbucks stores continue to outperform, and we continue to expect the Teavana tea platform – expand the Teavana tea platform through product innovation and new product offerings all around the world.

Globally, in Q2, Teavana sales in Starbucks stores grew by almost 10% with even stronger performance in traditional tea drinking markets like China and Japan. Also, tea has driven a point of comp in the U.S. in virtually every quarter since we launched the brand in our Starbucks stores about three years ago. That's the investment case for Teavana, and the Teavana business remains very much intact.

Let's move on to our 2017 targets and how we expect to finish the year. First, I want to reiterate that we expect stronger revenue growth in the second half, driven by mid-single digit comps including accelerating comps in our U.S. business. Revenue growth for the full year will be 8% to 10%, excluding approximately 2 points for the extra week in 2016 and 1 point for FX. But given performance in the first two quarters of the year, we are likely to be at the lower end of that range for the full year. We expect the back half of the year to be near the upper end of this range.

EPS guidance is revised as follows. Full-year GAAP EPS in the range of $2.06 to $2.10 and non-GAAP EPS in the range of $2.08 to $2.12. Third quarter GAAP EPS will be in the range of $0.54 to $0.55 and non-GAAP EPS in the range of $0.55 to $0.56. This implies a broader range in the fourth quarter, with GAAP EPS of $0.56 to $0.59 and non-GAAP EPS of $0.57 to $0.60.
I want to take a moment to explain both the change in total annual guidance and the wider Q4 range, and there are two main factors behind the changes. First, we see the opportunity to accelerate certain investments as we move through the balance of 2017. These investments are mainly in our Roastery Reserve and Princi businesses, including the ramping of our Roastery openings and increasing our spend related to digital opportunities, including in-store digital and investments related to personalization and Starbucks Rewards. Both of these areas are critical to sustaining growth over the long term.

We now expect investments in 2017 for partner and digital to be over $250 million, accelerating as we enter the back half of the year and higher than our previous estimates. Second, as I mentioned earlier, underperforming Teavana mall stores will have a larger impact on earnings growth than we had originally forecast. I would further underscore that both ends of this EPS guidance range should be considered in your models. While we are confident regarding the second half top-line momentum, we will continue considering investing in opportunities that we believe will better position us to fully optimize our business and drive long-term shareholder value.

For consolidated operating margin, we still expect a slight improvement on a 52-week basis compared to fiscal 2016. As promised last quarter, we want to separately discuss our core and innovation G&A growth. As a reminder, we have set our long-term target to grow total G&A below the rate of revenue growth and core G&A at half the rate of revenue growth. I'm pleased to announce that we achieved both objectives during Q2, and are on track to achieve this for the full year.

Specifically, G&A as reported declined by 1%, but after adjusting for certain current and prior-year anomalies of approximately 6%, total G&A grew by about 5%. Core G&A, which comprises over 80% of the total was roughly flat, whilst innovation G&A increased significantly on an absolute percentage basis. Innovation G&A is comprised mainly of product R&D, digital innovation and certain costs related to Reserve, Roastery and Princi. We remain committed to managing the core growth rate while investing for the near and long term.

For segment operating margins in fiscal 2017, we now expect Americas operating margin to be slightly lower year-over-year, CAP operating margins to show moderate expansion despite the negative impact of FX, EMEA operating margins to approach 15% for the full year and channel development to post strong operating margin improvement, with second half gains moderating from the strong first half performance.

Looking at commodities and FX, our coffee needs for 2017 are almost fully price locked, and we expect commodities will be slightly unfavorable in the back half of the year. We also continue to expect an increased negative net impact from foreign exchange for the year, with revenue growth expected to be negatively impacted by about 1%, and earnings per share negatively impacted by 1 point to 2 points. The impact of FX will accelerate as we move into the last half of 2017. All other targets for fiscal year 2017 will remain the same.

We remain confident in our strategy and the areas of investments that will drive our future financial results in the second half of 2017 and beyond. Our store partners around the globe continue to go above and beyond to deliver the Starbucks experience for our customers every day. And the performance from our two major markets, in particular, U.S. and China, each reflect and justify the increased investments we will make over the near term.

Howard?

Howard S. Schultz
Executive Chairman, Starbucks Corp.
Scott, thank you. Kevin, congratulations on your first call. I think you did really well. And, Belinda, coming from China in the middle of the night, I could not be more proud of you. And the story you told really came through in terms of the success and the bright future we have in China.

