

An Analysis of Starbucks Corporation

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Abstract

In this paper, I will dive into a deeper understanding about the economics behind one of the biggest corporations. This paper will include the history of Starbucks Corporation, like where it started, its growth, locations, their products, their opportunities to give back to the community, and their message they want to put out. The Supply and Demand trends, such as their annual revenue and demographics. The Price Elasticity of Demand, going in depth of whether Starbucks is elastic or inelastic and why. The Costs of Production, like their annual and quarterly costs from the past decade, the overall market shares over the years 2017-2021, and a recommendation to make this already booming company improve through methods that they're already pursuing.

Title of Paper

There is probably not a single person in the United States you can ask who doesn't know what Starbucks is. This worldwide coffee chain has dominated the coffee industry for years, with their high quality coffee beans used and the experience you get at one of their locations. This didn't happen overnight, nor by accident. The purpose of this paper is to dive deeper into Starbucks Corporation, by looking at the many different parts played behind the scenes in the world of economy. The strategies used to bring in loyal consumers, the costs needed to run these stores, the revenue they bring in, and other factors explaining how Starbucks went from one little Starbucks location in Seattle, Washington, to more than 34,000+ stores all around the world.

History of the Company

According to the About Us page on Starbucks' website, Starbucks opened their first store in 1971 in Seattle's historic Pike Place Market. The name Starbucks was inspired by the classic tale of "Moby Dick", referencing the seafaring tradition of coffee traders in the early days. Ten years after opening their first store, a man named Howard Schultz, from New York, fell in love after stumbling into the store for the first time. He joined the Starbucks team in 1982. On a trip to Milan in 1983, Schultz was inspired to bring the same warmth and artistry of Italian coffee culture to Starbucks.

The company expanded towards Chicago, Illinois and Vancouver, Canada, then went to California, Washington, D.C., and New York. In 1996, they opened their first store in Japan, then to Europe by 1998, and China in 1999. Starbucks' mission is "to inspire and nurture the human spirit - one person, one cup, and one neighborhood at a time".

Coffee buyers for Starbucks personally travel to coffee farms in Latin America, Africa, and Asia to select the best Arabica beans.

On Starbucks' Company Profile Webpage (2019), as of today, Starbucks has opened 34,000+ stores in 84 markets. The countries include "Andorra, Argentina, Aruba, Australia, Austria, Azerbaijan, Bahamas, Bahrain, Barbados, Belgium, Bolivia, Brazil, Brunei, Bulgaria, Cambodia, Canada, Cayman Islands, Chile, China, Colombia, Costa Rica, Curacao, Cyprus, Czech Republic, Denmark, Dominican Republic, Egypt, El Salvador, Finland, France, Germany, Greece, Guatemala, Hong Kong / Macau, Hungary, India, Indonesia, Ireland, Italy, Japan, Jamaica, Jordan, Kazakhstan, Kuwait, Lebanon, Luxembourg, Malaysia, Malta, Mexico, Monaco, Morocco, Netherlands, New Zealand, Norway, Oman, Panama, Peru, Philippines,

Poland, Portugal, Puerto Rico, Qatar, Romania, Russia, Saudi Arabia, Serbia, Singapore, Slovakia, South Africa, South Korea, Spain, Sweden, Switzerland, Taiwan, Thailand, Trinidad and Tobago, Turks and Caicos, Turkey, United Arab Emirates, United Kingdom, United States, Uruguay, and Vietnam.

Starbucks offers many different products that their consumers can drink in store, on the go, and also at home. They offer more than 30 different blends and single-origin premium coffees. They also do their own handcrafted beverages like their Frappuccino blended beverages, and Starbucks Refreshers. Besides their drinks, they also sell food at their many locations. They offer baked pastries, salads, protein boxes, sandwiches, and other snacks. For the consumers who want Starbucks at home, there are many selections people can have to make and drink on their own. Starbucks sells whole-bean and ground coffee, Instant, K-Cup pods by Nespresso, and Teavana Verismo pods. Ready-to-Drink selections include the bottle Frappuccino drinks, chilled cup coffees, Bottled Cold Brew, Teavana craft iced teas, and many other selections.

