Barclays Americas Select Franchise Conference

Company Participants

- Troy Alstead, CFO, Chief Administrative Officer

Other Participants

- Jeff Bernstein, Analyst, Barclays Capital
- Unidentified Participant, Analyst, Unknown

Presentation

Jeff Bernstein {BIO 7208345 <GO>}

Good morning, everyone. Thank you, all for joining us this morning. And I should say good evening to those in the States who are about to go to bed. Thank you for joining us for day two of our Americas Select Conference here at Barclays.

My name is Jeff Bernstein. I am the restaurant analyst from Barclays, based out of New York. I have the pleasure of kicking things off this morning, introducing our next presenting company at the conference, Starbucks Corporation.

For those not familiar, if that's possible, they are what we believe is one of the leading global growth stories across not just restaurants but broader retail, with an industry-leading US retail coffee platform and significant international growth opportunities, led by China as one of the many forces outside of the US. And then a developing consumer products segment which management believes will one day rival the worldwide retail platform. So a pretty large opportunity from a consumer product standpoint.

With that said, joining us today to share details on the story we have Troy Alstead, who is the CFO and CAO; and JoAnn DeGrande, who is the Director of Investor Relations. Troy will kick it off with some prepared remarks, background on the story; and towards the end, if there is any extra time, we will open it up for Q&A. So hopefully people will join us for that component.

But with that said, it is our pleasure to introduce Starbucks and Troy Alstead.

Troy Alstead {BIO 5724238 <GO>}

Thank you, Jeff. Thanks for joining me at this early hour, everyone. I appreciate the chance to be here with you.

I will spend some time with some prepared remarks. And then as Jeff mentioned I look forward to taking whatever questions you might have at that point in time. Jeff introduced JoAnn DeGrande; also she is here to help with any questions. She is our Vice President of Investor Relations and will help.

Now by way of just brief background for those of you who I don't know, I've been with Starbucks for more than 20 years now. I joined the Company when it was a privately held, small coffee company in Seattle, Washington. The big aspiration of the Company at that point in time was to consider opening coffee shops as far away as California, which at that point in time that seemed like a long stretch in the Company. There was a lot of skeptics about whether the concept would work in a warm weather environment. So we have clearly come a long way in that span of time.

Over my 20 years with the Company I have been in the finance function really all over the world. And then on a few occasions have stepped out of finance into general management roles. Many years, ago on an interim basis I ran our EMEA operations headquartered out of Amsterdam; had Latin America reporting to me; I have run Japan at different times; and I have been the Chief Operating Officer of our business in China for a period of time. So I have had the opportunity over that span of time, in addition to my finance roles, to really understand the business at quite some depth; and I'm looking forward to spending some time providing an overview of that for you, for those of you a little less familiar with the story.

We have, over the 40 years of the Company of Starbucks, over our history have built a portfolio of brands and recently have added into that portfolio of brands. But I would point out that our -- the activities of the Company, the brands. And even some of the recent acquisitions we have done and the many initiatives that we have going on in the Company are all very closely focused around the core of the coffee and tea experience. The heritage of the Company is in coffee and tea. And all of our activities really circle very closely around coffee and tea and the experiences associated with the coffee house.

We are in 62 countries now globally. We have almost 19,000 stores around the world.

And what is important and increasingly an important part of the Company's strategy beyond the expansion of our store base, which is the original roots of the Company, is an increasing presence in Channel Development. Channel Development is the part of our business that really includes everything outside of the Starbucks store -- foodservice, CPG, vending in places, anything that happens outside of that core Starbucks store experience is in our Channel Development business. We will come back to that shortly. But it is a key, critical strategy as we continue to grow around the world.

The roots of the Company are in the coffee shop, the Starbucks store. It really is that store that has allowed us over time to introduce customers to our products, to the experiences of Starbucks, to provide that daily habit and ritual. The store is a key driver of revenue and profitability and great capital returns in the Company.

