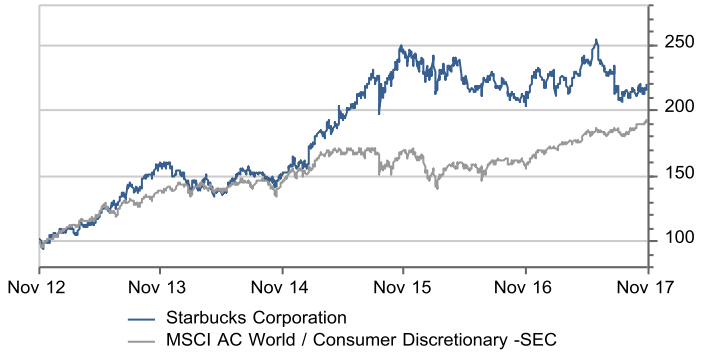
Starbucks Corporation

Isin / FactSet Code	**US8552441094 / SBUX-US**	Market cap (in EUR mn)	**69 638**	52-week high	**64.87**	Rating	**BUY**
Sector	**Consumer Discretionary**	Market cap (in local curr. mn)	**80 902**	52-week low	**50.84**	12-month target price	**62.00**
Industry	**Hotels Restaurants & Leisure**	Local currency	**USD**	YTD return%	**0.92**	Last price (03/11/17)	**56.03**
Benchmark	**MSCI AC World / Consumer Discretionary -SEC**	Free-float	**97%**	12-month return%	**8.23**	Potential upside	**11%**

Investment Case:

- Starbucks is a leading global brand, which commands stable domestic sales and has a strong potential for international expansion. Its focus on China in particular, where it plans to double the number of stores to 5 000 by FY21, should support earnings growth in the long term. Starbucks also commands strong brand loyalty (13.3 mn active Starbucks Rewards members in 4Q17), which should facilitate comparable-store sales growth.
- The company increased its investments in people and digital initiatives by ~USD 250 mn in FY17 (+56% YoY). This, along with its promotions and increased penetration of Mobile Order and Pay (~10% of the US transactions in 4Q17), should support its commitment of delivering FY18E EPS growth of 12–13%.
- We expect Starbucks to continue trading at a premium against peers, driven by its better sales growth potential and strong balance sheet. However, given the weaker long-term comparable sales and EPS growth guidance, we lower our target price to USD 62.00 (from USD 64.00), valuing the stock at FY18E P/E of 26.6x.

Five-year Performance vs. Benchmark (rebased to 100)



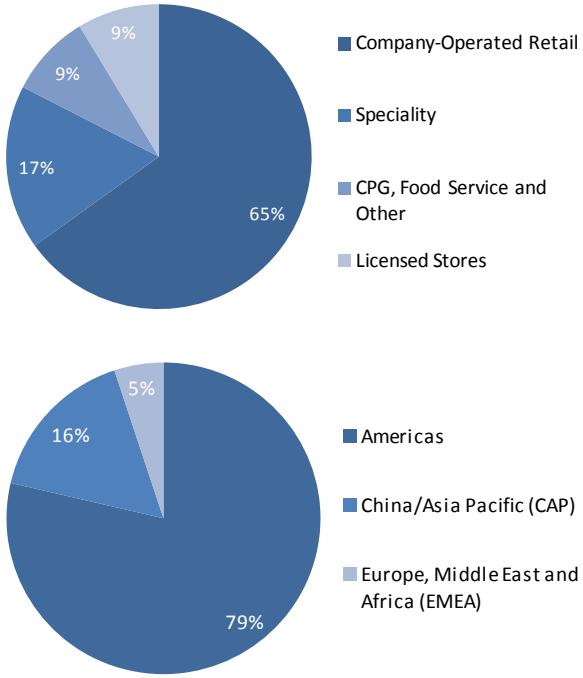
Sources: SGPB, FactSet

Company Description:

Starbucks manufactures and sells coffee, tea and other beverages and food items through company-operated and licensed stores, other retailers and its online store. The company's brand portfolio includes Starbucks Coffee, Teavana, Tazo, Seattle's Best Coffee, Evolution Fresh, La Boulange and Ethos.

Revenue by Key Segment & Geographies: FY17

(FY ending September)



Sources: SGPB, Company, FactSet

Recent Developments Analysis:

- FY17 results were mixed. Revenue increased 5% YoY to USD 22.39 bn, in line with consensus. Operating income fell 0.9% to USD 4.13 bn, missing consensus by ~7% due to higher operating costs and negative impact from temporary store closures due to hurricanes in the US. Global comparable sales rose 3% on improvements in the US (+3%) and CAP (+3%). GAAP EPS climbed 3.7% to USD 1.97, achieving top-end of the management guidance.
- The Americas and CAP revenues gained from higher comparable sales and new store openings. EMEA revenue declined, due to impact of adverse FX movement and model shift to more licensed stores. Channel Development revenue rose on market share gains in packaged and roasted ground coffee categories. The company sold its Tazo tea brand to Unilever for USD 384 mn in order to focus on the Teavana brand. It expects the transaction to be completed by 1Q18, post regulatory approvals.
- The management expects FY18 global comparable sales to grow 3–5% (lower than ~6% historically). Starbucks reduced its long-term EPS growth guidance to at least ~12% annually from ~15% previously. The company estimates FY18 EPS of USD 2.30–2.33, benefitting from the EPS accretive East China JV and Tazo transactions.

