

Starbucks Corp Investor Day

Company Participants

- John Culver, Group President of International, Channel Development and Global Coffee & Tea
- Kevin R. Johnson, CEO, President & Director
- Matthew Ryan, Executive VP & Global Chief Strategy Officer
- Michelle Burns, SVP of Global Coffee & Tea
- Patrick J. Grismer, CFO & Executive VP
- Rosalind Gates Brewer, COO, Group President of Americas & Director
- Thomas D. Shaw, VP of IR

Other Participants

- Adam Harry Sindler, Senior Analyst of Consumer & Retail, Unicom Capital LLC
- Brian John Bittner, MD and Senior Analyst, Oppenheimer & Co. Inc., Research Division
- Dennis Geiger, Director and Equity Research Analyst of Restaurants, UBS Investment Bank, Research Division
- Jeffrey Andrew Bernstein, Director & Senior Equity Research Analyst, Barclays Bank PLC, Research Division
- Karen Holthouse, VP, Goldman Sachs Group Inc., Research Division
- Mark J. Sptel, Investment Analyst, Schaper, Benz & Wise Investment Counsel, Inc.
- Nerses Setyan, Senior VP of Equity Research & Senior Equity Analyst, Wedbush Securities Inc., Research Division
- Priya Joy Ohri-Gupta, Director & Fixed Income Research Analyst, Barclays Bank PLC, Research Division
- Robert Marshall Derrington, MD & Senior Research Analyst, Telsey Advisory Group LLC
- Sara Harkavy Senatore, Senior Research Analyst, Sanford C. Bernstein & Co., LLC., Research Division
- Sharon Zackfia, Partner & Group Head of Consumer, William Blair & Company L.L.C., Research Division
- Unidentified Participant, Analyst, Unknown

Presentation

Thomas D. Shaw {BIO 15317835 <GO>}

All right. Good afternoon, everyone. I'm Tom Shaw, Vice President of Investor Relations. On behalf of our leadership team and all the wonderful partners that help

contribute to today's event, I want to officially welcome you to Starbucks 2018 Investor Day.

As many of you experienced, we started our day with an exclusive first look at our New York Roastery, which we'll be officially opening to the public tomorrow. So hopefully, those of you joining on the webcast will have the opportunity to visit the store as well in the near future.

Before we begin the presentation, let me provide a few housekeeping items to help guide you through the day.

Starting with the agenda. And we do appreciate a little bit of your patience today as we had a slightly later start than we originally intended. We'll begin with a coffee tasting, followed by presentations from Kevin Johnson; Roz Brewer; and John Culver. From there, we will have a break until 4 p.m., which will include the opportunity to try a variety of our latest beverage and food innovation in our lobby area outside.

We will conclude the formal presentations with our new CFO, Pat Grismer. And then host a Q&A session with our leaders.

Finally, we will have a cocktail hour, lasting until approximately 6 p.m., to continue the conversation with our team.

For those of you joining the webcast, you'll be able to follow the presentation online, which also will be available for all of you to review following the conclusion of today's event.

For those of you here today, if you haven't figured it out already, you could access WiFi through the SBUX attendees network. And as you'll see, you should have charging stations at each of your tables.

As always, please notify any of the IR team, including myself, if you got any questions throughout the day.

Finally, let me pause a moment to review our safe harbor statement as we will be making forward-looking statements throughout the day.

So as you know, we start many of these meetings at Starbucks with the coffee tasting. So today, I'd like to introduce Michelle Burns, a 23-year partner with Starbucks, who leads our coffee team. Her role includes sourcing some of the highest-quality arabica beans around the world, C.A.F. E. Practices in support of our farmers, agronomy research and Farmer Support Centers and proprietary roast curves that create the Starbucks flavor profiles that we all know and love.

So please welcome, Michelle Burns.

Michelle Burns {BIO 20642917 <GO>}

Thanks, Tom. Good afternoon. How's everyone doing? Good. Hopefully, you had a great morning. As Tom mentioned, my name is Michelle Burns. And I have the pleasure and the privilege to lead our global coffee team. I say privilege. I'm a 20-year partner, 23 years. And I have grown my career here through many parts of the business, retail, store development, operations. But today, I stand before you in a very humble place, leading coffee in a dream come true.

People often ask me why have I been a part of Starbucks for 23 years. And when I started, I started with the company that had a mission and a value and a sense of purpose in this really great entrepreneurial spirit. I stand before you today and I have those same feelings and that same excitement that this is a company that still shares those mission and values that I do, still has an incredible sense of purpose and probably, most important for me, for all of us, a core in coffee and a love for coffee.

So as has mentioned, we traditionally do a coffee tasting, just coming around for all of you. And as I do that though, I wanted to share, if I could, a couple of things. One is coffee is often referred to as the heartbeat of our brand. We source the highest-quality arabica coffee from over 380,000 farms in 30 countries. We've been doing this for a very long time. We largely source from very smallholder farmers. So if you think about it, a farmer has less than 5 hectares, most often, where we are sourcing our coffees, these farmers are depending upon us not just to pay the premiums for the highest quality. But also to provide great technical tools and farmer support so they can continue to grow the highest-quality coffees around the world.

I wanted to share one brief story with you, if I could, about a very recent experience that I had in Colombia. I was in Colombia 3 weeks ago in a region in which we've been working for over 30 years. And we spent the last two years working with the team down there with young farmers and helping them with technical tools, laptops, 500 farmers on a test with laptops, some simple P&L management and a lot of the technical skills of how to increase their productivity. As I sat around with these 5 young farmers between 17 and 22 years old, what they shared with me was what they were looking for is the technical skills that we provide them and being there on the farm through our agronomists to help them grow their future. The best quote I heard was we've gone from a place where they saw themselves as coffee pickers, to owners of coffee companies. It's just a very small example. But it shares, hopefully, with you, the passion, the commitment of what we can do in a micro and scale it as a company in all these regions around the world.

So with that, I'd like to do what we do best, what we normally do. I think, does everyone have coffee? Looks like you do. Okay. Well today, we're going to celebrate with Christmas Blend. Christmas Blend for us really speaks to heritage and tradition. 34 years in the making for this coffee. So from the time when roasted coffees coming out of Pike Place, to where we sit today, I like it, a little music, the tradition continues. This is still our largest coffee in a seasonal offering by a landslide. So if you can indulge me, take a sniff and slurp. Indonesian coffee, really smooth blend, blended with Central Americans. Then we have this unique piece of the Aged Sumatra, which

gives it, for any of you who are connoisseurs, a little bit of cedar-y flavor. Almost a peat-like, Scotch is often used for those of you that may see that in the flavor profile. So it's really meticulously blended coffee.

But what I've just shared with you is, large coffee drinker or not, a part of the experience and the tradition is the sense of place that it gives you. So my hope is that this has just been a nice start to a great afternoon. As I said, I'm very proud to be a part of this company, proud to welcome you. And I really wanted to share a bit of our tradition. And thank you very much for being a part of wherever and wherever this coffee may transport you in your holiday traditions. Thank you.

(presentation)

Kevin R. Johnson {BIO 3773960 <GO>}

Well. Good afternoon. Welcome to the 2018 Starbucks Investor Conference here in New York. How many of you had an opportunity to visit the Starbucks Reserve Roastery this morning? Great. What did you think? Beautiful. Wonderful. Well I'm glad you had that opportunity. And I'm glad you're here today.

We're delighted to spend the time with you this afternoon. And we have the entire Starbucks leadership team here. We have many leaders, our leaders -- international leaders from around the world. And Mike Ullman, the Chairman of Starbucks, is right here, joining us today. So from Starbucks, to you, we welcome you here today.

Now my Starbucks journey began nearly a decade ago when I joined the Board of Directors. It was in 2015 that I joined the management team as Chief Operating Officer. And it's been now 18 months, roughly, in the role as CEO. And it continues to be my honor to serve Starbucks, one of the world's most admired and trusted brands.

The leadership team and I work in service each and every day of our partners, our customers and you, our shareholders. Now the Starbucks journey is a special one. It began 47 years ago, 1971. And over that period, has built this great brand. We have tremendous consumer reach, serving 100 million customers a week, with the kind of repeat frequency that is unheard of in the food and beverage industry.

Over the past two years, we've successfully made the transition from founder-led to founder-inspired. And we have a world-class leadership team. And over the last 6 quarters since I've been CEO, I've been working with our leadership team to really set the foundation and lead us to this next chapter of growth, a chapter that requires us to have the wisdom to know what to honor and preserve from the past. But also the courage to boldly reimagine our future.

The leadership team and I have worked together over this past year to lay the foundation for the next chapter of growth that we call growth at scale. Now growth at scale acknowledges 3 things. First, it acknowledges that Starbucks has grown

significantly over our 47-year journey, with 29,000 stores and FY '18 revenue of \$24.7 billion. We are growing off of a large base. Number two, we acknowledge customer behaviors are shifting rapidly, whether it's embracing the digital lifestyle, amplifying the need state of convenience, a desire for more premium, personalized experiences or a trend toward more healthy food and beverage choices. This strategy acknowledges we must continue to adapt and adapt rapidly to meet our customers where they are. And third, certainly, we acknowledge that the competitive landscape is evolving as many others see a large and growing addressable market around all things coffee, which requires us in the strategy to amplify our competitive differentiators as we capture the next wave of growth.

Now what does growth at scale mean for shareholders? Well first, it's about brand. You're investing in one of the world's most admired and trusted consumer brands. Second, this growth at scale strategy is about driving predictable, sustainable growth and returns to shareholders. And finally, this is about a leadership team that is executing with focus and discipline on creating that shareholder value.

Now what you're going to hear today, you're going to hear clear strategic priorities that have been co-created by this leadership team. You're going to hear about the detailed operating initiatives that are driving results. In fact, we saw progress in virtually every operating metric that we track in Q4. And we continue to see evidence that this strategy is working. You're going to hear about customer experience evolution and innovation. And you're going to hear about how we are amplifying competitive differentiators. But importantly, you're going to hear about the foundation of building the brand consistent with our past and building that brand that creates that emotional connection to the customers we serve. All of this adds to the confidence that our strategy is working and supporting the long-term growth model.

Now growth at scale has 3 major building blocks. The first is streamline, which is to enable more focus on the core value drivers and more agility in our innovation agenda. That focus then is applied to 3 strategic priorities that allow us to focus management attention, our capital, our partner resources and execute with discipline. Then finally, building and amplifying the Starbucks brand is about continuing to expand our reach and amplify what makes Starbucks different from all other competitors.

Now I'm going to provide you the growth at scale framework today. And Roz and John are going to take you through detailed initiatives around the strategic priorities. Then later today, Pat is going to come up. And he's going to outline the long-term growth model that supports this growth at scale agenda.

Now we're confident in our approach simply because we have evidence of business outcomes from the initiatives we're driving that are working.

Now we started our streamline efforts roughly 6 quarters ago around 3 main initiatives: retail market alignment; business simplification; and Global Coffee

Alliance. Retail market alignment is around leveraging the appropriate business model to fuel growth and create value in each market. Business simplification is eliminating complexity so that Starbucks partners can spend more time creating and delivering the Starbucks experience. The Global Coffee Alliance is around expanding the Starbucks CPG presence in new geographies and on the Nespresso platform.

We recently launched a fourth initiative to increase the velocity of innovation aligned with those priorities.

Now let's take a look at the actions we've taken over the last six months in each one of these areas. Let's start with retail market alignment.

Now as you're aware, we have transitioned many markets over the last 6 quarters to licensed partners. Now keep in mind, we have long-term relationships with these licensed partners who are experienced in building the Starbucks brand in other markets. In fact, their understanding of the local market, their ability to deploy capital, the operational excellence they bring, ensures that these markets will stay true to the Starbucks brand. In addition, we deployed capital to acquire 100% of the East China joint venture so that we could unify China Mainland, our fastest-growing market, as a company-operated market. This is enabling us to accelerate growth in China and maximize shareholder value creation.

Business simplification. I believe in empowering my Starbucks partners so that they can focus on the things that make Starbucks great, elevating the customer experience in our stores. Now in many ways, scale and complexity can be barriers. To focus on the most important things, we've simplified work, we've deployed technology, for example, to automate administrative tasks, such as improving scheduling in our stores for our partners and enhancing inventory management. It frees up time performing administrative activity so they perform more of their time on customer-focused activities.

Now we've taken many actions, including closing or divesting of noncore slow growth businesses, simplifying how we work and leveraging technology. That is allowing us to put more of our energy into what matters the most, the customer experience.

Global Coffee Alliance. A little bit of background. We built a very powerful and strong CPG and Foodservices business in the United States and Canada. And that Foodservices business and CPG business has acted as a brand amplifier to customers who would visit our stores because they could -- simply, they could go then at grocery or mass merchant and find Starbucks-branded products to buy and consume at home, amplifying the brand.

And the fact is, we're in 78 different countries around the world. And in all -- most all those other countries, CPG and Foodservices business was either nascent or nonexistent. So we had 2 choices. We either go down the path and build CPG and

Foodservices organically over the next decade, or we find a strategic partnership. And Nestl  turned out to be the perfect strategic partnership. And we're very excited about the firepower behind these 2 great brands. And it is a growth opportunity. Single-serve platforms of Nespresso and Dolce Gusto will now be an opportunity for Starbucks coffee on those formats. And Nestl  brings the global reach of 5 million points of presence in 190 countries around the world. Together, we share a common commitment, a commitment to support coffee farmers around the world. This Global Coffee Alliance will be accretive in fiscal year '20. And this Global Coffee Alliance will grow and pay dividends to Starbucks shareholders for years to come.