The stores also play a critical role in creating a platform to introduce our products to customers. What we have learned over time, as we have grown from being more than just that Starbucks store around the world to really being a global consumer brand in a category -- coffee and tea -- that people interact with in so many places in their lives -- in a coffee shop, in your home in the morning, at a hotel, in the office, on your way to work, at a restaurant. The core products offerings that we have are such an integral part of people's lives that the store gives us the chance to introduce what Starbucks is about to the customer and then leverage that outside of the store into other channels. Down the grocery aisle, in restaurants, on airplanes, anywhere and everywhere someone may want to look for a cup of coffee we have a chance, increasingly over time, to be a part of that experience.

The store also provides the opportunity to provide that engagement. Increasingly we are leveraging and deepening that customer interaction with the barista into the digital channels. We will come back to that shortly; but our loyalty, our digital presence, social media, all have allowed us to really fuel and expand our relationship with the customer very powerfully and very effectively for us.

The history of the Company is deeply rooted in ethical sourcing of our coffee, in our community involvement. By definition a coffee shop -- anybody's. But certainly Starbucks -- is a part of communities. It is a part of neighborhoods.

What has happened organically over our long 40-year history is that our stores have often become that launching pad for our store partners -- that is what we call our employees, our partners in our Company -- to be deeply engaged in our communities. As a Company we have a target of having 1 million hours, 1 million service hours into our local communities by 2015. And we are well on a path to that level of community involvement and volunteer activity in our communities that ranges from all kinds of areas of cleaning up parks to working with food banks, working with shelters around the world in whatever communities we operate.

Our coffee. And the quality of our coffee. And our engagement with the farming communities has also always been critically important to us. We have had long-standing relationships with organizations such as Conservation International, such as Fair Trade and many others, all around ensuring high-quality coffee. And the sustainability of coffee. And the health and sustainability and responsibility that we hold to our farming communities around the world. It is a part of our responsibility we take very seriously and are extremely active in around the world.

And environmental sustainability has always been a core pillar and platform of the Company. As an example, all new Starbucks stores that are built are LEED certified, one of many areas where we believe we can have a critical impact as we continue to grow from here.

Now, in addition to that deep commitment to our communities and to our growing regions around the world, we are also deeply committed to providing healthy and growing financial returns to our shareholders and through really a balanced combination of driving top-line growth and delivering margin expansion and earnings growth faster than driving the top-line.

We have had a sustainable target, as many of you know, of driving revenue growth greater than 10%. We've delivered against that for a number of years and expect to deliver against that 10%-plus revenue growth again this current fiscal year and at the same time driving improvements in margins. We expect about 100 basis points of operating margin expansion in the current fiscal year.

That combination of the strong growth in the top-line and margin expansion has allowed us to consistently deliver earnings growth in the 15% to 20% range, which has been our long-term target and where we have sustainably and consistently for a number of years delivered. Our earnings per share target for the current fiscal year -- and our fiscal year ends at the end of September -- is in a range of $2.12 to $2.18. Compared to last year's $1.79, that is growth of 18% 22% EPS growth. So very much at the top end of our target range is where we expect to deliver earnings growth in this current fiscal year.

Now let me walk you through each of our four operating units around the world briefly and give you some highlights from each of them. Starting with the Americas, clearly our largest business unit we have, the core of which is our US business. This region is the engine of growth and profitability in the Company.

It is still dominates our overall revenue mix in the Company. It is an almost $10 billion business a year ago; and in this current fiscal year the Americas will be well over a $10 billion business for us. High profit.

And as large as the Americas is and as large as the US business is for us, we continue to drive revenue growth through both new store additions, profitable, steady, sustainable growth of new stores across the US in this whole region. And increasing focus on driving same-store sales. We will come back to volumes per store here shortly. But average unit volumes in the US today are at an all-time high of $1.2 million per store per year.

And that is growing while we are also elevating margin through revenue growth. But also through heavy focus on the efficiency of our operations, through applying Lean principles within our stores. Labor deployment, waste management, all the many activities that as we continue to grow we continue to seek out a multitude of initiatives that allow us to deliver a very mature business into increasing levels of profitability.

