

Starbucks in India

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Introduction

Howard Schultz looked over the financial data. Starbucks generally preferred a strategy of premium prices, using a menu and store layout somewhat modified for local tastes. This strategy had been working well in India. However, local and foreign specialty coffee retailers were proving increasingly formidable competitors. India's larger cities were becoming saturated. Many competitors had now turned their attention to expanding into smaller cities. India was a large, but complex market, fragmented along age, geographic, income, and demographic lines. Continued success was not certain. It was not yet clear how Starbucks should best adapt.

Starbucks' History

In 1971, English teacher Jerry Baldwin, history teacher Zev Siegel, and writer Gordon Bowker, opened the original Starbucks Coffee, Tea and Spice, in Pike Place Market in Seattle (Strickland, 1999). The store began by selling scoops of freshly roasted coffee beans. The founders named their store after Starbuck, a ship captain in Herman Melville's *Moby Dick* novel who drank a lot of coffee. A logo was designed that featured a two-tailed mermaid, to reflect the sailing traditions of the first coffee merchants. The company slowly grew to include a roaster and 4 retail stores by the early 1980s.

Meanwhile, Howard Schultz was working for a Swedish houseware company (Strickland, 1999). He discovered that Starbucks ordered more drip coffee makers than Macys, and decided to visit Seattle to find out why. Schultz was impressed with the specialty coffees for sale, as well as the customer experience the store created. He decided he wanted to join the team.

After some initial hesitation, Starbucks hired Schultz as the director of operations and marketing in 1982 (Strickland, 1999). In 1983, Starbucks sent Schultz to a housewares fair in Italy. While there, Shultz learned about the local coffee bar culture, which provided a social experience along

with mixed coffee drinks. Schultz realized the potential for introducing this concept to American consumers as a way to differentiate Starbucks from its competitors.

Starbucks agreed to experiment with Schultz's ideas in a single store (Strickland, 1999). Although it was successful, the founders were leery of expanding the store's original scope to



more locations. Thus, in 1985, Schultz opened his own coffee bar, *Il Giornale's*, which quickly expanded.

Schultz was very successful. In 1987, Baldwin and Bowker decided to sell Starbucks to him (Strickland, 1999). *Il Giornale* bought Starbucks' assets and trademark, and renamed the combined business Starbucks Corporation. From only 11 stores in 1987, Starbucks grew to 19,657 stores in 62 countries by 2013 (Starbucks, 2013).

The Starbucks Experience

Starbucks' success involved continuous quality improvement for both its menu and the customer experience. Starbucks offered high quality coffee, an assortment of other beverages, sandwiches, and desserts (Campos, 2013). The customer experience was enhanced through a warm and inviting store atmosphere with excellent customer service (Schultz & Yang, 1997), along with fast and free Wi-Fi Internet (Graser, 2013).

Brewing Trouble

In 2000, Jim Donald took over as CEO, and Schultz became chairman (McDonnell, 2011). Growth remained impressive until 2007. At that time, worsening economic conditions in the US made many consumers reluctant to spend a lot of money on premium coffee. This downturn in demand came after Starbucks' rapid expansion throughout the US with company-operated stores. In July 2008, Starbucks reported a third quarter net loss of \$6.7 million, compared to a profit of \$158.3 million in the third quarter of 2007 (Coleman-Lochner & Stanford, 2008). Starbucks was stunned by its first loss since 1992, and realized it had no choice but to retrench. Starbucks decided to close 600 US stores, which resulted in an additional loss of \$168 million.

Adding to the economic issues was a perceived dilution of the Starbucks experience. Stores began to offer musical entertainment and Wi-Fi Internet (Quelch, 2008). Starbucks sought to expand further into grab-and-go market segments. The Express store format was launched, which prioritized faster service times over social interaction with the baristas. Rapid growth led to market cannibalization and declining employee morale.