Now the final component of our streamline work has been around accelerating the velocity of innovation, which really is based on 3 things we've been driving. Number one is focusing our innovation agenda on the key priorities we've set for the company. Focusing those innovation projects and resources on the things that matter the most. The second is embracing more modern-day methodologies of innovation, including things like human-centered design and working in smaller, cross-functional teams. In fact, we have a mantra that says we want to go from idea to action in 100 days. Small teams, 12 to 15 partners from different functions, given a mission and empowered.

To do this, we've reorganized the leadership to eliminate roles that had overlapping mission so that we could accelerate decision-making. And we've reallocated resources. This is about empowering smaller teams to drive these new ideas, reducing the number of roles to get velocity. Now this will make us a more efficient company. But the primary objective is to accelerate the velocity of innovation.

Now this is creating energy within Starbucks, energy in how we innovate, accelerating the velocity that is relevant to our customers, inspiring to our partners and meaningful to our business.

Now streamline has enabled us to sharpen our focus and gain operating leverage to drive progress against our 3 strategic priorities: number one, accelerate growth in our targeted long-term growth markets, the U.S. and China; number two, expand the global reach of the Starbucks brand through the Global Coffee Alliance; and number three, increase returns to shareholders.

Now let's take a look at each of these strategic priorities. Now we've declared China and the U.S. as our 2 targeted long-term growth markets. Why? Those 2 markets represent a significant opportunity for growth. The addressable market and the growth of that addressable market in those 2 markets is our priority. The Starbucks brand resonates with customers in both of those markets. But there are some unique attributes of those 2 markets that's important to note. The stage of market development is very different in the 2 markets. In many ways, the consumer behavior shifts are different in those 2 markets. And in fact, the competitive dynamic is different in those 2 markets.

Market development stage. Growth in China will mainly come from new store expansion and establishing the Starbucks brand experience in more places, in more cities to capture a first-mover advantage. Therefore, 80% of the growth in China is going to come from new units versus same-store comparable. Now we'll balance the 2. But building out our first-mover advantage in China is the priority.

Growth in the U.S. will be much more balanced between same-store comparable and store expansion. Store expansion will be much more targeted, much more targeted at the markets that are underpenetrated, such as the Sunbelt. And we'll share more details on that with you today. So comp and new units is more balanced in the U.S.

Let's talk about consumer behavior shifts. The Chinese consumer has embraced the digital lifestyle far faster than any other market in the world. Data point: in China, digital payments at Starbucks represents approximately 70% of total tender as compared to 40% in the U.S. Social gifting in China has seen significant growth. Alibaba digital properties alone have more than 600 million users. In fact, Alibaba and Starbucks share a common vision around what we call new retail, which is why the China digital partnership is so important. In China, consumers have embraced experiences around the need state of convenience far faster than other markets. This is driving a wave of innovation around delivery, which is beginning to propagate to other markets around the world.

Now we've rapidly implemented Starbucks Delivers in China and applied our learning to begin implementation of Starbucks delivers in the United States. You're going to hear more about that today.

And finally, on the consumer front, China is predominantly a tea-drinking culture. Now we're introducing that tea-drinking culture to premium arabica coffee. And as we introduce more customers to arabica coffee, we will see over time the emergence of the daily ritual that exist today in the U.S. and Europe.

Now competitive landscape. Given the large and growing addressable market around premium coffee, we're seeing more competition enter the market. It's to be expected. In the U.S., there's been a wave of consolidation of food and beverage brands. And we expect to see that continue. In China, there are many more startups and a much more fragmented landscape of competition. And we expect to see that as well.

Now there's no question that coffee is an attractive market. It's one of the fastest-growing beverage categories globally.

Now this is data from Euromonitor, research data that shows the global specialty coffee shop category, really, the core of our business, remains very healthy and is growing at a 6% CAGR. In fact, over the last five years, 2012 to 2017, it grew to 6% CAGR. And Starbucks outgrew the addressable market, taking share. The growth at scale agenda is projecting with the Euromonitor that it's going to continue to grow at

that rate. And we've laid the foundation for us to continue to grow faster than the addressable market and take share.

Now I commented on the drivers behind the decision to establish the Global Coffee Alliance with Nestl . And with that alliance in place, we are now focused on execution. 3 important points. This alliance is about growth, new markets, new platforms. This alliance is a brand amplifier. Nestl  brings 5 million points of presence across 190 countries to highlight Starbucks-branded products at CPG and Foodservices. And this partnership is aligned around a common set of values in support of coffee farmers around the world.

Nestl 's global reach and their knowledge of CPG and Foodservice business will act as a catalyst for growth of Starbucks in these markets. Now John is going to take you through all the details of how we're operationalizing the plan, the progress we're making and the optimism we have for the path that we're on.

Strategic priority #3. Shareholder value creation. We're committed to return \$25 billion of cash to shareholders over the years' fiscal '18 to '19 -- or '20. And streamline is a key driver of this commitment. In fact, with streamline, we have freed up \$8 billion of capital from the actions we've taken. We have redeployed approximately \$1.4 billion of that capital to acquire East China and unify China Mainland. In addition, we've increased our leverage more in line with our current growth stage. In fiscal year '18, we returned approximately \$9 billion of cash to shareholders in the form of dividends and buybacks. And with the after-tax proceeds from the Nestl  Global Coffee Alliance transaction, we initiated an accelerated stock buyback of \$5 billion on October 1.

Streamline has enabled us to return a significant amount of capital to shareholders. But that's only one aspect of this priority. Pat, this afternoon, is going to walk you through our capital allocation approach that we're using as part of the growth at scale agenda that ensures we fund necessary investments for the long-term success of Starbucks, while at the same time creating an ongoing predictable way to think about dividends and buybacks that are woven into our value-creation model.

Now the final and perhaps the most important building block in our growth at scale agenda is our focus on building the Starbucks brand and doing this while staying true to our mission and values.

Now we reach out and we get a lot of feedback from customers on what makes Starbucks special to them. And so let's just take a quick look at what they say.

(presentation)

So the foundation of our growth at scale agenda requires we stay true to the brand promise that built this great company. We understand intuitively. But we also ask customers why they choose Starbucks. And in the research, the comments and the taxonomy of their feedback is consistent. It's 3 things: it's, number one, it's the

Starbucks experience we create in our stores; number two is the quality of our coffee; and number three is our corporate reputation for doing good.

You look at the kind of comments that come back in the surveys in the research that we do, the fact that our Starbucks partners in our stores make an effort to connect with customers, the service we deliver, the inviting atmosphere. It's about the quality of our coffee, everything from how we source it to how we roast it, to how we create personal handcrafted beverages. And it's about the pursuit of doing good, the fact that we are a company that takes care of our Starbucks partners and commits to serving the communities in which we operate.

Now these 3 attributes are captured so elegantly in our mission statement. They dominate the way we build Starbucks, the Starbucks brand, through the customer experience we deliver in our store.

Now how do we know when we're delivering the Starbucks experience? For each of us, we can close our eyes and imagine that perfect Starbucks experience for us. Perhaps when you open the door and walk in the store, the aroma of coffee, the music, the familiar faces you see in the store, the perfect handcrafted beverage. Perhaps, you're on your way to work and you've issued a Mobile Order and Pay. And there is your order prepared for you, hot and ready for you to grab and move on with your next activity.

The Starbucks experience really begins by ensuring that we create the right environment in our stores, the location, the design aesthetic, the aroma, the welcoming environment. But our research confirms something that we always knew intuitively. And that is the role of the Starbucks partners who proudly wear the green apron. They are the ones that create the special Starbucks experience. Enabling our partners to practice their craft of personalizing handcrafted beverages for each and every customer, inspiring our partners around a mission that is bigger than any one of us, investing in our partners in support of their dreams and aspirations, the experience we create in our stores is the result of the investments we make in our partners in both wage and benefits.

Now we've long been recognized as a company that takes care of our partners by providing meaningful, culturally relevant benefits for part-time workers of 20 hours or more a week. Let me give you 2 examples of how this is a differentiator. In the U.S. today, we now have over 12,000 U.S. Starbucks partners participating in the Starbucks College Achievement Plan and Pathways to Admission programs with ASU, partners that are on their way to earn a 4-year college degree and graduate debt-free.

In Starbucks China, our Starbucks China partners consistently expressed an aspiration around caring for their parents as they age. We worked to create a new critical illness insurance program for Starbucks partner parents to address catastrophic health care incidents that they may encounter. These are 2 examples about how we take care of partners because we know if we take care of Starbucks

partners, they take care of customers. Data shows that our retention rates are 15 to 20 points higher than industry averages for food and beverage. When we take care of our partners, they take care of our customers.

Quality of coffee. Now once customers visit Starbucks, they quickly realize that we serve the highest-quality arabica coffee roasted to create a unique flavor profile that Starbucks has perfected over a 47-year period. 3 ways that are key differentiators for us. The fact that we source our own coffee, green coffee, from over 380,000 coffee farmers that we've had relationships with around the world for the last 47 years and stay true to the C.A.F. E. Practices to ensure that there's transparency and that the money that we pay for that coffee goes to those coffee farmers, that allows us to have access to the world's finest coffee. We buy our own coffee. Our coffee-buying team, under Michelle's leadership, they know where to find the best coffee and how to buy the best coffee and ensure that Starbucks serves the world's highest-quality arabica coffee.

Number two, the way we roast our coffee. Now we roast our own coffee to a set of what is called roast curves. Roast curves have been perfected over 47 years. These roast curves are the relationship between time and temperature that creates the unique flavors in our coffee. These roast curves are proprietary to Starbucks. And we've developed them and perfected them over a 47-year period.

And when those roasted coffee beans reach our stores, we then create personalized handcrafted beverages for each and every customer. Everything from how we source, the roast curves and the fact that we personalize each beverage for our customers are differentiators for the Starbucks Coffee Company.

But the third and final element of the brand alchemy is our commitment to doing good. Research would show that 60% of consumers are belief-driven buyers. They see brands like Starbucks as a force for change. And we have organized our social impact agenda around 3 pillars: sustainability; opportunity; and community.

Sustainability starts with making coffee the first sustainable agricultural product to the sustainability of the -- serving that coffee, strawless lids, recyclable cups, sustainability of our stores. And we just recently launched a greener apron program around sustainability of how we operate in our stores.

Opportunity is about hiring from diverse populations that make us better, like veterans and military spouses or opportunity youth. It's about creating opportunity for those partners once they join Starbucks through the Starbucks College Achievement Plan.

And the third pillar around community is ensuring that we're doing things that are important in those communities, the day of service, the month of service. The fact that we're doing FoodShare in the United States is an example, or helping with the unsheltered families in Seattle and FoodShare across the country, those are all examples.

Now we're going to remain committed to the pursuit of doing good, not only for our partners. But pursuit of doing good in the communities that Starbucks is a part of.

You put that all together, we build the brand every day when the customer comes into our store. We build that brand through customer experience and customer engagement. We then serve the world's finest coffee. And we stay true to who we are, the pursuit of doing good. We then amplify the brand in 3 unique ways.

In fact, the Starbucks Reserve Roasteries is one example of how we amplify the brand, with the ultimate experience around all things coffee. You think about the iconic representation of the Starbucks Reserve Roasteries in Seattle, Shanghai, Milan and now New York. Shanghai opened a year ago. The Shanghai Roastery opened a year ago. And since then, we've seen over 1 million customer occasions to the Shanghai Roastery. And just last Saturday, in the Milan Roastery that's been open less than 90 days, this video was taken of the line outside of the store that wraps down around the building and behind the building of customers waiting to visit the iconic Starbucks Reserve Roastery in Milan. These are examples of brand amplifiers. We have 2 more Roasteries that are in the pipeline. Tokyo will open in February of 2019. And Chicago Starbucks Reserve Roastery will open in later calendar year '19.

Now amplifying the Starbucks brand also happens through the Global Coffee Alliance with Nestl . We know for a fact that customers come to Starbucks, they develop a flavor preference for our coffee, create relationships with our partners in the stores. For them to then, down the aisle or at other Foodservices locations, see Starbucks-branded products, it amplifies the brand. And third, we amplify the Starbucks brand through the digital engagement we have with customers. Now that digital engagement has grown not only in the U.S., with active Rewards customers. But also digitally registered customers in the U.S. And we're going to share a bit more about how we're continuing to expand that. But it's also significantly expanded in China through our relationship with Alibaba. And we'll share some news with you on some of the new things that are unfolding in that China digital partnership with Alibaba.

So by the end of today, it's our aspiration that we have reaffirmed why Starbucks is one of the most attractive investments in consumer brands. Predictable, sustainable growth strategy, the strength of the Starbucks brand globally, the fact that we are growing faster than a large and growing addressable market. And there's clarity of our strategic pillars, what differentiates us. And a road map ahead.

Now for those who look to invest in consumer-focused brands, we believe this is one of the strongest brands in one of the fastest-growing categories, coffee, with a clear strategy. And we have evidence that our strategy is working, not only in Q4. But as we look -- as we go forward, we continue to see evidence that the initiatives we've chosen, the energy we're putting behind them, is moving the needle.

And so with that, I thank you for being here today. And it's time to now take a look at more of the details behind our growth at scale agenda. Thank you.