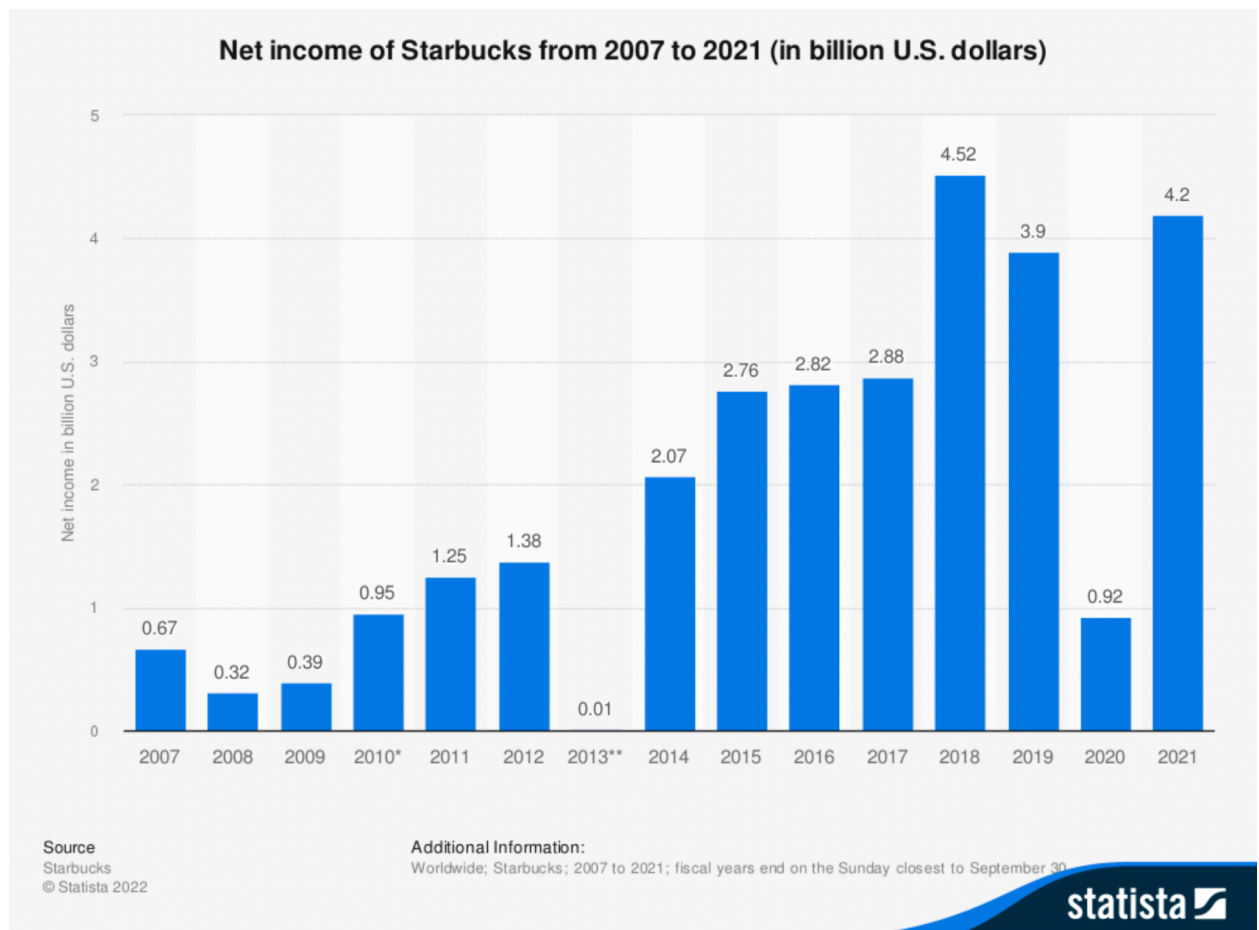
The Starbucks Company Profile includes the investor information. Starbucks went public on the stock market on June 26th, 1992. They were sold at a price of \$17 per share and closed the trading that first day as \$21.50 per share. Starbucks Corporation's common stock is listed under the trading symbol SBUX on NASDAQ.

Starbucks is said that they can - and should- have a positive impact on the communities that they serve. Their vision is to create positive change in the areas they can have the biggest impact in. Their goal is to become resource positive by storing more carbon than they emit, eliminating excess waste, and providing more clean freshwater. They also believe in supporting communities by volunteering for local neighborhoods. They also invest in opportunities through education,

training and employment. They will hire veterans and military spouses, Opportunity Youth and those who were formerly incarcerated and refugees in hopes of helping them build their own futures while working with Starbucks.

