



Jenny DeWhitt | Kyle Floyd | Gib Lopez | David Wang

Team B3

## Sweetening the Coffee Experience

### INTRODUCTION

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There are many attractive entertainment opportunities on the horizon for Starbucks Entertainment (SE) to expand into the music industry. These ideas may seem enticing but they are luring Starbucks further away from their coffee core. Not only does coffee have a higher profit margin, it's Starbucks' iconic brand and culture. SE's strategy to enter into the international music scene should fundamentally focus on **supporting** coffee; using music to **enhance** the coffee experience. Although we would like music to take a subtle role, it is still a crucial element in creating the perfect coffee experience. We do not recommend that SE take on any course of action that could threaten the quality of the Starbucks coffee experience. Customer response and analyst sentiment has shown that a push to sell music in Starbucks shops leads to less satisfied customers and a deterioration of the coffee experience. We believe that music can enhance coffee as long as it remains personal, easily accessible, and inconspicuous. In order to accomplish this we propose:

- Installing directional speakers to create a personal space (Music Havens) for customers to discover music,
- Implementing listening receipts that make music more accessible by telling customers which songs they were listening to while making their coffee purchase,
- And by increasing our focus on digital card sales which keeps music merchandise less obtrusive.

One crucial part of the coffee experience is the fact that it's very personal. Customers can order coffee tailored to their specific desires, so why isn't the music personal?

### Music Havens

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Music Havens take advantage of directional speaker technologies. By installing directional speakers over certain tables, it allows the customer sitting at that table to listen to **only** what the speaker is playing while tuning out ambient noise. Each table under the directional speaker will have a simple user interface which has just six buttons that control what music is being played. The choices would be listed on the standard "what's playing" LCD in shops now. This is a service that allows the customer to further personalize his Starbucks experience. At the least, a Music Haven prevents the customer from losing focus on the coffee experience by avoiding any music he doesn't want to hear. Used to their fullest, Music Havens provide a small, private area for two people to enjoy coffee in a more intimate setting. Music Havens could also be used to sample music that is available for purchase in store, or on iTunes. Above all, the Music Havens are meant to provide a service for our customers. They will complement and improve the Starbucks experience, while keeping the focus on coffee.

Panphonics is the leading candidate for providing the directional speaker technology. At \$770 per speaker, each Haven represents a relatively low capital expenditure. With labor and interface material costs, we estimate that it will cost Starbucks around \$2,000 per Haven, assuming no bulk discounts.

### Discovering the Playlist

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A key component of the international music strategy is using music to bring Starbucks stores closer to their community. We would offer global, local (country/region), and community (neighborhood) musical choices in our stores. Each store will have a designated Hear Music representative, who is an employee that has a passion for music. This person would be responsible for finding musical acts in the Starbucks community. Music reps all around the world can be connected to

each other via an extension of the MyStarbucksidea.com social network. This would allow reps to pick up music if an artist from a surrounding area is quickly gaining popularity. An artist that started out simply at one Starbucks in Japan to be discovered by customers in a Starbucks in Seattle because the rep believed the music fit the patrons. By empowering our partners, we provide a powerful music discovery service for our customers. Additionally, this initiative strengthens the international Starbucks community as baristas and employees connect with each other across the globe through music.

### **Accessibility**

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The best music in the world is useless without a way for customers to access it. Our goal at Starbucks Entertainment is to provide the simplest, easiest method of accessing music while being unobtrusive. We propose two ways in which to accomplish this. First, print the last three songs played in the store on the receipt. This allows customers to take an interest in what's being played if they want to, but can otherwise be easily ignored. Customers can purchase songs or albums online after they leave the store. We also suggest an increased focus of digital album sales internationally. These provide strong margins and also bridge the technology gap between CDs and iTunes.

### **Implementation**

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Implementation is a crucial aspect of the overall solution. We recommend that deeper country research be conducted between tomorrow and six months out. From six months out the receipt initiative should be implemented and a year from today the Music Haven will be fully implemented. Countries that are high priority and represent markets that appear very attractive will be the initial focus.

### **Financials**

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The initial phase will roll out in 15 countries the first year. We anticipate, based on past same store growth rates, that same store growth rates will climb to very high levels. Currently, we expect same store sales volume to increase at near 10% over the next five years. This is 3% higher than the international growth rate for FY 2007. The increase in sales growth compared to a constant 7% growth rate results in an NPV of \$411 million. This is calculated taking the WACC of SBUX as the discount rate. The NPV is very conservative as we believe the renewed focus on customers will drive growth to record levels.

### **Summary**

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Starbucks is the global leader in coffee. We have established one of the strongest and most recognized brands in the world. Customers trust Starbucks to deliver high quality and highly personalized products. However, customer satisfaction has been waning as monetization of customers has taken precedence over the experience. This is dangerous territory as competitors like McDonald's are going into the market. Starbucks will continue to lead the market if it can maintain its brand. Thus, as we have stated before, Starbucks entertainment needs to focus on enhancing the experience. This will drive the success of Starbucks into the future.