Beyond just the core US business, which is a big, dominant part of this Americas region, we have been in Canada for a long time. We have about 1,000 stores in Canada and are increasingly recognizing that we have a much bigger opportunity in

Canada than we perhaps have exploited even over the last five to 10 years. So with new management in Canada over the past year, we really re-architecting and developing our growth plans for that part of the Americas region and believe we have a tremendous opportunity for additional store growth, revenue growth. And increased profitability out of Canada.

Then, Latin America for us is newer. But high growth, high margin. It is a part of the world we are very excited about.

Today, the biggest part of Latin America for us is Mexico, which we operate through a fully licensed partnership, very profitable and a good healthy marketplace for us. Then newer, an opportunity such as Brazil, where we have perhaps only 50 stores today but see the opportunity over time to grow with great economics a very large business in Brazil and through the rest of Latin America.

Europe, Middle East. And Africa has been a much tougher part of the world for us. The biggest part of that world is here in the UK. Much of our challenges in this part of the world, frankly, are of our own doing. That dates back many, many years ago, where we had a flawed strategy and chased some real estate and made some decisions that we should not have made here.

The focus of the past two years with the team here in the UK and in our European headquarters has been to really restructure and reposition our business in Europe. That restructuring has included closing stores that were unprofitable, that frankly we should not have opened in the first place many years ago. It has included relicensing parts of the region.

For example, Ireland used to be a Company-operated market for Starbucks. We were never able to make money in Ireland. It is not large enough for us to be able to deploy our capital and our infrastructure into driving that marketplace forward.

A year ago we sold that to a licensee. And now it is profitable for them and it is profitable for us. It is a reflection of our strategy of being much more thoughtful about where we deploy Company-owned capital to get the returns we need and be effective and be able to leverage our infrastructure in the right and appropriate ways.

Even within the UK we have done some licensing of some stores in some venues where it is more sensible to let somebody else who is far more capable to operate in that location, operate in that location. Not unlike the strategy we have applied historically to the US, for example. But have not approached it quite right here over the years.

So we are in the process of working our way through that. We have done a great deal of cost restructuring both in the G&A organization here in the UK and in Europe, in our supply chain. We historically had a very unwieldy, high-cost, ineffective distribution system in the UK. We spent about a year and a half, almost two years turning that upside down and re-initiating that in a consolidated distribution model, which is already much more effective. And by itself we expect to add about 200 basis points to gross margin over the next two years.

Then beyond the cost work, significant consumer-facing initiatives, really learning from the success we've had in the US, dating back to 2008 and 2009, when we really drove a significant improvement in our US business. We focused on things like customer satisfaction in stores, cleanliness of stores, how the customers measure our service levels.

We have remodeled stores, freshened up stores; we have more of those to do. We have begun to introduce our loyalty program into the UK and into some markets on the Continent. All of these initiatives are newer here than in the US. But we are optimistic that each of them over time will be able to help us move this region in the right direction.

With all that said, we are beginning to see the early signs of improvement here. We have a long ways to go. We think it will be several years of progression forward.

But I would anticipate every year, including 2013 and then each year forward, for us to improve margin slowly into the double digits here in Europe, with an ultimate target somewhere in the mid to upper teens. Now, we have confidence in that path even though it will take some time, because we have pockets of our business here in the UK and pockets -- countries around Europe that are equally high cost structure that are already operating at that kind of margin level.

We know we have a model that can work effectively. We just have to reposition the business to get to that place.

I would contrast that with China/Asia Pacific, which is our fastest-growing geographic region anywhere in the world and also the highest-margin geographic region we have anywhere in the world, with margins sustainably above 30% and, with the growth we are driving all across the region but really dominated by China, driving revenue growth of greater than 20% fairly consistently.

Our oldest market and our largest market today in this region is Japan, which is a highly profitable, fairly stable, moderately growing. And sustainably steadily growing business for us both in terms of store count but also the other channels outside of the Starbucks store.

Rapidly growing in China, which before long will become our second-largest market anywhere in the world. Very powerful unit economics. And we have got a long runway we believe for very profitable, high capital-returning growth to navigate in China. All the way to some of our newer markets such as India, which we just opened a few months back. And Vietnam, which we just opened a month or two ago. Tremendous growth opportunities and a very healthy economic model across this region that we are very excited about.

