Australasian Marketing Journal 18 (2010) 41–47

Contents lists available at ScienceDirect

Australasian Marketing Journal

journal homepage: www.elsevier.com/locate/amj

How the local competition defeated a global brand: The case of Starbucks

Paul G. Patterson *, Jane Scott, Mark D. Uncles

School of Marketing, Australian School of Business, University of NSW, Sydney, NSW 2052, Australia

ARTICLE INFO

Keywords:
Service brands
Service quality
Global branding
International business
Starbucks
Coffee

ABSTRACT

The astounding growth and expansion of Starbucks is outlined, both on a global scale and within Australia. The focus then shifts to the abrupt closure of three-quarters of the Australian stores in mid 2008. Several reasons for these closures are described and examined, including that: Starbucks overestimated their points of differentiation and the perceived value of their supplementary services; their service standards declined; they ignored some golden rules of international marketing; they expanded too quickly and forced themselves upon an unwilling public; they entered late into a highly competitive market; they failed to communicate the brand; and their business model was unsustainable. Key lessons that may go beyond the specifics of the Starbucks case are the importance of: undertaking market research and taking note of it; thinking globally but acting locally; establishing a differential advantage and then striving to sustain it; not losing sight of what makes a brand successful in the first place; and the necessity of having a sustainable business model.

1. Introduction

"Shunned Starbucks in Aussie exit"
(BBC News, 4 August 2008)

"Weak coffee and large debt stir Starbucks' troubles in Australia"
(The Australian, 19 August 2008)

"Memo Starbucks: next time try selling ice to Eskimos"
(The Age, 3 August 2008)

"Taste of defeat for the mugs from Starbucks"
(Sydney Morning Herald, 31 July 2008)

"Coffee culture grinds Starbucks' Australian operation"
(Yahoo News, 3 August 2008)

When the announcement was made in mid 2008 that Starbucks would be closing nearly three-quarters of its 84 Australian stores there was mixed reaction. Some people were shocked, others were triumphant. Journalists used every pun in the book to create a sensational headline, and it seemed everyone had a theory as to what went wrong. This case outlines the astounding growth and expansion of the Starbucks brand worldwide, including to Australia. It then shifts focus to describe the extent of the store closures in Australia, before offering several reasons for the failure and lessons that others might learn from the case.

2. Background

Founded in 1971, Starbucks' first store was in Seattle's Pike Place Market. By the time it went public in 1992, it had 140 stores and was expanding at a breakneck pace, with a growing store count of an extra 40–60% a year. Whilst former CEO Jim Donald claimed that "we don't want to take over the world", during the 1990s and early 2000s, Starbucks were opening on average at least one store a day (Palmer, 2008). In 2008 it was claimed to be opening seven stores a day worldwide. Not surprisingly, Starbucks is now the largest coffee chain operator in the world, with more than 15,000 stores in 44 countries, and in 2007, accounted for 39% of the world's total specialist coffee house sales (Euromonitor, 2008a). In North America alone, it serves 50 million people a week, and is now an indelible part of the urban landscape.

But just how did Starbucks become such a phenomenon? Firstly, it successfully Americanised the European coffee tradition – something no other coffee house had done previously. Before Starbucks, coffee in its current form (latte, frappacino, mocha, etc.) was alien to most US consumers. Secondly, Starbucks did not just sell coffee – it sold an experience. As founding CEO Howard Schultz explained, "We are not in the coffee business serving people, we're in the people business serving coffee" (Schultz and Yang, 1997). This epitomised the emphasis on customer service such as making eye contact and greeting each customer within 5 seconds,

* Corresponding author. Tel.: +61 2 9385 1105.
E-mail addresses: p.patterson@unsw.edu.au (P.G. Patterson), janescott@primus.com.au (J. Scott), m.uncles@unsw.edu.au (M.D. Uncles).

1441-3582/$ - see front matter © 2009 Australian and New Zealand Marketing Academy. Published by Elsevier Ltd. All rights reserved.
doi:10.1016/j.ausmj.2009.10.001

cleaning tables promptly and remembering the names of regular customers. From inception, Starbucks' purpose was to reinvent a commodity with a sense of romance, atmosphere, sophistication and sense of community (Schultz and Yang, 1997). Next, Starbucks created a 'third place' in people's lives – somewhere between home and work where they could sit and relax. This was a novelty in the US where in many small towns café culture consisted of filter coffee on a hot plate. In this way, Starbucks positioned itself to not only sell coffee, but also offer an experience. It was conceived as a lifestyle café. The establishment of the café as a social hub, with comfortable chairs and music has been just as important a part of the Starbucks brand as its coffee.

All this came with a premium price. While people were aware that the beverages at Starbucks were more expensive than at many cafés, they still frequented the outlets as it was a place 'to see and be seen'. In this way, the brand was widely accepted and became, to an extent, a symbol of status, and everyone's must-have accessory on their way to work. So, not only did Starbucks revolutionise how Americans drank coffee, it also revolutionised how much people were prepared to pay.

