
CI6228 Managing Information Systems

NANYANG TECHNOLOGICAL UNIVERSITY -
WEE KIM WEE SCHOOL OF COMMUNICATION AND INFORMATION



**Title: *Competitive Forces of
Coffee Chain Industry: Starbucks Coffee***

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A Term Paper of Starbucks Analysis
with Porter's Five Forces Model
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Abstract

As digital devices and technologies permeate more and more in our everyday life, our society quickly finds itself saturated with tech-savvy consumers. Technological innovations can bring a competitive edge to not just in the coffee chain industry, but in any other potential businesses. Who would have thought that coffee and technology are marrying.

This paper looked at the case of Starbucks and investigated the success factors that have led to its achievement of Fortune's 6th Most Admired Companies in 2020 via the lens of Porter's Five Forces Model. In this regard, the approaches employed by Starbucks in its differentiation focus strategy reflected careful considerations to capitalize rather than mitigate the competitive forces, as a result, the Starbucks brand is often synonymously associated with loyalty, integrity and longevity.

Keywords: Coffee Chain Industry, Porters Five Forces, Technological Innovations

1 - Introduction

In the recent and upcoming years, major businesses in various industries are making technological innovations radically to transform the competitive landscape to keep up with the rapid advancement of technology, one of which are coffee chain industries. With an average consumption of three cups of coffee per day for coffee drinkers (E-Imports, 2020), independent coffee shops are generating \$11 billion in annual sales just in the United States of America alone (Rizea et al., 2014).

This paper aims to examine the competitive forces in coffee chain industry of Starbucks, with the objective of investigating factors that could have led to its current successes and achievement of Fortune's 6th Most Admired Companies in 2020, surpassing companies like Alphabet, Coca-Cola and Nike (Fortune, 2020). This will be accomplished via the lens of Porter's Five Forces Model.

1.1 - Glimpse into the Coffee Chain Industry

Being a relatively affordable beverage, no one would have thought about its flavour or any sophisticated attachment tied to the drink before the rise of the coffee chain industry . The estimated coffee consumption worldwide is over 9 billion kilograms worth of coffee beans annually — coffee is indeed big business (Kida, 2019).

Kida (2019) also noticed that the booming of coffee chain industry is mainly driven by the demand for specialty coffee due to our increase of disposable income as the economy becomes better. Eventually, competitions within this industry will arise as consumer expectations increases, technological innovations play an even larger role to keep up with the demands in our era, with cashless payment being a vital component in all coffee houses .

2 - Company background

Starbucks generally operates and often being used as a benchmark among the coffee chain industry to serve premium quality beverages. It had built the largest American coffee empire with over 180,000 employees across nearly 20,000 stores over 60 countries (UK Essays, 2018). Currently, it dominates the coffee chain industry that has prevailed to be in the moderately developed phase (Appendix 1). In terms of market share, both Starbucks and Dunkin Brands have comprised over 60% and with Starbucks dominating over 35% of the entire market (Appendix 2). With this kind of statistics, it possesses a considerable amount of influences in deciding the progression of coffee businesses (Geereddy, 2013). The company's vision is all about quality and people; To be regarded as a communal identity that enriches people's life with their premier neighborhood coffee houses.

2.1 - History of Starbucks



The original Starbucks logo in 1971 (Dejan, 2020)

The Starbucks Corporation originated in Seattle, 1971 was the first to introduce the new coffee culture which was almost non-existent during the 80s in the United States. It was started by three friends who had established a modest store in the trades of coffee. When a vision of transforming it into a country's café was proposed by its head of marketing, Howard Schultz (current Starbucks CEO), the founders had no intentions of deviating from its traditional model. It was until 1987, Schultz bought over Starbucks and the company embarked on to a meteoric course of expansion since then (Bondarenko, 2015).

3 - Literature Review

Schultz observed that novice consumers might sometimes feel uneasy in their stores due to lack of knowledge about cafés and fine coffees (Bondarenko, 2015), so the company adopted the customer-friendly approach by establishing a welcoming and sociable environment (NBRI, n.d.). It visualized itself as a venue where the community can dwell upon accompanying with delightful beverages and had effectively positioned itself to be 'third place' apart from homes and workplaces (Roll, 2017). With its comfy furniture and a cozy interior, not to mention the free WIFI, Starbucks stores are meticulously designed for consumers to linger and mingle, in turn making more purchases and be enticed for another visit. Besides, in order to maintain its extensive global chain, Starbucks has also started to prioritize by making considerable investments in digital enhancements.