The menu was expanded to include tea, juice, baked goods, and food (Jacobs, 2014). However, the more complicated menu fostered a mass-production environment that diluted Starbucks' warm and cozy, premium brand positioning (Quelch, 2008). A large number of drinks had to be customized (Quelch, 2008), and sandwiches had to be heated in ovens several steps away from the registers (Sozzi, 2014). This slowed down service times, (Quelch, 2008), which resulted in crowded stores (Sozzi, 2014), less time for socialization with the baristas (Quelch, 2008), rushed orders, mistakes, and compensation for poor service (Sozzi, 2014). Angry coffee enthusiasts

increasingly went to other exclusive brands (Quelch, 2008). Grab-and-go customers decamped for faster service, and improved, cheaper coffee, from McDonald's and Dunkin Donuts (Quelch, 2008).

Changes in Strategic Direction

Schultz returned as CEO in 2008 (McDonnell, 2011). He retrained all employees in the fundamentals of Starbucks customer service, even going so far as to close all US locations to do so. Schultz cut \$581 million in non-customer facing areas (Ignatius, 2010). He personally spoke to stores nationwide, brought in consultants, started a new advertising initiative, hired a chief technology officer to revamp the Starbucks website, switched its coffee to whole-bean, ground-on-site Pike Place Roast, improved the breakfast sandwiches, replaced old computers and registers, closed underperforming stores, optimized the supply chain, introduced a rewards card, reduced store book and CD collections, replaced several upper-level managers, re-designed store layouts, introduced merit pay for executives, successfully debuted an instant coffee brand, and doubled annual purchases of fair trade coffee (Groth, 2011).

Starbucks' financial outlook improved significantly. 2013 also saw a record \$14.9 billion in worldwide revenues (Starbucks, 2013). This was due to a healthy annual growth rate of 12%, and strong international expansion, especially in Asia.

International Expansion

Starbucks had a lot of experience operating abroad. It relied on the expertise of local partners for its international licensing operations. The partners chosen were usually the most prominent players in each country's coffee market. They provided access to desirable retail locations and local market knowledge. As shown in Table 1, Starbucks had more company-operated stores than licensees in the Americas, but favored licensing in other regions.

Table 1: Starbucks' expansion by region as of September 2013

Store Counts	Sep 27, 2009	Oct 3, 2010	Oct 2, 2011	Sep 30, 2012	Sep 29, 2013
Americas					
Company-operated stores	7,574	7,542	7,574	7,802	8,078
Licensed stores	4,415	4,516	4,731	5,011	5,415
Europe, the Middle East, & Africa					
Company-operated stores	911	847	872	882	853
Licensed stores	707	807	886	987	1,116
China/Asia Pacific					
Company-operated stores	409	439	512	666	906
Licensed stores	2,062	2,141	2,334	2,628	2,976
All Other Segments					
Company-operated stores	9	8	14	14	357
Licensed stores	548	558	80	76	66
Total	16,635	16,858	17,003	18,066	19,767

(Starbucks, 2013)

Starbucks opened its first store outside North America in Tokyo in August 1996 (Schultz & Yang, 1997). Starbucks held several events to introduce Japanese consumers to its unique offerings. Despite initial concerns that take out beverages were not a cultural fit, Starbucks' Japanese operations quickly became successful.

Starbucks later expanded into Europe, the Middle East, and Asia. By 2013, Starbucks' international operations contributed to 26% of consolidated total net revenue (Starbucks, 2013). Annual revenue growth in China/Asia Pacific was 27%, 11% in the Americas and 2% in Europe/Middle East/Africa. Table 1 shows a summary of Starbucks' expansion as of 2013.

Despite facing logistical and cultural challenges of oversight from Seattle headquarters half a world away, much of Starbucks' international growth was in Asia. One particularly strong, but challenging, market was India.

The Indian Coffee Market

Consumer Trends

Different governments in India often changed the rules pertaining to foreign ownership and trade. The root cause of this resulting uncertain business climate was a change in demographics. Half the population in India was under 25 (Bajaj, 2012). These young adults benefitted from new jobs that foreign companies created in India, after economic liberalization in the early 1990s. Such jobs brought more money and a desire for Western brands, which were increasingly seen as premium and aspirational (Corstjens & Lal, 2012). However, since the young adults relatively recently started their careers, they had not yet reached the earning power of their parents, and had less interest in taking the time to vote (Bajaj, 2012). This made it harder for the younger generation to influence government policy.

