A
Case Study
On
STARBUCKS: DELIVERING CUSTOMER SERVICE

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CASE 02

STARBUCKS: DELIVERING CUSTOMER SERVICE

Overview
Twenty years after its founding as a small coffee shop in Seattle, Starbucks has become a cultural phenomenon with thousands of coffee houses (referred to as “stores”) across North America and around the world. Recent market research, however, shows that the firm’s service is not meeting customer expectations. Speed of service is a particular problem. Management is considering increasing the amount of labor in each store, at a cost of $40 million company-wide, but the potential impact on revenues—and thus the bottom line—is unclear.

Study Questions

1. What factors accounted for Starbucks’ success in the early 1990s and what was so compelling about its value proposition? What brand image did Starbucks develop during this period?
2. How has Starbucks changed since its early days?
3. Why has Starbucks’ customer satisfaction scores declined? Has the company’s service declined or is it simply measuring satisfaction the wrong way?
4. Describe the ideal Starbucks customer from a profitability standpoint. What would it take to ensure that this customer is highly satisfied? How valuable to Starbucks is a highly satisfied customer?
5. Should Starbucks make the $40 million investment in the stores? What’s the goal of this investment? Is it possible for a megabrand to deliver customer intimacy?

Analysis

1. What factors accounted for Starbucks’ success in the early 1990s and what was so compelling about its value proposition? What brand image did Starbucks develop during this period?
In the Early 1990 Starbucks immerge as a big brand, known around the world

At this time, the company serves 20 million customers in over 5000 stores worldwide and continues to expand rapidly, on average opening three new stores a day.

But let’s examine changes between 1992 and 2002.

**Time of 1992**

Marketing experts generally agree that Starbuck’s success was rooted in a timely, well-integrated value proposition (VP) that was compiled with the needs of the target market.

**Value proposition.** The initial VP comprised three elements that can be represented on the board as three concentric circles:

- **Core product (a physical good):**
  - premium coffee, seen by Starbucks as “the highest-quality coffee in the world.
  - Quality is maintained by careful selection and control of as much of the supply chain as possible.
  - Along with that, additional menu items have been added to complement the array of coffee products offered in the stores

- **Focus on service (“customer intimacy”),**
  - recognized regular patrons, and customized their orders.
  - The *baristas* were more than just order takers and fillers—they came to fulfill a similar role to bartenders in a favorite bar and customers would chat with them.

- Attractive atmosphere and physical environment, with comfortable seating areas that encouraged customers to linger

- Also, Christine Day’s comment, “People come for the coffee, but the ambience is what makes them want to stay”.

- The upscale environment contrasted sharply with the more utilitarian surroundings found among other coffee shops (e.g., Dunkin Donuts).

**Target market**

People who fond of coffee, well-educated, white collar, aged 25-44, skewed toward female.
They were willing to pay a significant price premium over competing alternatives (e.g. 50 cents in a local coffee shop or donut store).

The customers themselves became part of the environment, helping to define and reinforce Starbucks’ positioning.

**Brand perceptions and consumption patterns.**

By the early 1990s, Starbucks’ early success had created a classy brand image, with a place with a European feel that offered the best coffee in the market.

Customers, who were willing to pay premium prices for the coffee (bundled with customized service and a pleasing environment), tended to switch at the stores.

As a result, its positioning places it high above most alternative coffee suppliers, with its brand associated not only with its coffee houses but also with its packaged coffee beans and coffee products sold through non-company-owned

**Relationship of employee satisfaction to customer satisfaction.**

Schultz has always believed that employee satisfaction leads to customer satisfaction.

And so Starbucks has offered all the benefits plus careful training in both hard and soft skills to ensure high service quality.

Reflecting high partner satisfaction (80-90%), well above industry norms, turnover has traditionally been low, which reduces the expense associated with constantly having to recruit and train new personnel.

2. **How has Starbucks changed since its early days?**

- The number of stores has increased sharply—from 1,886 in FY 1998 to 5,886 only four years later making the brand much more accessible and therefore, perhaps, less distinctive.
• Competitors remain mostly regional (e.g., Peets), but have benefited from the Starbucks phenomenon in terms of its creating primary demand for premium-priced coffee in nice locations which distinctive from the competitors.

