The Pursuit Of Sustainable Competitive Advantage

- A Profile of the Starbucks Corporation -

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Abstract

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Purpose: To study sustainable competitive advantages using Starbucks as a case study.

Methods: The qualitative method was utilized to collect the secondary data used in this type of thesis, being a case study. This approach applied to both the theories used in the analysis as well as the empirical data about Starbucks.

Conclusion: Nothing is sustainable in business including a company’s such as Starbucks competitive advantages. It is the pursuit of the utopian idea of sustainable competitive advantages that can actually be sustained. This approach does not guarantee success, but important components of a company’s pursuit are their leadership, innovative nature and relationship management. Accordingly these theories do not cover all aspects or offer a full explanation of Starbucks success. Therefore, it is recommended for others to research Starbucks using different theories and perspectives in order to draw out other analyses from the empirical case
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1. Introduction

This is a Masters level thesis examining the idea of sustainable competitive advantage in a case study on the Starbucks Corporation and the following section introduces the topic and its relevance in society today.

1.1 Background

Even while wars are being fought, the economy has become topic number one at the world’s current roundtable of discussions (AP-GfK Poll, 2009). The importance of a successful economy, based upon continuously successful businesses has never been clearer (Burns, 2008; Christos, 2009). But what makes a business succeed on a consistent basis? Politicians are now desperately trying to answer this question from a governmental and external perspective. No matter what the politicians’ answers are on this question, it is only half the solution.

The second half of the answer is taken from the perspective from business itself. Rijamampianina, Abratt and February (2003) established that for a company, business means competition and more often than not the winners of any competition are the ones with the advantages. Therefore, sustainable competitive advantages enable companies to consistently succeed in terms of profit and growth.

The question of what makes a business consistently succeed is not only relevant in today’s economic crisis, but is a question that almost every company executive, entrepreneur and business school faculty looks to answer (Oliver, 2000). The authors attempt to contribute to the answer of the question from the business perspective in this thesis and will leave the governmental policies up to the politicians.

From a business perspective Rijamampianina et al. (2003) found that companies succeed when they have some advantage over their competitors. This described advantage of a company over their competitors is expressed by the term ‘competitive advantage’ and is further defined by Kandampully and Duddy (1999) as a firm’s superior “ability to serve customers’ present and future needs (holistic needs)” (p. 51) compared to their competitors. Adding the word ‘sustainable’ in front of ‘competitive advantage’ is a way to describe, “an organization’s long-term success” (Kandampully & Duddy, 1999, p. 51).

The term sustainable competitive advantage can be a troublesome concept for some scholars as it is akin to a utopian idea of business. This is why Richard Oliver (2000) regards sustainable competitive advantage as more of a question than a statement as how can anything truly be sustained in business? He states, “Most business analysts are rapidly coming to the conclusion that not much is sustainable anymore” (Oliver, 2000, p. 7). Even so, there are companies that have
achieved long-term success and Starbucks is an example of such a company (Koehn, 2008).

1.2 A Case Study - Starbucks

Starbucks is an exceptional company where researchers and observers can gain valuable insights into what it takes for a company to achieve a sustainable competitive advantage. Starbucks is one of the quintessential companies of the recent past that have managed to continually succeed with a new take on an established product, coffee. Their growth rate of opening one store per workday for an entire decade (Koehn, Besharov & Miller, 2008) while their stock rose an astounding 2,500 percent (Capital IQ, 2008) is nearly unmatched in modern business. In this context a case study of Starbucks is presented and analyzed using the theoretical framework.

1.3 Purpose

As stated earlier, a common objective of companies is to have long-term success, which can be achieved by having sustainable competitive advantages. In this context the topic of this thesis is sustainable competitive advantage. From this statement we used a morphological analysis as described by Fisher (2007) to guide the procession of ideas and objectives to a specific focus. From this process the aim is to examine the topic of sustainable competitive advantage. The design of the thesis is to explore this topic through a case study that is focused on the Starbucks Corporation.

The purpose of this thesis is to study Starbucks sustainable competitive advantages by seeking to answer the research question, which is as follows: How did Starbucks obtain a sustainable competitive advantage?

1.4 Target Audience

The target audience for this thesis are business students, entrepreneurs and any organization wishing to succeed on a consistent basis. We believe this thesis will be beneficial to the demographics described above, because it constitutes a study regarding the contemporary topic of sustainable competitive advantage.
1.5 Thesis Limitations

This thesis’ limitations are mainly due to time constraints, which in turn also influenced other aspects of the research like the methods utilized and the nature of the data collected. As a matter of fact, the accelerated schedule of our Master’s program constituted a rather substantial obstacle to overcome throughout the process of writing this thesis. As mentioned before, time constraints made it impossible to gather primary data, which in turn affected the validity of this research. Another limitation is concerning the choice of profiling Starbucks through a case study. “Case studies inevitably lack representativeness, it cannot be claimed that what happened in one case is typical of all cases” (Fisher, 2007, p. 60). Establishing and discussing the limitations of the thesis brings the validity to the forefront of our minds during the researching and writing process of the thesis. It also brings the validity to the forefront of the readers’ minds. This full disclosure and transparency strengthens the information conveyed in this thesis and hopefully provides an enhanced level of confidence to the reader.
2. Theoretical Framework

A description and explanation of established relevant theories are provided in this section to guide the research of the empirical case and the subsequent analysis.

2.1 Sustainable Competitive Advantage

The topic of sustainable competitive advantage has been the dominant theme in the study of successful businesses for several years (Bain, 1956; Kay, 1994; Porter, 1980). In order to fully understand the business term ‘sustainable competitive advantage’ it must first be broken down into its parts ‘competitive advantage’ and ‘sustainable’.

First the term ‘competitive advantage’ simply describes the advantage a company has over other companies, which compete in the same market (Burn, 2008). Competitive advantage can also be described as the position a firm occupies in regards to its competitors (Porter, 1998). Competitive advantage can be explained as the resources and features of a company that helps it to do better than their competition (Chaharbaghi & Lynch, 1999; Sharp, 1991; Learning, 2009).

Competitive advantages, therefore, are the attributes that a given company can deliver over its competitors in terms of both tangible and intangible assets. A competitive advantage can be any innovation, product, service, patent, or anything else that differentiates the company in a positive way from the rest of the competition (Rijamampianina et al., 2003). Michael Porter (1998) emphasizes the importance of innovations and relationships to contribute to a company’s competitive advantage. As such both will be further explored and developed later in the theoretical framework.

Competitive advantage is a powerful concept where companies try and garner as many competitive advantages as possible (Reed & DeFillippi, 1990). The term appropriately has the word ‘advantage’ in it as it gives a company that possesses it an advantage in the market place, but it does not guarantee success. It is analogous to increasing the probability of success for a company. The term competitive advantage is a static concept and has no time component associated with it (Chaharbaghi & Lynch, 1999). Businesses do operate in a dynamic environment, not a static one (Burns, 2008). The reasons for it to be dynamic are to be found in the unpredictability and the instability of the environment a given company operates. Therefore, it is vital to introduce a time component to competitive advantage.

The word or term ‘sustainable’ contributes the necessary time component to the concept of competitive advantage. Adding the word ‘sustainable’ in front of competitive advantage is a way to describe a firm’s lasting success in the market (Kandampully & Duddy, 1999). However, the link between the terms
‘sustainable’ and ‘competitive advantage’ seems to be rather complex. Due to the world’s highly dynamic global marketplace, ‘sustainable competitive advantage’ is somewhat of an oxymoron. Some of this confusion occurs with the definition of the word ‘sustainable’. The term ‘sustainable’ can literally assume a wide spectrum of meanings depending from which angle the issue is looked at. Just to give few examples, the term sustainable can mean defensible, endurable, supportable, passable, penetrable, and so forth. In a world and industry where the only constant is change, sustainable is used to add an idea of something that is consistent amongst all the change. Some business thinkers regard sustainable competitive advantage with the famous idiom that it’s a journey not a destination (Chaharbaghi & Lynch, 1999).

Sustainable competitive advantage is more than just one product or service. The existing products and services “which made a company successful yesterday [are] unlikely to work today as the business environment has changed dramatically” (Oliver, 2000, p. 7). “The term ‘sustainable’ considers the protection of such attributes and resources have to offer over some usually undefined period of time into the future for the organization to maintain its competitiveness” (Chaharbaghi & Lynch, 1999, p. 45). An important component of a company’s sustainable competitive advantage is the leadership that a company’s leader provides. No other single entity has more control or influence over an organization than its leader and the leadership they demonstrate (Burns, 2008).