Supply and Demand

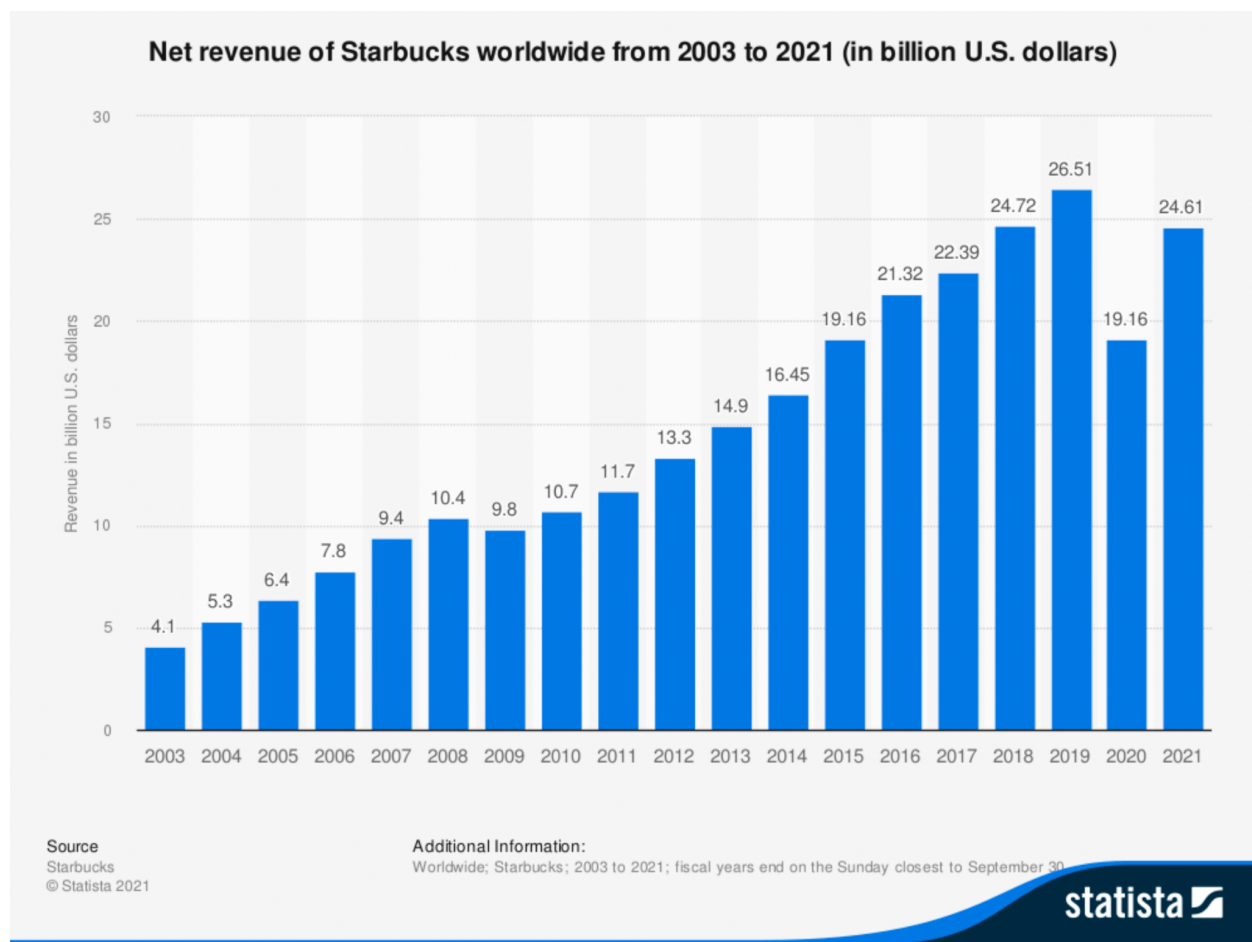
When looking at the net income of Starbucks from the years 2007 to 2021, it is evident that there is an extreme growth throughout the years. In 2007, Starbucks had a net income of 0.67 billion dollars. This past year, their net income was 4.2 billion dollars. It was recorded that there was a decrease of over 3 billion dollars from the previous year. Lock (2022).