(presentation)

Rosalind Gates Brewer {BIO 15034309 <GO>}

So what you just saw is happening each and every day around our stores, not only in the U.S.. But all around the world. And we've been capturing these conversations around coffee. And you'll see us show some more work in this area just like we did with our series around Upstanders because this is who we are as a company.

So first of all, thanks for being here this afternoon and spending some time with us. This is my first Investors Day. And actually, I'm just completing my first year with the company. And it's pretty exciting. It's been a really busy year this year. But looking back, I want to talk a little bit about my decision to join Starbucks.

When I think about it, it was actually more of a calling than accepting my next new role. It started the moment when I met Howard Schultz. I had a chance to interview him at a leadership meeting at Wal-Mart Stores. So our lives collided. And through Howard, I got a really good sense of the history of the company, the heritage of coffee and true entrepreneurship. Then quickly, Howard introduced me to members of the board. And shortly after that, I joined the board. Then I got a chance to meet the members of management. And I experienced Kevin's leadership as he took the helm as the new CEO of Starbucks Coffee Company. And I was hooked. And I've been hooked ever since. And along the journey is something really interesting has happened. I've fallen in love with the company. And it's sort of like the way you do when something just hits you right in your gut and you feel good about the work you're doing and you feel good about the mission and you get excited about the challenge.

So it's been exciting to be here. And since the very beginning, Starbucks has shown me and everyone else that you can serve your shareholders, you can support your employees -- and our employees, who we call partners. And we can make a positive impact. And all of that can be achieved in unison. And that's a rare find. So for me is what it means to work with a purpose and live out your values each and every day. And I get that opportunity here at Starbucks. So thank you for listening for just a minute to get a background in terms of why I'm here.

But before I get too far, I want to share with you a little bit about fiscal year '18. I want to get us grounded in terms of the results that happened last year. And it was a year of learning. Last year, total U.S. sales were up 7% to deliver \$15.3 billion in sales, with the biggest driver being our new noncomp stores. We opened 676 new stores, which expanded our drive-through operations to 339 locations. And our membership in Starbucks Rewards increased 15% year-over-year to 15.3 million members. Our customer connection scores, they gained momentum, showing year-over-year improvement across each and every daypart. And our full year comp growth was 2%. And although that's lower than previous years, I believe the initiatives that I will discuss with you this afternoon will help you see how we will sustain the momentum we saw in Q4.

So at the same time in fiscal year '18 when we continue to see this momentum, we began to build on our rich heritage around our partners. And around the time of our IPO many years ago, we turned our employees into partners. And we did that by extending stock options and a 401(k) program. We provided access to health care benefits 20 years before the ACA, the Affordable Healthcare Act. And later, we extended 100% tuition to our partners. And we pay sick time to our eligible U.S. workforce. We know our partners are a critical component to our growth. The power of connection and the power of the experience that they have in our stores is critical to our growth. And today, our industry-leading Rewards program is 3x the value of comparable retailers in the space. And it's our key lever for attracting and retaining our top talent in our stores.

So equally important to these investments, because these investments really pay off for us, they pay off for our partners and they pay off for the business. So we've hired more than 20,000 veterans and military spouses in the past five years. And we've opened over 50 military family stores across 25 states. These are places where veterans and military families can come and connect. They're also stores that outperform across the entire portfolio.

So as Kevin mentioned, we have more than 12,000 partners participating in the Starbucks College Achievement Plan. These individuals stay 50% longer. And they're promoted nearly 3x at the rate of their peers. Our customer, Susan, said it best in the video. Not only does she have the money. But the money that she has, she's going to spend it with companies who do the right thing. So we're very proud of our front-ended look, our front fast-forward look in our partners and the returns that we're seeing as a result.

Now it's true that these investments, along with ongoing technology spend and the shift in our product mix, has resulted in a decrease in operating margin for fiscal year '18. And this highlights why our focus on operational efficiencies and discipline is key to our success in the future.

To help us get there, we've made significant foundational changes around developing a clear understanding of today's consumer and how we can quickly adapt to meet their changing needs because they are changing. So we've become much more sophisticated users of consumer insights. And we're using data to identify how to drive transactions and improve performance overall.

Let me share a few examples with you. As Kevin mentioned, the health of our brand is strong. Fortune included us in its top 10 list of most admired companies 7 out of the last 10 years. Consumers, they have a strong love for our brand. We lead in awareness. We lead in consideration and first choice, with a large margin in first choice. And we're well positioned with millennials and centennials.

You also heard Kevin reference the size and growth of the specialty coffee market. In the U.S. alone, we see similar stats, with specialty coffee growing historically at about 7%. But Starbucks is growing at about 9%, ahead of the market. That market is

comprised of more than 180 million people, adults, engaging in away-from-home coffee and tea at least once a month, with 40% of those coming to Starbucks monthly. All of this underlines why our work this year will focus on 3 initiatives. And this will continue to help us elevate the customer experience and improve operational excellence. You've likely heard me talk about this in Third Quarter earnings and Fourth Quarter earnings. And those 3 are: enhancing our in-store experience; secondly, delivering beverage innovation; and third, driving digital relationships. I'll walk you through some of these areas and give you some details and talk to you about the progress we're making in each.

So first of all, enhancing the in-store experience. Our customers, they come to us for the best coffee. But they stay in our caf  s for the best moments that we create. And some of the best moments come from the little things that happen in our caf  s. But we haven't always made it easy for our partners to slow down for a second, look our customers in the eye, make that connection and keep them coming back each and every time.

We have really bombarded our partners with complex tasks. We've given them unclear expectations. And those things often get in the way of them doing the best job and leading with their customer connection. So this is why it's important to really understand how our partners work in the stores, what is the work that they have to do. We need to understand this so we can make their jobs easier and make their jobs more enjoyable. And we do that by freeing up more time for them to engage.

A recent assessment that we conducted found that more than 25 of the 65 people hours scheduled each day are spent on noncustomer-facing task. Partners also, they step away from our customers up to 22 times an hour. And that's during peak. And they do that to replenish their stations. Overall, our partners spend 40% of their time on nonfacing-customer tasks. So to shift this balance, we're resetting task management and data-driven inventory management with the goal of improving capacity and throughput so partners have more time to spend with customers.

One of the first steps that we've taken is shifting the cleaning task to later in the day to after closing. And partners are calling it clean play. It's been a huge hit. They're excited about it. And I want you to take a look at something.

(presentation)

I especially love Haley's comment about her customer connection scores really making her building see a real boost in her performance. Now it's real early in this process for us. But we are consistently hearing these comments back from our partners. And it's translating into incremental lift across the portfolio.

So our partners, they're also active in our internal social channel where they give us feedback on best practices. It's a great way for us that are in the support center in Seattle to really learn real time what's happening and what they're experiencing every day. And shifting these very critical cleaning hours to later in the day has had a

very positive impact on who they are as a partner and how they interact with the customers.

The second thing we're doing is deploying technology to automate product planning and product replenishment and to track inventory in near real time. This allows us to do several things. First of all, we eliminate the clutter, the clutter in the back room and the clutter behind the bar. This will allow us to reduce our inventory quantities and then eliminate the need for partners to move away from their stations.

It's really exciting to see how this impacts even some of the work we're doing around our new store renovations. In terms of new store renovations and optimizing our real estate portfolio, it's really important about the work we do to support the customer experience as well. We have targeted a 2-year renovation strategy. This 2-year renovation strategy will uplift our stores in a couple of ways. First of all, it'll allow us to put our equipment innovation in place. It'll raise our decor. And it'll allow us to introduce new format changes. In that period, we anticipate we'll reach about 1/3 of the portfolio with newness. And this plan fits squarely within the fiscal year '19 capital guidance that you all have learned about. And we look to reach even more stores at a lower average cost in the renovation model.

Our renovation approach also calls for implementing format changes to meet the increasing demand for the need state of convenience. And you can see how it's influencing our mix. In the last two years, the sales mix of both drive-through and Mobile Order & Pay combined have increased by 10%. Mobile Order & Pay continues to excel. And as it grows, we're continuing to evolve our early express store formats to include the newest digital innovations. Those 2 combined really address the need state of convenience. So we're prioritizing projects that drive the strongest ROI by leveraging data from historical renovations and on our store performance with sales trends and consumer patterns.

These modifications will create a higher financial return and help partners by enabling more capacity and by improving efficiencies. So there's also a significant opportunity to expand our portfolio in underpenetrated areas. So take a look at this heat map. The areas you see in the blue are the biggest opportunity given both population per company-operated store. They're also where we have more opportunity for drive-through locations. Drive-through overall has performed very well in the past several quarters, outpacing our traditional café comp by more than 4%.

And as we shared before, the majority of our store openings this fiscal will focus on drive-through, represented in more than half of our U.S. company-operated stores.

Now in locations where drive-through isn't infeasible, we're continuing to innovate and test platforms like delivery. So as you know, we've been running an Uber Eats pilot in Miami. And it's receiving high remarks. I want you to take a look.

(presentation)

So that's why I'm thrilled to announce today that we're bringing Starbucks Delivers in partnership with Uber Eats to nearly a quarter of our U.S. company-operated stores by the end of Q2 this year. It's an exciting move. It'll bring meaningful and scalable growth to the U.S. operations. And we're making it easy for our partners by integrating the ordering and technology directly into our systems. And this is eliminating additional steps for our baristas and creating the fourth channel in our stores, walk-in café, first channel; second channel, Mobile Order and Pay; third channel is drive-through; and a new channel, Starbucks Delivers.

So our second initiative is delivering beverage innovation. Now espresso continues to be our #1 driver of revenue in margin. We're also seeing incredible growth in our cold coffee platform. And that includes our iced espresso, our cold brew and our Starbucks Refreshers, which combined have contributed to more than 80% of our beverage growth over the last two years.

In contrast to Frappuccino, these categories are more habitual and create more brand affinity. As you know, our primary softness has been centered around Frappuccino. The customers who come to us for these occasions, they tend to have less brand affinity. And their frequency in these categories is relatively low, meaning they're not your regular beverage routines.

So while the rotation from Frappuccino to other categories has been challenging for us in the short run, due in part to the higher price point, the longer-term benefit is really compelling. And so we're innovating in categories now that create the most brand affinity for Starbucks. It provides us consistent routines and customer value over time. And Nitro is a great example.

One of the big deliverables this fiscal is to expand Nitro from the current 2,500 stores to all remaining company-operated stores in the U.S. And what I love most about this is a little bit of the theater that this really provides when you walk into a Starbucks store, just seeing the levers getting pulled, the taps getting pulled on Nitro. It's really nice to see. It's a real experience that differentiates us from our coffee fast competitors. And we're seeing strong performance with incrementality. And it's a more habitual product that's growing in popularity.

And we're continuing to innovate from our core, testing and learning from our customers to quickly bring new beverages to market. For example, this summer, we trialed a few new drinks in Nashville, Tennessee, our summer's macchiato, it's extraordinary.

So we have some of our New York partners coming in to help us pass out the beverage. I'd like to welcome them and thank them for all their hard work. And I get to have one, too. Thank you. So much. It's really good. So as you all are getting your drink -- it's a nice beverage. So this beverage, it really builds on our growth in iced espresso and core macchiato, about \$1 billion platform for us. It's a really beautiful drink. It features smooth, cold-pressed espresso, our core, velvety spice meringue in a cold foam, no whip cream, dusted with winter spices. When you sip it, just take a

second, let it just sit on your tongue for a second. And it's really great, really refreshing. I think everybody enjoyed that. So this drink is inspiring our new cloud macchiato and other ingredients that are launching this spring. It's a great example of how we're combining our core of forward-looking coffee and innovation with customer insights. We know our customers are loving the cold platform. It allows us to develop authentic, original beverages that keep our customers coming back time and time again. So I want to thank the partners who helped us do this little coffee tasting here.

So now I don't want you to think we've taken our eye off the opportunity that exists with food. We've talked to you all a lot about our food business. But we're pleased with our recent traction. And we continue to see the ongoing strength of our offerings. We promised you that we would be accelerating our food over a 5-year period, out through 2021 to get to a 25% balance of food in our portfolio. We're currently at 22% of our food penetration in our business. But we are a beverage-first business. And our challenge and our opportunity is to drive transactions. And we know, first and foremost, that comes from our beverage offering. And we need that with more customers coming throughout the store each and every day.

So let me ground you in our third initiative. Our third initiative is driving digital relationships. Our Starbucks Reward member, their growth accelerated to 15% last quarter, helped in part by our ability to convert a portion of our 10 million registered customers. And these are customers registered outside of the Rewards program. Our spend per member has grown consistently the past three years. This is led by our Mobile Order and Pay adoption and the quality of new members joining the program, which we achieved through the better targeting work that our marketing group is doing and also through more timely engagement.

For instance, our digitally engaged customers purchased a greater variety of products, nearly 3x as many customers who don't even engage with us at -- in this way at all as a Starbucks Rewards member. They're also more likely to purchase products that have low awareness but high taste scores. So like Refreshers and Nitro and Sous Vide Egg Bites, they usually grab that attention. But overall, we view digital as an enabler. It enables us to be more convenient. It enables us to drive awareness. And it drives value. And I'll break that down for you in real detail.

First of all, convenience. Convenience is tied to how customers are consuming today and impacts how they interact with our stores. Shopping habits are changing, not only in coffee caf  s. But our customers expect us to provide a seamless experience, much like what we're seeing in the omnichannel across all of retail. And this is where delivery comes in. We drive awareness through our app and our e-mail engagement and the cost of marketing to our customers through these channels is extremely low.