3.1 - Technological Innovations

In this age of the digital revolution, coffee retailers like Starbucks have begun to look towards information and communication technologies (ICT) as a source of competitive advantage. This focus was driven by the increase of digital-savvy customers, changing customer demands, technological advancements and greater competitive pressures (Frohman, 1982).

Apart from offering free WIFI, which have already become a norm amongst cafés due to consumer demands of connectivity at all times, the factors mentioned above have culminated in the introduction of Mobile Application, Starbucks Card Payment and Member Rewards Program. Starbucks' continuation of betting big on technological innovations and digital customer experience have resulted consumer spendings increased by a minimum of 20% across all types of consumers (Appendix 3).

3.1.1 - Mobile Application

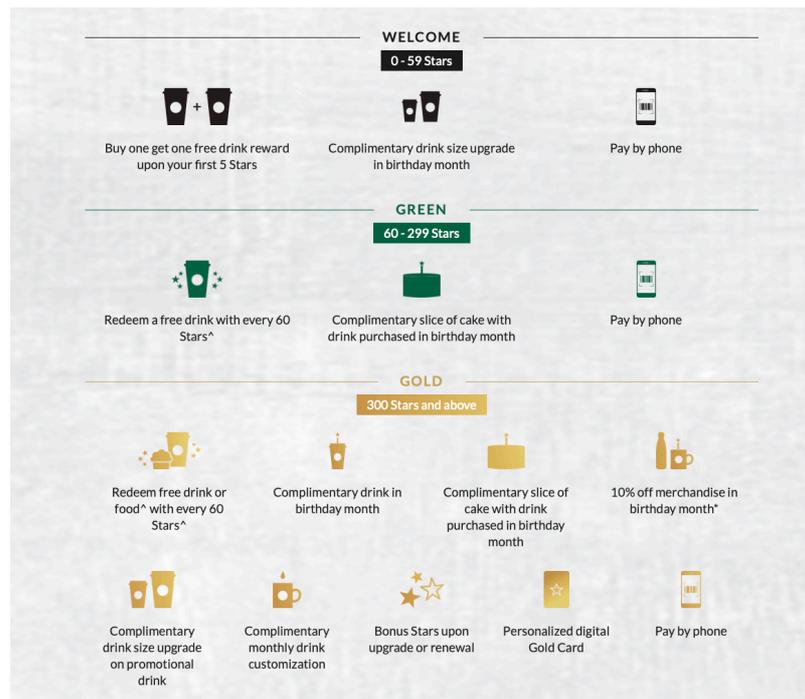
Starbucks launched its mobile application in 2009 and its primary digital assets was to provide a digital payment platform, a customer loyalty program as well as a personalized experience with machine learning technology (Starbucks Stories, 2011). For starters, coffee is something very personal and habitual, so when consumers receive personalized order suggestions based on their contextual awareness such as store proximity, trending selections, forecast and their previous orders, they are very likely to receive and order something that they will enjoy (Sokolowksy ,2019).

3.1.2 - Starbucks Card Payment

Starbucks also uses its mobile application to bring convenience for consumers to make their daily Starbucks run. Rather than waiting in line and proceed on with the troublesome physical payment, consumers are now able to effortlessly carry out payments in a couple of clicks (Salem 2015). Consumers can easily pay either via credit payments, or their Starbucks Card to accumulate rebates. The Starbucks Card exists in both digital and physical forms, bringing convenience to its utility and can be reloaded with various methods even with the balance from another card. Oragui (2018) noted that for Apple Watch users, the barcode of the card can be integrated into watch and for users who are constantly on the go. These wide variety of order and payment methods eventually which encourages greater sales.

The company revealed that it has acquired an annual revenue of \$150 million just from its pre-paid cards alone and it is foreseen to multiply as more and more consumers start to enrol onto its platform. This passive working capital component has since been rendering serious cash flow for the coffee giant (Christy, 2017).