2.2 Leadership

Leadership is paramount to the success of organizations (Stamm, 2009; Burns, 2008). Leadership is a broad and complex topic, difficult to define and is awash in a multitude of theories in the academic and business worlds. Paul Burns (2008) describes leadership in terms of strategy, communication, motivation and the setting a direction. This definition and perspective take on leadership is congruent with the theory of ‘transformational leadership’. It can be further defined as a leadership style that “influences the fundamental attitudes and assumptions of an organization’s members creating a common mentality to attain the firm’s goals” (Victor, 2008, p. 299).

Transformational leadership is necessary now more than ever in today’s ever more rapidly changing and information rich society in order to guide the structure of the firm into useful innovations (Burns, 2008; Carneiro, 2008; Victor, 2008). This leadership approach accomplishes the task of creating competitive advantages through relevant innovations by instituting a system in the firm that is based on knowledge (Carneiro, 2008; Innovation and Leadership, 2008; Victor, 2008). Knowledge itself is worthless and only creates value when it is applied in a manner that contributes to a firm’s attainment of their goals. In this respect the
transformational leader enables the company to incorporate, share and apply the relevant knowledge in an innovative way (Burns, 2008; Victor, 2008).

Leadership can manifest itself in many forms in a firm. Specifically, leaders are emphasized because they are typically in the most influential positions of a firm. A central concept to transformational leadership is about how to effectively communicate the leader’s vision of the company through creating an appropriate organizational culture that controls its performance (Burns, 2008). The term visionary is instrumental and essential when describing a successful leadership approach (Burns, 2008; Richardson, Gregory & Turton, 1994; Nwankwo & Richardson, 1996; Galbreath & Rogers, 1999).

In the context that it’s been discussed, vision is defined as “a shared mental image of a desired future state – an ideal of what the enterprise can become – a new and better world” (Burns, 2008, p. 90). Usually the substance of the vision is more qualitative than quantitative (Burns, 2008). Bartlett and Ghoshal (1994) convey that the vision of a company stewarded by its leader is the foundation to motivate employees by showing a purposeful organization. A leader must articulate the vision of the company effectively to the workforce and this can take many different forms. Just as there are no steadfast ways to lead, there are no steadfast ways to communicate. The best way to lead a group of people or communicate a vision to them is completely situational based and there is no one size fits all approach (Burns, 2008). What has been generally agreed upon is that the vision of a company should motivate its people and it must be a shared vision for it to be effective. This motivated workforce brought together by a visionary leader gives companies their competitive advantage (Oliver, 2000). Thus a company can consider a leader who implements this leadership approach that brings together and motivates its employees toward a common vision as a sustainable competitive advantage.

In order to effectively communicate their vision a leader must listen to their employees, their customers, and to themselves. More specifically, it takes a conscience effort on the leader’s part to actively listen to what the people have to say in order to seek out new ideas or innovations (Stamm, 2009).

Leaders practicing transformational leadership must have an understanding of how to create an environment through sharing their vision thus enhancing the performance levels of a company’s employees (Carneiro, 2008; Victor, 2008). It is a company’s leadership that “contributes to increase innovative efforts and innovation positive results” (Carneiro, 2008, p. 176). To support Carneiro’s position, an article in the journal, Strategic Direction, says that, “leadership plays a critical role in fostering the right climate for innovation” (2008, p. 37). Victor (2008) also supports this direction connection of transformational leadership to stimulating innovation and thus creating advantages for an organization. These supported views and assertions by these authors compel us to further investigate innovation and the role it plays in a firm’s sustainable competitive advantage.
2.3 Innovation

Throughout the study of sustainable competitive advantage and its determinant factors, a key element that emerged from the literature is innovation. Innovation has been studied by researchers from a wide spectrum of perspectives. Studies on innovation can be found in many sciences and disciplines such as engineering, sociology, technology, economics and business. The perspective that is taken under analysis with this thesis, for evident reasons of relevance to the research topic, is the business perspective.

The theoretical connection between the innovation's nature and sustainable competitive advantage, found in the literature taken into account, can be summarised in four factors. Firstly, innovations that are harder to imitate are more likely to lead to sustainable competitive advantage (Clark 1987; Porter, 1985). In simpler words, the harder the strategy is to imitate, the longer the advantage is (Porter, 1985). Second, innovations that reflect more accurately than others market realities, are likely to lead to sustainable competitive advantage (Deming, 1983; Porter, 1985). Innovations of this kind are often based on “applying modifications of existing technologies in new ways for new markets” (Lengnik-Hall, 1992, p. 4). A classic example of this type of innovation in business literature is Miller's (1990) example of Federal express introduction of night service; a new application of an existing technology or process into a new market. Third, innovations that facilitate the timing characteristics of a firm in its relevant industry can bring sustainable competitive advantage (Betz, 1987; Kanter, 1983). Also Teece (1987) argues that good timing can introduce a strong source of uniqueness and therefore advantage over the competition. And last but not least, innovations based on technologies and resources that are easily accessible by the company, are also considered to be beneficial to sustainable competitive advantage (Ansoff, 1988; Miller, 1990). As a matter of fact, for a company willing to obtain sustainable competitive advantage, “effective management of resource allocations is an essential prerequisite” (Lengnik-Hall, 1992, p.6).

From these theoretical standpoints, it seems evident that innovation (in a broader sense) is strongly related and sometimes determinant to sustainable competitive advantage. However, before preceding any further with this connection a clear definition of the term innovation might be appropriate. As defined by Paul Burns (2008), with influence from Joseph Schumpeter, innovation is a “single ‘mould-breaking’ development in new products or services or how they are produced or how or to whom they are marketed that can be linked to commercial opportunity and successfully exploited” (p. 287-288).

Oliver (2000) makes the important distinction between innovations and how innovations are created and implemented in his discussion of sustainable competitive advantage. This is because no particular innovation or tangible advantage
is sustainable, but it is possible to create a structure and environment that is conducive to new innovations, thus giving the appearance of a sustained advantage over the competition. It is this ‘source’ of reinvention or renewal that is possible to maintain for a significant period of time (Oliver, 2000).

Oliver claims that corporate learning viewed as a way to innovate is the only sustainable temporary advantage and the “speed at which companies discover, digest, and disseminate new knowledge will determine the success of their enterprise” (Oliver, 2000, p. 7). Just as true cash flow is the measure of the viability and successfulness of a company, Oliver states, “the only corporate currency that really matters today is innovation” (Oliver, 2000, p. 7).

Innovations are the results of motivated employees (Oliver, 2000). With the workforce being the ‘source’ of ongoing innovation Oliver states “the primary focus of corporate strategy today should be on corporate learning and on the people inside companies who make it possible” (2000, p. 8). Not only should companies strive to attract the best candidates to their company, but “the most profitable investment they can make for both parties is in continuous education” regarding their existing employees (Oliver, 2000, p. 8). Oliver’s position here is supported by empirical data that “reveals that a majority of employees believe growth opportunities and a sense of worth are just as important as the salary level” (2000, p. 9).

As Oliver (2000) claims, continued education of the workforce is what will produce a sustained advantage for a company. This is simply a practical application of the affirmation that the only thing constant in business is change. The change or ongoing education today of the workforce will provide the best environment to produce tomorrow’s successful innovations ensuring that the company is one step ahead of the competition; thus maintaining their ‘sustained temporary advantage’.

Often companies have an initial advantage over the competition which gives them early prosperity and profits, but that advantage has almost nothing, or at best very little in helping a company maintain a leadership position in their market. This concept includes practical products, but also structures within the firm and their associated strategies. The basic principle of “just because the strategy has worked up until now doesn’t mean that it will work in the future” (Duddy & Kandampully, 1999, p. 52). To support this assertion it is pointed out that, “virtually every large company that has gotten into trouble has been criticized for not changing rapidly enough” (Duddy & Kandampully, 1999, p. 52). It is imperative that a firm’s core competence includes ongoing innovations and flexibility into their product offerings.

Another key position that Duddy and Kandampully discuss is that “an organization’s long term success in a market is essentially determined by its ability to expand and maintain a large and loyal customer base” (1999, p. 54). The ways in which a company can offer loyalty to the stakeholders is to “fulfill customers’ present needs, to anticipate their prospective needs and to enhance the ongoing relationship”
(Duddy & Kandampully, 1999, p. 53). This anticipation is of paramount importance according to the authors and which includes even forecasting beyond what the customers would ever consider that they might need or want is crucial for sustained success because “it is the trend creator that wins the game” (Duddy & Kandampully 1999, p. 54). If a firm waits for the customers to determine what their future needs or wants are then the firm has already lost the advantage. “As Popcorn (1991) indicates, ‘if your customers reach the future before you, they’ll leave you behind’” (Duddy & Kandampully, 1999, p. 51). The authors use other scholars such as Pilzer (1990) to support their claim as they quote him stating, “the first law of modern business is no longer, ‘find a need and fill it’, but ‘imagine a need and create it’” (Duddy & Kandampully, 1999, p. 52).