Now I've previously mentioned we have just started to build relationships with customers outside Starbucks Rewards. We see opportunity in fiscal year '20 and beyond to drive incremental sales from this group as we develop and improve marketing relationships with them and our capabilities around that work and to learn

how they respond to us. So we expect to be a greater source for new SR members in the future.

Today, we expect roughly about 1 to 2 points of comp growth to come from 3 drivers. First and foremost, our new member acquisition and the related spend lift that we get from that. Second, that comp performance comes from Mobile Order and Pay adoption and the routine that it drives. And thirdly, it comes from the upcoming reward program enhancement that are coming this spring.

We're not including delivery in this estimate. But as I mentioned early, there's sizable opportunity in that space. Now our Starbucks Rewards customers are really valuable. We need to provide them value at the same time we're building additional incentives for our nonmembers to drive acquisition. So starting this spring, customers will have more choice and flexibility in how they want to use their rewards. They also will be able to begin redeeming their awards within 2 to 3 visits. And to amplify these enhancements, we've designed a cross-platform campaign. And this campaign will drive acquisition. It'll broaden our member base. And it'll expand our Starbucks Rewards Gold members in a meaningful way.

So we've talked about innovation and some of the things we're going to do to make the business stronger. But I think it's important that we talk about how we're improving our operating margin and creating capacity in our P&L. And there are 5 key areas that I'll touch on. First of all, Kevin talked about the ways of working. Smaller groups working on fewer, more critical priorities. And that enables us to move with speed and deliver the innovation with acceleration.

Our supply chain. Our supply chain remains focused on building a network that enables efficient, reliable speed and speed to market for the new products that you just saw me talk about.

Our labor efficiency. Our labor efficiency is focused on automation and improving throughput and effectiveness considering our barista's time in the caf  s.

Our efforts around front and back of the house and how it's organized depends on the autoplanning and replenishment that helps us with waste reduction. And we're continuing to evaluate our portfolio of products. You recall sometime last year, we did pretty significant work on SKU rationalization to simplify our lobbies to be less cluttered and to improve the shopability of our caf  s.

So to sum it up, our focus on improving stores, adding critical capabilities, deepening relationships with customers remains consistent and is beginning to show traction.

Our progress in the past few months has required a lot of heavy-lifting behind the scenes, including studying how our partners work in the stores, identifying these through our priorities. And then learning how to work in new ways. This combination

is allowing us to unlock the innovation and speed. And our focus now is to accelerate. We have to accelerate in each one of these areas.

I'll leave you with these key messages. It's all about the customer. The customer is at the center of all of our decision-making. There's momentum in the business. And we saw it in the Fourth Quarter. We have plenty of room to grow our U.S. footprint. We're doing it in a disciplined manner. And we're executing with speed.

I want to thank you for your time. I look forward to questions during Q&A. And right now, I'll turn it over to John Culver.

John Culver {BIO 15817924 <GO>}

Well thank you, Roz. Good afternoon, everybody. And it's so great to be back in New York and appreciate everybody being here today as well.

I'm here today to share with you the tremendous opportunity that we have and we see for our business in China and with the Global Coffee Alliance with NestlÃ©. But before I get started, I wanted to share a little bit about myself and how my experience at Starbucks positions me to lead Starbucks' next phase of growth across our international business and our channel development businesses.

I joined the company 16 years ago as part of what is now our channel development business, leading our foodservice organization. And over the last 12 years, I have had the opportunity to lead the growth and the expansion of our international business around the world. Today's Starbucks stores are present in 78 markets. And our international store portfolio represents more than 50% of the total Starbucks store portfolio, with China being the second largest market we operate in.

I often get asked when I travel and talk to people, "What has enabled Starbucks to be so successful across all these diverse markets?" And I've seen this play out time and time again. And the answer is quite simple. It's our culture, it's our values, the fact that they know no borders. And more importantly, it is the way our partners bring them to life and the emotional connection that this creates for them to be part of something bigger than themselves.

Take a look at this short video.

(presentation)

That is a great video. And I hope you can see firsthand really the passion and pride that our partners have for the company and the positive impact that we, as a company, have for them and their families.

The true differentiators for Starbucks has been and will always continue to be our passionate partners, the heritage we have around sourcing, roasting and serving the highest quality coffee and the unique experience our partners bring to life for our

customers each and every day. There is absolutely no other company at our size and scale that is able to replicate what we do.

Now as I -- as Kevin shared earlier, he has been very clear in what the strategic priorities are for the company. And he's laid those out for all of us, not just the leadership team. But down throughout the organization. Two of those priorities, China and the Global Coffee Alliance, are the areas that I want to talk about.

Let me first start with China. Today, in China, we operate more than 3,600 stores across more than 150 cities, serving more than 7 million customers each and every week. And as a matter of fact, in January, we celebrate our 20th anniversary in what has become Starbucks' second home market.

Now I know many of you in the room were with us in Shanghai in May, where we shared our purpose-driven growth agenda and our vision for the business going forward. And I want to take this opportunity and give you an update on the progress that we've made since the time we've met.

The growth agenda is centered around our partners and our goal of building a different type of company in China for China. It delivers a sharper focus on the third place experience in our stores, the fourth place opportunity we see with digital and the tremendous white space that exists to reach our customers at home and away from home.

Let's start with the third place, our retail stores. In 2018, we opened 585 stores. Beginning this year, we're committed to accelerating to opening 600 stores per year. And over the next four years, we will grow to over 6,000 stores across 230 cities. This acceleration allows us to gain first-mover advantage. And it also positions us to capture the opportunity that we see. And especially coffee market that is expected to grow nearly 50% in the next four years.

Now equally important is the fact that our new stores' profitability, ROI continues to deliver best-in-class results. Whether you're in a top-tier city or a lower-tier city, we are generating very, very healthy returns.

So let's take it, economics. First-mover advantage, growth of the coffee market, the strength of our Starbucks brand. Combined, all 4 of these gives us great confidence that our strategy to continue to aggressively grow is the right one.

This slide here gives you a view of the top 13 cities in the country. These cities have an addressable population of 152 million people, nearly half the U.S. This chart also shows that we have plenty of room to grow our store base for a very long time.

Over the next four years, 60% of our new stores will be built in these cities. And as we expand, we'll expand based on 3 key factors: first is the opportunity we see for first-mover advantage to reach more customers; second is being able to capture

prime real estate based on our development and market plans; and third, being able to rapidly develop new store formats to fit our customers' needs and the emerging trends that we're seeing.

Now as we grow, there are 2 important metrics that we will watch closely. First is total revenue growth for the market. This is important because, as Kevin highlighted, 80% of our revenue growth is driven by new stores and roughly 20% by comparable store sales. Second, we're focused on growing total transactions across the market. And as I shared on our most recent earnings call, our total transaction growth delivered double digit.

Now as we expand, we will also watch very closely sales transfer. And I know this has been brought up before by this group. Our assumptions are that as we open our new stores over the next four years, we will manage sales transfer at the historical levels we have seen in the market.

These pictures are another proof point to the power and the relevance of our brand in China. This shows the excitement and the anticipation that customers have when we open our stores. Starbucks is absolutely a beloved company in China. And we have built our business over the last 20 years. And in doing so in a way that elevates the company in the eyes of our partners as well as the eyes of our customers.

And the greatest expression of our ability to lead around all things coffee in China is the Shanghai Roastery. The Roastery is an immersive retail experience unlike any other, committed to delivering a unique coffee experience that further educates and excites our customers.

Just last week, as Kevin shared, we celebrated our one-year anniversary at the Roastery opening. And I can tell you what an incredible year it has been. Over 1 million customers have walked through the doors. The Roastery has quickly become the top destination for those who live in Shanghai as well as for those who visit.

These pictures that you see here and the ones that I shared earlier speak to the pent-up demand and the opportunity we have to continue to lead the growth of the coffee culture in China for many years to come.

When you couple that with the fact that per capita coffee consumption is less than 1 cup per year compared to 300 cups in the U.S., again, there is no other company better positioned to capture this opportunity.

Now let me take a moment and talk briefly about the environment in China. While there has been much written about the rapid growth of competitors, Starbucks remains focused on our strategy and the long-term opportunity we see for the market. We respect all competitors. And we feel that we are positioned to navigate any of the fluctuations that take place over time in what is a rapidly changing economic and competitive environment. We are positioned to win.

Now our confidence in this comes from, again, those true differentiators: it's the quality of our coffee; it's the unique third place experience; and it's the emotional connection that our partners have built with our customers across all our stores.

Let me now shift and talk a little bit about the fourth place and the digital future in China. In early August, we announced our most significant digital partnership in China with Alibaba. In early August -- I'm sorry, the partnership itself encompasses the entire Alibaba ecosystem, including Ele.me, Hema, Tmall, Taobao and Alipay. The partnership itself enables delivery, order fulfillment, membership integration and a new virtual store platform. Together, Starbucks and Alibaba will create a seamless and even more personalized experience off-line and online that will completely transform the digital reach for Starbucks in the market.

Let me talk a little bit about delivery. Starbucks Delivers is not an ordinary delivery program. The program reflects discussions that started between both our companies more than a year ago. And what emerged is a unique, customized delivery experience that was meticulously designed with our customers in mind each and every step of the way.

Let me share a little bit more detail on some of the experience around Starbucks Delivers. First, we've developed beverages specifically designed for delivery. Second, we've created specially designed spill-proof lids for hot and cold beverages. We've created tamperproof packaging seals to help ensure quality and safety. And we've designed unique delivery containers to ensure orders will remain hot or cold regardless of the item ordered.

Now as a consumer, you have the ability to order through either your Starbucks, Ele.me or other Alibaba apps. As you order, you have the opportunity to customize and personalize your favorite beverage. And once you order, your order will be routed to the best store to fulfill it based on a unique fulfillment algorithm that has been specifically designed with Alibaba for Starbucks Delivers. And finally, your order will be delivered by a dedicated Starbucks-trained Ele.me driver within 30 minutes.

Now not only will delivery be offered through Starbucks stores. But we also have the opportunity to leverage the growth and scale of Hema supermarkets with the introduction of Star Kitchens. Starbucks is the first retail brand to establish a dedicated back-of-house location in their supermarkets. Star Kitchens will be able to utilize their distinct fulfillment and delivery capabilities and, ultimately, extend Starbucks to their 10 million customers.

Starbucks Delivers is a first of its kind up-level delivery experience built in China for China.

Take a look at this video.

(presentation)

We announced the partnership in early August and since that time, the team in China has moved at China speed to implement and execute Starbucks Delivers. At the end of September, we were in 150 stores in Beijing and Shanghai. In early November, Kevin was in Shanghai and announced at that time that the program had been expanded to 1,100 stores in 17 cities. And I'm pleased to share with all of you today that after four months from the announcement, we have accelerated and expanded the program to now reach more than 2,000 Starbucks stores across 30 different cities. Now to put that into context, since we launched Delivery in the first store in September, the China team has activated 1 store every single hour for the past 84 days. That's China speed. That's a can-do attitude.

Now as we move forward and as we roll out delivery and get it stood up, we're focused on, number one, building; number two, gaining trial and repeat; and number three, continuing to optimize delivery coverage around our stores. These are the very early days of our rollout of the program and we anticipate that as we ramp the program, we're going to gain a much better understanding as to the overall impact for the business.

Now beyond Starbucks Delivers, we're also rapidly expanding our partnership with Alibaba in other areas. Our next opportunity that we're launching today is the very first-ever virtual Starbucks store, which enables customers to enjoy a one-stop Starbucks experience, utilizing the Starbucks app or Alibaba customer-facing mobile apps. In a few hours, when the day begins in China, hundreds of millions of Starbucks and Alibaba active digital users will have access to this virtual store. Customers will experience a seamless and easy-to-use interface across multiple digital platforms. Let me give you an example of this "first of its kind" experience. I want to have a little fun here.

Let's say John Ivankoe wants to send a Starbucks gift to John Glass right here, okay? He wants to send them a gift. And sends them a Starbucks gift through Say it with Starbucks, right? John would access the Starbucks virtual store through his Alipay app where he can then purchase a digital gift card. At the same time, it's the holidays, right? I want to give a little something else. A little piece of merchandise maybe, right? You can also add a physical gift like a holiday tumbler from Starbucks Tmall flagship store. And as you're doing this, you say, well, what about me? I want my beverage, my favorite beverage. What do you drink?

Unidentified Participant

Black coffee.

John Culver {BIO 15817924 <GO>}

Black coffee, okay. I want a grande black coffee, right? Well now you can order that grande black coffee through Starbucks Delivers and have it delivered by an Ele.me rider. What was previously done across 3 different apps can now be completed without the customer leaving their Alipay app, all while earning Stars on the Starbucks Rewards program.

This latest digital innovation revolutionizes the traditional off-line to online model and meets an emerging customer demand and customer trend we're seeing. And it also effectively extends the reach of the Starbucks Experience into the everyday lives of our customers regardless of where they are or what time of day it is.

Now to kick off this new digital experience, Starbucks is partnering with Tmall and dedicating today as Starbucks Super Brand Day. This will give us top placement across all of Alibaba's major online properties. And the day will focus on using targeted marketing campaigns to reach customers and introduce them to this revolutionary digital experience.