The older generations' greater spending power and longstanding relationships gave them greater leverage over official policies towards foreign companies. Older adults remembered India's break from Britain's empire and ensuing socialist policies that encouraged economic self-sufficiency (Bajaj, 2012). They feared that foreign corporations would create economies of scale and operational synergies that would force local companies out of business, while sending the profits back to the parent country. Many Indian politicians belonged to this age segment, and thus advocated protectionism.

The Indian Coffee Industry

The Indian coffee market in particular was an intriguing proposition. India was the sixth largest coffee producer worldwide in 2013 (Jain & Shukla, 2014). However, Indians have historically preferred tea to coffee (Wharton, 2011). In 2011, Indian per capita coffee consumption was

approximately 85 grams, far smaller than 4.5 kilograms in France, 4.6 kilograms in Japan, and 6 kilograms in the US. Most of that coffee consumption occurred in southern India, which grew 90% of India's coffee (Jain & Shukla, 2014). However, coffee consumption has been increasing in northern cities as well.

The ways in which coffee was consumed in India were different than in the West. 80% of US coffee was purchased as take out for mobile consumption, but this was only true for at most 20% of India’s consumption (Gopalan, 2014). 70% of coffee sales in India were through small shops known as *kiranas*. 25% of Indian coffee sales came from regional retail players, such as Hindustan Unilever’s BRU World Café, and Tata Coffee. An increasing number of offices and public places offered coffee vending machines. Coffee cafés, which young adults in urban areas viewed as a social space, have grown to an estimated \$290 million market in 2013.

The specialty coffee industry was becoming increasingly competitive in India. There were several well-established local firms, and a growing number of foreign firms. All were vying to expand while profitably serving price-sensitive Indian consumers (Gopalan, 2014). The competitive landscape was constantly shifting, as Costa Coffee (Bushan & Chakravarty, 2014), Gloria Jeans (Bailay & Chakravarty, 2014), Barista Lavazza (The Hindu, 2014), and Di Bella (Pinto, 2014) renegotiated master franchise agreements with their Indian partners. Table 2 shows the number of store locations for major coffee retailers in India.

Table 2: Indian retail coffee locations

Brand	Headquarters¹	Store Count
Starbucks	US	50 ²
Barista Lavazza	Italy	190 ³
Café Coffee Day	India	1,500 ⁴
Costa Coffee	UK	100 ⁵
Mocha	India	19 ⁶
Gloria Jean’s	Australia	30 ⁷
The Coffee Bean & Tea Leaf	US	30 ⁸
Dunkin Donuts	US	38 ⁹
Di Bella	Australia	10 ¹⁰
BRU World Cafe	India	7 ¹¹
Krispy Kreme	US	17 ¹²

1. Tripathi, 2013
2. Tata Starbucks Ltd., 2014
3. The Hindu, 2014
4. Café Coffee Day, 2015
5. Bushan & Chakravarty, 2014
6. Mocha, 2014
7. Bailay & Chakravarty, 2014
8. The Coffee Bean & Tea Leaf, 2015
9. Jubilant Foodworks, 2014
10. Pinto, 2014
11. Hindustan Unilever, 2013
12. Sushma, 2014

As coffee became more popular in India, retailers branched out into a wide variety of new locations. These included along busy highways, hospitals, colleges, kiosks, and office vending machines (Bararia, 2012). These locations offered a visually appealing, digitally enabled customer experience, along with coffee blends and complementary menu items that appealed to local preferences.

As the competition for prime locations and market share became fierce, retailers soon realized there was also a shortage of qualified labor. Staff needed extensive training to ensure a consistent, high quality customer service experience (Wharton, 2011). Some companies have dealt with this challenge by opening their own training schools. Other brands have brought in experienced staff from their home countries to train local recruits.

