**Starbucks Corporation**

**Forecast & Analysis Assignment 1**

**FINC 430 6380 Financial Management**

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**Introduction**

Starbucks Corporation, who trades its common stock as “SBUX” on the NASDAQ, is “the premier roaster, marketer and retailer of specialty coffee in the world” (Starbucks, 2016). The company is comprised of seven brands, which include: Starbucks Coffee, Teavana, Tazo, Seattle’s Best Coffee, Evolution Fresh, La Boulange and Ethos (Starbucks, 2016). Starbucks operates both company-owned, and licensed stores, and also operates a sizeable business by selling its products through third-party accounts. The company has five segments of business in which it operates 23,043 stores in 68 different countries, and in fiscal year 2015 those segments represented the following, as a percentage of total revenues: Americas (69%), China/Asia Pacific (13%), Europe, Middle East and Africa (6%), Channel Development (9%), and all other segments (3%) (Starbucks, 2016).

McDonalds and Dunkin Donuts, two of Starbucks’ main competitors, have not seen the same positive growth across their key performance indicators in recent years. “Not surprisingly, investors have caught onto the fact that McDonald’s and Dunkin’ may be hurting one another – and not Starbucks – as evidenced by recent moves in Starbucks, Dunkin’, and McDonald’s shares” (Lim, 2014). However, some challenges that Starbucks faces in the near future are the rising price of coffee beans, higher wage payments and the continuing increase in the price of its products (Team, 2016). With these challenges, it will be necessary for Starbucks to be strategic in its future business decisions to protect the historical positive trending sales growth. The following paper will analyze the outcome of an eVal financial forecast completed on Starbucks, and will detail future growth rates, projected financial statements, financial ratios and other assumptions.

**Explanation of Growth Rates**

Starbucks has seen positive year-over-year sales growth of 12 %, 10.6%, 16.5% in 2013, 2014, and 2015 respectively, and eVal forecasts that the company will continue to see positive growth into 2026. The terminal growth rate forecasted for Starbucks by eVal is 3%, which is a solid financial outlook for the company. In the short-term, the company should continue the process of “leveraging its consumer loyalty and lack of elasticity among its consumers by continuously passing on increases in costs…to its customers” (Team, 2016). By continuously raising the price of its products, the company can protect its operating margins, and not sacrifice the quality of its product and/or locations. When the price of products becomes too high for the consumer, Starbucks can move to maximize the atmosphere, and offer an experience even better than previously offered, to offset the price of the product with an experience.

The eVal forecasts sales growth in 2016 to have an increase of 15.3% compared to a forecasted increase of only 4.2% in 2025. The next 10 years are forecasted to be positive, but not as positive as the previous, leading to a plateau in business. According to a recent financial press release, Starbucks plans to “add 12,000 stores globally –to a total of 37,000 – by 2021” (Starbucks, 2016). The expansion of stores internationally is the biggest opportunity to for the company. With the planned expansion, Starbucks will gain forecasted net sales of more than $29 billion from 2015 to 2025 according to the eVal.

**Explanation of All Other Assumptions**



*Table 1: eVal Assumptions for Financial Forecast Using eVal*

As mentioned previously, sales growth is forecasted by eVal to continue to remain positive into 2025, but slowly decrease in its velocity from 16.5% to 3% in 2015 and 2025 respectively. The eVal assumes all other indicators above, referenced in table 1, to remain constant into the future. Cost of goods sold are forecasted at 68.7% constantly over the next 10 years, showing investors that Starbucks will be able to maintain healthy relationships with its suppliers, and that buyers and negotiators will be able to maintain stability as it relates to costs. In addition, the ending operating cash/sales ratio remains forecasted at a constant 8.4%, informing investors that Starbucks will continue to turn the sales it earns into cash to use for business. Shareholders should also notate the constant 36.9% dividend payout ratio forecasted, as this informs them to expect a continuous growth of their investment. This high pay-out ratio will most likely hold true based on the recent announcement of its intent to open 12,000 stores globally (Starbucks, 2016). It should also be noted that the eVal forecast did not take into account this announcement, and the financing assumptions will most likely change. With the planned expansion of stores, Starbucks will most likely incur increases in its long-term debt as a result of additional leases. According to Starbucks’ Form 10k, the company currently has about “12,235 company-operated stores, almost all of which are leased” (Starbucks, 2016).