The resulting strategy as brought forth by Duddy and Kandampully (1999) emphasizes the close ties between all stakeholders and where management creates an environment where new innovations can enhance the value of the product offered. In order to sustain a competitive advantage, “firms will have to out-innovate the competition continuously so that it is the customer who constitutes the ultimate beneficiary” (Duddy & Kandampully, 1999, p. 55). An important aspect of this ongoing innovation must occur in a firm’s culture, philosophy, operations, and procedures. This ‘service innovation’ adds value to the firm’s product, thusly the consumer benefits. This concept is connected to the leadership theory discussed previously and will also be connected to the concept of ‘relationship marketing’ discussed in greater details below.

Ongoing innovations are a necessity in cultivating relationships to capture and keep loyal customers. The successful firms create environments with close ties between all the stakeholders to accomplish this difficult task every day. The most successful strategy that a firm can adopt is one where the focus is on the future and enabling the environment within the firm to innovate solutions today, for the customers of tomorrow. Moreover, innovation is only relevant and will only help a company succeed if it is created with the understanding of the needs and desires of the customer (Galbreath & Rogers, 1999).

In recent years, there has been an “evident quantum shift, with firms concentrating more than ever on the creation of a relationship with their customers and other stakeholders” (Duddy & Kandampully, 1999, p.53; Gummesson, 1996). This approach, better known as ‘relationship marketing’, as well as its relevance to the topic of sustainable competitive advantage is presented in the section below. “Competitive advantage, in most industries, is achieved, developed and maintained through relationships” (Duddy & Kandampully, 1999, p. 53).
2.4 Relationship Marketing

The importance of relationship marketing as a contribution to a company's sustainable advantage has never passed unnoticed in business. From a purely logical point of view, some could argue that having a long-lasting relationship with customers is widely recognised for giving a company competitive edge, and therefore not be considered as a new phenomenon. As Grönroos explains, “the relationship orientation is probably as old as the history of trade and commerce” (2007, p. 25). Also other researchers in the field, such as Sheth and Parvatiyar (1995) for instance, have shown that trade and commerce have historically been more relationship oriented than not (Sheth & Parvatiyar, 1995, pp. 397-418). In the service industry especially (where Starbucks operates), relationships are given a central place in the development of marketing models aimed at maintaining the interaction between customer and service provider (Bitner, 1995, pp. 51-70).

In the exchange of money for a given service, contact with the customer always occurs. “The customer has always to interact with the service provider in some way” (Grönroos, 2007, p. 25), therefore every aspect of these interactions, in terms of quality output, must be closely audited by marketers in order to have a pleased customer that might eventually repeat business.

The concept of relationship marketing has been widely used over the past decades, and it was first introduced in the marketing literature by Leonard Berry in 1983, through his publication “Emerging Perspectives on Service Marketing” for the American Marketing Association. More recently, Christian Grönroos, with his book “Service Management and Marketing” (2007) thoroughly analyzes and brings to evidence the importance of relationship marketing as a key factor in a company's quest to competitive advantage. Before defining Relationship Marketing, it might be appropriate to define what a relationship is. As Håkansson and Snehota (1995) explain, a relationship between customer and service provider exists when the customer understands that there is a mutual and shared way of thinking between the two parties. Fine-tuning with the customer is therefore of vital importance in a relationship marketing approach aimed at creating competitive edge over the competition.

Relationship marketing as a business concept, as Grönroos explains, it is opposed and in some cases antithetical to the concept of transaction marketing which has dominated the marketing divisions of many companies for the last decades. This latter marketing approach has naturally led to business models and practices “geared towards the task of creating exchanges”. As a consequence to this phenomenon “the major focus of marketing programs has been to make customers buy regardless of whether they are old or new customers” (Grönroos, 2007, p. 24). Only a small part of the marketing budgets were spent on the trial of maintaining solid and florid relationships with the existing customers. As mentioned earlier, in the literature, this
marketing approach is called *transaction marketing*, where the marketer “tries to win customers over and over again, regardless of whether they have made purchases before or not” (Grönroos, 2007, p. 24).

In situations where markets are constantly growing, and there is no need for considerable interactions between customers and suppliers, this kind of strategy has proven to be successful, and will probably continue to be so. However, “as markets mature, at the same time as competition increases and in many contexts become increasingly global, winning customers as the main or dominating focus of marketing is too limited” (Grönroos, 2007, p. 28). Some industries, on the other hand, have the only option of focusing on transactions since the contact with the end user can be often impossible. Consumer goods can be a good example of such industries, where the producer never encounters the consumer at any stage of the purchasing process. Another aspect to be taken into consideration, as Grönroos argues, is the development of information technologies, which in turn make these interactions with the end customer thinner and thinner every time.

Starting from the 1970s, a somewhat new marketing approach has emerged “based on the notion that interactions between service providers or suppliers of goods and industrial buyers and their customers are important elements in marketing, because the way these interactions are managed has an impact on the purchasing behavior of customers” (Grönroos, 2007, p. 24). The above-mentioned approach radically changed the mindsets of the marketers embracing it, in the sense of no longer viewing the customer as a cash cow but rather as a ‘relationship partner’. The radical change of this new perspective lies mostly on the fact that “relationships between parties and the interactions that occur between them are considered the core phenomenon in marketing” (Grönroos, 2007, p. 25). This is what is called a *relationship perspective*, in contrast to the traditional *exchange perspective* (Gummesson, 1999). According to this perspective, singular transactions are not of the essence, what really matters is the intensity of the relationship that the company can create with its customers.

Grönroos continues with the assertion that in all cases mentioned above “the service process leads to some form of cooperation between customer and service provider. A customer relationship may emerge. If this relationship is not satisfactory to the customer, the exchange of the value for money stops” (2007, p. 25). And the customer may then turn to another service provider, which in turn might be offering a higher value service, at a *caeteris paribus* condition. However, as Grönroos sustains: “although services, and therefore the marketing of services, are based on relationships, there are sometimes situations where the customer does not want this relationship to be emphasized. The important thing to keep in mind is that services are inherently relationship-oriented” (Grönroos, 2007, p. 25).

In regards to the optimization of such relationships and the consequent competitive edge they bring along, Grönroos suggests three main strategic and tactical
elements for a successful relationship strategy. These three tactical elements are, “to seek direct contacts with customers, to build a database and to develop a customer-centric service system” (2007, p. 30). As he explains, on the other hand, the three important strategic requirements in order to build a sustainable relationship strategy are, “to redefine the business as a service business, to look at the organization from a process management perspective and to establish a network to handle the whole service process” (2007, p. 30). As stated by Grönroos, being ahead of competition requires a company to understand that customers look for a complete holistic service offering delivered in a “friendly, trustworthy and timely manner” (2007, pp. 30-31).

Customer loyalty is cultivated by their trust being won on a continual basis by the company differentiating themselves from the competition. It is not the action, but the “intention behind the action that distinguishes a firm’s offering” (Duddy & Kandampully, 1999, p. 51).

2.5 Conceptual Framework

The final theoretical framework is an assembly of the theories presented above. The three theoretical approaches that are considered fundamental to a company’s sustainable competitive advantage are leadership, innovation and relationship management. The graphical description of the relationship between the concepts is shown below in Figure 1.

![Diagram](image_url)

**Figure 1:** A graphical representation of the assembled theories, which constitutes the
theoretical framework.

Sustainable competitive advantage is the focus of this thesis and is the goal of all the theories. This is why all three theories presented in the framework lead to sustainable competitive advantage. The box with sustainable competitive advantage has a dotted edge and is a shade lighter in color because there is no guarantee that these theories or any theories for that matter lead to sustainable competitive advantage, although, it has been theoretically established that the three theories do increase the probably of a firm obtaining sustainable competitive advantages.

Leadership is at the top of the model to signify its importance and show that the other theories are directly affected by a firm’s leadership. It directly contributes to sustainable competitive advantage of a company as well. A firm’s leadership does not exist or occur in a vacuum and is influenced by the firm’s innovations and the firm’s ongoing relationships which are why the arrows are pointing back at the leadership rectangle.

Innovation and relationship management are given equal space and location on the graph to show that they are of similar importance to a company’s sustainable competitive advantage. There is an arrow between them as well because they are complementary theories with interdependence. It is relationship marketing that helps identify the holistic needs and desires of the customer thereby helping the innovations to be based on the customer and in turn, their usefulness. Also innovations can be very useful in cultivating relationships that help contribute to a sustainable competitive advantage.