My role on today's call and on all calls going forward is obviously different than in years past, with Kevin and the team leading the call. So my role today is really to be the unscripted closer to summarize what's been said, and I thought I'd do that through the lens of trying to put myself in your shoes, and that is the shoes of an investor. What did you hear today? What did I hear and what's my conclusion?

I think there's a short-term issue and a long-term story. The short-term issue is, clearly in the first half of the year, we had compression and headwinds on comps and revenue. And as Scott and Kevin have covered, we feel very confident that we're going to see a significant change in both comps in the mid-single digits and revenue returning to historic levels in the second half of the year.

You also heard from Belinda the success that we're enjoying in China. And unless you've seen it firsthand, you can't imagine the footprint we have in China, the opportunity we have and the growth and development of that market. And as I've said in the past and just having been there two weeks ago, there's no doubt in my mind that China is going to be bigger, stronger and more robust than any market in the world over time, including the U.S.

Over the long term, you have to ask yourself a bigger question. And that is, given the seismic change in consumer behavior and how disruptive online shopping and mobile shopping has been to traditional bricks-and-mortar businesses and companies, who's going to survive and who's going to win? So I think there's two bifurcating questions. One in the short term, one in the long. The short-term question is, in terms of Starbucks U.S. business and comp growth, is the bloom off the rose? Is the glass half empty or half full?

Now, I've been here almost 40 years. I've seen many cyclical changes in our core business. And I can tell you sitting here today, I have never been more confident that the comp growth that we have seen in the first half of the year, over time, beginning in the second half of the year and beyond, will be a distant memory. The pipeline for innovation, both in terms of product development, digital development, mobile development, and if you just look at what happened in the last two weeks, was something that was really probably the most stunning example of our understanding of digital and social media and Instagram, what happened with Unicorn, drove significant traffic, incrementality, awareness, brand affinity. And just stay tuned, because we have a lot more coming.

So in the short term, the bifurcating question for you is, do you believe that U.S. comps are going to return and Starbucks' U.S. business is going to be as robust as it has been in the past? And I can tell you sitting here today, there's no doubt in my mind that the answer to that question is yes.

Over the long term, I can tell you, as I've told you in the years past, that we anticipated and we saw very early on that there was going to be a very, very significant disruptive and almost cataclysmic change in the landscape of physical retailers. The number of store closures, consolidations, we're in the nascent stage of that. And there are going to be many, many losers. And the bifurcating question is, is Starbucks Coffee Company going to be one of the winners? What is it going to take to win? And, Kevin, I think, articulated that very clearly.

One, every retailer that is going to win in this new environment must become an experiential destination. Your products and services for the most part cannot be available online and cannot be available on Amazon. In addition to that, what evidence do we have? Well, we're opening 2,000 stores a year. And here is another year at a time when there's so much pressure in the operating environment and we have another year, another consecutive year, of demonstrating best-of-class new performance in our U.S. stores. To me, personally, that is
better evidence of the health and strength of the brand, unit economics and the relevancy of Starbucks stores in our existing comp number.

In addition to that, you have to believe that in order to win and win big, domestically and globally in this new environment, that a company's capability and competency as a four-wall bricks and mortar retailer must be as good digitally and on mobile in all things that make the brand as relevant outside of the store and on a mobile device as it is inside the four walls of the store. We had a leadership position in our loyalty program in mobile payment, in Mobile Order & Pay, and I can tell you given what is in the pipeline in terms of the investments we're going to make over the long term and our ability to toggle back and forth between the physical and the digital world is only going to make our four wall retail business stronger in the future.

So that the net result and the answer to these questions that I strongly believe, if I was an investor, if I was a shareholder, if I was analyzing Starbucks is, yes, we've had a tough first half of the year. We've got issues with Teavana, but that basically are diminutives when you look at the size and scale of Starbucks revenue and earnings power. We have the largest most important market in the world where we are already the leader with 2,600 stores and one opening up every day and our brand affinity second to none, and that's China. We have a national and global footprint now of over 26,000 stores, 90 million customers a week and still recognized as one of the most respected and recognized brands in the world.

