STARBUCKS REINVENTED

Nancy Koehn's new case on the rebirth of Starbucks under Howard Schultz "distills 20 years of my thinking about the most important lessons of strategy, leadership, and managing in turbulence."

by Julia Hanna

Harvard Business School Professor and historian Nancy Koehn has studied Starbucks and its leader, Howard Schultz, for close to 20 years. For her, the company represents much more than a phenomenal success story.

In a recently published case, "Starbucks Coffee Company: Transformation and Renewal," (available soon) Koehn and coauthors Kelly McNamara, Nora Khan, and Elizabeth Legris trace the dramatic arc of the company's past seven-plus years—a period that saw Starbucks teeter on the brink of insolvency, dig deep to renew its sense of purpose and direction, and launch itself in new, untested arenas that define the company as it exists today.

"This case distills 20 years of my thinking about the most important lessons of strategy, leadership, and managing in turbulence in the frame of a very relevant company," says Koehn, the James E. Robison Professor of Business Administration. "As a brand, leadership, and entrepreneurship scholar, I've been dogging Starbucks for a long time."

On a 1995 trip to Seattle, Koehn visited a Starbucks store for the first time and was struck by what she saw and felt. The notion of a "third place" between home and work to relax and enjoy the small, affordable luxury of a special coffee beverage seemed to resonate with the social and economic moment, she recalls. Six months later she met Howard Schultz, an entrepreneur who acquired the company in 1987, and was struck by his seriousness of purpose and the breadth of what he wanted to accomplish.

The case, Koehn's fourth to focus on Starbucks, opens in February 2007. Schultz, no longer Starbucks' CEO but still its chairman, is worried the company is losing its ability to be true to its values while providing a store experience that conveys a sense of comfort, connection, and respect for its product and the communities Starbucks serves.

So Schultz composed a heartfelt, searching memo to senior leadership. In it, he bemoaned decisions (for which he accepted responsibility) that improved efficiency and increased economies of scale but robbed stores of some of their essential magic, such as the smell of roasting coffee and the sights and sounds of traditional Italian espresso machines and baristas at work.

He also cited the company's rapid expansion and the potential "commoditization" of the Starbucks brand. "[W]e desperately need to look into the mirror and realize it's time to get back to the core and make the changes necessary to evoke the heritage, the tradition, and the passion that we all have for the true Starbucks Experience," Schultz wrote.

The scope and richness of Koehn's case gives it the feel of a page-turning novel; in that sense, Schultz's memo is the inciting action for all that follows.

REMAINING TRUE TO CORE VALUES

The challenge that had confronted Starbucks in the early- and mid-2000s was one common to many organizations: Could the
company continue to grow while preserving its culture and values? In some areas, the drive to expand, egged on by Wall Street, was compromising the company's ability to invest in its partners (Starbucks' term for its employees), deliver personalized customer service, and maintain a close connection to the local community.

In addition, McDonald's and Dunkin' Donuts had emerged as serious competitors, offering their own lines of specialty coffee beverages. Even so, Starbucks' financials for 2007, the year Schultz composed his memo, didn't look so bad. But the entrepreneur became concerned as he dug more deeply into the numbers. Sure, revenues were up almost 21 percent over the previous year, but had slowed by over a third; transactions per store were up 1 percent, versus 5 percent the year before. Same-store sales rose only 5 percent, the smallest increase in five years.

In January 2008, Schultz returned as Starbucks CEO, replacing Jim Donald, the man he and other senior colleagues had chosen to lead the company.

**Starbucks Sails Again**

The case chronicles the blizzard of decisions and initiatives that follow what could have been the company's death knell as the financial crisis hit home and consumers cinched their belts.

"Schultz understood that you can't lift your foot off the gas pedal when you're attempting to transform a company," Koehn says. "Severe as its financial needs may be, you also have to figure out what you will invest in. Schultz knew that if he waited until the company was out of the woods to invest in new products, communication channels, and ways of doing business it would be too late—Starbucks would no longer be relevant."

From the start, Schultz sent the clear, unwavering message that Starbucks' transformation would represent a return to its roots and an uncompromising commitment to core values, such as health care benefits for any partners working at least 20 hours a week.

At a March 2008 gathering of 200 senior-level company leaders, Schultz unveiled a Transformation Agenda that included seven "Big Moves":

1. Be the undisputed coffee authority;
2. Engage and inspire our partners;
3. Ignite the emotional attachment with our customers;
4. Expand our global presence—while making each store the heart of a local neighborhood;
5. Be a leader in ethical sourcing and environmental impact;
6. Creative innovation growth platforms worthy of our coffee;
7. Deliver a sustainable economic model.

The case provides a behind-the-scenes look at how the coffee company moved forward on these goals, including the introduction of the milder Pike Place Roast; the story of its VIA Ready Brew line; the launch of a loyalty program; investment in and engagement with social media; focus on a global expansion strategy; and the extension of social programs. The company closed stores, restructured its manufacturing and supply operations, and, perhaps most significantly, took steps to reengage its partners and store managers. In February 2008, Starbucks closed more than 7,000 of its stores across the country for "Espresso Excellence Training," taking the time to work with approximately 135,000 baristas to ensure they could pour a perfect espresso shot and steam milk properly.

For Schultz, however, that wasn't enough—he wanted to reach the company's store managers, recognizing them as essential to the transformation process.

"I needed an unfiltered venue for expressing my empathy about all that we were asking our partners to do and telling them plainly what was at stake," he wrote in *Onward: How Starbucks Fought for Its Life without Losing Its Soul*. The answer, in Schultz's mind, was a three-day conference in New Orleans in October 2008, a moment when the global economy happened to be tanking. Starbucks' fourth quarter profits were down 97 percent from the same time a year earlier; for the fiscal year, net earnings were down 53 percent to $316 million. The Starbucks board was reluctant to send 10,000 partners to New Orleans at a cost of $30 million, but Schultz stuck to his guns.

In addition to rolling up their sleeves and taking part in community service projects to aid areas of the city still recovering
from Hurricane Katrina, partners participated in team-building events that reviewed the company's guiding principles and reminded them of their central role in the customer experience. Schultz also brought in Bono, lead singer of U2, to announce a partnership to channel proceeds from holiday beverage sales to the Global Fund in support of AIDS relief programs in Africa.

The New Orleans conference was a turning point for Starbucks; in the "novel" of Koehn's case, it's the climax.

"Investing in a conference of that size is such an unusual thing to do when faced with a cash crunch," Koehn says. "Schultz understood that what saves and breaks businesses is much more than cash. In the midst of so much turbulence, it's all too easy to pull levers on the low-hanging fruit of cash and logistics. But you don't save a business and turn it around without speaking to, focusing, and calling on the spirit of your people."

Schultz's experience qualifies him for closer study in Koehn's HBS course Power and Glory in Turbulent Times: The History of Leadership from Henry V to Steve Jobs. Not all managers are confronted in their careers with the sort of transformation challenge faced by Starbucks, but Schultz's reflections and actions are instructive for anyone charged with finding sources of strength, innovation, and renewal in today's turbulent business environment, Koehn says.

About the author

Julia Hanna is associate editor of the HBS Alumni Bulletin.