A paper reads from top to bottom and that is why sustainable competitive advantage is shown at the bottom. The way to sustainable competitive advantage is varied, but no matter the journey it is the goal.
3. Research Design

*In this section the methods and techniques that were used to collect data will be explained and justified in order to strengthen the validity of the thesis. The thesis logic is also described.*

3.1 Research Methods

In this sub-section the qualitative and quantitative methods of research are discussed after it is established that this thesis constitutes a case study.

In order to properly explain and justify the research methods it must be first established that this thesis is primarily a case study. The characteristics of this thesis, a company (Starbucks) profiled with many variables analyzed using various theories in order to study certain factors are congruent with the characteristics that Yin (1994, p. 13 in Fisher, 2007) points out in Fisher whereby the most important characteristic is an “investigation [in] a contemporary phenomenon within its real life context” (p. 59-60). The variations and possibilities in a case study are many and the authors are given the latitude to tell the story from as broad a perspective as necessary (Fisher, 2007).

The two main types of research methods are qualitative and quantitative according to both thesis guide publications written by Fisher (2007) and by Bryman and Bell (2007). Qualitative material usually takes the form of interviews and documentary exegesis while quantitative material usually takes the form of questionnaire surveys and databases (Fisher, 2007). Further explained, the intent of the quantitative approach is to analyze the theories by examining the association between the theories and the research with emphasis on testing the theories (Bryman & Bell, 2007). Conversely, the intent of the qualitative method is to generate theories through an inductive approach by which the observations and findings result in new or modified theories (Bryman & Bell, 2007).

The method employed in the thesis is the qualitative method. The qualitative method is more beneficial than the quantitative method when there are small focused samples of data. Also, it is more effective than the quantitative method when the researcher is trying to comprehend how and why particular outcomes were accomplished (Holiday, 2007). This comprehension is precisely what we are trying to achieve as the research question is focused on studying the measures taken by Starbucks in order to induce long-term success by having a sustainable competitive advantage.
A limitation of the qualitative method is that often it comprises smaller groups of information as compared to quantitative (Holiday, 2007). It is interpretive and can be influenced by the personal beliefs of the researchers (Bryman & Bell, 2007). The values of the researcher in the form of preconceived notions and preconceptions can bias the results. It is important to note that “research cannot be value free” (Bryman & Bell, 2007, p. 30) so the presence of values does not necessarily constitute a negative aspect, but is a limitation that the researchers and readers should be aware of. We have been cognizant of these limitations and have tried to be open and objective throughout the study.

3.2 Primary Data

In this section primary data is defined and discussed within the context of this thesis. No primary data is used in this thesis so it is only briefly discussed to establish why it was not used.

Primary data is original data direct from the source that is in its purest form and is the void of any interpretations (Fisher, 2007; Bryman and Bell, 2007). A variety of methods can be utilized to collect primary data such as interviews, surveys and/or direct observations. No primary data was used in this thesis because there are no Starbucks stores or offices in Sweden as well as the direct inquiries to the corporate headquarters were unanswered by the publish date of this thesis. With additional resources and time we could have further strengthened the data collected in the thesis with primary data. This illustrates an important limitation of primary data in that it can be difficult to obtain. Also primary data is only reliable as the person (researcher) or apparatus used to measure and collect it. Nothing is foolproof the researcher must always be conscience of this fact when dealing with any form of data. Primary data can also be difficult to process and the moment it is processed which judgments made by another person it becomes secondary data (Gronhaug, 2005). Primary was not necessary for this thesis as the copious amounts of secondary data proved more than enough for us to formulate an accurate depiction of Starbucks and their sustainable competitive advantages.

3.3 Secondary Data

In this section secondary data will be defined and discussed within the context of this thesis. The ways in which it was searched for and collected as well as its limitations are discussed as well.

Secondary data is defined as data that has been collected, assembled and interpreted by someone else and is often referred to as second hand information (Gronhaug, 2005). Secondary data is useful in providing already established ideas and
theories. Some of the advantages are that it’s relatively cheap and abundant; especially for a well-known company like Starbucks. Secondary data is also an important component to obtain possible useful information that Starbucks safeguards as trade secrets and would never be available as primary information from the company directly. Secondary data is useful in providing already established ideas and theories. This allows the authors of the thesis not to ignorantly repeat what has already been accomplished.

One of the most useful sources, which will provide numerous insights is the book titled, *Pour Your Heart Into It* by Starbucks founder and CEO, Howard Schultz. Because Schultz is still tied to the company as CEO while he co-wrote the book, therefore he cannot be considered an unbiased source, yet there are still valuable insights to his thoughts on the inner workings of Starbucks that could not be obtained any other way.

Another book titled, *The Starbucks Experience* was researched and written by journalist, Joseph A. Michelli. The book was written with the assistance of Starbucks and it is reasonable to expect that this relationship between the author and Starbucks influenced the author’s perceptions and opinions. The events and situations depicted in both books are believed to be accurate and factual, yet they have been collected and retold by another researcher making them secondary data.

Interviews with Starbucks employees and management are also being considered secondary data because we did not conduct the interviews ourselves. We have no way of knowing if the questions were given to the respondents ahead of time or exactly what the arrangement was between the interviewer and the interviewee. Nonetheless pre-recorded interviews conveyed important information to us. We were able to not only listen to their answers, but were also able to observe their disposition, body language and get a general impression when each question was asked. Even our own observations are still considered secondary data because we were not at the interview in person and have no way of fully accounting and recording the true environment and context of the interviews. Also, with no direct contact with Starbucks or the interviewees, we were unable to administer any follow up questions for further clarification on the topics discussed. Although the interviews with Starbucks management can be regarded as valid and reasonably reliable for this thesis because Starbucks and the views of the employees of Starbucks regarding Starbucks are the primary focus of the thesis and the questions being asked.

The secondary data for this thesis was gathered by using the full resources of Mälardalen University library in the avenues of searches in multiple relevant databases Emerald and Business Insights, which mainly pertain to the subjects of business, economics and organizations. The key words used to search were ‘Starbucks’, ‘competitive advantage’, ‘sustainable competitive advantage’, ‘innovation’, ‘leadership’, and ‘relationship marketing’. General academic databases were also used, namely EBSCO and Oxford University Press. The same key words
mentioned above were used to search these databases. The majority of articles originate from peer-reviewed journals that follow the standard protocol of an academic journal whereby they are reviewed and criticized before being published. This level of oversight contributes to the quality and validity of the content, yet does not diminish the limitations of secondary data as described at the end of this section.

An important component to the data collection was Starbucks Annual Report. It helped us evaluate Starbucks measurable performance factors in terms of profits and growth. We chose to treat all data from the annual report because people author it and it is possible that the data is not perfectly reported. Regardless of the laws requiring factual data to be reported in a public company’s annual report in the United States, laws are not always followed and there is no way to unequivocally prove the data true. We were mindful of the intent behind the different portions of an annual report regarding the reported historical performance figures and the future projections made.

Finally, the limitations of secondary data have to do with the very nature of the data in that’s its secondary. Since secondary data that has been processed and developed by an author or researcher, their intent and agenda must be taken into consideration. Furthermore, the purpose of the secondary data’s author must also be considered. The perspective taken in secondary data, although it may be a useful and a valuable one, must be kept in the context that it is subjective. Extra caution and prudence must be taken when using such data.

3.4 Thesis Logic

A deductive logic was followed for the thesis. Bryman and Bell (2007) describes deduction as a process in which the theory is first formulated and presented with observations and findings that follow. The following figure (Figure 2) is a graphical representation of the logic behind the thesis.
Figure 2: Illustrates the deductive logic behind the thesis.

More specifically the process of the thesis begins with the topic of the sustainable competitive advantage being introduced by citing its relevance in the current global economic situation. The specific focus of the topic is explained in the objectives, aim & purpose section where the research question is also posed. Next the theoretical framework adapts and develops existing theories (Fisher, 2007) formulated to help answer the research question. This theoretical framework is established before the empirical case of Starbucks in order to guide the data collection (Fisher, 2000).

Subsequently, the Starbucks Corporation is profiled in the empirical section. There, Starbucks sustainable competitive advantages are fully established along with specific aspects of what helped contribute to their success. The findings in the empirical data are examined and compared through the perspective of the theoretical framework to help answer the research question. Finally from the analysis conclusions are made.
4. The Empirical Case

The following empirical data presented provides an all-encompassing account of Starbucks, which is meant to properly set the stage for what we consider as a holistic description of Starbucks sustainable competitive advantages.