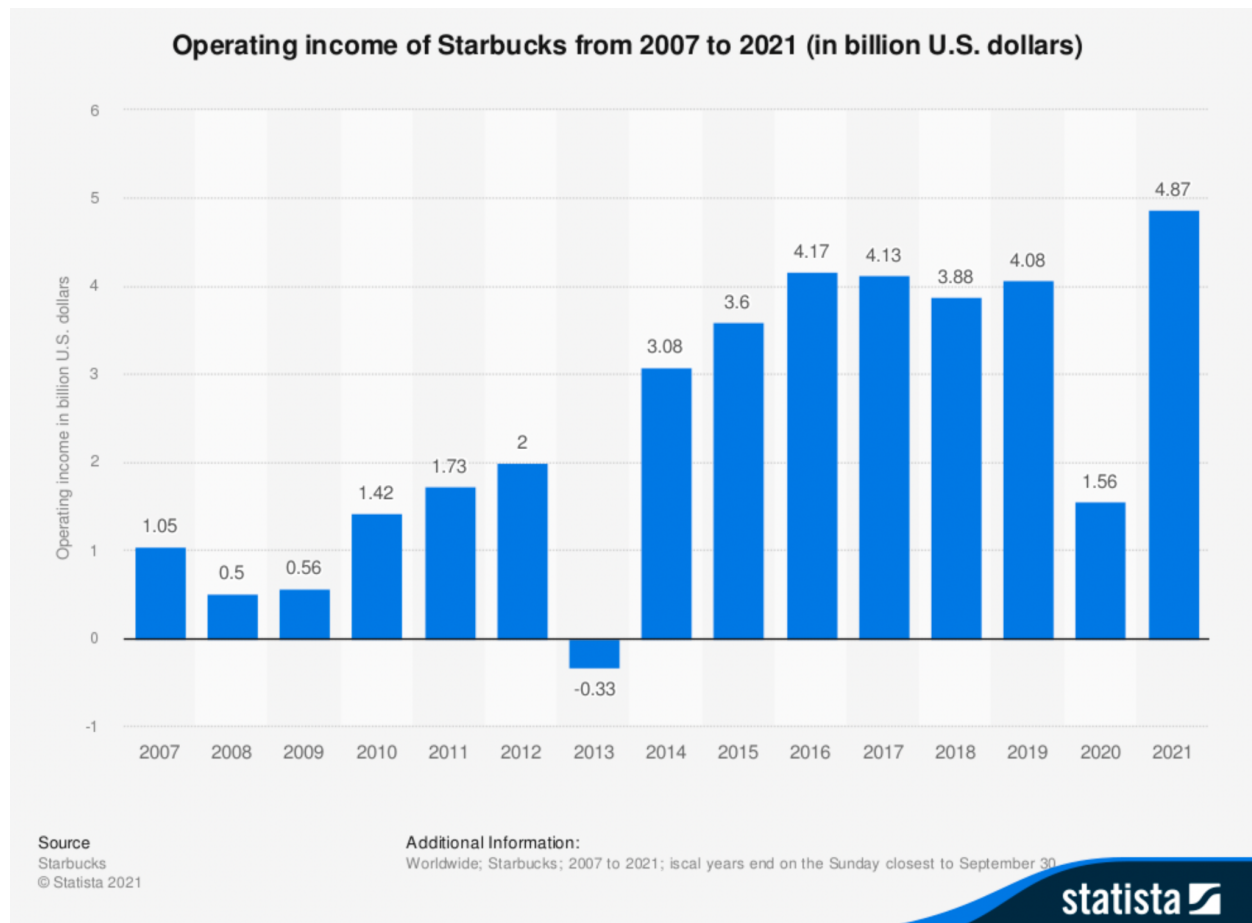
Straying away from Starbucks' competitors, we can look at their demographics and target audience. Starbucks' target market is described as "affluent or high income, meaning around \$90,000". It is rare to find a high class neighborhood that doesn't have a Starbucks nearby. However, more and more cafes have been opening around middle-income neighborhoods. Although they may not have a large income, those consumers are willing to spend the extra money on the premium coffee beverages. Bean-Mellinger (2019). 49% of the revenue that Starbucks receives comes from the age group of 25 to 40 years of age. Seeing where Starbucks locations are predominantly located, they're able to stay there for longer because their target demographic is able to afford the higher prices of their coffee. When looking at the future of the

stock prices, 27 analysts offering price forecasts for Starbucks Corp. have a median target of 92.000, a high estimate of 116.00, and a low of 76.00. Overall, the median estimate shows a +26.50% increase from their last price of 72.73. Gaille (2016).

Going from the overall trends in demand, I'll switch over to the specific data on demand of Starbucks. Looking at the net revenue of the company from the years 2003-2021, there is a steady increase with each year, rarely ever having less billions than the year before. Focusing on the past five years, the annual net revenues are listed as: 22.39 billion (2017), 24.72 billion (2018), 26.51 billion (2019), 19.16 billion (2020), and 24.61 billion (2021).



When taking a look at the operating income of Starbucks, the numbers reflect a similar pattern to the net revenue. It was 4.13 billion (2017), 3.88 billion (2018), 4.08 billion (2019), 1.56 billion (2020), and 4.87 billion (2021). Lock (2021).



Looking more at the supply side of Starbucks, there are no accurate dollar amounts available that specify the cost Starbucks pays to produce a cup of plain coffee. There are amateur speculative estimates that can range from \$0.20 to \$0.75. However, Starbucks' cost structure is straightforward, and shows the same as any other "high-end fast casual restaurant." Looking at the technological advancements Starbucks has to offer, they do not want to eliminate human employees. Krikorian (2021). They have the idea of "using AI for humanity" by using artificial

intelligence to give space for human connections. They want to have fewer employees having to work with machines and mindless tasks, and have more opportunities to form connections over coffee. By this, Starbucks invisions the making and delivery of products to be done by humans so the human to human connection thrives in the workplace. Instead, they want to use AI for non-value-added jobs like cleaning and inventory. As of right now, the majority of the tech enhancing features Starbucks have is done through their mobile app. Launched in 2011, it has given people an easier way to make payments and track their rewards. It has now been able to tell stories and make recommendations to the user. Around 20 million regular users use the Starbucks' Mobile Order & Pay system, which allows you to order your drink through the app and skip the line. As of today, almost 25% of all of Starbucks' transactions are done through mobile orders. The loyalty program allows for users to earn rewards and free drinks and foods through how many purchases you make through the app. To Starbucks, this app provides valuable data for their customers preferences and trends. The drive-thru was also an addition that greatly helped consumers, especially after the pandemic forced many places to shut down. As of the first quarter of 2021, orders done through the drive-thru have increased 10% more after the pandemic began. The app has now combined ways for you to order through the app and pick up at the drive-thru. A strong principle of Starbucks is inclusivity. They have partnered with Aira to offer free asisternace to those who are visually impaired. Aira Tech Corp is a company that connects those who are visually impaired to visual interpreters through a phone app. Nambiar (2021).