Starbucks Coffee Company is built to last. Starbucks Coffee Company is built to build a great and enduring company. And there's no question in our mind as we sit as a management team and as we address you today on the heels of a tough first half that our best days are in front of us. And for those of you who have covered the company for many, many years, who know me personally, I would not be here banging on the table and telling you how strongly I feel about the growth, development, and what we have in store in terms of the innovation of the company, both inside the four walls of our store, the building of the Reserve brand, the unbelievable experience, the roasteries, what's going to happen in all these cities.

And one thing about the roastery that I should point out is that as strong as the roastery has been in Seattle, 20% comps, being profitable, it's not a city in which we can have the global halo that New York, Shanghai, Tokyo, Milan and Chicago will have when those roasteries open. It's a roastery that basically is catering to mostly local Seattle people and West Coast tourists. Wait till these roasteries open in these other markets. It's going to change the company.

So net-net, those two bifurcating questions is Starbucks U.S. comps half empty or half full? Let me tell you, they're half full, not half empty. On the bifurcating question is Starbucks going to be one of those companies that is going to navigate through the unbelievable challenges that the bricks and mortar physical retailers are going to have, the question is undeniably, yes. We are going to be that company that is going to be the winner.

So with that, that's my unscripted summary of how strongly I feel about the growth and development of the company, the leadership team, Kevin as our new CEO, and I thought again we told a great story today, especially Belinda in the middle of the night from China.

So with that, I'll just turn it back to Kevin or the operator for Q&A.

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Kevin R. Johnson
President and Chief Executive Officer, Starbucks Corp.

Yes, we'll go ahead and open it up for questions, operator. Thank you, Howard.
QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Sara Senatore from Bernstein. Sara, your line is now open.

Sara Harkavy Senatore
Analyst, Sanford C. Bernstein & Co. LLC

Thank you very much. Yes, Scott, I would just like to ask about the earnings algorithm going forward, just in the sense, that at the analyst Investor Day four months or five months ago, there was a reiteration of that long-term growth. This year, obviously now expectation is lower because of investments. Does that mean that if we think about it longer term, that we should sort of rethink that earnings algorithm in terms of I think the double digit revenue growth, 15% to 20% EPS growth?

And I guess on a related question, we’ve seen other companies, maybe use their balance sheet more aggressively. Again is that something that you contemplate doing in terms of just, again, going forward, thinking about the puts and takes, the top line, maybe a step up in just the normalized rate of investments? And then what margin for error your balance sheet offers? Thank you.

Scott Harlan Maw
Executive Vice President and Chief Financial Officer, Starbucks Corp.

Thanks for the question, Sara. I think, the first thing I'll say is we are still reiterating our long-term guidance of 10% on the top line and 15% to 20% on the bottom line. To your point, we understand why the question is being asked and it's being asked a lot more frequently by the street given what's happened in the last two quarters where we haven't quite gotten to the low end of our revenue guidance. But I think as you look at the back half of the year and acceleration back up to 10% revenue growth, we remain confident in that being the fuel for 15% to 20% earnings guidance.

And I think I'd also talk about every year as we set our long-term guidance, we go through our strategic planning process in the spring and we look at all of the drivers on the top line, all the things around innovation for product and digital, all the things we can do in the middle of the P&L to drive sales leverage, and cost of goods sold savings and G&A. We've been increasingly using the balance sheet and I'll come back to that to help a bit with earnings growth as well. And we ask ourselves, can we reiterate those long-term targets? And we're at the beginning of that process.

Again, this spring, we'll go through it with our board over the next few weeks. If in that process we decide that the long-term growth targets have to be adjusted, then we'll come to you, we'll explain it to you, and we'll talk about why we're changing things. But as we sit today, we remain confident give than acceleration that we'll see those long-term goals still come into line.

As it relates to the balance sheet, we have over the last three years taken long-term debt up pretty significantly. I think, we had $750 million a few years ago. We're up close to $4 billion now. And as you know, buybacks have increased pretty significantly over that time as well. And we'll continue to be opportunistic on the balance sheet. I think last second quarter, we bought back over $1 billion in stock. This second quarter, it was over $600 million, it's about a $1 billion in total cash return for the quarter. So we have been selectively adding leverage .We have been taking advantage of opportunities to buy the – buy our stock back and that will continue as we move forward.
Hi. Thank you very much. I'd like to follow-up on the growth rate question, if I may, but dig in a little bit deeper on the Americas. Obviously, the Americas is your biggest segment. At least the calculation that we did around the analyst day, it looked like the Americas needed to grow something like low to mid-teens a year for the next five years to contribute to your overall earnings growth algorithm. And yet in the first half of the year, operating income growth was around 2% with pressure on both the cost of goods sold line and occupancy, as well as operating expenses, in other words labor.