By leveraging this unique partnership with Alibaba, we will continue to push the boundaries and bring disruptive innovation to the market to further strengthen Starbucks' digital leadership position. And I'm very, very excited and I know the China team is as well, about this partnership and about the opportunity.

Now the last area I want to cover relevant to the fourth place is the future of our loyalty program in China. As you've heard on many occasions, the current rewards program in China, it's a very different program than what we have here in the U.S. It's a paid membership program that we introduced seven years ago and today has more than 7 million active users. Last week on December 5, we up-leveled the program to Starbucks Rewards in order to recognize and reward members in more relevant and meaningful ways. Leveraging our learnings from the U.S., the new program allows customers to register for free from either the Starbucks app or all of the Alibaba apps.

Now as part of the new program, customers can prepurchase coupons, they can load cards, they can move to the next level and they can continue to reward themselves based on what they're buying in our stores. This change, together with the strong referral pipeline from Alibaba, enables us to accelerate member growth and build a more direct connection with our customers. It is a very exciting time for the fast-moving digital landscape in China and really, the rapid evolution that is taking place. And now more than ever, we feel we are strategically positioned to capture and, more importantly, to lead on this emerging opportunity.

Now I'd like to switch and comment a little bit on our progress in East China. As many of you know, we've worked for a full year on the integration of the business and are incredibly pleased with the progress that we've been able to make. We have successfully integrated all of our East China partners and harmonized all salaries and benefits. For our stores in East China, our returns remain healthy. They're in line with our expectations. And we have confidence in our growth prospects in this part of China going forward.

This acquisition was the largest ever in Starbucks' history and benefits our business on the Mainland across multiple areas. It allows us to speak with one voice to our customers and our partners. A big unlock. It allows us to strategically prioritize our investments across the entire market. It allows us to move at China speed in a rapidly

changing market, while streamlining decision-making and, ultimately, it allows us to provide clarity of focus on what we need our partners to do in order to deliver our growth aspirations going forward.

As a reminder, beginning in January, East China will enter the comp base for the total China market. And important to all of us, we're ahead of our initial projections, which we shared on our deal model call earlier this year.

So let me now shift and talk about the opportunity we see in the at home and away from home channels in China. Building on the success of our bottled Frappuccino and Doubleshot beverage platforms, in June, we launched our Chilled Cup. We talked about that at the May conference. The Starbucks Chilled Cup has been incredibly popular with Chinese millennial customers and the success of the Chilled Cup has enabled us further grow our double-digit market share within the RTD coffee category.

Today, RTD coffee in China is worth about \$1.2 billion annually and estimated to grow double digits over the next five years. During the same time, we expect our business to grow from 50,000 points of distribution to 125,000 points of distribution. And from 40 million servings annually to 200 million servings annually.

And now, we have an even greater opportunity in China through our recently announced Global Coffee Alliance with Nestl   to capitalize on the tremendous whitespace that exists in building the at-home coffee, single-serve and foodservice segments. The alliance gives us the opportunity to gain first-mover advantage, unlock the at-home and the away-from-home channels, while leveraging the strength and expanding the reach for Starbucks across Mainland.

So let me spend a little bit of time and talk about the Global Coffee Alliance. This is a unique and powerful partnership where 2 leading global companies have come together to leverage the unique capabilities of both organizations to accelerate growth of coffee around the world. I've had the unique opportunity to understand firsthand the power and potential that this alliance can create. As I shared with you earlier, I've been with the company now for 16 years. But prior to coming to Starbucks, I worked at Nestl   for 16 years.

With Starbucks, you have the most recognized premium global coffee brand in the world with the largest global retail footprint that continues to grow and accelerate. With Nestl  , you have the world's largest food and beverage company, with a presence in 190 markets and a deep history and focus around coffee. Nestl   has also built the fastest growing at-home premium single-serve platforms with both Nespresso and Dolce Gusto.

And the power of the alliance is created when you leverage our leadership position in premium coffee and the awareness of our brand and the Nestl   infrastructure and capabilities across all these markets to sell, to distribute and to grow Starbucks within the CPG and foodservice channels.

So building on those strengths, the alliance is focused in 3-key areas: First, growing our share of Starbucks capsules on Nespresso and Dolce Gusto platforms; second, accelerating our leadership position in North America; and third, expanding the international presence of Starbucks coffee in those channels. It's been just under four months since we've combined our efforts and I want to give you a sense of the work that we've done to date. As we announced on our last earnings call, we've now transitioned over 500 Starbucks partners to Nestl  in North America and in Europe. The alliance has been working at an unprecedented pace to prepare for the global rollout of the Starbucks at-home coffee portfolio.

Working together, teams from both Nestl  in R&D and coffee have developed a range of Starbucks-branded products that meet our quality standards and the flavor profiles customers have come to expect. Products have been specifically formulated for Nespresso and for Dolce Gusto. And later on during the break, if you have not done so already, we have some samples of the new Starbucks-branded Nespresso capsules out in the lobby that I would encourage you to taste. They're absolutely outstanding. It will blow you away.

Now beyond the product side of it, we've also been working on how we want to go to market in the market launches and how we're going to go about doing that. We launched, beginning this spring. And we continue throughout the year and we're going to launch in strategic markets where we see the biggest opportunity and based on the current size and scale of Starbucks' presence today. All products are going to be available in traditional CPG and foodservice channels. And we're very excited about the possibilities that this is going to create for us and for them.

Now given the final details of the closing, we now expect this deal will become accretive to the company in fiscal 2020 and which is a bit ahead of the prior guidance that we have provided of three years or sooner. And a little bit later, when Pat comes up, I know he will share more details about how you should be thinking about that in his presentation.

I want to take a moment to just recognize the partnership we've built with Nestl  in a very short period of time. It's been clear that in working together, we have a common purpose and that we're aligned on what we both want to achieve. I'm looking forward to having the opportunity to continue to work on capitalizing on this opportunity to continue to find ways to create value for both companies and to have a positive impact for the coffee industry overall.

Now in closing, I recognize that I've shared a lot over the last 30 minutes. But I think it's important that all of you understand the optimism we have for the opportunities in China and with the Global Coffee Alliance. I have no doubt that by continuing to take a long-term view in building this business, executing our plans we've laid out that we will deliver growth aspirations going forward and make our partners and our shareholders very proud. Thank you very much.

Thomas D. Shaw {BIO 15317835 <GO>}

All right. Great. So thanks, John. So now we're going to take that break. So again, time to get up, stretch a little bit, refresh and try some of the food and beverage offerings, again highlighted by Nespresso that John mentioned. So we'll be back here to resume the presentation at 4:00 p.m. Thanks.

(Break)

Hi. Welcome back, everyone. Looks like we're all taking a moment to get settled here. So to kick off the second part of the day, I'd now like to introduce our new CFO, Pat Grismer. So Pat joined Starbucks, yes, just a 5 short weeks ago. So he's gone through a lot here. He's brought over 30 years of finance and leadership experience from The Walt Disney Company, Yum! Brands and, most recently, as CFO at Hyatt.

So without further ado, I would like to now welcome Pat to the stage to discuss our growth model.

Patrick J. Grismer {BIO 15965217 <GO>}

Thank you, Tom. Good afternoon, everyone. It's terrific to be back in the category. And it's great to look out into the room and see so many familiar faces. Yesterday marked my 1-month anniversary with Starbucks. And I was thrilled because I passed my 30-day probationary period. Then Kevin pulled me aside and he said, "You know, Pat, we need to extend that probationary period by 24 hours to account for the conference today." There's nothing like a little bit of pressure to motivate you to bring your A game.

Now speaking of A game, I have to tell you, I was quite fascinated by some of the reports that were published in the wake of my announcement speculating what focus or approach I would bring as the new CFO at Starbucks, everything ranging from asset-light guy to a thinly veiled characterization as a sandbagger. Now I will speak for myself. And in the seven years that I've had the privilege of serving as a public company CFO for great, branded enterprises, I have been guided by 3 things. The first is to build a great team. The second is to champion growth. And the third is to maintain a tight focus on long-term shareholder value creation while maintaining an open dialogue with the investment community. That is my commitment. And that's what you can expect from me here at Starbucks.

So why did I join Starbucks? The answer is really quite simple. It's rooted in 3 things: the brand, the company's mission and our growth potential. Starbucks is an iconic global brand that is celebrated around the world. And what a privilege it is to be part of that. The mission is honorable. And it's underpinned by noble goals that form the foundation of a culture that is very distinctive. Who wouldn't want to be a partner? And the third is the growth potential. And as Kevin mentioned, Starbucks already has enormous scale. And yet, Starbucks has a very long runway for growth. And how exciting it is to be a partner who is going to help design the flight plan.

So it's only fitting that the theme of my presentation is about growth, double-digit EPS growth at scale. And today, I will walk you through our growth algorithm that we characterize as an ongoing growth model. And what I mean by that is that it's a growth model that can sustain double-digit EPS growth for years to come. Now there will be years where noncore or nonrecurring events and items change the profile of our growth rate in a particular year. And we will take care to clarify for you when that happens, as is the case in the current year. And with this presentation, we are reaffirming the guidance that we provided for fiscal '19 in conjunction with our Fourth Quarter 2018 earnings call. And later in the presentation, I will provide you the bridge between the ongoing growth model and fiscal '19 guidance.

So at the highest level, what this growth model calls for is annual non-GAAP EPS growth of at least 10%. This is before, as noted, noncore items to the current business and ongoing growth model. I'll share with you the building blocks of this growth model. And it's really quite simple when you think about it, comp growth, unit growth and margin management, all underpinned by a disciplined capital allocation model that is instrumental to our ability to drive that growth and to deliver compelling shareholder returns.

So I'll take each one of these in turn, starting with comp growth. And as a reminder, when we report comp growth, it's for our company-owned stores. And here, I've segmented it into our 2 key markets, the 2 key markets you've heard about today, the U.S. and China. So globally, we're expecting comp growth of 3% to 4%. That is led by our largest market, the U.S., at 3% to 4%. This includes a roughly equal mix of transactions, pricing and average spend growth. Now for China, we're expecting a more modest rate of comp growth, 1% to 3%. And that may seem low to you in the context of what this business has delivered historically and what we all know to be the potential that China has for the long term.

But there are 3 factors contributing to this relatively modest rate of comp growth. And you heard John talk about these. Sales transfer, which is deliberate and planned because of how aggressively we're moving to capture that first-mover advantage, to lay claim to those premium locations in cities across the country. So we expect there's sales transfer that will weigh on our comp growth.

Competition. We have to acknowledge that competition is intensifying. Now it's our belief that, that competitive impact is relatively short-lived because of the strength of our brand proposition in China.

Then third, the economy. The Chinese economy continues to grow at a very robust pace. But it has softened in recent years. And we're seeing that in our comp. Now John also mentioned that with the acquisition of East China, East China will enter our comp base starting in the Second Quarter. And we do expect that, that will dilute, to some extent, our comp growth for the overall market. But I want to make very clear that even as we set a modest expectation for China comp growth, our enthusiasm for the long-term potential of this business is undiminished. And our confidence in the strength of our competitive position is undiluted.

So let's move to the next building block in our growth algorithm, net new unit growth. And again, I'm segmenting it into our 2 key markets, U.S. and China. Globally, we're expecting robust new unit development -- net unit development of 6% to 7%. In the U.S., we're expecting 3% to 4%, which, when you consider how heavily penetrated the U.S. market is, highlights that for Starbucks, we still see significant opportunities to expand our footprint. And as Roz described, we're taking a very careful look at where there are compelling opportunities to increase the representation of the Starbucks brand. And that's what's guiding our development effort. Within the U.S., 3% to 4%, that equates to about 550 net additions annually. So that incorporates the effect of store closures as we optimize our portfolio. And about 60% of those will be company-owned and operated. In China, we're anticipating, again, aggressive growth to capitalize on the potential of the market, mid-teens growth. That represents a pace of about 600 new store openings annually.

So let's move to the next building block, which is revenue growth, which is a composition of comp and units as it relates to our retail business, our more dominant business. That drives enterprise revenue growth of 7% to 9%, with the retail business contributing 8% to 10%. Then you can see channel development delivering a more modest pace of growth at 4% to 6%, an important part of our business that is now strengthened through the Global Coffee Alliance. We do expect channel development will contribute more significantly to total revenue from fiscal '22 onward, given the expected ramp-up in international market penetration through our partnership with Nestl  .

So let's move to operating income margin. And here, the way I'd like to talk about it is in terms of the operating income margin that we are confident we can deliver. We're expecting operating income margin to be relatively stable in the range of 17% to 18%. Now because we are anticipating fiscal '19 to be a relative low point, given the year 1 impact of the Global Coffee Alliance as well as the annualization of tax reform-related investments in our partners, we're expecting slight margin accretion over the ensuing two years.

Now as noted on the page, this is a complex equation, a number of factors, some accretive to our margin, some dilutive. And to us falls the responsibility of finding that right balance, in the interest of strengthening our brand for the long term, to drive the growth and realize the full potential of our business. So on the accretive side, absolutely, we're anticipating our comp growth to support meaningful sales leverage. At the same time, we're expecting to continue to leverage our global supply chain infrastructure to yield efficiencies. You also are aware of the commitment we have made to realize efficiencies above the store in G&A. And that will contribute to margin improvement over the next couple of years. Then finally, you heard Roz talk about what's happening at store level, store level productivity efforts to drive efficiency, to create capacity, to accommodate transactions particularly at peak. So a number of things we're doing between sales driving and process engineering to unlock margin opportunity. But importantly, that also creates room for us to make the very necessary investments to further strengthen our brand and drive for long-term growth.