Starbucks' biggest competitors are McCafe and Dunkin' Donuts. When looking at the supply side, you need to see the prices of the different substitutes there are.

For this example, I will compare the cost of a medium sized black coffee from the three stores. Starbucks' coffee costs \$2.10. The same coffee costs \$1.29 at McDonalds, and Dunkin Donuts coffee costs \$1.89. It is evident with the higher quality beans that Starbucks uses, that the price would be higher than its competitors. However, there isn't much of a difference in the prices, so why would Starbucks net income be lower in more recent days.

A simple explanation could be with the issues that this world has faced this past couple of years. With the pandemic, many people had lost their jobs or faced a decrease in income. Many people just wanted their daily intake of caffeine, and since Starbucks is known to be on the pricier side, people would turn away to get the cheapest option they could get. In 2019, Starbucks revenue amounted to \$29.509 billion dollars, which was the highest their revenue had been. However in 2020 when the pandemic began, the revenue decreased by 11.28% and with the whole world recovering from the effects of the pandemic, Starbucks is not the exception.

Looking at the number of firms in the market, Starbucks is the largest coffeehouse in the world with 34,000+ stores across the globe. Their year-over-year growth has almost doubled in the past 10 years.

Price Elasticity of Demand

When it comes to the price elasticity of demand for Starbucks Coffee, they tend to view their price of the demand for its products as elastic, but more of a low level type of elasticity. If the products were considered inelastic, it would place the products in the category of a "necessity" that people would obtain no matter the price because they cannot live without the coffee. As of

now the elasticity of coffee demand is at 0.3. It is considered elastic because it is a luxury. In the event the prices were supposed to rise due to a high market of competitors, the demand will decrease. By creating a more loyal customer base, it welcomes a higher number of customers who are willing to pay the higher prices. “Study” (2021). Over the past five years, the price of coffee inputs has decreased, but the price of the company’s drinks has increased since of the loyal customer base. In the coffee sector, pricing is a heavily discussed topic, as the price of coffee affects the farmers, traders, and roasters all over. For example, if Starbucks’ price increased, the demand for quantity would decrease, while a decrease in price would increase the demand for coffee. However, because Starbucks prides themselves with “Quality Coffee”, the demand curve shifts to the right because of their loyal customers who pay for Starbucks coffee’s taste. Coffee is considered an inelastic good. Although coffee is more expensive than its competitors, they’re also selling the “coffee experience”. They also increase the amount of caffeine in each drink, thus keeping their customers loyal. Dawson (2021).

While Starbucks has many competitors in the coffee industry, they have the competitive advantage of product differentiation. However the availability of Starbucks competitors are neck and neck with them. McDonald’s has over 38,000 locations in the world and Dunkin’ Donuts has more than 11,300 locations worldwide. So when it comes to the availability, Starbucks is slightly overpowered by McDonalds.

When looking at the passage of time, it increases the elasticity of demand for many goods since the time allows the price to change so customers pick the price they like, allows for more production of the good, and allows the people to earn more income. It is shown in the above

graphs of the net revenue and operating income that the passage of time has greatly benefited Starbucks.

When it comes to the Starbucks product, it is considered a luxury rather than a necessity, also proving that it is elastic. People do not need to go out to a Starbucks store nearby to get their coffee every day. There are plenty of cheaper alternatives that consumers can get and make at home without having to spend money every time, thus showing it is a luxury.

The market structure in economics is “described as the outline of a firm in terms of differentiated or categorized products”. The structure of Starbucks is a monopolistic competition. This means that there are different firms that sell different types of products and little barriers to enter. In reference to the coffee selling industry, there are many producers and consumers intertwined, and the goods and the services are mixed up, but the firms are able to tell about their products. Starbucks understands the way their market structure is like, and has worked it to their benefit. They’ve maintained this through their knowledge of the labor market, their quality private goods, and creating customer loyalty.

With Starbucks understanding their market structure, they’re able to use it to maximize their profit. Starbucks uses value based pricing to reach their maximum profits by using consumer analysis and research their formulated target prices that can bring in the most amount of customers that are willing to pay the price without turning them away. It is rare to see companies actually using this type of method to increase their profits. In order to compensate for previous customers who switch to another substitute such as McDonald’s, Starbucks will increase their prices to their customers who can afford it and depend on the higher quality coffee. Rather than

lowering the prices to compete with their competitors, they raise the price and reinforce the “premium image of their brand and products”.