Consistency of product across stores, and even national boundaries, has been a hallmark of Starbucks. Like McDonald's, Starbucks claims that a customer should be able to visit a store anywhere in the world and buy a coffee exactly to specification. This sentiment is echoed by Mark Ring, CEO of Starbucks Australia who stated "consistency is really important to our customers . . . a consistency in the product . . . the overall experience when you walk into a café . . . the music . . . the lighting . . . the furniture . . . the person who is working the bar". So, whilst there might be slight differences between Starbucks in different countries, they all generally look the same and offer the same product assortment. One way this is ensured is by insisting that all managers and partners (employees) undergo 13 weeks of training – not just to learn how to make a coffee, but to understand the nuances of the Starbucks brand (Karolefski, 2002) and how to deliver on its promise of a service experience.

The Starbucks formula also depends on location and convenience. Starbucks have worked under the assumption that people are not going to visit unless it's convenient, and it is this assumption that underlies their highly concentrated store coverage in many cities. Typically, clusters of outlets are opened, which has the effect of saturating a neighbourhood with the Starbucks brand. Interestingly, until recently, they have not engaged in traditional advertising, believing their large store presence and word-of-mouth to be all the advertising and promotion they need. Starbucks' management believed that a distinctive and memorable brand, a product that made people 'feel good' and an enjoyable delivery channel would create repeat business and customer loyalty.

Faced with near-saturation conditions in the US – by 2007 it commanded 62% of the specialist coffee shop market in North America (Table 1) – the company has increasingly looked overseas for growth opportunities. As part of this strategy, Starbucks opened its first Australian store in Sydney in 2000, before expanding elsewhere within New South Wales and then nationwide (albeit with 90% of stores concentrated in just three states: NSW, Victoria and Queensland). By the end of 2007 Starbucks had 87 stores, enabling it to control 7% of the specialist coffee shop market in Australasia (Table 1). By 2008, consumer awareness of Starbucks in Australia was 90% (Shoebridge, 2008), with each outlet selling, on average, double the number of coffees (270 a day) than the rest of Australia's coffee shops (Lindhe, 2008).

3. Expansion into Asia

Starbucks currently operates in 44 markets and even has a small presence in Paris – birthplace and stronghold of European café culture. Beyond North America, it has a very significant share of the specialist coffee shop market in Western Europe, Asia Pacific and Latin America (Table 1) and these regions make strong revenue contributions (Table 2). It is in Asia that they see the most potential for growth as they face increasing competitive pressure in their more traditional markets. Half the international stores Starbucks plans to operate in the next decade will be in Asia (Euromonitor, 2006; Browning, 2008). Indeed, Starbucks has done well in international markets where there has not traditionally been a coffee drinking culture, namely Japan, Thailand, Indonesia and China. In effect it has been responsible for growing the category in these markets.

The first Starbucks outside the US opened in Tokyo in 1996, and since then, Starbucks' Japanese stores have become twice as profitable as the US stores. Unsurprisingly then, Japan is Starbucks' best performing overseas market outside North America. More than 100 new stores open each year in Japan, and coffee is now more popular than tea in terms of both volume and value (Lee, 2003; see also Uncles, 2008). As opposed to their entry into the Australian market, Starbucks made small changes to its formula for the Japanese market; for example, the invention of a green tea frappucino, and the provision of smaller drinks and pastries to conform to local tastes.

Starbucks arrived in China in 1998 and by 2002 had 50 outlets, and 165 outlets by 2006 (BBC News, 2006), quickly becoming the nation's leading coffee chain. Starbucks now sees China as its key growth market due to the size and preferences of the emerging middle class. In the Asia–Pacific region, Starbucks command of the specialist coffee shop market grew from 15% in 2002 to 19% in 2007 (refer to Table 2).

The total market for cafés in China grew by over 135% between 1999 and 2004 to reach US$2.6 billion. It is projected to grow another 144% by 2008 to reach US$6.4 billion in sales. More specialty coffee shops are opening across China as a middle class with strong purchasing power emerges, although this rise in coffee consumption is highly concentrated in large cities such as Beijing, Shanghai and Guangzhou. Starbucks has said that it expects China to become its biggest market after the US and the plan is to open 100 stores a year (Euromonitor, 2006).

Significantly, certain Western brands are valued by Chinese consumers and Starbucks appears to be one of them. A growing number of China's 500 million urbanites favour Starbucks for its ambience, which is seen as an important signal of service quality,

Table 1
Starbucks' share of the specialist coffee shop market in each major region.

Region	2002 (%)	2007 (%)
North America	44	62
Western Europe	17	21
Asia Pacific	15	19
Australasia	6	7
Latin America	0	18

Source: Euromonitor (2008b).

Table 2
Starbucks' regional sales performance by outlets and value 2006.

Region	% of company sales (outlets)	% of company sales (revenue in $US)
North America	79.0	80.5
Asia Pacific	13.3	10.8
Western Europe	6.7	7.7
Australasia	1.1	1.0
World	*100.0*	*100.0*

Source: Percentage of company sales in each region is calculated from retail sales within this market in 2006, with sales data drawn from Euromonitor (2007).

and Starbucks' design concept rests easily with China's consumers, who tend to lounge with friends while sipping coffee. Its outlets in China frequently maintain larger seating areas than average outlets in other countries, and plush chairs and davenports are provided to accommodate crowds that linger.