So this – are comps enough, I guess, to change that? I mean, when we go from a 3% comp to a mid-single digit comp. Is that enough to begin to see leverage in that line, or are there perhaps other things that can happen in your business, lapping partner investments, running a more efficient store if that makes sense. Maybe some benefits from lower commodities or lower rents especially as other retailers vacate their properties, that can maybe give some more visibility of margin expansion in the Americas segment than what is currently apparent at this point?

I don't want to underestimate what a couple more points of comp would do for overall profit growth in the U.S. So being up in that high single digit to 10% range in total revenue growth in the U.S., that is a major driver of additional profitability. So, again, as we get into the back half of the year that should start to rectify itself.

The second thing is the partner and digital investments we're making in the U.S. as a percentage of revenue, over the next few years that will start to decline. So we will continue to make investments but the reality is the rate of growth in those investments, the delta, if you will, that will start to come down and we'll be able to lever it as revenue growth increases. So that's not saying that wage investments are going to go down; rather they're going to go up.

But if you look at this year, we went up $250 million for partner and digital investment, and the vast majority of that is in the U.S. That kind of impact on margin is not going to continue after we get out a couple more years. So both of those give us confidence in the growth algorithm. John, would you add anything?

John Winchester Culver
Group President-Starbucks Global Retail, Starbucks Corp.

No. I would just add, John, that also what gives us confidence is the new store performance. And you look at new stores, it contributes over 4% of our top line revenue growth in the Americas. We've consistently done that for 12 consecutive quarters and we anticipate that that's going to continue.

So we're making these partner investments up front, to Scott's point. We feel that those partner investments are the right thing to do and also at the same time, we're starting to see traction as it relates to not only partner
satisfaction and we sequentially improved turnover by two points versus Q1 and also at the same time, our customer service scores sequentially improved from Q1 to Q2 as well. So, I feel very good about the investments that we’ve made and that, in fact, we’re seeing payback from that.

Operator: Your next question comes from the line of John Glass from Morgan Stanley. John, your line is now open.

John Glass  
Analyst, Morgan Stanley & Co. LLC

Thanks very much. You talk a lot about retail environment and that’s presumably the implication it’s a headwind to your sales. But competition doesn’t come up much on Starbucks calls. There is more and better places to get coffee today than there ever has been. And I understand roastery and Reserve is sort of a way of targeting that, but how do you think about the role competition is now playing in your sales trajectory today versus a year ago, let’s say? Is that a contributing factor in your minds? And how would you close on that?

Kevin R. Johnson  
President and Chief Executive Officer, Starbucks Corp.

Yeah, John, this is Kevin. I’ll comment and then I’ll ask Howard to comment on the view on roasteries and at the very high end. Look, we’ve always had competition, and typically, I look in markets where we’ve had a first mover advantage and we establish a presence of a number of stores and the Starbucks brand in those markets, that is a very defensible position.

And if I look at where we’re at in the United States and in China in our major markets, we are not – we not only have established a very defensible position, but we’re expanding that with new store growth. In fact, let me have Matt comment a bit on thoughts on new store growth and how we’re thinking about as we’re building new Starbucks stores in our core brand, how that’s helping us further strengthen that proposition in an environment where there is competition. There’s always been competition. Matt, do you want to comment on that?

Matthew Ryan  
Global Chief Strategy Officer & Executive VP, Starbucks Corp.

Yes, domestically in the U.S., we have to look at this is not one market, but a collection of many markets. And as we look across geographies, we continue to see enormous headroom for store growth across the U.S. Just like we see differentials in store presence international to U.S., we see the same thing within the U.S. That means that there is a lot of opportunity for us to continue to expand in places where our strength has not been as traditionally great as it has been in certain urban and many western markets. So you’re going to continue to see store growth, you know, ramp for us to grow into the future.

Kevin R. Johnson  
President and Chief Executive Officer, Starbucks Corp.

And Howard, do you want to comment on the roasteries?

Howard S. Schultz  
Executive Chairman, Starbucks Corp.