Costs of Production

When looking for Starbucks’ costs of production, I came upon this article that really makes me think about how much it really costs. Benaroya did an article called “Starbucks’ cost for a coffee is \$1. Unless you Sit”, and goes through how much it costs for just a singular cup of coffee. For the coffee and the milk, it costs \$0.36, but adds 8 more cents if you add the cup, stir, and the lid. It will cost \$1.00 for the direct labor of the barista, cashier, and other staff for that cup of coffee. From Starbucks’ 2018 Annual Report, the SG&A expenses at Starbucks are 15% of the sales, or \$0.64 per cappuccino. The rent for a store in Manhattan is \$878 per square foot, plus the 20% for utilities. The nationwide average for a Starbucks store is 15 square feet, giving an annual cost of \$15,800 per seat. One location is open for 15 hours a day, giving the cost per hour at \$2.89. Benaroya (2019).

Moving away from the cost per cappuccino example, we can take a look at Starbucks’ annual costs of goods sold. The tables show that the annual cost for goods sold in 2021 was \$8.739 billion, in 2020 was \$7.695 billion, \$8.527 billion in 2019, \$7.931 billion in 2018, \$7.066 billion in 2017, \$8.509 billion in 2016, \$7.788 billion in 2015, \$6.859 billion in 2014, \$6.382 billion in 2013, \$5.813 billion in 2012, and \$4.916 billion in 2011.

Starbucks’ Annual Costs of Goods (in Billions)

<u>Year</u>	<u>Cost</u>
2021	\$8.739
2020	\$7.695
2019	\$8.527
2018	\$7.931
2017	\$7.066
2016	\$8.509
2015	\$7.788
2014	\$6.859
2013	\$6.382
2012	\$5.813
2011	\$4.916

We can take a closer look over the last decade by looking at Starbucks' quarterly costs of goods sold. On March 31st, 2022, the quarterly costs of goods sold was \$2.466 billion. It was \$2.527 billion on December 31st, 2021, it was \$2.491 billion on September 30th, 2021, \$2.206

billion on June 30th, 2021, \$1.992 billion on March 31st, 2021, \$2.049 billion on December 31st, 2020, \$1.977 billion on September 30th, 2020, \$1.484 billion on June 30th, 2020, \$1.998 billion on March 31st, 2020, \$2.236 billion on December 31st, 2019, \$2.140 billion on September 30th, 2019, \$2.200 billion on June 30th, 2019, \$2.012 billion on March 31st, 2019, \$2.176 billion on December 31st, 2018, \$0.361 billion on September 30th, 2018, \$2.553 billion on June 30th, 2018, \$2.515 billion on March 31st, 2018, \$2.502 billion on December 31st, 2017, \$0.381 billion on September 30th, 2017, \$2.249 billion on June 30th, 2017, \$2.141 billion on March 31st, 2017, \$2.295 billion on December 31st, 2016, \$2.252 billion on September 30th, 2016, \$2.060 billion on June 30th, 2016, \$2.010 billion on March 31st, 2016, \$2.186 billion on December 31st, 2015, \$1.983 billion on September 30th, 2015, \$1.954 billion on June 30th, 2015, \$1.860 billion on March 31st, 2015, \$1.991 billion on December 31st, 2014, \$1.723 billion on September 30th, 2014, \$1.712 billion on June 30th, 2014, \$1.629 billion on March 31st, 2014, \$1.795 billion on December 31st, 2013, \$1.634 billion on September 30th, 2013, \$1.598 billion on June 30th, 2013, \$1.530 billion on March 31st, 2013, \$1.621 billion on December 31st, 2012, \$1.459 billion on September 30th, 2012, \$1.446 billion on June 30th, 2012, and it was \$1.412 billion on March 31st, 2012. “Starbucks Cost of Goods Sold 2010-2022 | SBUX”.

Quarterly Costs of Goods (in Billions)

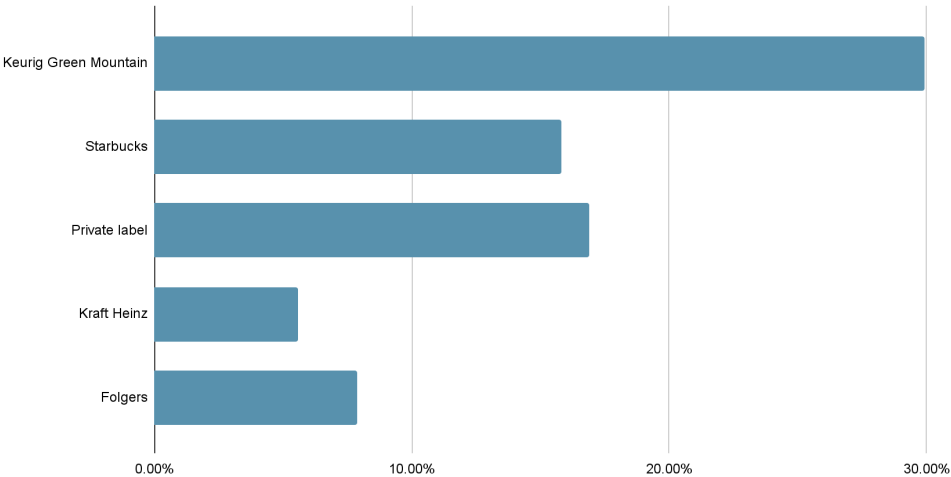
<u>Year</u>	<u>March 31st</u>	<u>June 30th</u>	<u>September 30th</u>	<u>December 31st</u>
2022	\$2.466	-	-	-
2021	\$1.992	\$2.206	\$2.491	\$2.527