So what's diluting our brand -- or our margin performance in the next few years? Wages, particularly in the U.S., whether as a consequence of legislation or competition and certainly from the standpoint of continuing to do what we have done to invest in the employment value proposition that allows us to attract and retain the very best talent that is instrumental to our ability to deliver a highly differentiated third place experience that is at the heart of Starbucks.

Product mix. As we expect to continue to build our food business, that adds to our absolute operating profit. But it does have a dilutive impact on our operating margin percentage.

Strategic investments. Many of you had the opportunity to experience the Reserve Roastery store. That's an example of a strategic investment that we are making to further elevate our brand or, as Kevin said, to amplify our brand in ways that, again, strengthen our point of competitive difference and help forge the way for continued growth. Another example would be new equipment platforms that underpin the product innovation that is going to help to fuel the top line.

Investments in digital, the fourth place that, again, contributes to that steady top line performance. So very deliberate, very focused, highly disciplined strategic investments that are an important part of driving the long-term growth of the company.

Then finally, commodities. Given where coffee prices are at today, we do expect that coffee prices will creep up over the next few years. And that is baked into our model. So again, a complex equation, multiple factors that we are managing carefully with a view on how we're going to set up our brand and the business to maximize our full -- and realize our full potential.

So let's talk about cash because, as I mentioned before, I want to talk about and share with you our thinking around capital allocation. And it starts with the amount of cash that we generate from our business. The fact is, that our business generates a very significant amount of cash. In the last three years, our operating cash flow has averaged \$4.5 billion. And we expect in fiscal '19 that we will generate more than \$5 billion of operating cash flow.

And so that raises the natural question of, what do we do with all that cash? And that's where disciplined capital allocation comes into play, to fuel growth and fuel returns.

Long term, our capital generation does come primarily from operations. But I would highlight that we top that up with moderate new debt issuances, consistent with our leverage cap at 3x lease-adjusted EBITDA and a minimum credit rating target of BBB+, Baa1. You can see that we're expecting our capital allocation to be fairly evenly distributed across each of 3 categories.

First, investment, investment in growth, because we see the opportunity to realize for our shareholders significant returns from these growth investments. And I'll talk in a minute about the top category of investment for us, which is new store development, which is concentrated in our key markets of the U.S. and China.

Second would be a competitive dividend. Our earnings payout ratio is in the range of 50%. And that has yielded a dividend yield or return of about 2%, which we find very compelling in the context of our growth rate as a company. And we know that our shareholders appreciate this return.

Finally, ongoing share repurchases. Now what I mean by ongoing is what we believe our ongoing growth model will sustain outside of any noncore or nonrecurring sources of cash that allow us to top up those share repurchases, as is the case in '18, '19 and '20. So we expect, on an ongoing basis, this growth algorithm will support an EPS benefit from share repurchases of about 2%. And that's after interest at the 3x leverage target that I mentioned earlier.

So let's talk about new store development, because as I mentioned, we see significant return opportunities. And we -- I will have to say, just based on my experience and what I'm learning about the return model that we have in the U.S. and China and how that compares to what I've seen before, these are quite enticing returns. You can see less than a 2-year cash payback on new units that we built in the U.S., less than 1.5 years in China. And there are 2 factors that are contributing to these extraordinary returns. The first is that you can see, in both instances, a very high sales-to-investment ratio of approximately 2x. You also see very high cash returns. And it's the powerful combination of these 2 factors in that investment return equation that yield overall returns on investment that are nothing short of tantalizing, unlike anything I've seen in this space. And that's why we give such preference and priority to that part of our capital allocation model, to unlock these returns for the benefit of Starbucks shareholders. And I love the fact that this investment not only creates value. But it drives growth.

So let's add it all up. Revenue growth, 7% to 9%; operating income growth of 8% to 10%. And here, you see that slight accretion in our operating income margin percentage that we're expecting in the next few years. Laddering up to EPS growth of at least 10%, double-digit EPS growth at scale. And again, this is an ongoing model that we expect will sustain for the foreseeable future. And as I mentioned, significant noncore items and events change the shape of this model in a year where we have those kinds of events. And a great example would be the Global Coffee Alliance. So I'll talk about that just a little bit further, building on what John shared earlier.

What you see here for fiscal '19 and '20 is the impact on consolidated financial metrics versus prior year. What we're anticipating in fiscal '19 is that we will lose about \$500 million of revenue, taking segment revenue for channel development from \$2.3 billion to \$1.8 billion. On a consolidated basis, that dilutes our revenue by 2% to 3%. The impact to operating income is more pronounced in the range of 7% to 8%. However, given the strong cash proceeds, after tax, related to the upfront

payment as part of this agreement with Nestl  , we are in a position to upsize share repurchases to an extent that limits the EPS impact to 1% to 2%.

Then in fiscal '20, given the continued benefit from share repurchases and how that flows over from '19 to '20. And we're lapping the income statement impacts of the alliance, we're seeing accretion to EPS. That is earlier than we had anticipated, as John had mentioned. And that's entirely a function of the final accounting treatment for that upfront payment and how that enters our revenue stream.

So I mentioned to you that I was going to provide a bridge between what I've described as an ongoing growth model and what we have guided for fiscal '19. And I also want to share an outlook as to what that looks like in '20 and '21. So for fiscal '19, what you see here is a conceptual reconciliation, highlighting the puts and takes that bridge that ongoing model to the guidance that we had given, that we are reaffirming today.

So you see streamline items and events like acquisitions, divestitures, investments, restructurings. There's a lot of noise in the numbers. But you net it all out and what you see is, that our fiscal '19 results will be lower than that ongoing growth model. And again, the numbers here are consistent with previous guidance. But the reverse is true in fiscal '20 and '21.

So here is a high-level outlook of what we expect those two years to look like on average. We're getting the benefit of share repurchases and continued contribution from our G&A efficiency efforts to yield EPS growth of at least 13% when you look at the two years combined on average. Now given the cadence of our share repurchases, we would expect fiscal '20 to be above that number and fiscal '21 to be below.

So we're very excited about this ongoing growth algorithm that sustains double-digit EPS growth for years to come. And we're confident that the plans and initiatives that the team has shared with you today will unlock the brand's potential and deliver the results that I've talked about.

Again, I'm excited to be back in the category. I look forward to spending time with many of you. And at this stage, we're thrilled to take your questions. And so I will invite to join me up here on stage our presenters, Kevin and Roz and John as well as our Global Chief Marketing Officer, Matt Ryan. Thank you very much.

Questions And Answers

A - Kevin R. Johnson {BIO 3773960 <GO>}

Okay, questions. Do we have microphones for the questions? Yes. Let's start over here, Kev.

Q - Robert Marshall Derrington {BIO 1517514 <GO>}

Bob Derrington from Telsey. Two-part question. One, on -- as we think about Uber Eats in the U.S. and the opportunity there, how do we think about the economics or the contribution? Obviously, positive to earnings. But how should we think about the margin impact of those sales as they come into the pool? Then I've got 1 quick follow-up.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Okay. Roz, do you want to take that?

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

I'll take that. So that's a very good question, because we are monitoring that in terms of the size of the ticket in reference to the price of delivery. And one thing I will say is that we are seeing an expanded ticket because of the number of items that are in the order. So we're monitoring that. The second item that I will tell you that we're seeing in this work that we're doing is that, that number is varying. If we're in a very dense market, we're seeing a really good ticket and really good performance. In less dense, we're not seeing as good performance. So that's one of the things that we're monitoring as we roll out. We're rolling out initially in some of the more dense urban metro markets. We'll learn more. And then we'll come back to you and be able to say really what we're seeing and really pool that together. But it is something careful that we need to really watch that.

Q - Robert Marshall Derrington {BIO 1517514 <GO>}

As the second part of that question, as we look at that incremental -- the delivery, we know there were some issues with Mobile Order and Mobile Pay at one time. How do you avoid those kind of issues overloading a store location that may not have the capacity?

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

Absolutely. So a couple things we're doing. We have put a tremendous amount of focus on the software integration piece. And so at this point, we are integrating the software. When you see in most QSRs, you'll see several different iPads in the back, we will not have that. It will be 1 ordering system where it comes in. And so that work is happening right now as we go national.

Q - Robert Marshall Derrington {BIO 1517514 <GO>}

So the stores have the capacity in the urban markets? Or will there be a delivery kitchen?

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

Right now, there's capacity to produce in the store. And so we're producing right there behind the bar. It's working.

A - Kevin R. Johnson {BIO 3773960 <GO>}

I would just also add. We are open to learning from the Star Kitchens that John talked about in China. So that is also a tool that we could use in the U.S. But I think as Roz says, it's early days. And I think the work that they've done for us to really learn and adapt is the right work.

Is there a microphone? Okay, over here, then we'll come back to the middle.

Q - Jeffrey Andrew Bernstein {BIO 7208345 <GO>}

Jeff Bernstein from Barclays. Kevin, as we think about the U.S. business, or Roz as well. But in terms of traffic, I mean, we look back over the past couple of years and traffic has been flat to negative. It seems like that's a challenge, whether it's capacity constraint, competition, cannibalization. It seems like there's a variety of factors, let alone the macro. But I know in your comments earlier, you made it sound as if, last quarter, you saw an uptick in pretty much every metric. And that seemed to have continued this quarter. So I'm just wondering, when do you presume you'll get back to consistent positive traffic? It sounds like the 3% to 4% comp guidance includes 1/3 effectively positive traffic. So it sounds like you're expecting that over time. But is that something you'd expect in fiscal '19? And of all the initiatives that you talked about, like which -- could you just prioritize maybe the top -- couple that you say would be the driver that would get you back to traffic positive whenever you expect that to happen?

A - Kevin R. Johnson {BIO 3773960 <GO>}

Yes, let me start and then I'll let Roz add to this. I think, number one, the transaction growth we see in our transactions, if you look at the overall food and beverage industry or restaurant industry, transactions have been down in the restaurant industry. We've outperformed that. But that said, we still have been slightly negative -- well, I think 1 point negative on transaction growth last quarter. The things that start to change that certainly are the experience in the stores. We see that in the morning daypart, we are growing transactions in the morning daypart because of all the work that went into increasing throughput at peak. And then we lose some of those transactions after 2:00 p.m. The reason we were losing some of those transactions after 2:00 p.m. was because a lot of the cleaning in the store was happening after 2:00 p.m. And as Roz took you through, all the initiatives that the team has been driving are starting to fix those things. So for us, we have to stay very focused on the initiatives that Roz outlined: the store experience, beverage innovation and digital. We think those are the keys to transaction growth. Roz, I'll let you add.

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

I think you nailed it, Kevin. Then I think this other piece around delivery is sort of helping us to flatten out the business over time. And so we're watching that carefully as well. And that's not in our number for this year. But we believe that, that's some upside as well as we go forward with delivery.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Let's go here in the middle, if we can get a microphone over here.

Q - Unidentified Participant

One of the things you were talking about was beverage. Cold beverage seems to be kind of a subtheme with regard to the U.S. comp. Frappuccino having been a drag. And some of the cold beverage seemingly picking up steam here. Are there any -- when you look back in the last year, is -- are you going to think about the below average or below what your guidance is in terms of comps as a little bit of a cold beverage problem that you're now past? And if that's the case, is it the Frappuccino drag is diminishing now and you're beginning to really get to scale on some of these other platforms? And maybe there's some numbers you can put on that.

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

Yes, yes. So I don't know if we can go deep into the numbers. But one thing I will tell you is that as we saw the Frappuccino business in terms of the ticket that it delivers to us, we are seeing a really nice movement and a replacement in some of those -- in -- per beverage and what we're seeing in the cold platform. I will tell you that we also, in the Fourth Quarter or second half of fiscal year '18, we did premium Frappuccino. And so as we elevated the Frappuccino business itself, it did well. So we're not moving away from the Frappuccino drink. We're just adding to that cold platform and really responding to what the customer really wants. So there's no movement away. We're trying to elevate the Frappuccino business. There's still demand for it. But we're trying to take that up. So in terms of, are we out of the water in that position, there's competition out there with Frappuccino. And we're just trying to elevate it and then add to the cold platform.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Yes. The evidence last quarter was the fact that of the 4percentage point comp that we delivered, 3 points of that came from beverage. And a lot of that has been the work that Matt has been leading to really reshift the way that we're driving marketing. And maybe, Matt, you want to add to -- a little bit to the focus on how we're driving demand for the beverage industry.

A - Matthew Ryan {BIO 18012513 <GO>}

Absolutely. We're focused very much on transactions. And we have 2 levers. We have this incredible advantage with the number of relationships we have with the customers in Starbucks Rewards, adding to that now additional relationships, digital relationships that are non-Starbucks Rewards. That allows us, in general, compared to everybody else in our sector, to have a lower spend on paid advertising, which is important. That said, we continue to leverage paid advertising when we need to. So for instance, in a season like the current one when we have a lot more occasional customers coming in for the holidays, we're able to be very targeted. And we've gotten more sophisticated in our marketing as we were able to do closed-loop measurements, where we can tell when somebody has seen an advertisement, especially digitally, what happens to the behaviors in the store. And we've gotten more and more refined in terms of knowing what messages work with what customers. And that's making our marketing performance something that we can be a little bit more confident in moving forward.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Let's go over here.