However, success for Starbucks in China is not a given, and they will face several challenges in the coming years. China's accession to the WTO has led to the gradual relaxation of the policy governing foreign-owned retail outlets, and this will lead to more foreign investment and thereby competition (Lee, 2004). Several multinationals are engaged in selling coffee (including KFC, McDonald's, Yoshinoya, and Manabe), and a number of local brands have recently emerged, some even imitating Starbucks' distinctive green and white logo and its in-store ambience (notably Xingbake in Shanghai). Furthermore, the reduction of import tariffs on coffee will also encourage foreign investment in coffee.

4. The Australian retail coffee industry

Australia's taste for coffee is a by-product of the waves of immigrants arriving on the country's shores following World War II. European migrants, predominantly Greeks and Italians, were the first to establish the coffee culture, which was later embraced more widely in the 1980s. For decades Australians enjoyed a variation of the 'lifestyle coffee experience' that Starbucks created from scratch in the US. Australians did not need to be introduced to the concept of coffee as many other countries did. Savouring a morning cup of coffee was already a ritual for many consumers.

It is fair to describe Australia's coffee culture as mature and sophisticated, so when Starbucks entered Australia in 2000, a thriving urban café culture was already in place. This established culture saw Australians typically patronise smaller boutique style coffee shops, with people willing to travel out of their way for a favoured cup of coffee, especially in Melbourne where coffee has developed an almost cult-like following. For Australians, coffee is as much about relationships as it is about the product, suggesting that an impersonal, global chain experience would have trouble replicating the intimacy, personalisation and familiarity of a suburban boutique café. Furthermore, through years of coffee drinking, many Australians, unlike American or Asian consumers, have developed a sophisticated palate, enjoying their coffee straighter and stronger, and without the need to disguise the taste with flavoured, syrupy shots.

This love of coffee is easily quantified. The Australian market is worth $3 billion, of which $1.8 billion relates to the coffee retailing market. For every cup of coffee consumed out of home, two cups are consumed at home (AustralAsian Specialty Coffee Association, 2006). Per capita consumption is now estimated at 2.3 kg-twice as much as 30 years ago.

Whilst Australians are among the highest consumers of instant coffee in the world, they are increasingly buying coffee out of the home (Euromonitor, 2008c). More than 1 billion cups of coffee are consumed in cafés, restaurants and other outlets each year, representing an increase of 65% over the last 10 years. Even between 2000 and 2005, trade sales of coffee have increased about 18%. In 2007, the growth in popularity of the café culture resulted in trade volume sales growing at an annual rate of 5%. Some 31% of the coffee sold through foodservice is takeaway, and it is thought that 'fast coffee' will be a growth area in future years (Euromonitor, 2008d). There is also a trend towards larger takeaway sizes, with 400 ml cups increasing in popularity (Euromonitor, 2008d). One might argue that Starbucks drove these trends, especially in regards to larger sizes.

There are almost 14,000 cafés and restaurants serving a variety of coffee types in Australia, and during 2006/07, they generated $9.7 billion in income (Australian Bureau of Statistics, 2008). However, despite these statistics, the coffee business does not guarantee success. As Paul Irvine, co-founder of Gloria Jean's notes, "Australia is a tough retail market and coffee retailing is particularly tough". According to official statistics, the café business is not always profitable, with the net profitability of cafés falling to about 4%. For a café to be successful, it has to offer marginally better coffee than local competitors, and do so consistently. Coffee drinkers in Australia are discerning, and they will go out of their way to purchase a good cup of coffee. They are not as easily persuaded as people from other countries simply to visit their nearest café. Secondly, for a café to make a profit, it needs to turn over 15 kg of coffee a week. The national average is 11 kg, so a café has to be above average to begin with to even make a profit. Any newcomer needs to understand this before entering the market. The other significant constraint on profitability is the cost of hiring baristas, with a good one costing between $1000 and $1500 a week (Charles, 2007). However, it seems that this is a necessary cost in order to deliver a superior product.

The question that then begs to be asked is: How well did Starbucks understand this existing coffee culture? Did they under-estimate the relational aspect of coffee purchasing in Australia, as well as the importance of the quality of ingredients and the skills of the person making each cup? Did they overestimate the value consumers attach to the in-store experience and the 'third place' concept? Or did they just look at the statistics regarding coffee consumption and think that operating in Australia was a license to print money? Did they simply see Australia as the next logical step to global domination?

Starbucks has 87% of the US specialty coffee shop market, and only now is it beginning to feel pressure from non-traditional competitors such as Dunkin Donut, 7 Eleven, McCafé and Krispy Kreme (Burritt, 2007). However, in Australia, the competitive landscape is different. Gloria Jean's dominates the high-street part of the coffee retailing market and McCafé dominates the convenience end (Shoebridge, 2008). Other significant competitors include The Coffee Club and Wild Bean Café (an add-on to BP petrol stations) and Hudson's Coffee (see Table 3). All offer a similar in-store experience to Starbucks, with McCafé from 2007 onwards refurbishing many McDonald's stores to imitate the Starbucks' experience, albeit at the economy end of the market.