2020	\$1.998	\$1.484	\$1.997	\$2.049
2019	\$2.012	\$2.200	\$2.140	\$2.236
2018	\$2.515	\$2.553	\$0.361	\$2.176
2017	\$2.141	\$2.249	\$0.381	\$2.502
2016	\$2.010	\$2.060	\$2.252	\$2.295
2015	\$1.860	\$1.954	\$1.983	\$2.186
2014	\$1.629	\$1.712	\$1.723	\$1.991
2013	\$1.530	\$1.598	\$1.634	\$1.795
2012	\$1.412	\$1.446	\$1.459	\$1.621

Overall Market

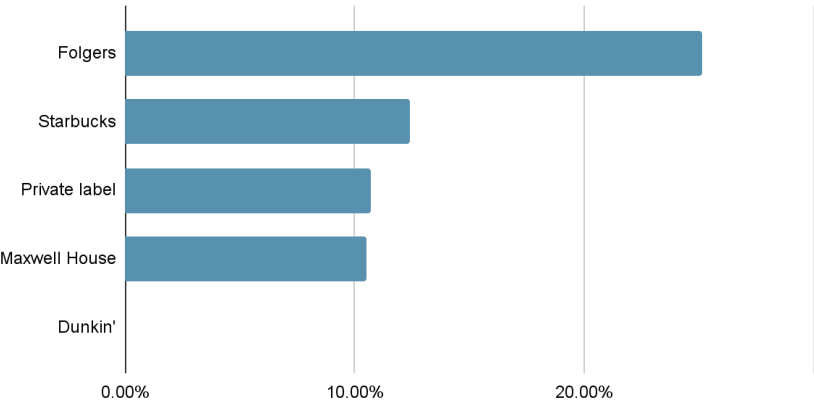
When looking for the overall market share for leading coffee vendors, I was not able to find 5 years worth of data. Rather, I have found data from the years 2017, 2020, and 2021.

Market Share of the Leading Single-Cup Coffee Vendors in the United States in 2017



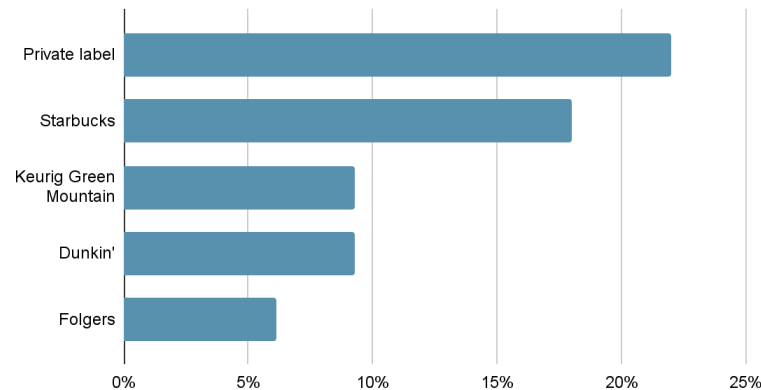
Grocery Headquarters (2017)

Market Share of Ground Coffee in the United States in 2020, by Leading Brands



Beverage Industry Magazine (2020)

Market Share of Single-Cup Coffee in the United States in 2021,
by Leading Brands



Beverage Industry Magazine (2021)

When looking at the barriers of entry for Starbucks, I'm taking a look at Porter's Five Forces Analysis of the Retail Coffee and Snacks Industry.

When it comes to the "Threat of New Entrants", there is a moderate threat. This is because the barriers to entry are not high enough that it would discourage new competitors from entering the market. For new entrants, initial investments are not as significant as they can lease all the items needed to begin. At a localized level, smaller shops can compete with the higher competitors such as Starbucks. There is a high barrier for new entrants as they can change themselves from Starbucks' products.

The “Threat of Substitutes” is high. There are many different beverage substitutes for coffee. These can include soda, water, energy drinks, tea, etc. When it comes to the social aspect, bars and pubs can offer non-alcoholic drinks that can compete with the social experience at Starbucks. Consumers also have the choice of making their coffee at home. This can cut the cost spent at Starbucks tremendously.

When it comes to “bargaining Power of Buyers” the threat is moderate to low. There are a lot of buys in the industry, and no individual buyer can demand a certain price concession. It offers a vast array of differentiated products with a wide range consumer base, which in turn, creates a low volume of purchases, and erodes a buyer’s power. Even though there is no switching costs with high availability of substituted products, industry leaders, such as Starbucks, can price their product mix in relation with their rival stores and do so with prevailing market price elasticity and challenging premium pricing.

