Rhea Mogoginta
Babson College

Starbucks Model Forecast

Thesis:

Opinion 1: Coronavirus has caused Starbucks' total revenue to fall significantly due to store closures and a huge drop in order traffic. However, I believe that Starbucks will recover slowly and strongly over the next few quarters due to its positive outlook during the first half of 2021. This positive outlook is also driven by analysts' view on the company and the management itself expecting significant growth YoY, which can be seen on the management's guidance and management's comments from the MD&A. According to The Wall Street consensus, the stock is bullish with a 12-month price target that is 17% above the current share price and bullish market-implied outlook. Wall Street analysts also rated SBUX either buy or hold (33% more buy rating than neutral), with no bearish ratings.[1] Hence, we expect higher growth and better revenue for these upcoming years.

Opinion 2: After conducting research on the restaurant industry, the food and beverage sales by the end of this year is projected to increase by nearly 20%. The most important takeaway from the National Restaurant Association mid-year update was the transition towards a more digitalized food industry for ordering and paying.[2] It is also important to note that restaurant sales are on the rise. This is mainly due to the easing of travel and restaurant restrictions and number of vaccinated people in the country. However, food costs are also on the rise due to wholesale food prices and supply chain costs (gas and fuel prices are increasing). Additionally, transactions in the US are starting to go back to normal with the help of drive thrus and mobile apps, and international sales especially in China where growth is expected to rise significantly. Thus, we are expecting higher sales, increase number of new stores, and EPS growth, but also increase in operating expenses.

Impact:

Company-Operated stores Revenue: Management guidance believes that sales in the US is expected to increase by 22% due to increased consumer mobility, mobile orders, to-go orders, and people's desire to socialize post-pandemic. However, I did not choose the higher percentage range because there are still a lot of people working remotely, which means that morning coffee run is still on halt.

International-Operated stores Revenue: The international comp store sales growth is in the high single digits just as the best-case scenario from the management guidance. This growth forecast is driven by a positive outlook in the China market and increased usage of loyalty programs.

New stores: Starbucks in expected to open 55,000 stores by the end of 2030, this ambition is translated in my forecast in which I have inflated the number of new stores opened quarterly for both licensed and company-operated stores for the US and international market. The company

[1] https://seekingalpha.com/article/4459417-stronger-outlook-for-starbucks
[2] https://restaurant.org/association-releases-mid-year-soi

must ramp up its plan to open new stores to be able to reach the target by 2030, because SBUX was not able to follow its plan in 2020 due to COVID.

Operating Expenses: Store operating expenses is expected to slightly increase in the upcoming quarters due to regulations governing post-pandemic cases and alleviating possible transmissions. Another reason why I increased this line item is because of potential benefits paid to employees.

Capital Expenditure: As a result of my forecast regarding ramping up new stores in the next few quarters, SBUX's capex to revenue will also increase. This is because SBUX is undertaking new project, hence it must invest in property and advancing its technology.

Share Repurchases: According to SBUX latest 10Q, there are 48.9 million shares available for repurchase but the company have been suspending its repurchase program. This is because of its poor performance in 2020 due to the pandemic, which resulted in an astonishingly low free cash flow. SBUX is waiting for free cash flow to improve before starting its repurchase program again. Furthermore, since my thesis assumes a positive forecast for SBUX in the next few years I believe that its stock repurchase program will resume in 2022. Also, according to the Biennial Investor Day management guidance, it is expected "to yield EPS benefit of about 1% net of incremental interest expense as we maintain our long-term leverage target." Hence, the $2 billion share repurchase by the end 2022. For this, I forecasted an increase of 2% in stock price for the first year, followed by an increase of 5% for 2023-2024, and maintain 2% increase for 2025-2026. This is based upon SBUX previous YoY growth and analysis of Institutional Investors that SBUX will hit a higher target price as it bounces back from the pandemic. Additionally, the amount of share repurchases for year 2023 increased by 10% from the previous year to $2.2 billion. The rationale behind this is because the company has not been repurchasing shares in 2020, and to achieve the target of 10% EPS growth from the previous year.

Balance Sheet: The main changes made to the forecast has to revolve around the impact of number of new stores and going back to business pre-pandemic. First, operating lease increased due to renting property for new stores or creating new drive thru locations. Second is the increase of intangible assets due to the company's advancement in technology and focusing more on innovation. Such that expanding in Asian countries requires SBUX to integrate better information technology for branding and marketing purposes. Next is the increase of accrued payroll and benefits, which is mainly driven by the increase of new stores and compensation for potentially new rules for employment post-pandemic. The last line item is total investments as a percentage of assets, I revert the percentage back to pre-pandemic levels at 2% which seems logical because SBUX is slowly going back to normal.