I would say a few things. First of all, there’s no evidence whatsoever that any national company, even those companies that are discounting coffee significantly, with McDonald’s nationally or Dunkin’ Donuts in New England, what Panera is trying to do, there’s no evidence whatsoever that we have, that there is anything that they are
doing that is affecting us adversely. So I just want to get that off the table. The competitive issues question is just a nonevent for us.

I want to talk about the Roastery and Reserve brand, not through the lens of competition, but what you're going to have to do to win in the future. Every retailer is going to have to create an experiential moment, and if you're in the food and beverage business, you have to go to craft. You have to go to art. The interesting thing about the Roastery is, the average ticket to Roastery is $20. The average ticket in a Starbucks store is $5. People in the Roastery are spending significantly more time there than they do in the Starbucks store.

The day-parts in the Roastery are afternoon and evening driven, which as you know is not Starbucks strong suit. The Reserve bars that we have opened are demonstrating enough interest from the customer and customers are trading up, which has given us even more understanding about the opportunity we have to elevate the Reserve brand in existing Starbucks stores.

And when the first Reserve store opens in Chicago, I'm not talking about the roastery now, I'm talking about the Reserve store with Princi food, we'll have another – we'll more evidence about the opportunity we feel to grow those stores in ways that'll be highly complementary and bring a halo to the brand. But the short answer is the competition across the street, or the competition nationally and even those companies that significantly are discounting their coffee is not affecting Starbucks.

Operator: Your next question comes from the line of David Palmer from RBC Capital Markets. David, your line is now open.

David Palmer
Analyst, RBC Capital Markets LLC

Hi, thanks. Your rewards and digital mix of sales is still growing nicely, 400 basis points or 500 basis points or so on a year-over-year basis. Looking at your active rewards membership, it's growing 11%. And that's maybe half the growth it was a little over a year ago. So it looks like that growth or the deceleration in your rewards member growth is correlating with your slowdown in sales. Do you think that that's an important metric? Is rewards member growth a key thing that you're looking at and targeting to reaccelerate in the future? And how are you going to do that? Thanks.

Matthew Ryan
Global Chief Strategy Officer & Executive VP, Starbucks Corp.

Thank you, David. Matt Ryan here. When we look at the rewards program on the digital flywheel, we can’t just focus on any one single metric. We have to look at the totality of its contribution to the business. And we’re at a point right now where in the U.S., the digital flywheel has been the largest single driver of comp growth and we’re very confident that’s going to continue. And I think it’s important to reiterate a couple of things that Kevin said.

We have in fact seen 11% year-on-year growth in membership, but we have also seen record growth and spend per member. And when you take 13-point-some million members and you multiply it by an 8% increase year-on-year, that turns out to be one enormous number, and that’s been a major contribution to our business.

Scott Harlan Maw
Executive Vice President and Chief Financial Officer, Starbucks Corp.

And I would just add that’s the power of personalization that Matt and his team have been driving. So taking that big installed member base and driving additional transactions via personalization. that’s what’s driving that spend,
remember. And, David, if you go back a couple of years ago when we were adding a lot of members, the incremental spend per member was flattish. It might be up 1% or 2%, but this quarter it was up 8%. And so we see an opportunity to accelerate that over time.

Operator: Your next question comes from the line of Sharon Zackfia from William Blair. Sharon, your line is now open.

Sharon Zackfia
Analyst, William Blair & Co. LLC

Hi. Good afternoon. I guess another maybe strategy question. Given the phenomenal response of customers to Mobile Order & Pay, have you rethought that hurdle of having people preload money in order to utilize it?

Kevin R. Johnson
President and Chief Executive Officer, Starbucks Corp.

Matt, do you want to take that?

Matthew Ryan
Global Chief Strategy Officer & Executive VP, Starbucks Corp.

Yeah, Sharon. Matt Ryan here. It is one of the things we will be looking at as we look across the future. But I just want to remind that a theme that we reiterated at the Investor Conference, which is we continue to have a lot of people who join the program as soon as they become familiar with it, and our biggest barrier is familiarity with the program. So continuing to let that word get out there and help people understand what the program is all about is critical.

In addition, we have an easy low-hanging fruit in front of us, which is to get people into the program once they begin the sign-up process. So you’re going to continue to see a lot of improvement to the sign-on process and to the way in which we guide customers to go from where they are today, not being members, into being full members with the store value card loaded. And we see a lot of opportunity there in the short term. And we’ll, of course, be looking at other options like the one you suggested, in the long term.