5. Growth grinds to a halt ... store closures

In recent times however things have started to go wrong for Starbucks. Internationally, company earnings declined as cash-strapped consumers faced record petrol prices and rising interest rates meaning they have had to pull back on gourmet coffee and other luxuries. Sales fell 50% in the last 2 years, the US share price fell more than 40% over the past year and profits dropped 28% (Bawden, 2008; Coleman-Lochner and Stanford, 2008; Mintz, 2008). Consequently, Howard Schultz, the founder and chairman of Starbucks, resumed the position of CEO in 2008 with the aim of revitalising the business. He slowed the pace at which stores were opened (and in fact closed more stores than he will open in the coming year), introduced key performance targets (KPTs) and an employee rewards system in the US, and simultaneously shut down every store in America for three and a half hours of staff training (Muthukumar and Jain, 2008). Customer-oriented initiatives have included the addition of more food, the launch of the Starbucks card and Starbucks express, and the provision of high-speed wi-fi internet access (Hota, 2008). Notably, Schultz acknowledges that the company's focus has been more on expansion than on customer service – the very thing that was at the heart of its unique value proposition.

Table 3
Competition in the Australian specialty coffee chain market (chains arranged in order of the number of stores operating in Australia).

	Number of stores in Australia	Year established in Australia	Business model	Price of an espresso coffee (e.g., flat white, cappuccino)	Performance highlights and lowlights
Gloria Jean's	500	1996	Franchise	Regular $3.25	• Overall Winner, 2005 Franchisor of the Year • Sales rose 18% to an estimated $240 m for 07/08 driven by new stores and growth from existing stores
McCafé	488	1993	Some store-owned, some franchise	Small $3.25	• The fastest growing café brand in Australia and NZ • Number of stores up from 60 in 2002
Coffee Club	220	1989	Franchise	Standard $3.40	• Winner, 2008 Food Franchisor of the Year • The number of stores reported here includes NZ
Wild Bean Café	105	2004	Part of a franchise with Wild Bean Café (BP) Connect	Regular $3.40	• Plans to open more sites
Hudson's	45	1998	Franchise	Small $3.10	• Plans to expand store numbers by 20–30% 08/09
Starbucks	23	2000	Store-owned	Tall $3.60	• Prior to closures in August 2008 there were 84 stores

Sources: Various company reports as at the end of 2008.

However, it seems that these measures were too late for the Australian operation. On 29th July 2008, Starbucks announced that it would be closing 61 of its 84 Australian stores (i.e., 73%) by August 2008, resulting in a loss of 685 jobs. All of these stores had been under-performing (8 were in SA, ACT and Tasmania, 28 in NSW, 17 in Victoria and 8 in Queensland). This decline of Starbucks in Australia was not as sudden as many would have us believe and in fact some reports (Edwards and Sainsbury, 2008; Shoebridge, 2008) indicated that by late 2007 Starbucks already had:

- accumulated losses of $143 million;
- a loss of $36 million for that financial year;
- lost $27.6 million the previous financial year;
- loans of $72.3 million from Starbucks in the US;
- was only surviving because of its US parent's support.

These closures saw 23 stores kept open in prime locations in Sydney, Melbourne and Brisbane. But this begs the question: can a 23-store chain be viable for the brand in the long-term? Based on the approximate numbers in Table 3, Starbucks had a 6% share of stores in Australia before the closures; this has now fallen to a share below 2%. Even before the closures, Australasia represented only 1% of company sales (Table 2) and now the figure is expected to be much lower. This may not make much commercial sense as it will be difficult to achieve economies of scale in terms of marketing and purchasing, and such small numbers are totally out of step with the clustering strategy adopted in its strongest markets – the US, Japan and China. However, it could also be argued that with Starbucks' strategy of global domination, it is unlikely that it will ever close its Australian business entirely.

Whilst Starbucks' management have been keen to suggest that "this decision represents business challenges unique to the Australian market and in no way reflects the state of the Starbucks business in countries outside of the United States", the US market has also suffered. By September 2008, 600 stores had closed (or were due for closure), with about 12,000 workers, or 7% of Starbucks' global workforce affected (Mintz, 2008). It should be noted that the situation in the US has only worsened as a result of the global financial crisis.

6. So what went wrong?

Opinions abound as to why Starbucks failed in Australia. Our research suggests there is some truth to many of these opinions. Whilst the troubled economy might seem an easy scapegoat, with people tightening their belts and eating out less, it is unlikely that this was the core problem as evidenced by the continuing growth of their competitors. Indeed, coffee is no longer considered a luxury item by many Australians, but rather an affordable part of their daily routine. Instead, there is substantial evidence to suggest a number of factors combined to bring about Starbucks' demise.

6.1. Starbucks overestimated their points of differentiation and customer perceived value of their supplementary services

> *"I just think the whole system, the way they serve, just didn't appeal to the culture we have here"*
>
> Andrew Mackay, VP of the Australian Coffee Traders Association, in Martin (2008)

Whilst there was initial curiosity and hype about Starbucks, after trying it, many Australians quickly found that it failed to offer a particularly unique experience that was not offered by other chains or cafés. Given the strong established coffee culture and discerning palates of Australians, the core product – coffee – was not seen as particularly different from, say, a latte or short black from a good suburban barista, Gloria Jean's or Coffee Club. Its point of difference in Australia, where a coffee culture already existed, had to be in its supplementary or value-adding services – i.e., its unique servicescape, engaging customer service, brand image and so on (Lovelock et al., 2007). But was this worth a premium price, especially as the competition began replicating Starbucks in-store experience? Starbucks has since been harshly criticised by Australian consumers and the media. Their coffee has been variously described as 'a watered down product', 'gimmicky', and consisting of 'buckets of milk'. These are not the labels you would choose to describe a coffee that aspires to be seen as a 'gourmet' product. It has also been criticised for its uncompetitive pricing, even being described as "one of the most over-priced products the world has ever seen" (Martin, 2008). Even the idea of the third place has come under criticism – "why would you want to sit around a pretend lounge room drinking a weak and expensive coffee when you can go around the corner and have the real thing?" (Wailes, 2008).