4.1 The Beginning

The Starbucks Corporation is an exceptional company that has relatively long history of having many prolonged competitive advantages. Their sustainable competitive advantages are almost unmatched in terms of longevity and their core product, coffee, is a simple example that will illustrate the concepts and theories already presented.

Starbucks founder and current CEO, Howard Schultz, states that Starbucks growth is not by chance or an anomaly, but was based in leadership, focused strategy and design (Schultz & Yang, 1997). It is true that a presentation of one company with prove or disprove the assertions made above, but it will assist the reader in comprehending the theories, their relation to one another and will offer an explanation for the success that is now Starbucks.

Starbucks appeared on the American business arena in 1971. Back then the company's philosophy was markedly different from what it is now. As a matter of fact, Starbucks began its journey as a pure specialty coffee roaster and retailer. At Starbucks, coffee was strictly sold by the bag, and unless a very special client wanted to try a new or different blend of coffee, there was no chance of having an espresso. From a macro perspective, however, coffee as a product was not doing that well in America, especially after the boom of the soft drink industry. According to Nancy Koehn, in the American market, per-capita coffee consumption was on the verge of a precipice, and no one could have envisioned what was about to happen in the coffee industry (Koehn, 2001, p. 211). With a rather simple concept of customised high-quality coffee drinks, offered in a friendly manner, Starbucks began expanding at a vertiginous pace. In mere monetary terms, the coffee retailer went from around $10 million turnover, as Howard Schultz acquired the company, to more than $1 billion turnover in 1999 (Koehn, 2001, p. 245). By 2009, Starbucks turnover point was slightly over $10 billion, and the retail store-count around the world reached the number 16,000 (Michelli, 2007).

From a financial point of view, Starbucks stock's price rose from $2 in 1995 to a value near $39 in 2006 (Capital IQ, 2008). However, in late 2006, Starbucks stock price began an unexpected negative trend, which caused the loss of almost half its value in a matter of a year (Capital IQ, 2008). After highs and lows, Starbucks found itself facing a challenge that nobody in the executive team ever
expected to happen. Given the seriousness of the situation, in 2008 Howard Schultz resumed his position as CEO (which he left in 2000) taking the reins once again, with the purpose of bringing Starbucks back to its original path.

4.2 The Business Environment

Before Starbucks' roaring entrance in the industry, the American specialty coffee segment, was confined to a niche of connoisseurs. However, in a matter of few years, things started to change. “Several factors lay behind the coffee boom. American consumers had become increasingly interested in specialty foods, including organically grown produce, fine wines, and artisanal chocolate and cheese” (Koehn, 2001, pp. 235-236). As Nancy Koehn explains, in that time frame, annual income was increasing for many households in America and people were prepared to pay premium prices for small luxuries and specialties, coffee being one of them.

The market trend was so positive and seemed to be so profitable, that other experienced players’ thought about joining the competition as well. Starbucks main competitors, besides thousands of neighbourhood-based coffee shops, were Peet's Coffee & Tea and Caribou coffee. However, other retailers that did not operate in that specific market segment thought about entering the market with a quite aggressive agenda. Dunkin' Donuts for example, a national donut chain, began introducing coffee in unusual flavours such as caramel, hazelnut, and toasted almond (Dunkin’ Donuts Website, Coffee Menu, 2009).

With similar timing, McDonald's decided to join the market by opening a series of cafés inside their restaurants, which would be called McCafés. In spite of initial scepticism, their product offering came across as capable of standing the fierce competition. As a matter of fact, a Consumer Reports' taste test, confirmed that McCafé's drip coffee was more appreciated than both Starbucks and D.D. (Consumer Reports, 2007). Probably, the fact that McDonald's coffee cost only $1 against $ 2.50 of Starbucks, also influenced the result of the test.

“McDonald's and Dunkin' Donuts prices were not always lower than Starbucks for comparable products. However, they marketed their specialty coffees as thriftier, less pretentious alternative to Starbucks blends” (Koehn, 2008, p. 3).

Besides McDonald's and Dunkin Donuts efforts to enter the market, other coffee chains were benefiting by the coffee boom started by Starbucks. Such chains were Peet's Coffee & Tea (born in the S. Francisco Bay Area), The Coffee Bean & Tea Leaf (from the LA area) and Caribou Coffee (from the mid-west). Just like Starbucks, these chains highlighted the quality of their premium coffee offerings along with a unique in-store experience (Koehn, 2008).
4.3 Expansion

Starbucks business concept seemed to be working out fantastically well from both a commercial and social point of view. By the year 2007, the Starbucks Corporation had become the largest coffee retailer in the world (Michelli, 2007). Its numbers were definitely impressive, operating more than more than 15,000 store locations around the world and revenues of about $9 billion (Starbucks 10K, 2007). The majority of its locations were still in the United States, even though Starbucks had plans to further expand its business model beyond the North American boundaries.

In many metropolitan centres of North America, Starbucks owned multiple stores very close to one another. “At one intersection in Seattle there were Starbucks stores on three corners, and the company was considering placing a store on the fourth as well” (Palmer, 2007, in Koehn, 2008, p. 5). Starbucks stores were literally at everywhere.

For obvious reasons of market knowledge, commitment and experience, the American market was the main market, nonetheless the most profitable. In spite of that fact, Starbucks international presence was augmenting substantially too. The first Starbucks store ever opened outside the American continent was in Tokyo, back in 1996 (Schultz and Yang, 1997). By 2007, Starbucks Corporation operated over 4,000 stores outside the United States, with 100 stores in Tokyo alone (Starbucks store finder, 2009).

From the very start of this vertiginous expansion's venture, Howard Schultz had focused most of his efforts and his team to build a company that “provided generous benefits to its employees, delivered outstanding service based on personal relationship with customers, and acted as a responsible corporate citizen” (Kohen, 2001, p. 205). Actually a big statement for a company that was opening nearly one store a day (Michelli, 2007; Palmer, 2007).

With such impressive numbers, some could argue that Starbucks expansion strategy to be aimed at saturating the market before anyone else could move in. From a customer point of view, as Koehn (2008) explains, for some reason people have always seemed to appreciate the opening of a new Starbucks store in their neighborhood, rather than some competitor's. “Opening new stores tended to have positive effects on the neighborhoods in which the stores operated and for participants in Starbucks' supply chain” (Koehn, 2008, p. 6). Obviously enough, the opening of a new Starbucks store was a blessing for few and castigation for others. Sometimes, smaller coffee retailers in the same neighborhood as the coffee giant would see their turnover diminishing substantially if not disappearing at all. On the other hand, the increasing number of Starbucks stores had positive effects on employees, coffee growers and, most importantly, investors. “Enlarging the business created more jobs and more demand for coffee and other inputs purchased from suppliers” (Kohen,
Farmers and employees were pleased with the company's expansion strategy, and of the same opinion were the investors in wall street. “Expanding the store network and product line allowed Starbucks to consistently boost its revenues, ensure continuing returns for its investors, and increase its market valuation” (Koehn, 2008, p. 6). Still on the investor's side, stakeholders strongly backed up Starbucks' expansion efforts as long as the stock price was going to keep and eventually increase its value (Michelli, 2007). Although experiencing some ups and downs in terms of performance, the company's stock price increased by 2,500% since its initial public offering, back in 1992 (Capital IQ, 2008).

4.4 Innovations

Starbucks has had many innovations, coffee based and non-coffee based alike, throughout their history that has contributed to their success. The innovations have greatly expanded the menu at Starbucks where there is a variety of flavored syrups, toppings and even different types of milks to choose from adding up to over 87,000 possible drink combinations (Starbucks Nutrition Info, 2009).

Beginning with the coffee based innovations they have taken traditional and classic espresso based beverages for instance, a ‘café mocha’, and modified it to make what they call a ‘white chocolate mocha’. A few other new espresso based innovations are ‘cinnamon dolce latte’, ‘pumpkin spice’, and ‘peppermint’ of which the latter two are seasonal beverages offered during the winter Christmas holiday time.

A very important innovation occurred in 1994 when a district manager in Santa Monica, California began experimenting with an ice-blended coffee beverage that later became known as the Frappuccino. Prior to the invention of the Frappuccino, Starbucks store traffic would decrease whenever the weather became quite warm and there were limited options for chilled beverages in the stores (Schultz & Yang, 1997; Michelli 2007). The district manager was able to demonstrate the new ice-blended coffee beverage to Starbucks upper management and was adopted by all Starbucks stores across America by the beginning of 1996. The innovation by an employee or ‘partner’ contributed $52 million or 7 percent of Starbucks revenue for 1996 (Schultz & Yang, 1997).