Now, the core of all of those geographies, before I move outside of the Starbucks store, are the economics of the store. We will open about 1,300 new stores globally this year, split relatively evenly between the Americas and China/Asia Pacific, with very few stores in Europe. Our European growth will be predominantly licensed as we go forward.

Globally about half of our stores, roughly, are Company-operated and the other half are licensed. I would anticipate over time that split of ownership, while it will vary moderately based on region and geography and venue to remain reasonably in that 50-50 split as we go forward.

Now for most of our history, the Starbucks store was really what defined our Company. It was the early parts of the business, long before we really realized there was much of an opportunity.

And for most of our history our aspiration really was around that Starbucks store. It was about being a premium operator of coffee shops all around the world.

In our history usually when we spoke about what the opportunity was at some point in time, it was always centered around how many stores we might have. What has happened to us over time is that the customer has pulled us out of the door into other parts of their life. And that has opened up for us opportunities to drive consumption at home, to look for opportunities where people consume coffee anywhere. And that has led to our opportunity to take our various products and categories, leverage them into other form factors. And pursue increasing market share outside of the Starbucks store.

All of that activity is what falls into our Channel Development business. Channel Development is a relatively newer strategy for us. We have been in some of the CPG channels for a number of years. But really only in the last three to four years have we begun to concentrate on developing a deep capability in this space and a real strategic direction to at some point in time drive Channel Development, our business, outside of the store closer to the size ultimately we think of what our store business can represent for us over the very long term.

It is a high-margin business for us, margins in the mid 20%s now. Will add about 100 to 150 basis points of margin improvement this year, largely aided by commodity costs which have been easing and progress this margin structurally, we believe, closer to the upper 20%s and at some point in time, in the not too distant future, up closer to 30%.

It is the business that is predominantly driving things like at-home consumption with singleserve, our large and more mature package coffee business. And also large and mature food service business. Most of these numbers today are concentrated in the Americas and largely concentrated in the US.

Over time. And it is beginning now, the real opportunity is to begin to mature these channels aggressively into other regions around the world. Our strategy generally is to build out the brand and the consumer awareness, the whole proposition of Starbucks, using the Starbucks store first; and then once we reach some tipping point in that brand awareness and that understanding of what Starbucks is all about, then we began to stretch and leverage that into the channels outside of the Starbucks store.

For example, we have been in China for 13 or 14 years now, since the late '90s. We are just getting closer to the point where we believe that marketplace is ready for us to really begin to pursue product launches and opportunities outside of the Starbucks store, using things such as our ready-to-drink beverages, as an example.

Now historically, most of our growth has been organic; and I would fully anticipate that we will always be a predominantly organically growing Company. But we have recently added in some tuck-ins, relatively small acquisitions, which are really about leveraging some opportunities much more meaningfully than we felt we could really achieve organically.

One example of that is La Boulange. It is a small acquisition that we did in San Francisco which deepens our capabilities around food. Food is approximately 19% of the sales mix of a Starbucks store globally -- it is also about 19% in the US -- with a range of low teens in some markets to upper 20%s, even north of 30% share of that store sales in some markets around the world.

With that said, food has always been the category where we have disappointed our customers the most and where we've had the most opportunity to drive more volumes, both as an attachment to an existing transaction and also ultimately, as we convince the customers that we have a more appealing food program, we believe food can be a more meaningful traffic driver for us.

Particularly in the US around those afternoon dayparts, we know that food is a more meaningful decision factor for a customer in the afternoon, which is a slower time of our business in the US, than it is in the morning. A tremendous opportunity for us to innovate and elevate that food program. La Boulange, in the very early days of our testing, is elevating that both in terms of how customers rate our food program but also how much they are buying and that's -- we are seeing some very early signs here.

All the way to tea on the other side, which we believe can be a meaningful contributor to incremental growth in the years ahead. The original name of Starbucks was Starbucks Coffee, Tea and Spices; tea has been in the core of our business for more than 40 years.

It is the second most-consumed beverage in the world, only second to water. And yet in Starbucks it is tiny, low single-digit share of our overall sales. It has never been a focus of ours and nor have we ever put the kind of energy against it or had the capabilities in tea that we have historically provided within coffee.