It seems that Starbucks' rapid expansion, its omnipresence, somewhat standardised store design and recent insistence on staff achieving various sales KPTs (key performance targets) such as serving 'x' customers per hour, all combined to diminish the in-store experience. The introduction of sales targets for front-line employees, for example, meant staff and baristas had less time to engage with customers. It began to stray too far from its roots and the very values upon which the brand was built.

Some of these actions were forced upon Starbucks by emerging competitors seeking to imitate the brand, and thus gain a slice of the ever growing lifestyle coffee market. Starbucks' points of differentiation were systematically being eroded and, in a sense, the brand that taught the world that coffee is not a commodity was itself becoming one.

6.2. Declining service quality

The brand has also come under fire for declining customer service as it continued to expand. For example, the quality of baristas is said to have declined as Starbucks widened its pool of applicants in order to meet demand at new stores. Can a 17 year old high school student really compete with a boutique trained barista with a passion for coffee? By not offering a better experience and product than emerging direct competitors, Starbucks found itself undermined by countless high street cafés and other chains that were selling stronger brews at lower prices and often offering better or equal hospitality. Whilst they may have pioneered the idea of a 'third place', it was an easy idea to copy, and even easier to better by offering superior coffee, ambience and service. Now, with so many coffee chains around, Starbucks have little point of differentiation, even wi-fi internet access has become commonplace across all types of café. Furthermore, while customers were offered promotional rewards for returning to Starbucks, the card-based scheme is no more sophisticated than equivalent me-too cards at Gloria Jean's, Coffee Club, Hudson's and many independent cafés.

And as noted earlier, one of the things that set Starbucks apart from the competition – i.e., acknowledging customers (often by name for regulars) within a few seconds of entering the store and seriously engaging with them, began to unravel when Starbucks imposed both customer service *and* sales targets for its cafes. The imposition of these targets plus an ever widening range and complexity of coffees to remember and make to perfection, meant staff morale and inevitably customer service levels declined. In fact in the USA some staff were so disillusioned with the imposition of sales targets (because it meant they simply didn't have time to engage with customers) they posted blogs openly stating that Starbucks had lost its way.

Finally, it appears that Starbucks were not even delivering on their core promise of serving superior coffee in comfortable surroundings, thus justifying its premium price. By switching to vacuum packaged coffee, consumers are denied the store-filling aroma of the coffee beans. The switching of traditional coffee machines to automated espresso machines (which can make coffees 40% faster and move customers through the lines more quickly), has also resulted in a loss of 'theatre' (Grove et al., 2000) for people wanting to see their coffee made that way and has also had implications for taste. In-store, it has been noted that there are fewer soft chairs and less carpeting, and Starbucks recently lost ground in the 'service and surroundings' category of the Brand Keys 2007 Customer Loyalty Engagement Index (Cebrzynski, 2008). It seems that Starbucks is now less about the quality of the coffee, and is more about the convenience of faster service and being on every corner – whilst still charging a premium.

6.3. Starbucks ignored some golden rules of international marketing

Ironically, it seems that the very thing that made Starbucks successful in the first place, its ability to adjust the original (European) business model and coffee tradition to local (US) conditions, is the thing that let it down. Whilst Starbucks has made minor changes to its menu in countries such as Japan and Saudi Arabia, it generally offers the same products all around the world. When the company came to Australia, it brought its 'American' offering, simply bringing what worked in the US and applying it here, without really understanding the local market. But with more than 235 ethnicities speaking more than 270 languages and dialects, companies wanting to get ahead in Australia need to be aware that they are not dealing with one homogeneous market.

> *Unfortunately what worked in the US was "bitter, weak coffee augmented by huge quantities of milk and sweet flavoured syrups. Not so much coffee, as hot coffee-based smoothies". For the Australian consumer raised on a diet of real espresso, this was always going to be a tough sell*
>
> (Mescall, 2008)

As McDonald's Australia chief executive Peter Bush noted, US retailers that have had trouble making it work in Australia (e.g., Starbucks, Denny's, Arby's, Taco Bell) are those that have "introduced formulae developed for US palates and for the US way of doing business ... These formulae have, at best, modest relevance in Australia". Peter Irvine, co-founder of Gloria Jean's, also noted that "US retailers often arrive in Australia thinking the size of their overseas chains and the strength of their brands in other markets will make it easy for them to crack the local market. Their focus is on global domination rather than the needs of the local consumers". Further, there is a strong sense in Australia of buying local, supporting the community, having relationships with the people you buy from, and supporting ethically-minded businesses. Starbucks clashed completely with that, whereas local stores can differentiate themselves as being local and non-corporate. Furthermore, some would argue that Starbucks has become a caricature of the American way of life and many Australians reject that iconography. Many are simply not interested in the 'super-size' culture of the extra-large cups, nor want to be associated with a product that is constantly in the hands of movie stars.