Starbucks as continued to innovate in the area of ice-blended beverages and in 2008 ice blended beverages that contained added supplements of vitamins, protein and fruits were introduced. Starbucks was trying to appeal to the health conscience and active customers. These non-core offerings were a strategy to make Starbucks a destination even for those who didn’t want a cup of coffee. Part of the problem or dilemma is that a company cannot be all things to all people. As Starbucks ventures further and further away from their core offering of coffee they risk losing their focus and the very thing that made the so successful, coffee.
This dilemma is evident in the ‘successful’ debut of their hot breakfast sandwiches, which quickly became popular with their customers. Although the breakfast sandwiches were successful, the aroma from them overpowered the smell of coffee and they were subsequently discontinued. This is an example of where a new innovation that customers even accepted and enjoyed ended up compromising the quality and Starbucks core product coffee and its aroma that helps create the atmosphere in the stores (Koehn, 2008; Michelli, 2007).

Starbucks innovations were not only meant for their stores. Other new products and applications of the Starbucks brand include premium coffee ice cream, coffee beans, coffee liquor and pre-bottled coffee beverages being offered in grocery stores (B. White, personal observation, January 5, 2009). All these things only contributed about 5% of total net revenues, but helped with Starbucks brand awareness and exposure (Starbucks Corporation, Form 10-K, 2005).

They began selling CDs in the stores in 1994 that all began with a store manager making a song playlist for the store and the customers began asking for copies of it. The customer comment cards solidified the idea to the top management at Starbucks that they should offer opportunities for their customers to buy the music that they heard playing in the stores. According to Schultz (1997) they reviewed two years worth of customer cards and there were hundreds of requests for the music in the stores. It is uncertain what decision Starbucks top management would have made if they did not have their customer comment cards to encourage them to sell CDs.

Starbucks purchased the Hear Music Company to expand their music compiling aptitude. Hear Music was already well had a large library of songs that fit the motif of Starbucks stores with a wide range of modern tracks to many famous classics. From all accounts Starbucks foray into the music business has been a success. In 2004 they won a Grammy award with an album by Ray Charles and consistently sell over 3 million CDs a year (Koehn, 2008; Michelli, 2007).

Based on the early success of the compiled music playlists and CD sells, Starbucks created an entertainment division in 2004 within the company in order to develop other media opportunities for the company, which consisted of publications and movies. The success of books and movies is more in doubt than the music produced by Starbucks. Many people were critical of this diversification by Starbucks and worried about Starbucks loosing their focus on their core product, coffee. Nancy Koehn (2008) provides useful insights into Starbucks reasons for this diversification when she says, “the broader objective underlying the ventures into music, books, and movies was to enhance the experience Starbucks provided and thus to enrich the brand. Product expansion also provided a source of incremental revenue that would help the company continue to meet investors' growth expectations” (p. 12).

Howard Schultz (2008) discussed the quagmire or predicament that Starbucks often at his speech at UCLA that Starbucks often finds themselves in with having to satisfy shareholders by consistently increasing profits, yet staying true to the
mission of Starbucks of serving great coffee in a comfortable setting. At this time there is no clear proper response to this conundrum, but it is clear Starbucks is cognizant of the pitfalls that a diverse strategy such as a coffeehouse being in possibly unrelated market such as the music business.

4.5 Relationship Marketing

Starbucks philosophy has been to take good care of their employees and they believe the employees will in turn take good care of the customers. If the customers are happy, then they will frequent the store and the subsequent profits will in turn please shareholders (Schultz & Yang, 1997; UCLA & Schultz, 2008).

This value set of positive creation reinforcement of Starbucks is largely based on an event that occurred in Howard Schultz’s life when he was seven years old. His father broke his leg delivering cloth diapers and was unable to work. His father had no health insurance or worker’s compensation and this plight on Howard’s parents greatly influenced Schultz when he was leading and establishing Starbucks value set that was apart of his vision for Starbucks (Schultz & Yang, 1997).

As part of this Schultz’s vision to be a benevolent employer, Starbucks implemented two very important initiatives. The first initiative occurred in 1988 when Starbucks began offering full medical insurance to all part-time employees working a minimum of 20 hours per week (Koehn, 2008; Michelli, 2007; Schultz & Yang, 1997). This healthcare program clearly has a direct connection to the plight of Schultz’s dad and his experience as a child.

The second initiative was implemented when Schultz managed to convince the other shareholders that it was important for the employees to share in the success of Starbucks. In this context, Starbucks began offering stock options in the company in 1991 even while it was still a private company (Michelli, 2007; Schultz & Yang, 1997). This initiative came to be called Bean Stock and employees are now always referred to as ‘partners’ and not employees. This ensured that the employees, especially the ones that had been with the company near its onset, would share and a voice in the company they helped create.

Both of these initiatives were considered innovative at the time as they were not at all common amongst companies of Starbucks size or position. Their cost is also substantial and now Starbucks spends more money on medical insurance than it does on coffee (Schultz, 2005). Even at such a substantial cost all indications are that these initiatives certainly have contributed to Starbucks success. This can be seen in the retention rates of Starbucks employees where they are 120 percent greater than compared to the rest of the industry (Michelli, 2007). This superior retention is a competitive advantage as Schultz (1997) affirms that Starbucks is able to create more of a sense of community and develop relationships with the customers when
employees stay with the company. Michelli (2007) and Koehn (2008) both agree with this assessment.

4.6 New Strategies

Howard Schultz resumed the reins of the company as CEO in January 2008. He replaced Jim Donald who had held the CEO position for eight years before Schultz returned.

Upon his return Howard looked to restore some of the vision, culture and success that had recently eluded the company as described earlier in the empirical data where Starbucks share price lost more than half its value from 2006 to 2008 (Capital IQ, 2008). At Starbucks 2008 investors’ meeting Schultz acknowledged Starbucks shortcomings and laid out a plan of major strategic moves to implement in order for the company to regain their sustainable competitive advantage in the marketplace (Koehn, 2008).

The first initiative was Starbucks would replace their large espresso machines with a smaller version that didn’t inhibit the line of sight between the baristas and the customers. The new machines, called the Mastrena, would also have additional features that gave the baristas more control over the ‘pulling’ of a shot of espresso. Second, Schultz also introduced a new coffee roast blend called, “Pikes Place” named after the location of the first Starbucks store that was promised to be the best drip coffee Starbucks offered.

The next was the Starbucks Card was introduced that would help keep customers loyal by offering perks such as free refills on drip coffee. The cards could also be used to pay for any Starbucks beverage or product by putting money on the card, similar to a gift card. The idea was to add value to Starbucks products and convenience of the customer.

The forth move was for www.MyStarbucksIdea.com to become a place where anyone could contribute their ideas about the company. This was a 21st century approach to the Starbucks comment cards that helped them decide to sell music in their stores 15 years earlier. This would allow easier and greater access by Starbucks management to their customers (Koehn, 2008). Schultz also mentioned in his interview at UCLA (2008) that they had discovered a proprietary drink in Italy which Starbucks management was very excited about although declined to further articulate the nature of the drink.

These tangible strategies that were going to be implemented were important to the future success through Schultz’s opinion, but it was clear that they were only a demonstration that Starbucks would return to the innovative ways and an open culture where it was encouraged to try something new. Schultz reiterated and emphasized that his return was all about Starbucks and how they would regain their sustainable competitive advantage.
5. Analysis

In the following analysis section the empirical data and factual evidence taken from the Starbucks case study will be closely evaluated and scrutinized. Key factors that contributed to Starbucks prolonged advantage over its competitors will be identified through the perspective of the theories brought to light and described in the theoretical framework.

5.1 Starbucks Initial Sustainable Competitive Advantages

This sub-section will analyze Starbucks initial successful period from when Howard Shultz took control over Starbucks in 1987 to 2006.

The Starbucks case reinforces the theory of leadership and especially the transformational leadership characteristics as defined by Burns (2008) and Victor (2008). Communication, motivation, vision and direction are qualities exhibited by Starbucks modern founder and current CEO, Howard Schultz, that have led Starbucks to unprecedented levels of consistent success. As described in the empirical section, Schultz was not one of the original founders of Starbucks, but was single handily responsible for the new direction Starbucks took in 1987 when he acquired the stores from his former business partners. Originally Starbucks just sold whole bean coffee to customers in the Seattle region, but Schultz insisted that Starbucks begin actually brewing and selling cups of coffee in the stores. Schultz was inspired and had a vision of what Starbucks could become after his experience in the Italian espresso bars in Milan (Schutz & Yang, 1997).