3.1.3 - Starbucks Rewards Program



Starbucks Rewards Program (Starbucks, 2020)

Starbucks further introduced its Starbucks Rewards Program in 2009 (Starbucks Stories, 2019), where members were able to translated purchases into rebates, being referred as Stars, and redeem them for a cup of beverage or merchandises over time (as shown above). This program is a tremendous successful with a staggering 16 million active members, attributing 40% of its total sales (Leah, 2020).

With the launch of its mobile application, the program was integrated and have seen impressive membership growth ever since, increasing the recurrence and spendings of both its frequent and infrequent consumers. This allows Starbucks to reinvent the relationship with their all types of consumers and generate consumer loyalty as well as revenue increasingly.

Ultimately, the true value of its technological innovations lies in its diversified and large volume of consumer data harvested, forming the foundation of Starbucks' digital strategy.

3.2 - Business Strategy

According to Starbucks (2020), its mission is “To inspire and nurture the human spirit — one person, one cup and one neighborhood at a time”. As Tay (2013) named it “The Starbucks experience”, Starbucks have a differentiation focus business strategy to focus, lead and innovate on a particular type target and market, alongside with consumers whom have the similar vision of requiring premium quality coffee and expenditure capability — notably modern metropolitan white-collar works and college students (UK Essays, 2016).

The other key standard is to stipulate a culture by providing services that consumers are able to feel upon and appreciate more than any other companies and is hard to be replicated. Starbucks workers are accustomed in the manners of Starbucks etiquette and behavior since the very beginning to provide every consumer a delightful experience without fail. They are trained to make an effort to connect with their consumers, not just getting their order right, but also by their name and their regular orders. Moreover, the “LATTE Method” serves as the protocol to mitigate unpleasant situations: “Listen and Acknowledge to customer’s complaint, and Take action by resolving the issue, then Thank them and Explain why the issue occurred” (Tay, 2013).

Nevertheless, Starbucks differentiation focus strategy touches upon every stakeholder; From sourcing of materials at the origin of suppliers and enhancing their farmers’ quality of life to cultivate good quality coffee beans (UK Essays, 2016), treating the employees as working partners in ways of making the difference with service-oriented minds, and connecting with consumers as well as keeping the flow of regular consumers in daily for their Starbucks run. As a result, the Starbucks brand is often synonymously associated with loyalty, integrity and longevity.

3.3 - Organization Structure

Starbucks has a Matrix organization structure whereby its business is being managed by a board of directors based in Seattle, Washington (UK Essays, 2018) and further distributed into area of authority where the regional managers are then appointed as native employers to oversee the employees at specific shop locations. By not adopting a franchise system, it enables Starbucks to ascertain strict quality control of its mission and guidelines. Besides, Starbucks structural design can be classified into the following main divisions:

3.3.1 - Geographic Divisions

There three main geographic divisions of Starbucks which are the Americas, Asia-Pacific (APAC) and, Europe, Middle East, and Africa (EMEA). As mentioned, every geographic division consists of a leading officer who is given the flexibility in realigning approaches and procedures in order to accommodate their particular regional requirements (Meyer, 2014).

3.3.2 - Product-based Divisions

Following that, it comprises of product-based divisions as well to address the product lines like coffee-related items, bakery-related items and merchandise goods (Sobiya, 2018). This enables Starbucks to focus with the development of its products with support through its organizational structure.