Starbucks' Growth in India

As with other heavily populated countries, India offered the potential to sell to a large number of consumers. Although India was prone to populist political swings ever since it achieved independence from Britain, there were some encouraging signs for foreign food retailers who considered entering the market. Eating at restaurants has historically not been popular in India (Kapor & Yadav, 2013). However, urbanization, smaller family sizes, higher salaries, advertising targeting children, expanded menu selections, and the rising popularity of cooking TV shows has led to a large increase in the number of local and multinational food establishments, from fast food to fine dining.

Starbucks saw great promise in these opportunities. Starbucks initially expressed interest in India as far back as 2007 (Bahree, 2012). Presumably, the turmoil in the US hindered Starbucks' ability to follow through at that time. In January 2011, Starbucks made an arrangement with Tata Global Beverages to purchase and roast premium coffee beans at a new facility in southern India (Bahree, 2012). In January 2012, this was expanded to an \$80 million retail joint venture (Bahree, 2012), Tata Starbucks (Times of India, 2013).

Tata proved to be a very valuable and trustworthy partner. It had a lot of real estate experience that facilitated introducing Starbucks to Indian consumers. Tata helped Starbucks negotiate for prime space on the heavily-trafficked ground floor of major shopping malls (Gopalan, 2014). Tata added Starbucks inside its existing upscale retail outlets. Tata also formed a partnership to offer Starbucks inside its luxury Taj hotels, and to form a product line of Taj foods sold at Starbucks.

Tata's expertise in local tastes and market conditions helped Starbucks learn more about doing business in India. Tata customized Starbucks' menu by adding pastries and ice cream (Bahree, 2012), helped modify the store layout to include locally sourced furniture and interior

decorations (Starbucks, 2012), helped solve logistical problems that hindered the sale of fresh food, and helped develop an effective human resources strategy (Schultz & White, 2014). Employees at Starbucks in India were given highly structured classroom and practical training, followed by additional product-specific and refresher workshops (Anonymous, personal communication, 2015). An employee referral program was implemented. Outreach to

nongovernmental organizations (NGOs) was initiated to hire, train, and retain employees with special needs.

Perhaps most important for success in a historically protectionist market, Tata's coffee bean farms and roasting facilities were successfully leveraged with Starbucks' proprietary roasting techniques (Schultz & White, 2014) to introduce a new premium, Indian-sourced brand, India Estates Blend (Times of India, 2013).

The coffee bean partnership helped Starbucks create a cost structure that was comparable to its local rivals. It ensured consistent quality control, and allowed Starbucks to avoid paying 100% import taxes (Gopalan, 2014). This kept costs comparable to local competitors, and offered a competitive advantage over multinationals that imported coffee.

The partnership with Tata was also consistent with Starbucks' ethical sourcing initiatives. The joint venture established the Café Practices program, to help local farmers improve coffee bean quality, receive above-market prices for their coffee beans, obtain seasonal loans, reduce coffee farming's environmental impact, and improve working conditions for farm employees (Starbucks India, 2015).

Conclusion

Starbucks expansion in India thus far has been successful. By November 2013, Starbucks had 30 stores in India, in the cities of Mumbai, Delhi, Bangalore, and Pune (Times of India, 2013). Its success in India was partly attributable to its unique classification as a hospitality, rather than a retail, business (Bahree, 2012). This allowed Starbucks to avoid constantly shifting restrictions on foreign ownership that have long plagued other retailers (Bahree, 2012). The reason for this classification was unclear. In 2004, the High Court of Delhi defined retail as "a sale for final consumption in contrast to a sale for further sale or processing. A sale to the ultimate consumer" (Prakash, 2008).

Starbucks has stated it plans to keep its global strategy of identical stores offering identical prices, with a modified menu (Gopalan, 2014). It is worth noting that other retailers that insisted on following standardized approaches outside the West have often not done as well as they could have. However, Starbucks also wanted to avoid direct competition with highly successful local competitors (Gopalan, 2014). Starbucks therefore plans to emphasize its premium social experience and foreign origins, as some European coffee retailers have done. Starbucks also seems to have accepted the possibility that it will be unaffordable to the younger generation, which ironically is more willing than older, wealthier customers to consider foreign brands (Gopalan, 2014). How Starbucks will ultimately fare in the increasingly competitive Indian coffee market remains to be seen.

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