Q - Sharon Zackfia {BIO 4804954 <GO>}

Sharon Zackfia with William Blair. Thank you for the detail on the margin expectations. I guess, one of the things I was surprised was missing was geographic mix shift, given that China, in particular, is so high margin. Is the inference there that China is going to normalize in its margin structure, therefore, not be a tailwind?

A - Patrick J. Grismer {BIO 15965217 <GO>}

We are not anticipating a material shift in margin progression between the 2 markets. The reality is that even as China will continue to grow its store footprint at a rapid pace compared to the U.S., the U.S. business will remain the dominant business. And therefore, the margins of the U.S. business will continue to shape what our enterprise level margin looks like. Bear in mind that when we talk about operating margin percentage, that is a function not only of store-level economics but takes into account our above store spending in terms of G&A and also factors in the profile of our channel development business. But we are not expecting between those 2 businesses to be a material difference in how the margin picture progresses over the next few years.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Kev, right here in the middle.

Q - Sara Harkavy Senatore {BIO 16508078 <GO>}

Sara Senatore, Bernstein. I wanted to ask about the MSR program in the U.S. In particular, one of the things that you pointed to were spend per member growth and also then the reward enhancements. And I was hoping to get a little more color on both. The -- it looks like the spend per member, the growth has kind of slowed maybe sort of meaningfully in the last couple of quarters. And I was just wondering if that's right and if it has to do with sort of the mix or just in terms of who the additional members, what they look like or if there's something else going on and if you can reaccelerate that. Then in terms of the reward enhancements, it sounds like maybe the rewards will be richer. So are there margin implications for either one of those?

A - Kevin R. Johnson {BIO 3773960 <GO>}

Matt, do you want to take that?

A - Matthew Ryan {BIO 18012513 <GO>}

Sure. With regard to the sort of spend per member issue, we continue to see growth in spend per member, which is healthy in the single digits. Now a couple years ago, we had the introduction of Mobile Order and Pay layered onto a step change in personalization that happened all at once. So we saw tremendous growth for a while in spend per member. What we're continuing to see right now is accelerated new

membership growth, which is terrific, because the more people we have digital relationships with, the better for us as well as continued growth at the time and spend per member. Now we have a lot of things we're doing to focus on keeping that going with technology and marketing innovation. So we're very confident that we're going to continue to see growth in spend per member. With regard to the program changes moving forward, the big set of changes moving forward will come next quarter when we will have a multitier redemption offer. And what that means is you'll be able to redeem your Stars on a lot more things. And you'll be able to start redeeming those rewards much faster than you currently do in our program. The way that we've structured this will actually help from a margin perspective as we are able to offer different tiers on different products, including some higher-value products, that will, net-net, in a pro forma, help margin moving forward.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Let's see. Let's go over here.

Q - Unidentified Participant

Could you please talk about what you anticipate to be the customer profile and the order profile of delivery and if there are any differences between what you're expecting in the U.S. and China? And also, would you ever have dark stores, I guess, if delivery were (important)?

A - Kevin R. Johnson {BIO 3773960 <GO>}

Let's have John start with China and what we've experienced with Starbucks Delivers in China. And then maybe, Roz, you can add what we learned in Miami.

A - John Culver {BIO 15817924 <GO>}

So I think for us, we're just now getting some traction on delivery in China, first off. So any of the results are still coming in to really validate it. We are seeing an initial uptick in the morning, all right? So that's usually a slower period in our business in China. We're seeing a higher attach, which is good news. The customers are generally millennial customers working in offices. But also, we're seeing people at home ordering delivery as well and people ordering larger-ticket -- a total ticket that's larger than the average spend in a store. So we're going to continue to ramp up the delivery program. I think the things that I hit around building the awareness, gaining trial is going to be a big unlock. We've got some work that we're doing with Alibaba to raise the awareness within the apps themselves and their access to Starbucks Delivers. Then when you look at it expanding beyond our Starbucks stores into the Hema kitchens. And we've opened 2 Star Kitchens with Hema markets, one in Hangzhou and one in Shanghai. These are kitchens that sit in the back of the house. And it's a dedicated area where we're basically producing Starbucks beverages that the Ele.me riders that come from that store grab the Starbucks order as well as whatever the customer is ordering from the supermarket. And so we see big opportunity with that. And we'll continue to roll that out. They do about 10 million customers a year right now. So I think we're going to unlock opportunity to reach those. Then in addition, when you look at the apps across Alibaba, Kevin quoted a number of over 600 million active users, we will gain access to those

customers. And we're working through what that's going to look like and how we can get those customers to attach into Starbucks and become part of our rewards program and part of the delivery program or order through the virtual store.

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

And on the U.S. side, I would say that we were in about 200 stores in Miami. Our performance was stronger when we were near like large office buildings or hospitals or some type of controlled facility. We did see food attach in that business. We did not -- we have not applied any marketing to it at all. It was all by pulling up the Uber app and then noticing that Starbucks was there. So we've got work to do to figure out, well, then who purchased and then follow through to really get the qualifications of who's purchasing. But right now, we know at least physically where those orders were going to. And we know what kind of ticket they were ordering.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Yes. I think average ticket in the Miami pilot was something like 2.5x to 3x what we see across our business in that range. That would be a range of orders. Some would be very large. Some would be single beverage. Let's go here in the middle.

Q - Brian John Bittner {BIO 17258322 <GO>}

Brian Bittner with Oppenheimer. So the new U.S. comp outlook is around 3% to 4%, slightly different than what it was. And 1% to 2% coming from digital, which I think you guys have talked about historically. So where does the other 2 points come from strategically when you think about the bottoms-up build?

Then just separate from that, it looks like you have about 10 million digital relationships outside the MSR program. What can we -- how can we think about what you're trying to do to convert those into higher, more frequent customers moving forward? Because I think this is at the largest that pool has certainly ever been.

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

Brian, I'll start off. And then, Matt, if you wanted to add anything. First of all, when you look at the comp performance, you're right about 1% to 2% from digital relationship. But then we have a little bit in there for price. Maybe -- we've always said about 1% to 2% on price. Then there's beverage innovation that's in there, new beverages that are in there. And so like Kevin said, our comp performance in the Fourth Quarter, 75% of it came from beverages. So when you put that combination together, that begins to bring that -- bring the total to about 3% to 4%. And Matt, you might want to talk about the second half of the question.

A - Matthew Ryan {BIO 18012513 <GO>}

Yes. So with regard to the -- specifically the question again.

Q - Brian John Bittner {BIO 17258322 <GO>}

Yes. It was just -- you have 10 million digital relationships.

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

The digital relationships. Right. Yes. Sorry about that.

Q - Brian John Bittner {BIO 17258322 <GO>}

And I was just wondering how you convert them.

A - Matthew Ryan {BIO 18012513 <GO>}

So the way to think about that is that those people represent the top of the funnel for us, because there are people that haven't yet joined Starbucks Rewards and we just begin to market to. Once we learn more about their behaviors and their histories, once we learn more about what they respond to, we're going to see more and more effort as we enable marketing that's more targeted and personalized. We have not really begun that yet, that is to come. But like we have already seen is the marketing we've done to convert them into Starbucks Rewards members has been one of the largest contributors to the acceleration of growth of the rewards program. So we know that it's a group of responsive people who engage with us. And then the trick is to get them to engage more through mechanisms like loyalty.

Q - Brian John Bittner {BIO 17258322 <GO>}

Can I just ask, what's restricting them from moving into the MSR program? Or what is the biggest hurdle from getting them into the MSR program, those digital relationships that you have?

A - Matthew Ryan {BIO 18012513 <GO>}

The biggest hurdle is to create awareness and understanding of the program. So people are always on a journey to learn about it. And once we get somebody -- people to understand the benefits of the program. And certainly, with the introduction of the multitier redemption coming very soon, there will be more reasons to join. And we think that we'll see an acceleration in membership coming from that group of customers into the future.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Let's go over here.

Q - Unidentified Participant

I have 2 questions. The first is, I think you've talked in the past about when you convert customers onto the MSR program, you get a 30% lift in their frequency. I guess, does that number still hold? And do you see that when you convert to the partial digital relationship? Or do you expect to see that when you convert to the sort of full MSR? I guess, how much of that lift have you seen when you -- on that 10 million customers?

A - Matthew Ryan {BIO 18012513 <GO>}

Sure. We continue to see within the MSR program the same kind of incrementality that we've always seen. So that story has not changed at all. We continue to monitor that very carefully. With regard to those other customers, the people with digital relationships who have not yet joined MSR, it's not the same customer. These are people who have not yet engaged or not respond to the loyalty mechanism. So you don't see that same kind of uplift upon somebody joining that. That takes more time and more work to get them there. But they become that large pool that you start to market to and bring people in over time.

Q - Unidentified Participant

But you still expect that lift to kind of be similar to what it's maybe been in the past?

A - Matthew Ryan {BIO 18012513 <GO>}

I wouldn't take the 30% incrementality number that you've been using for MSR over that when somebody signs up for a digital relationship with us. That's not proven yet. But what we'll see is more and more of those people, when we do convert them into the SR program, having that kind of incrementality.

Q - Unidentified Participant

And I just have 1 other question. Just in terms of what you've seen in China with delivery, are you seeing most of your customers access Starbucks Delivery. And I know it's early. But through the Starbucks app? Or are you seeing them use third-party apps? Then as you apply that to the U.S., do you expect them to come in and use Starbucks app or a third-party app? And I guess, it begs the question of, do you view Uber Eats as a competitor to the Starbucks brand or not?

A - John Culver {BIO 15817924 <GO>}

For us, in China, we've seen the partnership with Alibaba, obviously, customers that frequent the Alipay app, which is one of the most frequented apps in all of China, use very heavily. But they're also using the Starbucks app. They can also frequent delivery across other Alibaba apps as well. We don't see it through other third parties because we haven't built those relationships with other third parties. I think the power of the Alibaba partnership is the size and scale and reach that they have. The beauty of what we've created with them on the app side of things is that they have access, if it's Alipay, Ele.me, Tmall, they can go right into that app and click on to the Starbucks icon and go right into our app. So it's a 1 click. And that gets rid of a lot of the friction. Then they can also automatically sign up for the rewards program. So the beauty of the partnership is we've leveraged their size and scale, their technological know-how and really getting into much stronger customer relationships and increasing the reach and scale for Starbucks.

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

And on the U.S. side, eventually, you'll be able to access both through the Starbucks app and the Uber Eats app. And right now, we don't really view them as a competitor. We're working together to integrate the software. And so the partnership is very strong right now. So we don't view it that way. But eventually,

you'll be able to -- once we are into complete integration, you can access them both ways.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Let's go here and see where -- let's go right here. And then we'll just move our way back over to the other side of the room.

Q - Dennis Geiger {BIO 19694619 <GO>}

Dennis Geiger, UBS. Roz, I wanted to ask you a bit more about store productivity. You talked a lot about initiatives focused on optimization, throughput and efficiency. But just can you touch a bit more around productivity throughput, the opportunity there as far as timing, the magnitude potential impact on sales, how significant this could be going forward?

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

Right. So a couple of things I'll say there is that you can't underestimate, again, when we open up this relation between the partner and the customer, we know that, that is the real opening opportunity for us. I would tell you that we think that there's upside in a few things. One, when the automation comes in for us to really get our deliveries correct, right. So all the incoming goods that come into the store will reduce waste. Then our back rooms, as orderly as they can possibly become and right behind the bar, gives us some opportunity. Now in terms of putting numbers onto it, we're still learning what the numbers are. The biggest number that we have right now because we've been monitoring it so closely is our customer connection scores. Then looking at the stores with higher customer connection scores and looking at where their transaction numbers are, we absolutely see an improvement there. So those are the hard data numbers that we have right now. And we'll learn more as we put in the automation and then turn over the dollars. And you'll see it in terms of the margin.

Q - Dennis Geiger {BIO 19694619 <GO>}

Great. Then just 1 real quick follow-up, if I could. When you talked about the comp breakdown in the U.S., food wasn't really a part of that. That's driven probably 1 to 2 points at least over the last couple of years. There's probably a bunch of different ways to slice it. But can that be upside? It wasn't emphasized a whole lot today. But can food be the upside driver to the algorithm that you just kind of touched on?

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

Yes. Absolutely. You bring on a good point there, is that we -- food is definitely an opportunity for us. Where the work that we're doing with Mercato, which is primarily, right now, an 11:00 on meal opportunity for us, basically salads, you've possibly read about it. But yes, that is configured in this number when we talk about transaction growth. And so that all comes together. It also -- just one quick thing is that the digital relationship is we notify people that we've got food and that it's expanded, we're also seeing it grow.

A - Kevin R. Johnson {BIO 3773960 <GO>}

And we can deliver it. Okay, let's go over here. Let's go all the way to the side of the room. Yes. There we go.

Q - Adam Harry Sindler {BIO 16184643 <GO>}

Adam Sindler, Unicom. On the Uber Eats versus baba, one thing is different is it looks like the Alibaba employees are actually employees of Alibaba. Uber Eats drivers are really contract people. So how do you ensure, one, that the Uber Eats driver will help sort of adhere to a brand standard for something like Starbucks? Then, two, just around safety, right, like it's easy to tamper with a beverage that isn't locked or something like that. How do you sort of ensure that it stays safe throughout the process?