Starbucks has had many innovations that have contributed to their success and competitive advantage. The first and possibly the most important innovation they had was being the first company to bring specialty coffee to a mass market. This first mover advantage they enjoyed allowed them to get a jump start on the competition in terms of creating brand awareness, loyal customers enabling them to become a leader in the world’s specialty coffee market. In this context Starbucks innovation in being the first to bring specialty coffee to a mass market coincides with Clark’s (1987) and Porter’s (1985) description of an innovation as being difficult to replicate. This simple idea in hindsight was clearly an innovation that is next to impossible to duplicate as Starbucks advantage was in being the ‘first’ company.

A close innovation directly following Starbucks first mover advantage was their market saturation advantage ahead of competitors. An example of this is occurred at a busy street intersection in Seattle where there were three Starbucks stores on three of the corners (Schultz & Yang, 1997). This saturation inhibited other imitative competitor coffee stores by taking some of the best locations and quickly spreading Starbucks brand awareness. This innovation in saturation helped Starbucks
in their relationship marketing as described by Grönroos (2008) by quickly increasing the number of opportunities Starbucks had to interact with their customers. The more interactions Starbucks had with their customers, the more knowledge and feedback they could garner in order to develop additional innovations. This connection between the two theories of innovation and relationship marketing illustrates their interdependence.

Starbucks timing to enter the coffee market when coffee consumption in America was steadily declining again demonstrates the transformational leadership qualities exhibited by Schultz to communicate his vision to investor and to motivate them enough to take what was a great financial risk at the time (Schultz & Yang, 1997). This innovative approach to offer a modification to how the American public drank their coffee agrees with Teece’s (1987) position that good timing can introduce a strong source of uniqueness and thus a competitive advantage.

Schultz (1997) and Starbucks early on concentrated on the interaction they had with their customers and worked hard at enhancing their experience. The overwhelmingly positive ‘word of mouth’ advertising they received enabled them to spend almost zero resources on traditional advertising most companies rely on in the form of print ads or commercials. This is a result of Starbucks relationship marketing as described by Grönroos (2007) whereby the cultivated relationships are created by repeated direct contact with customers and a customer-centric system is developed. Schultz early on implemented this customer-centric system in the form of comment cards which he read personally for the first decade in order to actively listen to his customer’s needs and desires. This example also illustrates the necessary leadership characteristics as described by Burns (2008) of actively listening in order to better guide the company to bring to reality the leader’s shared vision.

Another innovation implemented by Starbucks was how they approached the entire supply chain of coffee and in particular the beginning of their supply chain, farmers. As a way to ensure a consistent quality of coffee beans they regularly entered long-term contracts with farmers and on average paid them an average of 23% above market prices (Koehn, 2008; Schultz & Yang, 1997). This act of ‘over-paying’ their suppliers was a manifestation of Schultz’s mission of creating a company with a conscience by doing the ‘right thing’. By treating their suppliers well, Starbucks was able to have more control over the entire supply chain, which helped them ensure the delicate coffee beans would reach their stores and customers in a condition of top quality, thus clearly becoming a competitive advantage as defined by Rijamampianina et al. (2003).

Schultz’s vision of Starbucks being a benevolent company didn’t end with their farmers and suppliers, but also included the baristas servicing the coffee in the stores. A strategy of Schultz’s that he effectively communicated to the rest of the company was that in order to excel in relationship marketing the Starbucks representatives or employees having the interaction with the customer must be well
compensated and recognized by management for their efforts. Therefore even before Starbucks was a public company and was only a relatively small private company Schultz made the innovative decision to offer stock options to all employees making them ‘partners’ in the company (Schultz & Yang, 1997).

Schultz’s leadership also lead to another innovation of offering all part-time employees working more than 20 hours a week full medical insurance. The results of these innovations appear in Starbucks superior employee retention rates compared to the rest of the restaurant service industry. This incredibly uncommon practice added considerable expense to Starbucks, yet Schultz and others (Koehn, 2008) believe this is another competitive advantage Starbucks enjoyed over their competition.

Schultz exemplified the traits of a leader by not wavering on his vision for Starbucks after the original owners of Starbucks resisted his idea. Schultz worked on communicating his idea and making his personal vision a shared vision throughout the company. A transformational leader is argued to be instrumental to a company’s sustainable competitive advantage and Schultz exemplified it in this context. It is clear that without Schultz’s visionary leadership Starbucks would not have become the resounding success they have become.

5.2 Starbucks Loss of Sustainable Competitive Advantage

The importance of leadership to a company was exemplified when Shultz was asked to return to the company as CEO in 2008 after taking a hiatus from ongoing operations in 2000. After Schultz left the company the leadership that he contributed also left the company. In his absence, Starbucks continued on the course they had been on as if on ‘auto-pilot’ and much of the culture, innovative environment and creativity fell into a static state. This complacency was underlined and described by Schultz in a famous memo that he distributed to the company managers upon his return in 2008. This complacency and the anaemic direction is a major reason why Starbucks success (profits, growth, stock price) had dramatically fallen since his departure (Kohen, 2008; Schultz, 2008). It is without question that the economy played a role in Starbucks hardships during his absence, but Schultz’s memo clearly shows the fundamental paradigm shift within the company. The increased challenges in the recessionary economy accentuated the problems at Starbucks bringing to light the company’s complacency.

The motivation, vision and direction of the company were missing while Schultz was absent from the company, although it took years for the effects to be realized by Starbucks in their loss of profits. This is because many innovations spearheaded by Schultz had a lifespan that continued to contribute even after he left the company. But what becomes apparent from this situation is that the change in leadership negatively impacted the general innovative culture that Schultz had
originally implemented. The structure of the innovative culture at Starbucks created by their leader, Schultz, is what was sustainable and clearly a competitive advantage over their competition. This is agreeable to Rijamampianina et al. (2003), Burn’s (2008), Oliver’s (2000) and Porter’s (1998) views what really constitutes a sustainable advantage in a continuously changing world. The sustainable component to Starbucks competitive advantage was and is Howard Schultz.

5.3 Starbucks Resumption of Sustainable Competitive Advantage

As highlighted by the case study, by 2006, Starbucks had begun a relentless defiance in terms of profitability and uniqueness of its service offering. As Howard Schultz defined it, recent decisions had led to the “watering down of the Starbucks experience” nonetheless the “ commodization of the Starbucks brand” (Exhibit 1). From a marketing point of view, Starbucks has followed a rather unusual, yet proven to be successful, agenda. As a matter of fact, the strategy pursued by the company was to focus all the attentions on the holistic experience at the point of purchase. Every single detail, from the coffee aroma to the bespoke customer service, which were in turn closely analyzed and properly audited by senior management, contributed to the optimization of each step along the value chain. This value package indeed, was constituted by a strong core product together with close relationships between the baristas and the customers. One of the authors that contributed to the theoretical foundations of this research Professor Christian Grönroos (2007) suggests that a close relationship with the clients sets the basis for a much healthier business rapport. As he argues: “Relationship Marketing is based on a notion of trusting cooperation with known customers. Hence [in order to best tailor the service to its customers], firms have to know their clients much better than has normally been the case” (Grönroos, 2007, p. 33). This approached seemed to be common practice among the retailer's baristas. Interestingly enough, in many Starbucks stores for example, employees knew their clients by name and often anticipated their drinks as they walked through the door. However, as the company expanded the personnel turnover almost made it impossible for the customer to have a bespoke service once again.

Howard Schultz's original idea, as he acquired the company in 1987, was to create a model company that would become recognized among the public thanks to its exemplary behavior as an employer and its outstanding service as a retailer. Starbucks, at least for its first years, never felt the necessity of investing in advertising campaigns, but the advertising focus was rather to create enthusiastically satisfied customers that would not only come back again as clients, but eventually tell friends and family about the unique experience of having a cup of coffee at Starbucks. As Schultz affirms, the only asset Starbucks possessed as they started was experience. In turn, that was represented by the expertise that the company possessed as a roaster and a coffee distributor in its very first business years. The wide variety as well as the

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high quality and refinance of the coffee brands already treated by the retailer constituted a strong selling proposition to begin with, and became soon popular amongst the Seattle area first, and most of the other major U.S. cities soon after.

Starbucks coffee stores had to resemble and recreate those vibrant social interaction dynamics of the Italian espresso bars, that captured Schultz’s attention in one of his trips to Milan. All, of course, wrapped by customized service and top of the line coffee roasts. As Grönroos suggests: “An acceptable outcome is an absolute necessity for good perceived quality, but an excellent service process creates a distinct and sustainable competitive edge” (2007, p.71). In simpler words, a good quality of the core product is important but the quality of the purchase experience is even more important. Grönroos' of sustainable competitive advantage is to focus on what he defines a ‘relationship marketing’ approach.