3.3.3 - Brand-based Divisions

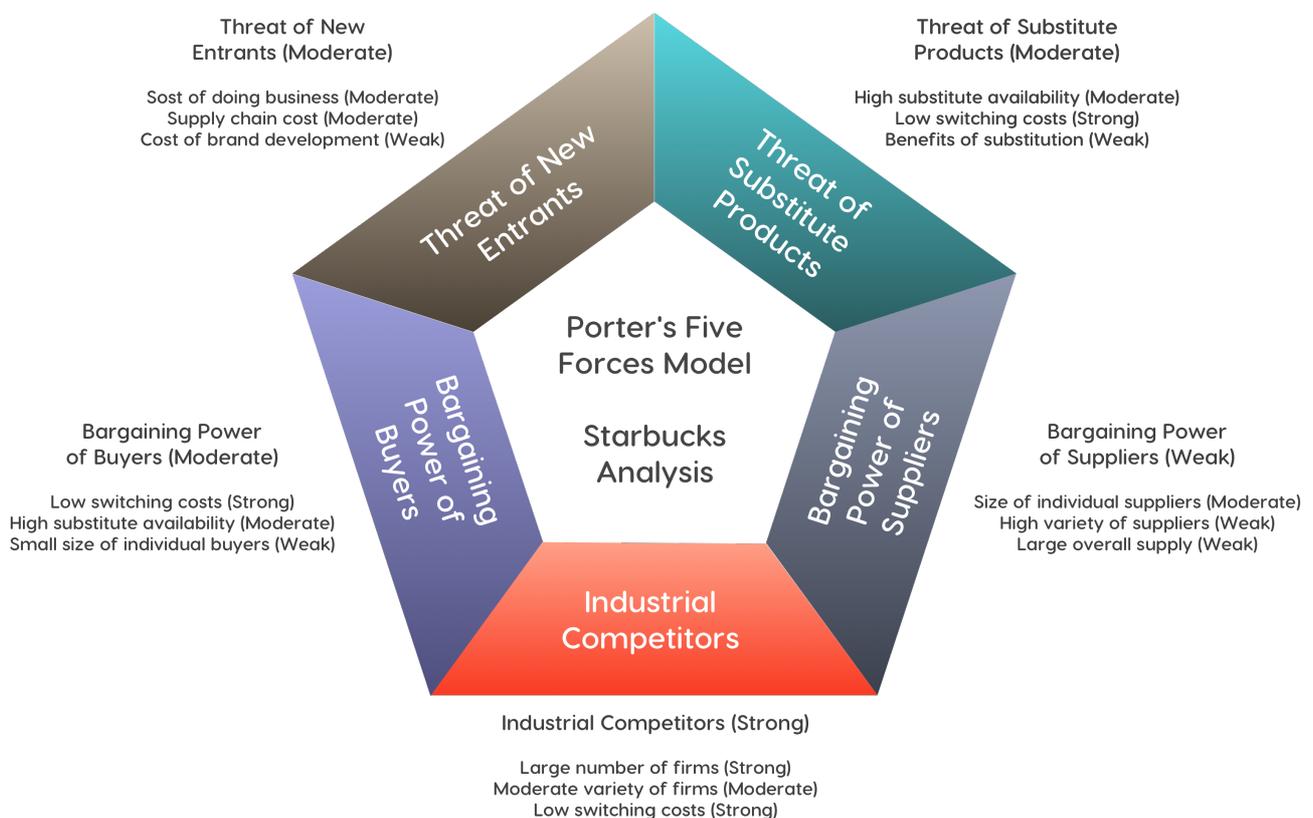
Lastly, Starbucks further advertises its commodities onto other labels that it owns which consists of Evolution Fresh, La Boulange, Seattle's Best Coffee, Tazo Tea and Teavana (Dudovskiy, 2017). Moreover, a variety of off-the-shelf Starbucks coffee and tea products are also marketed via channels like licensed stores, supermarkets and national foodservice accounts.

4 - Discussion

As different industries have different types of establishments, competitions and opportunities, in order to have a greater perception about the coffee chain industry, a thorough analysis using Micheal Porter's Five Forces Model (Porter, 1998) is being applied to examine their competitive positions in the industry.

4.1 - Porter's Five Forces Model

Porter's Five Forces Model aids to analyze to what degree companies are situated in regards to its strengths and weaknesses. It consists of five important forces which could influence its industrial standing among its rivals. This model has grown to be relatively applicable in the international industries especially for big businesses. The followings are the evaluations with Porter's Five Forces that influenced Starbucks competing standing in the coffee chain industry:



4.1.1 - Threat of New Entrants (Moderate)

Starbucks faces a moderate force in Threats of New Entrants as the business do not require huge funds to start-up, resulting in relatively low barrier and moderately high level of saturation. Besides, it also depends on the variability of implementing and sustaining the business as a coffee store itself (Greenspan, 2019). For instance, the managing and supply chain cost of smaller coffee stores are much lower as compare to a large coffee chain like Starbucks. Nevertheless, Starbucks gets mitigated to a large extent with its huge establishments of its framework, commodity value, technological innovations and most of all, the brand development that would require umpteen years for new brands to reach the level of Starbucks.