Operator: Your next question comes from the line of Jeffrey Bernstein from Barclays. Your line is now open.

Jeffrey Bernstein
Analyst, Barclays Capital, Inc.

Great. Thank you very much. Just focusing on the comp topics for the company and I guess specifically for the U.S., it seems like that's the side of things that you guys are extremely confident on, the mid-single digit for the full-year fiscal year 2017. If we focus on just the U.S. for a moment, I mean, do the 3% comp in the fiscal second quarter we know the compare of these what looks like 300 basis points starting in this April through June quarter.

So I'm just wondering, your confidence and then is it accelerating comps confidence beyond just the compares? Because, again, you would think that you would see that uptick just to keep the line steady. I'm just wondering what you characterize as maybe the most impactful new product or platform that you think in the back half is going to lead to a reacceleration in that two-year trend.
And then, Scott, just to clarify. Did you say for the fiscal 2017 earnings that the range you gave was wider and that if you make incremental investments you'll come in at the lower end of the range? Or were you implying that you can make investments that might lead you below the low end of that newly revised range? Thanks.

Scott Harlan Maw  
Executive Vice President and Chief Financial Officer, Starbucks Corp.

So I think I'll have John and Kris talk...

Kevin R. Johnson  
President and Chief Executive Officer, Starbucks Corp.

Let me just frame if first and I'll hand it over to John and Kris on this. Jeffrey, let me give you three things that I think in addition to – well, number one is the sequential acceleration that we saw throughout Q2, that has continued into April.

The second thing is as we look at this quarter, the work the team has done around the Frappuccino launch that was kicked off by the Unicorn Frappuccino and what we've done to really make sure that we've got innovation and line of sight to how we're going to execute in the stores against that. And if you recall, a year ago we had the launch of the transition of the Rewards program at the same time. So we've been laser-focused on how we execute better in store with that.

And then certainly, beyond that, there's been a great focus that Kris has placed on our partners in the stores connecting with customers and ensuring that we're getting that uptick in customer sat, and the work that Adam Brotman has been leading to increase the throughput at peak.

So the increase of throughput at peak, the work that Kris has done in terms of customer connection, the innovation in the Frappuccino and the focus on in-store execution all contribute to the confidence, in addition to the sequential monthly acceleration we've seen in comps.

And so maybe I'll have Kris touch upon a bit of what he's been driving in terms of store partner connection with customers. And Adam can touch a bit maybe on the Mobile Order & Pay. Kris?

Kevin R. Johnson  
President and Chief Executive Officer, Starbucks Corp.

Well, Jeffrey, I think we've got a number of things that we teed up, especially coming into the next two quarters, around operations particularly. And obviously customer connection is the most important thing we do, be it through MOP or cafe customer or whoever it was. But the reason I look to Q3 as a big opportunity is a number of things. First of all, I just think we've just gotten started on MOP service improvements. And we talked about that a good deal last quarter.

The things we put in place I know Adam will share in detail in a minute. But very, very confident that we've got huge opportunity in front of us around improving that service and making sure we get more people through the stores.

I think secondarily, strengthen beverage and food innovation. As I look to Q3, Frappuccino Happy Hour is going to be a huge home run this year. As Kevin mentioned, we acknowledged that we underestimated the interdependence of those two things, the Frappuccino Happy Hour and the launch of the MSR, or the conversion
MSR program last year. But we have got singular focus on Happy Hour this year. We've got this early spark with Unicorn out there that has really ignited, I think, interest in the product, in the platform.

We're going to bring at least one new entirely new drink into Happy Hour this year that is going to be as good as Unicorn or better. And we've extended our hours this year on some other tactical things to really make sure that Happy Hour is set up for success.

I look a little further out and I see some great products we're bringing in the back half of Q3 and into Q4. We've got an entirely new iced tea platform we're bringing into the stores that's going to be a winner. Cold coffee is on fire. Our core espresso platforms around cold coffee are some of our strongest growth we've seen over the last few weeks.

And food. We've talked a lot about food today, but I think the food performance in Q2 is indicative of what we're going to see in Q3 and Q4. Everything from Sous Vide eggs to our core around breakfast sandwiches have been fantastic. We're going to bring a lot of innovation in core food over the next quarter, and I'm very confident that is going to help us lift comps significantly over the next few weeks.