We are excited about the acquisition of Teavana, which allows us both to roll out a contemporary teahouse, first in the US then more meaningfully around the world ultimately. But then also then to bring those capabilities around tea back into the Starbucks store, to really use tea as a complementary beverage to that experience within Starbucks, with innovation around beverages, daypart kinds of innovations, food pairings, in ways that we have never approached historically.

That is all beginning now. And over the next one and two and three years we would anticipate tea being an incremental driver of revenue and profitability in the Company.

The umbrella over all of that for us has been a very powerful movement into all things digital. That ranges everywhere from some paid digital advertising to the mobile app, which is the fastest-growing mobile app for payments in the US, all the way to the Starbucks Card, which has been around for more than 10 years in our business as a transaction tool but more recently has become the tool by which our loyalty program sits on top of.

About a third of our transactions of a $13 billion revenue company are prepaid by virtue of the Starbucks Card in either the physical card format or the mobile app. And that is increasingly giving us not only a connection and engagement to the customer but also a sustainability, a stickiness to that transaction that we believe has allowed us to have more stability in what has been, particularly in the US, a bit of a choppy environment. Evidenced I think -- some others in the space out there, ours has been a much more stable kind of revenue and comp growth, driven by many things but we also believe heavily contributed by our loyalty program and the fact that people have the money loaded on their card. They're much less likely to pass by a Starbucks store if they are pre-loaded with the money on the card.

Social media, unpaid for us, has been a very authentic way for us to reach our customers. Starbucks has never been a big advertising company. But social media and people's ability to really engage with their friends around their experiences at Starbucks allows us to reach them in a very authentic, more genuine way that resonates with our demographic very powerfully.

Now we have the fortune of having a business that is very high cash flow on a routine basis. That has allowed us with cash from operations to fund all the appropriate investments back into the business -- new stores, renovations, investments in manufacturing. And systems and technology over time. And it has also allowed us increasingly to then return cash to shareholders.

We initiated a dividend about three years ago. We are committed to growing the dividend, both as earnings grow and also the payout ratio. We pay out today at about between a 35% to 40% target ratio. I would fully anticipate over time elevating that; we believe we have a cash flow that enables us to pay out a higher ratio than that.

We have been a moderate repurchaser of shares. I would expect us to continue to be a moderate repurchaser of shares as time progresses.

Our targets, as I hit a few of them earlier, for fiscal '13 are very consistent with our long-term targets. In all the investments we have made and that I have described in our business into those next layers of growth drivers in food, in tea, the loyalty program, what we can do with mobile payments -- all of that together, we believe, gives us the ability to be confident in driving 10% or greater revenue growth sustainably for about as far forward in our planning as we can see, driven by comp store sales in that mid single digit range both in the US, our biggest market. And also globally. Then through the margin expansion driving earnings growth consistently in that 15% to 20% range, again, with this current year being closer to the top end of that range is what we expect.

Then we are heavily focused on return on capital as a Company. We have progressed return on capital into the low 20%s and on a pace of improving ROIC every year to reach above 25% here within the next couple years. And we will sustainably -- believe we have an opportunity to sustain that and grow that further.

With that, I will pause in my prepared remarks and, Jeff, would love to just open up to whatever questions we might have.

Questions And Answers

Q - Jeff Bernstein {BIO 7208345 <GO>}

Great. Thank you, Troy. I would love to open up to any questions in the room, otherwise I have a few of my own. But I would rather hear yours.

Q - Unidentified Participant

(inaudible; microphone inaccessible)

A - Troy Alstead {BIO 5724238 <GO>}

Food, as I mentioned earlier, today is about 19% of the sales mix of the Company, almost 20%. So it is a greater than $2 billion category for us today.

With that we have a range, as I mentioned, around the world. Even if I just look at Starbucks stores, if I use that as the benchmark, from low teens in some places to markets that are performing better on their food execution of 25% to 30% or higher.

So we believe we have an opportunity over time to progress that 19% at least 10 points higher into the upper 20%s somewhere. And that is not an explicit target as much as we believe that is the opportunity of what we can do with food.