In regards to “bargaining Power of Suppliers” there is a low to moderate threat. The main inputs into the value chain are the coffee beans and the premium Arabica coffee grown at Starbucks that are standard inputs. This can make the cost of switching between different suppliers pretty low. With the size and scale that Starbucks possesses, it has the power to take advantage of their suppliers but also maintains fair trade certified coffee under their C.A.F.E (Coffee and Farmer Equity) program. This provides the suppliers with a fair partnership status, and yields them at low power. Starbucks’s suppliers in the industry pose a low threat when it comes to competing against Starbucks by the forward vertical integration, and lowers their power. In addition, Starbucks forms an incredibly important part of the supplier's business. With its scope and size, it makes the power of the suppliers low.

Finally, when it comes to the “Intensity of Competitive Rivalry”, the threat is high to moderate. This specific industry type is a monopolistic competition. With Starbucks having the largest market share and their closest competitors also have such a high market share, this can create immense pressure on Starbucks. The consumers do have a cost to switch to other competitors, and it creates a high intensity for rivalry. While it is important to note that Starbucks has a competitive advantage as it has a different assortment of products, it can cause a moderate level in intensity when it comes to competition. The industry has moderately low growth rate, and is considered mature, which causes the intensity of competition against rivals to be moderately high as all of them are looking to increase their market share from established firms such as Starbucks. The industry does not have over capacity as of now, and the factors can contribute to the intensity of rivalry to be moderately high Geereddy (unknown date).

Starbucks would be categorized into a monopolistic competition. A few defining traits of monopolistic competition are slightly different products and services, free entry and exit from the market, many companies, imperfect consumer knowledge, and profits. Indeed Editorial Team (2021). There is also a significant amount of non-price competition, or the idea that firms cannot compete on prices. An example from this article was the idea that a street vendor could sell their coffee for \$0.50 per cup of coffee, while Starbucks will be about \$5.00 for a cup of coffee. The street vendor cannot compete with Starbucks based on charging low prices because Starbucks differentiates their product through the coffee’s quality, good atmosphere, and the infrastructure of a Starbucks building. The industry is in a mature stage. Agarwal (2022). Both Starbucks and Dunkin’ Donuts make up more than 60% of the market share, and that gives them considerable market power. Starbucks also maintains 36.7% of the market share in the United States, and has

operations in 60+ different countries. It has been ranked 91st in best global brands of 2013, and is one of the most recognized brands. Because of their strong market position and brand recognition, it can allow Starbucks to increase their already significant competitive advantage in expanding into the international markets and reach higher growth in international and domestic markets. Geereddy (unknown date).

Recommendation

As Starbucks is already dominating the market, there isn't a whole lot said about how to manage its future production. However, in today's society, people are trying to become more eco friendly, and that would be an amazing opportunity for Starbucks to manage their future production. It is said that we can save \$26 trillion dollars by 2030 if we do a global shift to sustainable development. Costs of sustainable alternatives are declining, which would cut costs for Starbucks supply. Although they are already becoming more eco friendly, there are always more ways to promote the switch. Roberts (2018). According to the Starbucks website, Starbucks chief executive officer Kevin Johnson had announced a multi-decade commitment to becoming a resource-positive company. It is said that "[Starbucks] aspiration is to become more resource positive - storing more carbon than it emits, eliminating waste, and providing more clear, freshwater than it uses". Starbucks global operations and supply chain give their five strategies to prioritize work:

1. Expanding their plant-based options, moving towards an environmentally friendly menu
2. Going from single-use packaging to reusable ones

3. Investing in innovative and regenerative agricultural practices, and helping to conserve forests and water replenishment
4. Finding better ways to manage the waste of Starbucks' stores and their communities
5. And developing more eco-friendly stores, delivery, manufacturing and operations

Johnson also outlined the targets Starbucks has by the year 2030

1. 50% reduction in carbon emissions from Starbucks' direct operations and their supply chain
2. 50% water withdrawal for the coffee and operations
3. 50% reduction in waste sent to landfills from their stores

Since Starbucks currently dominates the market share, they have the safety and profit to spend more money and time into totally switching to eco-friendly resources. Since they've already done a lot to push more eco-friendly options, the price changes wouldn't leave as much of a dent compared to their supply costs already.

Going back to the demographics at Starbucks, it is said that 25% of Starbucks' customers say that purchasing organic groceries and coffee is important to them. This can give off the idea that these people care about where their items come from, and where they go after they're done with them. This also gives the impression that if Starbucks became totally eco-friendly, this could bring in an influx of customers who would rather spend their money on a place that doesn't create waste. Gaille (2016). It is said that Starbucks goes through 4 billion single-use cups per

year, and 99% of them are not recycled. Because of this heavy impact on the Earth, paying that extra bit to make cups biodegradable can increase their influx of consumers. Smith (2020).

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