Adam, do you want to talk about MOP?

Adam B. Brotman
Executive Vice President, Global Retail Operations and Partner Digital Engagement, Starbucks Corp.

Yeah, Jeffrey. This is Adam. First of all, in general, we're in the process right now of making real improvements in throughput and capacity in general. So we've got good momentum there, specifically as it relates to Mobile Order & Pay, as Kevin mentioned in his remarks. The first wave of new operational actions we've already taken in this regard have landed well in the field.

We're feeling really good about the results we've already seen, both in terms of improved throughput at peak, as we've mentioned, but as well as the customer experience in those stores around MOP in general for both Rewards customers and non-Rewards customers. We saw increased peak transactions in our busiest MOP stores. We saw the greatest improvement in customer experience scores for the quarter in the latest quarter in those busiest MOP stores, and that continues into April.

And we're also really pleased with how we've been able to deploy partner labor against these throughput improvements, particularly in these busiest Mobile Order & Pay stores. It's a really important part of how I think we're getting smarter in terms of shifting or reallocating labor to the morning peak opportunities occasionally, and selectively investing in labor where it makes sense to do so and where we feel good about that.

So net-net, we're really happy with the early momentum we have in terms of operational improvements around getting better at MOP experiences and just in general driving our business in this area.

Scott Harlan Maw
Executive Vice President and Chief Financial Officer, Starbucks Corp.

And I'll wrap up your question, Jeffrey. So, no, we're not indicating risk below the low end of the range. But I do want to acknowledge that if we see opportunities for investment or if the Teavana mall stores perform a little worse than we have forecast, that lower end is entirely in play.

Operator: Your next question comes from the line of David Tarantino from Baird. David, your line is now open.
Hi. Good afternoon. Scott, just on the guidance for this year, could you give a little bit of perspective on how much of the change was related to Teavana and how much of it was related to the investments you're making? And then I guess the second question related to that, assuming that the investments is a big part of this is why make that decision now? I mean, Starbucks has such a long history of delivering on their financial targets. I think the last time you lowered guidance was during the recession. So why now are you pulling forward investments and lowering the targets?

On the first part of your question, the larger piece is the investments we're making, although the Teavana mall store performance versus what we thought is meaningful. And to the second part of your question, David, I take the spirit of what it's asked. We see a significant opportunity in areas like digital and specifically what we see with returns on investments that we make around personalization, around things around Starbucks Rewards, things that we do in the app to make things easier for our customers. Those investments have the shortest payback and the highest returns of anything we do in Starbucks including new stores.

And so as we look at the back half of the year and we look at the fact that we're driving the majority of our comps from digital, I would argue we must make those investments because those will pay off both as we exit 2017 and as we head into 2018, and I think, it would be not the right thing to do to skip those. So the second thing I would say is on Reserve and Roastery, those have longer term implications for us as Howard talked about, So making those investments now as we build the Princi capabilities.

A lot of these capabilities are in the early phases, building out. The commissary capability for Princi Kitchens is building out. The roasteries that we have under construction across the globe and opening our first Reserve store soon, all of those things, needs the right level of design, the right level of merchandising, and it costs money to get those things setup right. The good news is as we move into 2018 and beyond, we'll start to leverage those investments as we begin to open more and more Reserve stores, open the roasteries, and we think that's the right thing to do.

And I think this just reinforces the fact that we're playing the long game. And in this period where this dramatic disruption is taking place in the retail industry, we are very clear that the transformative elements that we're focused on are digital, mobile relationships with our customers and branded, experiential retail. And the investments we're putting in are in those areas. It's about elevating the digital flywheel and it's about elevating the brand with the investment we're making in roasteries and Reserve stores and Princi. It's all about the future.
guys have been talking about that since kind of last fall. Can you maybe give us an update on how you think that's working and maybe what's left to do there?

Scott Harlan Maw  
Executive Vice President and Chief Financial Officer, Starbucks Corp.

So yes, mid-single digit comps globally for the full year, and I'll turn it to Matt for the second part of the question.

Matthew Ryan  
Global Chief Strategy Officer & Executive VP, Starbucks Corp.

Thank you for the question. We are very excited about personalization. And I would just reiterate what we've been saying and it remains absolutely true. We have only just begun. Right now, personalization, we did extend from email to the app about two quarters ago.