We come at that both from what we have seen in selected markets around the world and also what we hear from our customers. Today in the US, for example -- and this is reasonably true globally. But if I just focus on the US for a moment -- two-thirds of our transactions don't have any food item on them. So one third of the people who buy a beverage also attach some food item to it; two-thirds of the transactions in our stores have no food on them.

And of those two-thirds, when we spend a lot of time understanding that customer, those people -- we have already acquired them, they are walking in the door, their wallet is open, they want to give us money, they want to be in Starbucks. And yet -- and many of them want food. But they historically have not bought our food for one of two reasons. It either hasn't me their quality expectations -- we are working heavy to address that -- or it hasn't been appropriate to the daypart, to wherever they're at.

Our food program historically was mostly morning, bakery kinds of items. We have in the last few years heavily innovated against the midday daypart, in the US, for example. Heavily innovated against food that is more appropriate for that snack occasion in the afternoon.

What we are finding is, as we give people things that are of higher quality and matches the occasion, fits the time of day, matches the beverage pairing that they have, that they buy more food. Perhaps not a surprise.

So that leads us also to believe that we have got a tremendous opportunity to grow food faster in the years ahead than we do our core business. So I believe that our business can grow, again, from about 19% of sales mix to the upper 20%s over time, given the kind of pathway we can see. And that is while we are still growing the overall business. So that will be a fairly rapid growth in the overall size of food during that period of time.

Q - Unidentified Participant

Could you please just give us an update on the economics of the newly opened stores in China and the strength of the Chinese consumer you are seeing right now?

A - Troy Alstead {BIO 5724238 <GO>}

Yes. Our stores in China are approximately annual unit volumes of about $800,000; I benchmark it into dollars. Now by the way, that is about twice the volumes that they were just a handful of years ago. Our volumes in China have been growing quite rapidly both as we have opened up new stores at higher volumes, as the awareness of the brand has grown. And also by very powerful, strong comp growth in those stores over the last few years.

So AUVs today of about $800,000 in China. Store profitability, four-wall profitability in the mid to upper 20s. So a few points higher than our benchmark gold standard US business in terms of store economics.

Sales-to-investment ratio, that is a key ratio that we measure quite frequently. The first-year sales of a new store compared to the cost to build it, the capital cost of that store, that is 2-to-1 or a little bit greater than that in the US. It is about close to 3-to-1 in most of our new stores in China. So very good, healthy unit economics as we continue to grow in that marketplace.

I would also point out that as we have historically, as many others did, opened up in the Tier 1 cities in China, in the last handful of years we have begun to expand more meaningfully in the Tier 2 and Tier 3 and are seeing very comparable economics in those cities as we do in the Tier 1 cities.

We have about 850 stores I think today on Mainland China. We have targeted 1,500 stores by 2015. We're well on our pace to get to that benchmark.

And that is just a waypoint. We actually are quite confident we have thousands of stores of opportunity in China. So very good healthy economics.

Now, the Chinese consumer. I think there is no question that the rapid pace of that Chinese consumer has slowed a bit. Everyone else has seen it.

To be honest with you, I think Starbucks was a bit insulated from that for the last couple years. We know our friends at Yum! and others were experiencing that a little bit more quickly than we were. I would suggest by virtue of us being a bit smaller in that marketplace and a premium or aspirational brand that was just growing in China, that we were perhaps a little insulated from that impact.

But in the last quarter or two, we think around the edges we are seeing just a little bit of a slowing in the trajectory of growth. We still have very strong same-store sales growth in China. Our new stores are still opening up with the great economics. But you can see the consumer has just slowed up a little bit. And I think that is -- we're watching it very closely. But that is what it looks like to us.

Q - Unidentified Participant

Can you talk a bit about changing consumer coffee consumption patterns and how that is affecting you? Obviously, Nespresso has been very successful in Europe. I mean I will be honest, I was and still am a Starbucks customer. We have got an espresso machine in the office; I use that more than going out. How do you see that sort of consumption pattern unfold in the years ahead?

And following up on China, China is obviously not a coffee-drinking nation. Consumption per capita is significantly lower. If I look at players like Nestle with very strong coffee franchises, they have actually tried to localize content quite significantly in China. So how do you see that unfolding as well?

