**ERP Model**

**Forecast Thesis:**

*I believe that the Fed's impending tapering will set the stage for a deterioration in the economic environment and negatively affect future growth prospects. At last September's FOMC conference, Jerome Powell was more hawkish, confirming his willingness to implement the process "soon" and, based on comments from other Fed members, the expectation is for the end of this year. With Congress extending the debt ceiling discussion to December, I expect the effects of tapering to be delayed until 2022. In this regard, policymakers have not shown support for further increasing the government's balance sheet with new debt, and this could speed up the process. Therefore, I believe the Fed will be forced to begin aggressive tapering of securities purchases and to raise the Federal Funds rate. These expectations could translate into effects already visible in Q2-2022 and lead to an outflow from the stock market into the bond market, increasing the uncertainty (volatility) of the latter along with a higher required risk premium.*

* **Variable 1—The Federal Funds Rate:**

Worsening economic conditions and the start of tapering will put upward pressure on Treasuries by the end of 2021. I believe this will translate into widening spreads for the first part of 2022, with margin tightening likely in 3Q 2022E when the market incorporates a more hawkish view.

* **Variable 2—Treasury Spread (10-yr to Fed Funds):**

Fed's benchmark rate hike starting in 1Q 2022, with steeper increases in 2023 and 2024. The Fed has been pumping a lot of money into the economy leading to a structural increase in core inflation (3% projection in June). This lays the groundwork for a possible steeper increase in rates. +5 bps since 1Q2022E, with a more pronounced increase starting in 1Q2023E.

* **Variable 3—Equity Market Volatility (VIX):**

Tapering will not only reduce the amount of QE but will be seen as a proxy for tighter monetary policy to come. This combination could lead to periods of high volatility and rising rates in the bond market. I expect the VIX to rise due to an outflow of money from equities into the bond market. The outflow could make markets volatile throughout 2022.

* **Variable 4—Equity Market Return Projections:**

I expect the market to have some correction in the first 3 quarters of 2022, with a return towards historical averages and slower but steady growth.

[*https://www.brookings.edu/blog/up-front/2021/07/15/what-does-the-federal-reserve-mean-when-it-talks-about-tapering/*](https://www.brookings.edu/blog/up-front/2021/07/15/what-does-the-federal-reserve-mean-when-it-talks-about-tapering/)

[*https://www.cnbc.com/2021/09/23/heres-what-will-happen-when-the-feds-tapering-starts-and-why-you-should-care.html*](https://www.cnbc.com/2021/09/23/heres-what-will-happen-when-the-feds-tapering-starts-and-why-you-should-care.html)

**DCF Model**

* ***Assumption 1:***

***>> Increasing Operating Margins - US segment***

The increasing focus of Gen Z and Millennials on leading a 'healthier lifestyle is prompting a change in the purchase patterns of this group of consumers and, I believe, will be the driver for further growth for Starbucks.

Following this macro trend, the Company has already started adding alternative dairy products and plant-based foods to its offerings (food purchases represent about 20% of total sales). This phenomenon is certainly not temporary, and I expect an increase in the addressable market by Starbucks in the coming years; especially among young people, there is a growing desire to find healthier and more environmentally friendly alternatives. Starbucks following this trend could gain even more market share and leverage its brand recognition to become a frontrunner and thus drive revenues higher. I want to focus more on the marginality. These products usually have higher margins because the consumer is willing to pay a higher premium for food that is perceived as healthier, and this should significantly improve Starbucks' profit margins.

The two-effect combined can enhance the overall profitability and drive the company figures over the long term.

* ***Assumption 2:***

***>> Increasing Revenues – International segment (China)***

The Chinese Segment is the second largest for Starbucks after the US and there the company is keeping a leading position with about 36.4% of the total market. China has produced and consumed tea for centuries, but between 2008 and 2018, coffee consumption increased by more than 1000% mainly due to the influence of millennials (1/4 of China's population) and changes in consumption influenced by the drifting towards Western culture and higher disposable income than previous generations. The dominant position that the company has and the huge barriers to entry (characteristic of this country), makes it easier to take advantage of this trend and, as coffee consumption continues to grow, Starbucks can certainly increase its sales and place itself among the leaders in this market.

I believe that Starbucks' efforts in expanding customer relationships and engagement through online experiences that make mobile ordering even more convenient and personalized, together with the growth of the reference market, will drive sales in this segment and further consolidate Starbucks' dominant position in China.

**Price Multiple**

As for the Multiple Valuation, I decided to use the average PE calculated with NTM values because I believe it is more representative of how the "market" values the "relative industry" and it is a better predictor of the future value that the market might attribute to Starbucks. NTM values, in my opinion, more accurately reflect the expectations that the market has of the company under analysis and allow a more accurate analysis of the company's future performance.