Howard Schultz’s comeback as CEO in 2008, after he left the same position eight years earlier, brought about a new wave of confidence and optimism amongst both, Wall Street investors and partners. This confidence manifested in the audience’s enthusiastic applause that greeted Schultz upon his arrival at Starbucks 2008 annual investors’ meeting (Schwartz, 2007). He publicly announced Starbucks’ intention to resume the mission he set for the company back in 1988 when he acquired it; and in order to do so, he and the senior executives prepared a list of strategic implementations of immediate effect, directly aimed at restoring the Sustainable Competitive Advantage that Starbucks had benefited from for a long time, and that seemed to have gone lost for some reason in the last two years. Howards Schultz indentified these reasons and the new strategic agenda was supposed to resolve these issues. However, Howard Schultz’s main complaint was that by expanding in such a rapid fashion, the core values that were set at the very beginning of this incredible journey had been lost along the way.

In more details, the major initiatives to be implemented immediately constituted great updates in terms of both, innovation and relationship marketing. First, Starbucks planned to replace its automatic coffee machines for a new espresso machine called Mastrena. This machine was smaller than the ones used before, allowing baristas to be colloquial to the customers also while pulling the espresso shot. As Grönroos (2008) suggest, one way of implementing a successful relationship marketing strategy is to seek direct contact with the client. For Starbucks this has always been a must but somewhere along the standardization process, this important element of interaction between customer and service provider, had been forgotten.

On the innovation front, Starbucks introduced a new blend of coffee, which Schultz touted as being so fresh that would make people wanting to drink it black. This new kind of coffee was named after Starbucks very first store in Seattle, The Pike Place, and besides being good and fresh, it also constituted a budget option to the purchase of other more expensive coffee beans.
Two of the company strategic moves, were directly related to Starbucks relationship with its customers. One was a prize program associated with the Starbucks Card (a prepaid card that customers could only use for Starbucks purchases). Some of the major card’s benefits were free refill option on drip coffee and free customization options for various drinks. This card’s usefulness was not only represented by the higher degree of “lock in” created for the customer in possession of these cards, but rather by the fact that these cards could have been a means to analyze specific market trends and purchasing behavior that would have been otherwise more expansive to calculate. The proper auditing of these data will help Starbucks reacting to difficult situations by monitoring their client’s behavior.

The other initiative aimed at maintaining Starbucks relationships with its customer was the creation of a dedicated website called MyStarbucksIdea.com. This interactive web site invited clients to share their opinions on Starbucks about potentially every single aspect of the organization. Senior management and employees would then discuss this feedback and decide whether some suggestions should have been seriously taken into account or not. Again, this tool could contribute to the collection of some valuable data in terms of customers’ feelings and opinions, and promptly react in accordance to the situation.
6. Conclusions

The theoretical framework, the empirical data of Starbucks and the subsequent combined analysis illustrate the delicate and difficult nature of what it takes a company to have a sustainable competitive advantage in order to achieve long-term success. As stated earlier, many scholars believe that there is no such thing as sustainable competitive advantage (Rijamampianina et al., 2003; Oliver, 2000; Duddy & Kandampully, 1999), yet Starbucks prolonged initial success, decrease in success in Schultz’s absence and now current challenge to resume their successful structure does offer insights into what constitutes a sustainable competitive advantage.

“Most business analysts are rapidly coming to the conclusion that not much is sustainable [in business] anymore” (Oliver, 2000, p. 7). We have also come to the same conclusion based on the collective opinions garnered throughout our theoretical research as well as from the empirical case. Both the theoretical and empirical data show that there are prolonged or long term competitive advantages, but nothing is truly sustainable, especially in business. Furthermore, we along with researchers and business minds alike agree that no single product, service, innovation or advantage is sustainable in business, yet there are strategies in which companies can implement that allow them to succeed with competitive advantages more often by pursuing sustainable competitive advantages. It can be described that Starbucks leadership, innovative culture and approach to relationship marketing is not a competitive advantage, but allows them to create specific competitive advantages. Therefore we can speculate that collectively these three theoretical approaches are a portion of the sustainable aspect of Starbucks competitive advantages. Although, a conundrum is formed because it has already been established that nothing is sustainable in business. A more apt description of the theoretical approaches would be to say that they are major aspects of how Starbucks pursues a sustainable competitive advantage.

The importance of the term ‘pursue’ or ‘pursuit’ warrants further clarification. It has been used by many famous figures in quotations such as “the pursuit of happiness” written by Thomas Jefferson in The Declaration of Independence and both Albert Einstein and Gandhi wrote about the pursuit of truth (Gandhi 1993)(Einstein and Harris 2006) as well. The definition of according to Webster’s Dictionary (2009) is “the act of following or going after”. These famous examples demonstrate that ‘the pursuit’ is more than just a term defined, but is a philosophical idiom. It is a presentation of an idea of an endeavour to obtain concepts that are not easily defined as in the case of the stated examples, happiness and truth. The notion of obtaining, having or knowing truth is obscure at best and heavily based on one’s perspective, yet ‘the pursuit’ of truth or anything else is a perfectly logical
theoretical quest that can be sustained. It is within this quest of a difficult obtainment (Starbucks quest for a sustainable competitive advantage) that the philosophical idiom ‘pursue’ is realized.

It should be noted that although the three theoretical approaches described in this thesis do explain to a large degree Starbucks pursuit of sustainable competitive advantage, they do not cover all aspects or offer a full explanation of Starbucks success. Therefore, it is recommended for others to research Starbucks using different theories and perspectives in order to draw out other analyses from the empirical case that could be useful to other business students, entrepreneurs and any organization wishing to succeed on a consistent basis.
As you prepare for the FY 08 strategic planning process, I want to share some of my thoughts with you.

Over the past ten years, in order to achieve the growth, development, and scale necessary to go from less than 1,000 stores to 13,000 stores and beyond, we have had to make a series of decisions that, in retrospect, have led to the watering down of the Starbucks experience, and, what some might call the commoditization of our brand. Many of these decisions were probably right at the time, and on their own merit would not have created the dilution of the experience; but in this case, the sum is much greater and, unfortunately, much more damaging than the individual pieces. For example, when we went to automatic espresso machines, we solved a major problem in terms of speed of service and efficiency. At the same time, we overlooked the fact that we would remove much of the romance and theatre that was in play with the use of the La Marzocca machines. This specific decision became even more damaging when the height of the machines, which are now in thousands of stores, blocked the visual sight line the customer previously had to watch the drink being made, and for the intimate experience with the barista. This, coupled with the need for fresh roasted coffee in every North America city and every international market, moved us toward the decision and the need for flavor locked packaging. Again, the right decision at the right time, and once again I believe we overlooked the cause and the affect of flavor lock in our stores. We achieved fresh roasted bagged coffee, but at what cost? The loss of aroma -- perhaps the most powerful non-verbal signal we had in our stores; the loss of our people scooping fresh coffee from the bins and grinding it fresh in front of the customer, and once again stripping the store of tradition and our heritage? Then we moved to store design. Clearly we have had to streamline store design to gain efficiencies of scale and to make sure we had the ROI on sales to investment ratios that would satisfy the financial side of our business. However, one of the results has been stores that no longer have the soul of the past and reflect a chain of stores vs. the warm feeling of a neighborhood store. Some people even call our stores sterile, cookie cutter, no longer reflecting the passion our partners feel about our coffee. In fact, I am not sure people today even know we are roasting coffee. You certainly can't
get the message from being in our stores. The merchandise, more art than science, is far removed from being the merchant that I believe we can be and certainly at a minimum should support the foundation of our coffee heritage. Some stores don't have coffee grinders, French presses from Bodum, or even coffee filters.

Now that I have provided you with a list of some of the underlying issues that I believe we need to solve, let me say at the outset that we have all been part of these decisions. I take full responsibility myself, but we 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. While the current state of affairs for the most part is self induced, that has led to competitors of all kinds, small and large coffee companies, fast food operators, and mom and pops, to position themselves in a way that creates awareness, trial and loyalty of people who previously have been Starbucks customers. This must be eradicated.

I have said for 20 years that our success is not an entitlement and now it's proving to be a reality. Let's be smarter about how we are spending our time, money and resources. Let's get back to the core. Push for innovation and do the things necessary to once again differentiate Starbucks from all others. We source and buy the highest quality coffee. We have built the most trusted brand in coffee in the world, and we have an enormous responsibility to both the people who have come before us and the 150,000 partners and their families who are relying on our stewardship.

Finally, I would like to acknowledge all that you do for Starbucks. Without your passion and commitment, we would not be where we are today.

Onward…

8. References


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