A - Troy Alstead {BIO 5724238 <GO>}

Yes, let me speak to the last part first if I can. China, when we first entered China 15 years ago, had -- the contemporary coffeehouse that Starbucks represents and Costa here and others really didn't exist in any kind of meaningful way, shape, or form, other than a few probably independent little startups and copycats here and there. As we have grown rapidly, as others have grown rapidly in China, there is a dramatic change in -- (quickly) that younger generation adopting coffee as a beverage and adopting the whole coffeehouse lifestyle quite dramatically.

So coffee consumption per capita is tiny; but in the bigger cities and particularly among the younger generation, that aspirational generation in China, it is actually growing rapidly. Again we are certainly a part of that and many others are in China today.

Interestingly, when people first started in China to experience the Starbucks brand years ago, it wasn't so much coming in because of the coffee; it was coming in because of the experience, or what they may have seen in their travels. And what they may have seen in movie is that they would see Starbucks or something similar. That is often what brings people in. And the social aspect of what a coffee house is all about.

Then the coffee habit and the innovative beverages we can provide to them become something that develops later on. And that is how we have seen that in our several years now in China. That is how we have seen that progress and continuing to grow.

Now, there is two -- to the coffee market and consumption overall there is two very large, very significant changing consumer patterns happening. One has been a 20-year change from lower-end coffee to super-premium coffee, heavily in the US but really around the world, driven by many coffee players. Certainly Nestle and Starbucks and Costa here and many others have pulled people from what used to be in many markets around the world -- and I would just say particularly in the US -- really low-quality, poor coffee to something better, usually defined by premium arabica coffees. That has been one change. And that trend continues.

The newer change, of course, is to all things singleserve. That is more advanced in many markets in Europe.

It has been a relatively newer change in overall consumption in the US of course, where people have been rapidly shifting, I think in all parts of their life. It is much more than coffee. It is about this move into convenience and simplicity and speed that has led people to change their consumption from brewing 10 and 12 cups at a time to wanting the convenience of singleserve.

Keurig in the US has done a fantastic job getting their low-pressure brewed machines placed in people's homes. Nespresso in Europe has driven the more high-pressure espresso-based singleserve. But all that dynamic is, we believe, a freight train that will continue to roll.

The US moved from probably 0% consumption in singleserve five or six or eight years ago to 25% and rapidly growing now of consumption in singleserve. And we anticipate there is no reason that the US marketplace over a handful of years ahead of us can't progress to singleserve consumption like Germany, or like some many other markets in Europe that is more advanced.

We would fully anticipate that trend to continue. That has more strategic implications on Starbucks than others, where we are navigating and balancing a very big, mature, highly profitable packaged coffee business with continued leadership in the singleserve, where we can be a part of other people's equipment platforms.

I will point out one element of our strategy which is Starbucks has no intent to be an equipment company. We strongly believe our equities, our capabilities, what we can really do is around coffee. The brand of our coffee, the innovation of the coffee, the variety of coffee, choices you can provide to people. And tea. And other forms of singleserve.

Our interest is to partner with others who have the equipment platforms, which leads us to our Verismo partnership with Krueger; which leads us to our Keurig partnership, with Green Mountain. And over time we will explore more of these as those opportunities develop around the world.

Q - Unidentified Participant

(inaudible; microphone inaccessible)

A - Troy Alstead {BIO 5724238 <GO>}

On the store?

Q - Unidentified Participant

Yes.

A - Troy Alstead {BIO 5724238 <GO>}

We have never seen any impact between at-home consumption and store consumption. Both in terms of all the transactional data and what consumers say. They tend to be -- other than probably some movement around the edges, it tends to be very distinct consumption habits for people.

So people don't trade -- particularly the American consumer, they don't trade their at-home consumption even as it gets higher quality and more convenient with that store experience. What we have found that is very encouraging is, with the advent of singleserve, people consume more coffee. As it is easier to drink coffee, they drink more coffee.

We don't know how far that continues, by the way. But that has been an interesting trend and a very valuable one for us in the last handful of years.

