Starbucks to boost coffee prices in U.S.

SEATTLE (AP) — You'll soon be forking over an extra 11 cents for a gentrified java.

Starbucks (SBUX) says it will raise the average price of its beverages by 11 cents at 4,500 stores in North America Oct. 6 because of increases in the cost of coffee and sugar.

In its announcement Monday, the company did not reveal what the average price of individual beverages would be after the increase. Currently, a 12-ounce Starbucks latte ranges from $2.25 in Minnesota to $3 in New York City.

The price hike — first since August 2000 — will amount to an estimated 3% for all the company's drinks, Smith Barney analyst Mark Kalinowski said. (Related: Starbucks joins effort to help coffee growers.)

The company had announced previously that it would raise prices by the end of the year, saying coffee prices have risen 36% and sugar prices 39% the past year.

McAdams Wright Ragen analyst Dan Geiman said he does not believe the increase will hurt business: "It's 11 cents," he said. "That's not a huge amount when you're already paying a few dollars-plus for your beverage."

The higher prices do not apply at Seattle's Best Coffee, a smaller chain owned by Starbucks, company spokesman Alan Hilowitz said.

Latte Letdown:
Starbucks Set
To Raise Prices

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That frappuccino fix is about to cost you more.

Starbucks Corp., the coffee giant that acclimated millions of Americans to paying unheard-of sums for a drink once largely made at home, is planning to raise its prices for the first time in four years.

Citing higher costs for milk and other commodities, as well as higher rent and health-insurance expenses, the Seattle company plans to charge more across its beverage menu board. "Prior to the end of the calendar year, Starbucks will be taking a modest price increase," Chairman Howard Schultz said in an interview yesterday. The company is mum on how much.
Starbucks last raised its prices in August 2000, by seven cents on average, an increase of 2% to 3%. But that pocket change per cup, for a company with more than 8,000 highly trafficked locations worldwide, made headlines from coast to coast.

Given current pricing pressures, some restaurant analysts are anticipating Starbucks will bump up prices 4% to 5% this time, adding a dime or so to the average $2 to $2.50 drink. The increase affects the company's North American stores.

Some Starbucks fans detest the thought of any increase. "Ludicrous!" says Laura Napoles, a 44-year-old mother of two, after being told of a looming price hike as she left a downtown Chicago Starbucks, cup in hand. "I have kids, so my money has to go so many different ways," says Ms. Napoles, who adds that higher prices could steer her to a small restaurant near her office for her afternoon caffeine fix. "They need to get a grip."

A steeper price could push Starbucks' luck. Earlier this year, roughly two-thirds of regular coffeehouse customers surveyed by market-research firm Mintel International Group said that gourmet-takeout coffee is too expensive. Since many people go to Starbucks every day, they are well aware of exactly what their regular order runs, and some even approach the counter with the exact amount of cash and coins in hand. Some 30 million customers visit Starbucks nationwide each week, shelling out $3.50 to $4 a trip on average.

Buzz about a looming price hike was heightened last week when Starbucks reported its first dip in monthly same-stores sales growth at company-owned units in 10 months. Sales at stores open at least 13 months rose 8% compared with 9% in the same period last year. Those results, for the four-week period ended Aug. 22, exceeded the company's own 3% to 7% projections, but trailed those of many restaurant industry analysts. Starbucks and analysts attributed the weak showing to no single factor, but pointed to an apparent slowdown in consumer spending that has impacted other retailers, including restaurants.

Mr. Schultz, the chairman, has said he was able to resist a fifth price increase in a decade largely by belt-tightening. But in another interview last week, he said, "It's clear to us that there are certain financial issues that we can't control."

Ironically, coffee-bean prices aren't among them. Companies like Starbucks and Diedrich Coffee Inc.'s Gloria Jean's Coffees are generally cushioned from shifts in the coffee market, largely because of long-term contracts that lock them into above-market rates. According to the Long Beach, Calif.-based Specialty Coffee Association of America, coffee beans account for just 5% to 10% of the costs of making a cup of coffee.

The bigger price culprits are rising dairy and operating costs. Starbucks said that it has recently experienced double-digit costs increases in its health insurance plan, which offers all of its
80,000 full- and part-time employees worldwide. Costs for dairy and real estate also escalated, but the company declined to say by how much.

Pricing at Starbucks has intrigued everyone from consumer-product company executives to comedians. In the last decade, the company mainstreamed the once-edgy specialty coffee market -- making competitors of Allied Domecq PLC's Dunkin' Donuts and McDonald's Corp., among others. Despite being the butt of late-night comics' jokes, Starbucks made it seem normal somehow to spend $4.02 for a grande Frappuccino, the chain's signature creamy coffee.

Demand for prepared coffee tends to be fairly resistant to price increases, and economics professors often use Starbucks as an example of a company whose product seems to have little price elasticity -- that is, increases seem to have very little effect on consumer demand. By contrast, mass-market grocery brands such as Kraft Foods Inc.'s Folgers and Maxwell House coffees tend to be much more price-elastic, says Burt P. Flickinger III, managing director of Strategic Resource Group, a New York consulting firm that works with retailers and suppliers.

"In the end, Starbucks probably will be able to pass along a price increase without a very big falloff," says Frank Badillo, senior economist at Retail Forward Inc., a Columbus-based consulting firm.

In a spot-check of prices of specialty coffee shops in eight cities this summer, John Glass, a restaurant industry analyst for CIBC World Markets in Boston, found Starbucks coffee was actually cheaper than its cafe competitors by 4% for regular brews and up to 30% on iced blended beverages. "There's no question that they have room to raise prices," Mr. Glass says. "It's how much room they have."

In recent months, competitors like Caribou Coffee Co. also have faced rising commodity costs, particularly for milk. But Michael Coles, CEO of the Minneapolis-based chain, says it has no plans to pass those increases on to customers. However, Diedrich Coffee Inc., the Irvine, Calif., company that owns the roughly 450-unit Gloria Jean's, says its costs for premium coffee and dairy have risen more than 20% on average since last year. Martin Lynch, chief financial officer, says the company will likely follow Starbucks' lead. "By the end of the year, we're going to see what our costs are -- and how the big guy in the industry is going to handle it," he says.