6.4. Expanding too quickly and forcing themselves upon an unwilling public

In the US, Starbucks started in Seattle as a single store. In a nation bereft of a genuine café culture, that single store captured people's imagination, and soon became a second store, quickly followed by a third. Before long, Starbucks had become a demand-driven phenomenon, with everyone wanting a Starbucks in their local area. McDonald's grew exactly the same way in Australia, opening just one or two stores in each city – nowhere near enough to meet demand – thus creating an almost artificial scarcity, which created huge buzz around the brand experience. Krispy Kreme did the same.

But when Starbucks opened in Australia, they immediately tried to impose themselves with multiple store openings in every city – adopting the US-model of expansion through store clusters. Australians were not given a chance to 'discover' it. As Mescall (2008) points out "they took key sites, hung huge signs, made us order coffee in sizes and gave the coffees weird names. Starbucks said to us – 'that's not how you drink coffee. This is how you drink coffee'". They took the Coca-Cola strategy of being available wherever people looked, but this quickly led to market saturation. Their expansion did not hurt their competitors so much as themselves, and they found themselves cannibalising their own stores. Furthermore, by becoming too common, the company violated the economic principles of cultural scarcity and the novelty wore off. By having too many outlets, becoming too commercial and too widely used, it began to lose its initial appeal of status and exclusivity. It began to have a mass brand feel, certainly not the warm feeling of a neighbourhood café. Furthermore, they became more reliant on less affluent consumers who now, with a worsening economy, are spending less, making Starbucks more vulnerable to economic fluctuations.

6.5. Entering late into a highly competitive market

> *"In America, Starbucks is a state of mind. In Australia, it was simply another player."*
>
> Barry Urquhart, quoted in Delaney (2008)

From Day 1, Starbucks got off on the back foot. They lacked the first-mover advantage they had in the US and Asia, finding themselves the late entrant in an already very developed, sophisticated and competitive market. Indeed, the competitive landscape in the Australian retail coffee market is very different to that of other countries. Here, Starbucks found themselves competing with hundreds of independent cafés and speciality coffee chains (see Table 3), where the coffee was generally better and the staff knew their customers by name. Significantly, they were also the last of the major chains to gain a presence in Australia.

6.6. Failing to communicate the brand

Worldwide, Starbucks rarely employs above-the-line promotion, and this was also the case in Australia. Instead, they maintained that their stores are the core of the business and that they do not need to build the brand through advertising or promotion. Howard Shultz often preached, "Build the (Starbucks') brand one cup at a time," that is, rely on the customer experience to generate word-of-mouth, loyalty and new business. But in a market as competitive as Australia, with a consumer whose palate is discerning and whose loyalty often lies with a specific barista, advertising and promotion was essential to communicate the Starbucks message. The issue is not so much about building awareness – which, at 90%, is high – but to communicate what the brand means and to give consumers reasons for patronising Starbucks.

Their lack of advertising made this branding issue even worse, with many people unable to articulate why they should be loyal to Starbucks. At the same time, competitors were communicating their messages very effectively – McDonald's, for instance, is a heavy spending, award-winning, advertiser in the Australian market. Added to which, more subversive counter-messages were coming from those who saw in Starbucks a 'brand bully' riding rough shod over the nuanced tastes and preferences of local cultures (Klein, 2000; Clark, 2008). In other words, a range of strong contrary messages were undermining Starbucks' own very limited communications.

6.7. Unsustainable business model

Starbucks' product line is limited primarily to coffee. Sometimes a new product idea will be developed, such as the Frappucino, but these tend to have limited product life cycles and/or are seasonal. For example, the Frappucino has traditionally made up 15% of (summer) sales, but recently sales have been down, suggesting that customers are already bored with it (Kiviat, 2008). Furthermore, in the instance where other products were offered, people failed to purchase them as they only really associate Starbucks with coffee and generally seek food elsewhere. This is a very different model to The Coffee Club which has much more of a café feel to it, or McDonald's which has a full range of breakfast and lunch/dinner items that can be complemented by a McCafé latte.

Hence the average transaction value at Starbucks is lower than its competitors, and therefore more customers must pass through its doors to reach the sales and profit levels of its competitors. It also creates conflict with the Starbucks ethos of the third place (and allowing people to sit around for 30 minutes sipping lattes and reading, talking or surfing) versus the need to get people in and out quickly and not take up valuable 'real estate' (which in itself means that the average Starbucks store needs to be much bigger than the average café).

Unlike most of the other retail coffee chains, Starbucks does not use a franchise model, preferring to lease and fit-out its own outlets. This means more cash is being spent upfront, and in Starbucks' case, more debt accrued. But adopting a franchise model would have numerous other advantages than just minimising this. It would mean that local investors, with a good sense of the local market, put their own money into the business and take an active role in running it and shaping its direction.

7. What are the main lessons from this case study?

Several key lessons emerge that should be of interest to both domestic and international marketers.