4.1.2 - Bargaining Power of Buyers (Moderate)

For the Bargaining Power of Buyers, Starbucks experiences a moderate force in terms of its low switching costs whereby competitors can try to attract consumers using lower prices. With that being said, the diversification of Starbucks consumers and product mix indicates that buyers do not hold much influence, making them less sensitive to price fluctuations. Starbucks consumers are mostly inclined to fork out a premium amount for their Starbucks run and also leverage on the loyalty rewards program and 'third place' experiences.

4.1.3 - Bargaining Power of Suppliers (Weak)

The force of Bargaining Power of Suppliers is weak against Starbucks because it has a supplier divergence guideline to source its supplier ethically from multiple regions (Geereddy, 2013). On top of that, long-term contracts are also being used with suppliers to dilute potential price volatility and exclusively supply of their coffee beans, which could possibly place them into financial burden if they decided to supply other companies (UK Essays, 2017).

4.1.4 - Threat of Substitute Products (Moderate)

There is a moderate force of Threat of Substitute Products for Starbucks from the wide variety range of soft drinks to bubble tea and even instant beverage powders that allows consumers to easily fulfill their caffeine intake efficiently with a fraction of Starbucks price, especially during economic recession period. Also to address the health concerns, at any point of time, consumers might just switch to healthier beverages such as fruit juices, milk, herbal drinks or simply mineral water (UK Essays, 201).

Ironically, despite being a less healthier choice among the beverages mentioned, coffee has gradually gained preference as it is still relatively a healthy alternative as opposed to over soft drinks which are overly associated with fast food and its high level of sugar content.

4.1.5 - Industrial Competitors (Strong)

Finally, Industrial Competitors are the strongest force that Starbucks faces and is experiencing. Unlike the early days, when Starbucks was mainly competing with small-sized coffee retailers, the dynamics within the coffee chain industry has now changed drastically with the influx of companies of various sizes and impeding competitions by lower pricing and products differentiate improvements like offering unique beverages and techniques.

Perhaps the largest industry rival of Starbucks — McDonald's, who began selling numerous coffee related beverages under the name of McCafé. At the same time, Starbucks answered by adding drive-thru ordering and offering McMuffin-like sandwiches to their stores (UK Essays, 2017). All these implementations have drawn both companies close as arch competitors, due to the intrusions of each other's demographic markets that were being exemplified by both parties.

4.2 - Critique of Current Strategy

In regards to Porter's Five Forces Model analysis, industrial competitors are clearly Starbucks top-priority challenge, followed by having a low switching and high substitutions of products.

Being the benchmark of the coffee chain industry, Starbucks current strategies focuses on its intensive growth, providing high quality specialty beverages and heightening the user experiences of its existing consumers. These are its reflections of strategic responses to its competitions. With that being said, Starbucks is not addressing or targeting the budget market or new consumers which may result its competitors to capitalise with lower prices with similar quality beverages. Even Apple caters to the budget market by having its low-cost products like the iPhone SE to boost its sales (Nikkei, 2019).

5 - Future Recommendations

Starbucks may or may not address the new potential low-budget consumers with a new line of more affordable beverages to preserve its brand reputation, that can correspondingly build more brand awareness and a competitive edge. Regardless, these new affordable beverages can also include premium coffee packages and more healthy drinks like fruit juices and warm high calcium beverages to broaden its demographic spectrum to more senior citizens or boomers who have different value of lifestyle (UK Essays, 2016).

Lastly, in regards to Starbucks technological innovations, it should definitely continue to invest in both IS and IT systems, for instance, the use of semi-automatic smart coffee machines can reduce overload tasks of their employees to generate better partners satisfaction and eventually minimizing turnover rates, especially during the peak periods.