As much as we love our historical higher-margin packaged coffee business, revenue per serving and margin dollars per serving are dramatically higher, of course, in singleserve. So the economics are very powerful. And we are very excited about that move as time goes on.

Q - Unidentified Participant

Hi. Can you maybe expand a little bit on the tea platform that you are building with the Teavana acquisition and how you are integrating that?

A - Troy Alstead {BIO 5724238 <GO>}

Yes, I will. The acquisition of Teavana is really a threefold proposition for us, two high priority and one a little further down the road; and I will explain each of them. The first opportunity with Teavana is for us to continue to roll out the standalone Teavana store concept, not exactly as it exists today.

The Teavana store, for those of you familiar with it in the US, is predominantly a mall-based mercantile. Very little beverage presence at all. Largely dry tea, great selection of wonderful teas. And merchandise.

That is a very effective, great unit economics model. We'll continue to add Teavana stores in the appropriate locations that are consistent with the previous generation.

But what we are heavily working on together with the Teavana team that we have acquired is to bring to bear what Starbucks does so well, which is beverage innovation; it is theater in the store; is the beverage bar concept. And creating a new concept of a tea house, a Teavana based teahouse, that will feel very similar and very familiar to that Teavana customer but will, we believe, add another layer of revenue and profitability and growth into the Teavana concept, which is by bringing some innovative kinds of tea beverages into that concept.

So first leg of growth for us with tea is the Teavana store. Again, a new generation of Teavana store that will begin to open up later this year. And we believe there is hundreds of those kinds of stores, first focusing on the US. But ultimately in other markets around the world.

The second value to us of this Teavana acquisition is to now allow us to focus much more on how we bring tea to bear within a Starbucks store. One of the things we have learned from our customer, particularly in recent years as we've really tried to dig deeper into understanding our customer, is that the core Starbucks customer who is a coffee drinker is also a tea drinker.

Now I'll be honest with you. I don't think we understood that years ago. They are also a tea drinker. But we didn't get that tea consumption from them, even if we were getting that coffee consumption, because they never viewed that Starbucks had the quality of tea they wanted or were even aware that we offered tea meaningfully in our stores.

What Teavana allows us to do is deepen our capability around high-quality sourcing and blending of tea. And again by bringing together are beverage innovation capabilities in our R&D facilities we are developing a whole new platform of tea beverages that we think will be very exciting, that will come into the Starbucks store.

It is a very complementary daypart. To the American consumer in particular, tea tends to be -- if coffee to the American customer is a morning, on your way to work, fast kind of daily routine, tea tends to be a little bit more relaxed, zen-like, afternoon kind of experience. It is very complementary to the four walls of our store. So we are excited about adding that next layer of growth.

So second revenue driver and profit driver from the Teavana acquisition is within the Starbucks store. The third -- and the third will be a little further off, to be clear -- that is to then take tea and Teavana more meaningfully into the CPG channels. Tea down the grocery aisle is a huge category, all forms of tea, ready-to-drink, dried.

And we have an opportunity with a brand like Teavana, particularly as we build it through the Starbucks platform, to create more awareness, to elevate that brand, to create that proposition, to perhaps bring to bear Starbucks loyalty program, to move our customers and to make them aware that now they can experience tea down the aisle. And we will build -- we will layer that onto our CPG capability.

That is a little bit further off. But that will also be a part of that. So that is how we see that integration unfolding. And it is progressing nicely so far.

Q - Unidentified Participant

(inaudible; microphone inaccessible)

A - Troy Alstead {BIO 5724238 <GO>}

Teavana in CPG is probably two to three years off. The stores of Teavana are later this year. And bringing Teavana and increased tea presence in the Starbucks stores is this year also. The CPG presence will be a little further off.

Q - Jeff Bernstein {BIO 7208345 <GO>}

I think that's all the time we had for the formal Q&A. We have another presentation to follow. But we did want to thank Starbucks for joining us this morning, specifically Troy and JoAnn. And they will be with us here all day. But thank you very much.

A - Troy Alstead {BIO 5724238 <GO>}

Okay. Thanks, Jeff. Thank you, everybody.