7.1. Crossing international borders is risky and clearly Starbucks did not do their homework, or ignored their homework

Well conceived market research involving both primary and secondary data, including qualitative and quantitative approaches, would have uncovered the extent of the 'coffee culture' that existed in 2000 when Starbucks entered the Australian market. It seems inconceivable that Starbucks management, or at least its Australian representatives, were not sufficiently apprised of the extent to which many consumers were already well acculturated in terms of buying and consuming European styles of coffees such as short black, lattes and cappuccinos, nor the extent to which many customers were in fact loyal to their suburban café or competitive brands such as Gloria Jean's. As a late market entrant, Starbucks clearly failed to do thorough homework on the market before entry – this is a failure in terms of due diligence. Alternatively, they chose to ignore the messages that were coming from any due diligence that they had undertaken. This may or may not have been due to some arrogance on the part of Starbucks, or due to the fact that they considered they had a strong global brand which would meet with universal acceptance.

An example of where Starbucks did do its homework, and act on it, was in France when it entered that market in 2006, establishing a café in the middle of Paris. Research had clearly shown the American way of consuming and socialising over a coffee was an anathema to many French, so Starbucks held back from entering the French market and when they finally entered it was with great trepidation, expanding at a very slow pace and testing the market at every step.

7.2. "Think global but act local"

This familiar maxim in international marketing should be well understood. While Starbucks had brand awareness as a major global brand, it failed to adapt the product and the customer experience to many mature coffee drinkers in Australia. As noted earlier, all the evidence suggests that it simply tried to transplant the American experience into the Australian market without any adaptation. In particular, it failed to adapt either its core product or its supplementary services to create the intimacy, personalisation and familiarity that is associated with established boutique cafés in Australia.

7.3. Establish a differential advantage and then strive to sustain it

A question of strategy that Starbucks perhaps failed to address was, "Is our product differentiation sustainable in the long term and does it continue to justify a price premium?" As noted earlier, it can be argued that the core product in this case, that is the coffee itself, is essentially a commodity, and that Starbucks' coffee, according to many consumers, was no different to the competition, and in some cases inferior. Then Starbucks' points of difference clearly revolved around its brand image and supplementary services. It was these supplementary services, such as its unique servicescape and excellent customer service, that they used to justify a premium price. However, as competitors (e.g., The Coffee Club) quickly imitated the 'Starbucks experience' (i.e., their supplementary services, ambiance, etc.), by providing premium coffee and an intimate casual experience, Starbucks' value proposition began to fade. In other words, their key points of difference could be easily imitated and were not sustainable. Faced with this scenario, the onus was on management to re-fresh and evolve any lingering differential advantage that Starbucks might have had or, at the very least, give customers reasons to continue patronising Starbucks through its communications.

7.4. Don't lose sight of what made you successful in the first place

As more and more competitors emerged, both individual cafés and chains such as Gloria Jean's and The Coffee Club, competitive pressures forced Starbucks to impose rigid sales targets on their frontline staff including baristas to increase store productivity. However, the imposition of these KPTs and the pressure to serve more customers more quickly meant that Starbucks forgot the very thing that made it unique in the early days, namely, to provide a customer experience in an intimate casual setting that set it aside from competitors. As more pressure was placed on staff to have higher throughput, this meant that baristas and other employees had little time to engage with customers. In other words, Starbucks forgot about the very things that made it unique in the first place. This is akin to the Wheel of Retailing hypothesis (Hollander, 1960) where a no-frills retailer gradually moves upmarket in terms of variety of product, price and more services and within several years finds itself competing with the more established premium supermarkets that were the very competitors that they tried to distance themselves from in the first place. The only difference with Starbucks is that it reversed the direction of the Wheel – by gradually moving downmarket it brought itself into direct competition with cheaper operators and lost sight of what made it successful in the first place.

7.5. Consider the viability of the business model

It has to be questioned whether the Starbucks' business model is viable in the long term, or even the medium term. A business model that uses a premium price to justify the excessive floor space and elaborate servicescape, and allows customers to sit in this environment for an hour sipping one latte, has to be questioned. Given that Starbucks do not have the array of products that, say, a McDonald's might have and, as documented earlier in this case, therefore do not generate the same sales volumes and revenues, it is hard to see how the Starbucks' model is financially viable.

8. Conclusion

In summary, it appears on all the evidence that Starbucks not only misjudged the Australian coffee culture but also misjudged the extent of the competition, and failed to adapt its offering to the local market. Furthermore, with the advent of high quality barista training, the availability of premium coffee beans and the technology to produce a high quality cup of coffee (at a modest cost), sole operators who knew their customers by name, were able to set up business as viable competitors. Starbucks may have been responsible for growing the premium coffee category, but the emergence of Gloria Jean's and the Coffee Club (and McCafé, a premium coffee shop embedded in McDonald's restaurants) turned out to be serious competitors. Finally, questions have to be raised about Starbucks fundamental business model in a market where many small niche players can easily replicate the 'Starbucks Experience'.

References

AustralAsian Specialty Coffee Association, 2006. Australian Coffee Market: Key Facts for 2006.

Australian Bureau of Statistics, 2008. Cafes, Restaurants and Catering Services, Australia, Report 8655.0 for 2006–07.

Bawden, T., 2008. Starbucks reports first loss in 16 years. Times Online, 31 July. <http://business.timesonline.co.uk/tol/business/industry_sectors/consumer_goods/article4436398.ece> (accessed 15.08.08.).