6 - Conclusion

The case of Starbucks highlighted important key points for companies among the coffee chain industry who are hoping to leverage on the opportunities afforded by technological innovations. All in all, Starbucks not only leads in the coffee chain industry, but also serves as a representative of the entire global business industry. After identifying the company's five competitive forces, we can see that Starbucks is currently at a strong stance by progressively innovating on related diversification and differentiation strategies to establish the overall values of its products. Nevertheless, Starbucks will remain as the benchmark and should be aware of other companies like McDonald's, who is in pursuit to achieve its maximum potential.

With the astounding success of expansions and digital advancements despite of its competitive forces in the stable growing industry, it is safe to say, Starbucks is here to stay.

6.1 - Future Research Possibilities

This paper investigated Starbucks strategic journey in terms of its IT investments and competitive forces. Two possible avenues of research could be explored from this will be:

1) Proceed on to investigate other two views of Porter's value chain and the Resource-Based View of Starbucks strategic journey.

2) Analyse whether the IS Strategy Triangle Framework holds up to Starbucks organisational and information strategy in support of overarching its business strategy discussed in this paper. With recent trends of a digital business strategy, the adoption of ICT may precede rather than being driven by its business strategy. Therefore, technology itself, as Coltman et al. (2015) advised, may either drive the formulation of business strategy or is intertwined with strategy such that the distinction between business strategy and information strategy becomes blurred.

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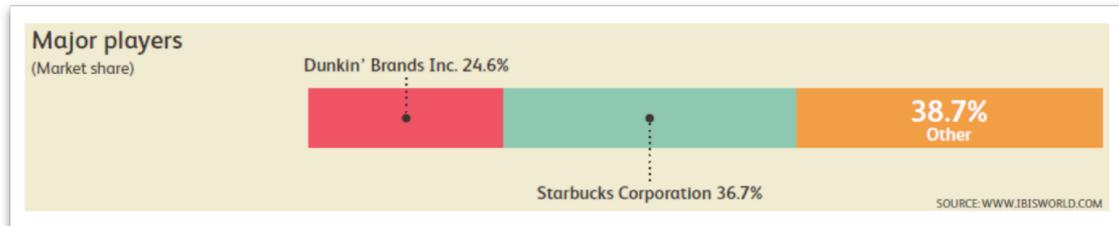
Appendix

Appendix 1

Industry Structure				
	Life Cycle Stage	Mature	Regulation Level	Medium
	Revenue Volatility	Medium	Technology Change	Medium
	Capital Intensity	Medium	Barriers to Entry	Low
	Industry Assistance	None	Industry Globalization	Low
	Concentration Level	Medium	Competition Level	High

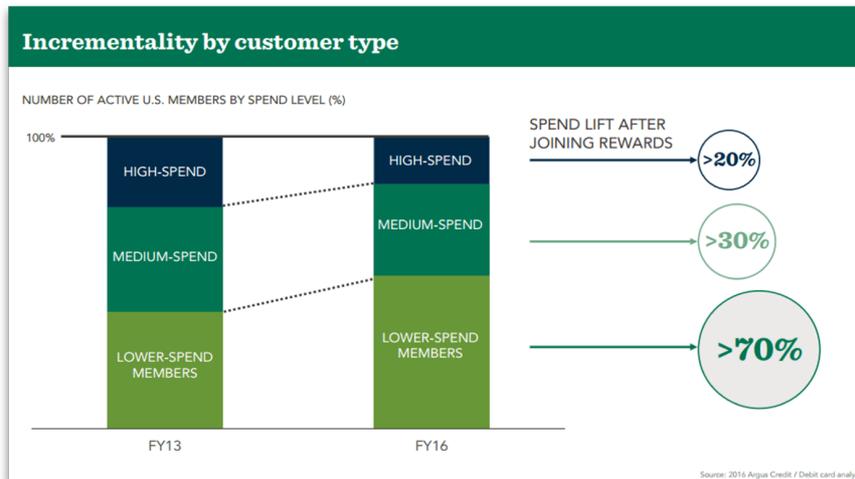
IBIS World: The Coffee & Snack Shop Industry in the US Report, October 2013;
Source: IBIS World Report.

Appendix 2



IBIS World: The Coffee & Snack Shop Industry in the US Report, October 2013;
Source: IBIS World Report.

Appendix 3



Incremental Spend After Digital Conversion, 2016;
Source: Starbucks Investor Presentation 2016.