We are seeing terrific results. It is the single biggest driver that we're seeing of the improved spend per member, and we just told you what that meant for us. So it's a big deal. We haven't done a lot of the things we dream about doing and one of the reasons why we continue to invest in technology is to be able to do those things.

Triggered responses to events, triggered responses to external data that we can use, continuing to put personalization elsewhere throughout the app, and then eventually extending personalization to other screens beyond the app as well. These are all on the roadmap and will be coming and we believe they'll drive significant value for the company. So we're very, very optimistic and bullish on it.

Scott Harlan Maw  
Executive Vice President and Chief Financial Officer, Starbucks Corp.

Maybe just one proof point to add to what Matt said. As you know, we launched this quarter suggested selling across the platform within the app. So as you're ordering your beverage, we're able to show pictures of food and other things you've either ordered in the past, or would go well with items in your basket. And we saw this quarter the ticket on Mobile Order & Pay actually go higher than the average ticket on Starbucks Rewards orders that weren't through Mobile Order & Pay. That wasn't the case over the last year. So for the first quarter we've seen that tick above as we thought it would when we launched personalization. And that's a good sign.

Matthew Ryan  
Global Chief Strategy Officer & Executive VP, Starbucks Corp.

And just to add, we have also seen acceleration through the quarter with regard to personalization. So as we entered the quarter, and as we exited, we saw personalization as one of those things we think is going to continue to drive comps up in the second half of the year.

Kevin R. Johnson  
President and Chief Executive Officer, Starbucks Corp.

And we saw higher attach on food in particular.

Matthew Ryan  
Global Chief Strategy Officer & Executive VP, Starbucks Corp.

That's right.
Kevin R. Johnson
President and Chief Executive Officer, Starbucks Corp.

Which is the highest since we launched La Boulange three years ago. So clearly personalization is playing a role in that success.

Operator: The last question comes from the line of Karen Holthouse from Goldman Sachs. Karen, your line is now open.

Karen Holthouse
Analyst, Goldman Sachs & Co.

Hey, another question on the sort of U.S. comp commentary. So stores that had those peak Mobile Order & Pay stores which were in 20% of transactions, you noted sequential improvement, but are we actually back to a point that those are positive year-over-year in traffic? And then when you're thinking about the improving into April, how much of that just relates to the disruption that we're lapping last year around Mobile Order & Pay or is that true on a two-year basis as well? Thanks.

Scott Harlan Maw
Executive Vice President and Chief Financial Officer, Starbucks Corp.

So, Karen, those highest volume stores were slightly negative last quarter from a transaction standpoint, and they're still slightly negative. But that – but it's improved significantly quarter to quarter.

Kevin R. Johnson
President and Chief Executive Officer, Starbucks Corp.

It [ph] was pre-adjusted. (1:19:37)

Scott Harlan Maw
Executive Vice President and Chief Financial Officer, Starbucks Corp.

Yeah. So we're seeing improvement, but still a little bit of negative transaction there.

Howard S. Schultz
Executive Chairman, Starbucks Corp.

Can I just clarify one condition myself? I want to make sure there's clarity and common language, because I think the question was also is comp improvement based primarily on low comparisons. The answer is no, right?

Scott Harlan Maw
Executive Vice President and Chief Financial Officer, Starbucks Corp.

So in both March and April we still had pretty big comparisons to lap over, so we're pretty happy with the overall comp growth and particularly transaction growth in April.

Howard S. Schultz
Executive Chairman, Starbucks Corp.

Yeah.

Kevin R. Johnson
President and Chief Executive Officer, Starbucks Corp.
And I think our comp – well, our comp performance for the back half is based on the level of innovation that we’re bringing in from a product standpoint, performance at happy hour as well as continued expansion of the digital flywheel.

Scott Harlan Maw  
Executive Vice President and Chief Financial Officer, Starbucks Corp.

Okay.

Kevin R. Johnson  
President and Chief Executive Officer, Starbucks Corp.

Great. Thank you, Karen. Thank you everybody. Tom?

Tom Shaw  
Vice President, Investor Relations, Starbucks Corp.

Yeah, thanks again for joining us today. And we look forward to speaking with you again on our third quarter earnings call, which we have tentatively scheduled for Thursday, July 27. Thanks again.

Operator: This concludes Starbucks Coffee Company's second quarter fiscal year 2017 earnings conference call. You may now disconnect.