BBC News, 2006. China central to Starbucks growth. BBC News, 14 February. <http://news.bbc.co.uk/2/hi/business/4712012.stm> (accessed 29.08.08.).

Browning, E., 2008. Starbucks hopes growth abroad will save its bottom line. ABC News, 31 July. <http://abcnews.go.com/print?id=5487961> (accessed 29.08.08.).

Burritt, C., 2007. McDonald's challenges Starbucks with cheaper lattes. Bloomberg, 11 September. <http://www.bloomberg.com/apps/news?pid=20670001&refer=&sid=a08JuUP7J6RY> (accessed 29.08.08.).

Cebrzynski, G., 2008. Starbucks-dominated category wakes up and smells McD's espresso rollout. Nation's Restaurant News 42 (3), 1–6.

Charles, E., 2007. In the trenches: Coffee. In the Black, May, 28–31.

Clark, N., 2008. Starbucks: The brand we love to hate. Marketing, 2 April.

Coleman-Lochner, L., Stanford, D.D., 2008. Starbucks reports first loss since 1992, predicts slower growth. Bloomberg, 30 July. <http://www.bloomberg.com/apps/news?pid=20601205&sid=aZxrjcNWyi5Q&refer=consumer> (accessed 29.08.08.).

Delaney, B., 2008. Starbucks to go. Guardian, 30 July. <http://www.guardian.co.uk/commentisfree/2008/jul/30/australia.starbucks> (accessed 29.08.08.).

Edwards, V., Sainsbury, M., 2008. Weak coffee and large debt stir Starbucks' troubles in Australia. The Australian, 31 July.

Euromonitor, 2006. Starbucks Ups Expansion Plans. Euromonitor International.

Euromonitor, 2007. Starbucks Corp – Consumer Foodservice – World. Euromonitor International.

Euromonitor, 2008a. On-trade Watch: Identifying Key Growth Markets to 2012. Euromonitor International.

Euromonitor, 2008b. Company Watch: Starbucks Wakes Up and Smells the Coffee. Euromonitor International.

Euromonitor, 2008c. Coffee – Australia. Euromonitor International.

Euromonitor, 2008d. Impulse Food and Drink Channels – Coffee – Australia. Euromonitor International.

Grove, S., Fisk, R., John, J., 2000. Services as theater. In: Swartz, T., Iacobucci, D. (Eds.), Handbook of Services Marketing and Management. Sage Publications, CA, pp. 21–35.

Hollander, S., 1960. The wheel of retailing. Journal of Marketing 25 (1), 37–42.

Hota, M., 2008. Starbucks: brewing more than just coffee. European Case Clearing House (ECCC), 508-025-1.

Karolefski, J., 2002. Conquering new grounds. BrandChannel, 11 February. <http://www.brandchannel.com/features_effect.asp?pf_id=78> (accessed 29.08.08.).

Kiviat, B., 2008. Wake up and sell the coffee. Time South Pacific (Australia/New Zealand edition) 7 (13), 52–56.

Klein, N., 2000. No Logo. Flamingo, London.

Lee, H., 2003. Japan: a nation of coffee lovers. Euromonitor International.

Lee, H., 2004. Coffee brews a future in China? Euromonitor International.

Lindhe, J., 2008. One skinny cap to go. Business Review Weekly, 7 August. <www.afr.com> (accessed 15.08.08.).

Lovelock, C., Patterson, P.G., Walker, R., 2007. Services Marketing: An Asia Pacific and Australian Perspective. Pearson Education, Singapore.

Martin, S., 2008. Starbucks: a study in liberal failure, Part II. Conservatism Today, 29 July. <http://www.conservatismtoday.com/my_weblog/2008/07/starbucks-a-s-1.html> (accessed 29.08.08.).

Mescall, J., 2008. Starbucks in Australia: where did it go wrong? Unleashed, 7 August. <www.abc.net.au/unleashed/stories/s2326971.htm> (accessed 29.08.08.).

Mintz, J., 2008. Starbucks closing 600 stores in the US. International Business Times, 1 July. <http://biz.yahoo.com/ap/080701/starbucks_closings.html> (accessed 14.09.08.).

Muthukumar, R., Jain, S., 2008. Starbucks suffers: Schultz returns. European Case Clearing House (ECCC), 308-152-1.

Palmer, D., 2008. Starbucks: what went wrong? AFN Thought for Food, 31 July. <http://www.ausfoodnews.com.au/2008/07/31/starbucks-what-went-wrong.html> (accessed 29.08.08.).

Schultz, H., Yang, D.J., 1997. Pour Your Heart into It: How Starbucks Build a Company One Cup at a Time. Hyperia Publishing, New York.

Shoebridge, N., 2008. Local palate bucks another US retailer. The Australian Financial Review, 4 August. <www.afr.com> (accessed 15.08.08.).

Uncles, M.D., 2008. Aroma Australia Pty Ltd goes to Japan. In: Schiffman, L., Bednall, D., O'Cass, A., Paladino, A., Ward, S., Kanuk, L. (Eds.), Consumer Behaviour, fourth ed. Pearson Education Australia, Australia, pp. 584–588.

Wailes, N., 2008. Taste of defeat for the mugs from Starbucks. Sydney Morning Herald 31 (July).