• The customer profile has changed. newer customers (first visited within past year) tending to be younger than established customers (first visited 5+ years ago); they are less well educated, with somewhat lower incomes (although still good), drinking slightly less coffee per week, and with less favorable attitudes toward Starbucks—much less likely to see the brand as high quality (-17 percentage points), as trusted (-20 pts), worth paying more for (-24 pts), best tasting (-11 pts) and highest quality (-15 pts). Ominously, only 15% of newer customers agree with the statement that Starbucks is “for someone like me (vs. 40% for established customers) and their overall opinion of the brand is 19 points lower.

• Pressures on baristas have increased. The increase in menu items means there are more products to delivered and the pressure to deliver customized drinks means there is less time to align with customers. Contrast this to the typical bar, where a high proportion of drink orders are relatively easy for bartenders to supply: beers, house wines, sodas, or simple mixed drinks (e.g. gin and tonic) rather than complex cocktails.

• Little image or differentiation in minds of specialty coffee house patrons between Starbucks and smaller coffee chains; however, independent coffee houses are seen as significantly different— the independents now have the brand meaning that Starbucks used to have!. Note the image of Starbucks as offering “good coffee on the run,” “place to meet and move on,” and “convenience oriented; on the way to work.” This suggests a different pattern of consumption in which speed and convenience rather than ambience have become dominant.

• Customer satisfaction seems to be lower among more recent customers—an ominous trend for a fast-growing chain.

3. Why have Starbucks’ customer satisfaction scores declined? Has the company’s service declined or is it simply measuring satisfaction the wrong way?

A broad concern for management is the emergence of two different types of customers—new vs traditional—with different expectations. It may be hard for Starbucks to satisfy both of these broad categories and these two broad segments cannot mix well within a traditional store.
We can infer that newer/older customers may have different priorities. For instance, fast service probably gets much higher emphasis from newer customers than long-term customers.

Management admits that “we’ve started to lose sight of the consumer”. But perhaps it would be fairer to say that they have failed to understand the different needs of newer consumers.

4. Describe the ideal Starbucks customer from a profitability standpoint. What would it take to ensure that this customer is highly satisfied? How valuable to Starbucks is a highly satisfied customer?

A highly satisfied customer visits Starbucks far more often than a merely satisfied customer (7.2 times/month vs 4.3 times), has a higher tab per visit ($4.42 vs $4.06). This translates to an annual spending difference of $381.84 vs. $209.52. The comparable
figure for an unsatisfied customer, whose patronage is likely to be relatively short lived, is \((3.9 \times $3.88 \times 12) = $181.56\). Highly satisfied customers have a customer “lifetime” of 8.3 years, versus only 4.4 years for merely satisfied customers and a mere 1.1 years for unsatisfied customers.

The longer a customer remains loyal, the more attractive financially she/he becomes. However, these data won’t show net profitability, because we have no case information on the cost of serving a customer on each visit. Because long-term customers may purchase more specialized drinks, require more customized (and therefore more time consuming) service, and occupy seats in the stores for longer periods, so it may be happened that they may generate a lower profit margin on each sale.

5. **Should Starbucks make the $40 million investment in the stores? What’s the goal of this investment?**

The primary goal of the proposed $40 million investment is to improve customer satisfaction by increasing speed of service. It will increase in annual operating costs (20 hours of extra labor per week per store) that will be incurred each year—and the total will rise as the number of stores increases—rather than a one-time investment. To recover this expenditure in the first year, how many satisfied customers would Starbucks have to convert to highly satisfied status? And how many from unsatisfied to satisfied?

- Annual value of satisfied to highly satisfied = \(($381.84 – 209.52) = $172.32\).  
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  \frac{$40,000,000}{$172.32} = 232,126 \text{ customers} \]
  *(based on revenues only, not net profits, since excludes direct costs, so actual figures required will be higher)*

- Annual value of unsatisfied to satisfied = \(($209.52 – 181.56) = $27.96\).  
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  \frac{$40,000,000}{$27.96} = 1,430,615 \text{ customers} \]
  *(see disclaimer above)*

These data should be seen in the context of 20 million individual customers worldwide. Assuming there aren’t wide differences in the costs of serving each group, focusing on currently “satisfied” customers appears a better bet than on “unsatisfied.”

Unfortunately, the case doesn’t tell us what proportion of customers fit into each of the three satisfaction categories, so we can’t calculate what percent of each of the two lower groups needs to be converted. Although satisfaction appears to be correlated with length of patronage, we cannot assume that all recent customers are less satisfied than all long-term customers.

*Thank You*