**Explanation and Interpretation of Projected Financial Statements**

Net sales of Starbucks were $19 billion in 2015, and are forecasted by eVal to reach $48 billion by 2025, more than double its current sales. This large increase in sales will most likely occur as a result of the company’s expanded footprint globally, and over the past 5 years, the company has seen similar growth, increasing net sales from $11 billion in 2011 to $19 billion in 2015. Net income aligns with net sales, forecasted at a continuous positive increase. The company also is forecasted to continue with a healthy 20% EBITDA. The non-operating income forecasted may be offset by a large litigation charge of $2,784 million to Kraft that posted to the company’s income statement in 2013 (Starbucks, 2016). In developing a strategy for the future, Starbucks should limit its partnerships with third-party companies on large scale agreements to diversify its financial risk.

On the historical balance sheet of Starbucks, the company maintained operating cash of $2 billion in 2011, yet is only forecasted for $1.8 billion in 2016. The company is forecasted to eventually reach its 2011 operating cash flow in 2017, with $2.1 billion, and continue on its positive trend. Other current liabilities also were also affected by the Kraft litigation payment, and may have skewed the forecast. When the 2013 other current liabilities were adjusted to reflect no litigation payment, the eVal forecast was not affected.

**Explanation and Interpretation of Overall Forecast Results & Financial Ratio**

Starbucks’ positive sales performance has a trickle effect on the financial ratios forecasted using eVal. As it relates to annual growth rates, sales, assets and common equity continue into 2025 positively trending, although slightly decrease year-over-year. In 2016, a 15.3% sales, asset and common equity growth is forecasted compared with a 4.2% growth in 2025. Earnings are about (0.1)% off of sales every year. Free cash flow to investors is forecasted as a huge spike in 2016, to 153.2% and then decreases to 19% the following year in 2017. This is most likely a skewed forecast due to the $2.8 billion arbitration payment made to Kraft Foods in 2014, as a result of breach of contract (Starbucks, 2016). Starbucks should invest heavily in its legal and risk departments to avoid future legal proceedings that may result in similar negative financial consequences.

As it relates to profitability, the eVal forecasts that Starbucks will remain consistent with its return on equity at 0.497 in 2015, and forecasted at 0.470 in 2025. The company is doing well with generating profits from shareholder’s equity, and in order to continue this trend, the executive leadership team should continue their growth strategy of expanding the company’s footprint of stores internationally. From 2015 to 2025, the gross margin, EBITDA margin and net operating margin are all forecasted at a constant. This forecast will likely be true for Starbucks if coffee bean prices align with top line sales. One of the challenges faced by Starbucks is the rising price of coffee beans, which can be attributed to weather conditions in the countries where it does business. “The primary contributor towards the rise in prices of coffee beans is the drought in Brazil and Vietnam, the largest producers of coffee beans” (Team, 2016). In order to maintain the constant healthy margins, Starbucks should seek out alternate, back-up locations for similar quality beans.

Short-term liquidity is an important aspect of any organization, as one needs to be able to pay its debts quickly in order to continue doing business. The current ratio of Starbucks increased from 2013 to 2015 from 1.017 to 1.191 respectively. The eVal forecasts that the current ratio will continue to remain at 1.91 until 2025. The quick ratio seen a slight decrease from 2013 to 2015 from 0.706 to 0.638 respectively. According to the eVal forecast, the quick ratio is also to remain constant through 2025. The consistency in the positive leverage that Starbucks is forecasted at, allows the company to continue its current daily operation while being able to protect itself from any financial need that should arise without notice, such as the Kraft arbitration.

From a profitability standpoint, Starbucks hits all the marks, showing effective maximization of assets, equity and investments. Management should take notice of the company’s liquidity, as the company has become less liquid over the past five years. Starbucks has increased its long-term debt but reduced its overall debt, and indicates to investors that it can pay its interest payments on time. Starbucks may have found its most effective asset management strategies as asset management ratios have maintained relatively neutral over the past five years. Historically Starbucks has had stellar financial performance, and is forecasted to continue the trend. With the expansion of its stores globally, the company is likely to see record sales and growth over the next 10 years.

**Appendix**

Appendix A – Income Statement Assumptions eVal



Appendix B – Balance Sheet Assumptions eVal



Appendix C – Financing Assumptions eVal



Appendix D – Short-Term Liquidity eVal



Appendix E – Financial Ratios eVal



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