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

Yes. So one of the things, just being in Miami, watching the process come through, our partners are actually seeing repetitive Uber drivers. So they're getting to know that Uber driver. And they're treating them as a partner. And so they're having -- they're building relationships in those localities. Then also to some of the work they were doing with Uber is to really address that situation in terms of what we believe food safety is and how the quality we want to maintain over a period of time. And that's why we're doing this work with Uber. And so we're having those conversations. And also, to the next leg to drop and the work for us to do is the packaging piece. And so that our packaging work is progressing as we learn more. And so I will say that China has -- we're adopting some of the work from China in terms of the packaging that they have. And so you'll see that be ongoing as we roll this thing out.

A - Kevin R. Johnson {BIO 3773960 <GO>}

I'll just say, even in the pilot though for food safety, we put a tamper seal on everything that was delivered to a customer. So if that seal was broken, the customer would know if they have some concern perhaps. Let's go over here, Kev.

Q - Nerses Setyan

Nick Setyan, Wedbush. I wanted to maybe revisit some of the headwinds on the margin you talked about, maybe get some more details there. When would you expect the wage headwind to maybe peak? Is it 2019? Is it 2020? The product mix, obviously, that seems to have improved with the larger beverage contributions. So that was a little surprising to see it in there. The strategic investments and, obviously, commodities, when are you thinking that we're going to see the headwinds in coffee? Particularly as the beverage has improved the contribution and with the G&A efficiencies, perhaps we were a little surprised to see only such a tiny bit of leverage from revenues to operating margin.

A - Patrick J. Grismer {BIO 15965217 <GO>}

Yes. Well there's no denying the fact that the U.S. hourly wage pressure is the most significant dilutive factor in that margin equation. Based on what we see happening by way of state legislation as well as competitive pressure for the talent that is so critical to the third place experience that we provide as well as, as I mentioned, the value that we place on having a competitive total compensation or total rewards

package that attracts and retains that great talent. So given the importance of that, we see sustained investment in that part of our P&L in order to protect that aspect of the experience. That is the #1 contributing factor to what I qualified as the dilutive impacts. But I would also highlight the continued increase in strategic investments, given their importance to driving the top line result. So whether, as I mentioned, new equipment and platforms, like the rollout of Nitro to provide the beverage innovation that forms a key part of driving the transaction growth and the growth in average spend, continued investments in technology to drive that point of difference as it relates to how we form and build on and leverage the customer relationship, all of those have a tendency to weigh on margin to mitigate what we would otherwise expect to be the accretive impact of sales leverage, to start with. But also all of the outstanding initiatives that are happening at store level as well as above store to drive greater efficiency. It is a complex equation. But much of what weighs on margin actually contributes to the top line performance that we're anticipating.

Q - Nerses Setyan

Just as a follow-up. Is there any flexibility there? So just in case, let's say, beverage contribution declines within the comp, I mean, can we pull back on some of these investments to maintain double-digit EPS growth? Or is this a very rigid algorithm? So if we do fall off by 50 or 100 basis points in the comp...

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

Maybe I can address some of that. So just to give an example, for the planning and replenishment, that's a software investment that's a onetime investment to bring in, to automate all of that work. If we need to slow down all of the items that we need to automate, we can do that, because they're all independent of each other. So we'll -- we can invest, look at performance, invest and look at performance if we needed to. So a lot of the tech investments are the same thing. Now I will tell you, the two are intertwined, because when we get these investments and we see the improvement to make reductions in other areas, that can fall to the bottom line or enhance the experience in the store. So they are intertwined. So -- but we'll -- we can manage it carefully. There's not a lot of long-term, consistent, hard, like multiyear -- we just completed a new platform investment at the company that was multiyear. A lot of what we're doing right now is not as multiyear as what we have done in previous years, if that makes sense.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Over here. Kev, over here somewhere. Just got a question. Yes, right here.

Q - Priya Joy Ohri-Gupta {BIO 15889787 <GO>}

Priya Ohri-Gupta from Barclays. Pat, I was just wondering if we could sort of clarify the point on leverage really quickly when you talked about sort of operating around the 3x level. Before the presentation in June, you guys had talked about operating inside of 3x. So sort in the 2.6x, 2.9x range. Then as we think about the cadence of share buybacks and the opportunity to sort of hit that number, should we expect that to be sort of loaded into 2019 where you sort of get to that number? Or will it be sort of multiyear?

A - Patrick J. Grismer {BIO 15965217 <GO>}

Yes. Thank you. So the way we think about leverage is that the 3x represents a cap. And the credit ratings represent sort of a floor, if you will. So we would not exceed the 3x lease adjusted EBITDA. And we would maintain a minimum credit rating of BBB+, Baa1. And so that gives us a range within which to work. As it relates to the cadence of share repurchases, as you know, we have very heavy share repurchases in 2018. 2019 started off with a very significant ASR. We would anticipate the balance of share repurchase activity against the \$25 billion total shareholder capital return goal to be more heavily weighted in '19 and '20. The '21 benefit is more of a carryover benefit from the share repurchases completed in fiscal '20.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Thank you. Let's go over here. We'll take 2 more questions. So maybe over here. Yes, right here. Microphone. Then we'll go over here on the side of the room.

Q - Karen Holthouse {BIO 17433865 <GO>}

Karen Holthouse from Goldman. One quick guidance clarification and then a question. When you were talking about unit growth, should we be thinking about the 550 in the U.S. and 600, as those are the ongoing sort of absolute unit targets? Or should we be thinking about percentage unit targets?

Then just on the overall algorithm, presumably over the next three years, there's going to be some pretty meaningful G&A savings that hit that corporate and other segment. But you're still guiding to a pretty constrained overall operating margin range. Is the offset that you expect continued margin compression in the Americas segment? Or is there something I'm missing?

A - Patrick J. Grismer {BIO 15965217 <GO>}

So first, on the unit growth, we articulate the growth model in percentage terms. And then I mentioned the 550 and the 600 as representing averages, if you will. But I would think more about the percentage growth and our ability to sustain that over time. I just wanted to give another point of reference in terms of what that might equate to by way of units. As it relates to margin progression and the role that G&A plays, we do expect the results of the streamlined work to continue to deliver benefits across the next three years. But really, as a consequence of some of those dilutive impacts, you're seeing then a tempered effect from those streamlined efforts in terms of how they can further support margin. But I think an important thing to keep in mind here is that the margin performance is, to a large extent, tied to what we expect our comp performance to be. So we do expect sales leverage from that range of 3% to 4%. But we need something closer to 4% to see a sustained margin expansion from sales leverage as against some of the offsetting pressures. So you would have to see a sustained closer to 4% comp to see more meaningful margin expansion over that period of time. I don't know if that answers your question.

Q - Karen Holthouse {BIO 17433865 <GO>}

Is that fair for the U.S.? Is that globally or fair also for the Americas segment?

A - Patrick J. Grismer {BIO 15965217 <GO>}

So that -- so the guidance is global in nature. As I mentioned before, we don't see a significant difference over the next three years in terms of segment-level margin progression and the extent to which those play into what we're seeing or expecting at the enterprise level.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Okay, we'll take the last question over here somewhere. Here, let's go here and I'll go, John.

Q - Mark J. Sptel {BIO 18945772 <GO>}

Mark Sptel from Schaper, Benz & Wise Investment Counsel. Just want to dig in on the G&A piece, just a little bit more, Patrick. There were some comments, sort of guidance given at one point that the G&A, as a percentage of revenue, was about 1 point higher than it should be. Just want to know if those are your thoughts and if that 1-point improvement is baked into the improvement that you had on the slide from the streamlined activities. And I'll just ask my second question right away. Digging into the comp anatomy a little bit more that's crucial for margin expansion or at least maintaining margin, how important or critical is transaction growth to maintain the 17%, 18% or growing the margin?

A - Patrick J. Grismer {BIO 15965217 <GO>}

Thank you. So I'll talk to both of those points. First, with respect to G&A, what we had communicated by way of a G&A savings target over the 3-year period is working and our long-term growth model. The impact of that is however mitigated by some of the dilutive impacts that I've talked about. So that is in there. In terms of my familiarity with that road map, that is something that I will be spending time on in this next year. So I have not yet had the time to dig into it, to the extent that I will, to inform, I think, a better point of view -- a stronger point of view on how we are set up to deliver against that. But we have incorporated that into our long-term growth algorithm. With respect to the composition of the sales comp and how much we're expecting by way of transactions, the importance of transactions is that we would expect the preponderance of incremental transactions to be beverage transactions, which carry a higher margin. And so that's why the transaction component of that base 3% comp is important in terms of the role that, that plays to provide the sales leverage necessary to help offset some of those dilutive effects that I've talked about.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Okay, we'll take the last question here, John, since you were kind enough to let Mr. Culver use you as an example for social gifting, you get the last question.

Q - Unidentified Participant

And I got my black coffee outside.

A - Kevin R. Johnson {BIO 3773960 <GO>}

That's right. It's perfect. Did we send John his?

Q - Unidentified Participant

We've been e-mailing back and forth about specifically what he wants. But yes, it will be something. And I'm not kidding about that. Okay. So -- and thank you, for an external client, for kind of involving us in that chat. So anyway we're having a good time. So thank you. And I do appreciate it. First, Roz, a question for you. I mean, you kind of tucked into your presentation hitting 1/3 of the stores in two years on the renovation strategy. I mean, you obviously -- a peer of yours. I mean, it's kind of like a very big part of the investment case of remodeling stores and adding capacity and digital functionality, what have you. So can we talk about how big of an idea that could be for Starbucks in the U.S., I mean, whether from a top line perspective or a margin perspective and then continue to talk about what the opportunity is for the other 2/3?

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

Sure. When we think about our renovation strategy, our #1 priority in that is to bring forward the equipment innovation. That will enable the beverage growth and the beverage innovation that we talked about. Now, typically, when we have to put in a new piece of equipment, it causes us to renovate behind the bar. So that's our first priority. The second priority is to incorporate different components of the need state of convenience. We'd like to do some work to remodel the area where MOP is and the landing spot where now we're getting into more convenience with pickup and delivery in our stores. So that's the second priority, again, fueling the top line. The third piece is sort of the decor piece. And so decor, to make sure that, that third place is maintaining exactly what we want in terms of the look and the feel of the stores. I will tell you, what's different in this is that we had typically gone to -- straight to a furniture improvement, right, or the lighting. And this time, we're going for functionality that grows our beverage innovation, that changes our transaction position. So that's the difference in this. And that's why it's so important. The last thing I will tell you is bringing on new formats. And so we're learning a lot more about -- we have a large percentage of caf  s. And we are looking at opportunities for total MOP stores in certain areas, small units, more drive-throughs. So looking at the throughput and capacity of a building. Then we have some buildings that are actually just too large. And so we're looking at that as well. What I hope you see when we finish this work is that we've almost created an ecosystem in 1 area of a store. So if you're a person that likes to pick up fast or you need to sit one day, the stores are 2 miles apart. You can decide which store you want to be in. So that's how that format piece will come forward.

Q - Unidentified Participant

And two years ago, maybe four years ago, we talked about the premiumization of Starbucks and potentially adding a lot of reserve components to the stores. I mean -- but that's, I guess, not necessarily a '19, '20 initiative or that would be done more on a one by one?

A - Kevin R. Johnson {BIO 3773960 <GO>}

Well keep in mind, the draft was created in the Starbucks Reserve Roastery and the Reserve stores. And much of the innovation is around cold and draft and nitro. And so that is at the center of what we are doing. I mean, that's an example of how we're elevating...

Q - Unidentified Participant

But not necessarily adding physical reserve bars, for example, like we see in certain stores?

A - Kevin R. Johnson {BIO 3773960 <GO>}

No. That's right.

A - Rosalind Gates Brewer {BIO 15034309 <GO>}

That's correct. You won't see those.

Q - Unidentified Participant

Okay. All right. Perfect. Then secondly, the question on cap. I mean, you were nice enough to kind of talk about what we needed for the Americas segment to grow margins. Your cap, it looks like, on a same-store margin basis, whatever that expression would be, you would delever on the comp guidance that you've given, given labor costs, rent costs, maybe even delivery costs in that market. Obviously, there's a lot of moving pieces in cap, there have been for years. So what do you think kind of what cap margins are when we think about a through the cycle margin cap? What should we be thinking about over the next couple of years as part of your algorithm?

A - Patrick J. Grismer {BIO 15965217 <GO>}

Well we were not and we are not intending to provide segment-specific margin guidance. We intend to keep it more at the enterprise level, recognizing that it is a function of not only our retail businesses but also our channel development business, which is changing with the Global Coffee Alliance, not to mention what sits above the segments as it relates to kind of corporate G&A. So it really is a composite of all those various things. And we think that it's most valuable and it's clearest to speak to what we believe that operating margin percentage to be over this period of time, in line with the level of comp growth that we're expecting as well as the transformation of our channel development business.

A - Kevin R. Johnson {BIO 3773960 <GO>}

Well let me ask Tom to come up and -- as we wrap up today. But we want to take the opportunity to thank all of you for the investment of time, your questions and your attention today. And I don't know, Tom, if you have anything to share about the logistics of this cocktail hour.

A - Thomas D. Shaw {BIO 15317835 <GO>}

No official logistics. We're just going to spread out here in this room. And we'll also have cocktails that will be outside.

A - Kevin R. Johnson {BIO 3773960 <GO>}

So I think we have cocktails and some food items and stuff outside. So please join us, help yourself. And we're here to spend some more time and visit with each one of you. So thank you very much. Thank you for your time.

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