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Starbucks Corporation

DESCRIPTION			VALUATION					GROWTH				PROFITABILITY			BALANCE SHEET		
FactSet Code	Company	Cap (mn€)	EV/EBITDA (e)		P/E (e)		Div. Yield	Sales Growth		EPS Growth		EBITDA Margin	Net Margin	ROE	Net Debt/ EBITDA		Net Debt/ Equity
			FY1x	FY2x	FY1x	FY2x	FY1%	FY1%	FY2%	FY1%	FY2%	FY1%	FY1%	FY1%	FY0x	FY1x	FY0x
MCD-US	**McDonald's Corporation**	117 586	15.7	15.8	25.8	24.1	2.3	-7.9	-10.8	13.7	7.4	45.5	23.4	na	2.6	2.5	na
YUM-US	**Yum! Brands, Inc.**	23 418	17.9	17.6	28.1	24.9	1.5	-7.1	-18.9	14.3	13.2	34.0	16.9	na	4.2	4.4	na
QSR-CA	**Restaurant Brands International I**	13 424	12.7	11.3	32.7	24.8	1.2	8.9	8.3	24.7	32.8	45.6	20.8	41.8	4.0	5.2	1.45
WTB-GB	**Whitbread PLC**	7 644	9.2	8.6	14.4	13.6	2.7	7.8	7.5	4.0	7.6	25.3	13.9	16.9	1.2	1.2	0.35
DNKN-US	**Dunkin' Brands Group, Inc.**	4 581	15.6	15.5	24.3	22.3	2.2	2.8	2.3	7.1	9.5	56.8	26.1	na	4.4	4.6	na
		Average:	**14.2**	**13.8**	**25.1**	**21.9**	**2.0**	**0.9**	**-2.3**	**12.8**	**14.1**	**41.4**	**20.2**	**29.4**	**3.3**	**3.6**	**0.90**
SBUX-US	**Starbucks Corporation**	69 638	13.8	12.5	24.1	21.1	2.2	9.5	9.4	12.6	14.2	24.6	13.4	64.4	0.2	0.4	0.23

na=Not available, nm=Not meaningful
Financial terms detailed in glossary
Sources: SGPB, FactSet

Risks To Our Investment Case:

- As the company's earnings are highly exposed to the US market (74%), a decline in coffee consumption or retail sales in this region would hamper its EPS growth. Lower comparable growth in the US market would impede earnings growth in the long term.
- Lower-than-expected growth in coffee consumption in China, where tea is preferred over coffee, would reduce returns from the ongoing capital expenditure in this market.
- Adverse commodity-price movements in coffee beans and dairy products (the major input costs for Starbucks, which the company hedges through derivative contracts) could stress its operating margin in the medium term.
- A lower-than-expected outcome of the company's multiple initiatives (e.g. Mobile Order and Pay) could dilute its earnings growth in the long term.

Business Quality Review:

- Starbucks is an industry leader in terms of same-store sales growth with an average FY13–17 ROE at 41.9%. The company also commands higher EPS growth and lower gearing.
- The management is committed to deliver the Starbucks Experience through the addition of new stores in key markets. Further, the company plans to upgrade the existing self-operated stores, and systems and technological infrastructure. Consequently, Starbucks estimates the FY18 capital expenditure at USD 2.0 bn.

Dividend Policy:

- Dividend paid in FY17 amounted to ~USD 1.5 bn with DPS at USD 1.05. Starbucks maintained a high FY13–17 payout at ~43.6%.
- On its Investor Day, Starbucks raised the long-term dividend payout ratio target to 40–50%.
- The company also repurchased stocks worth ~USD 2.0 bn in FY17.
- Starbucks offers a FY18E dividend yield of 2.2%.

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Financial Terms And Acronyms

BV (Book Value): is the total value of net assets of a company.

BV/S (Book Value Per Share): is the total value of the net assets of a company divided by the total number of outstanding shares.

C/I (Cost Income Ratio): is used for valuing banks. It shows a company's costs in relation to its income.

CAGR (Compound Annual Growth Rate): is a term used for the geometric progression ratio that provides a constant rate of return over a specific time period.

CAPEX (Capital Expenditure): is the fund used by the company to acquire or upgrade the physical assets such as property, industrial buildings or equipment. The most capital intensive industries include oil, telecom and utilities.

CAR (Capital Adequacy Ratio): is a measure of a bank's capital. It is expressed as a percentage of a bank's risk-weighted credit exposures.

CET I (Common Equity Tier I Ratio) : is a measure of the bank's common equity capital as a percentage of risk-weighted assets. It is generally compared to a defined benchmark stipulated by the regulatory authority to determine whether a bank is sufficiently capitalised.

COMBINED RATIO: It represents the total of acquisition and administrative expenses, and claims and insurance benefits incurred, divided by net premiums earned.

DIVIDEND YIELD: Dividend per share or DPS (total dividend paid out divided by the total number of shares) expressed as a percentage of current stock price.

EBIT (Earnings Before Interest and Taxes): profit before taking into account interest payments and income taxes.

EBIT Margin: Ratio that expresses EBIT as a percentage of total sales (EBIT/Sales*100)

EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortisation): profit before taking into account interest payments, income taxes and non-cash operating expenses (depreciation and amortisation).

EPS (Earnings Per Share): is the division of total net profit by the number of shares.

EQUITY is the difference between the value of the assets and the cost of the liabilities.

EV (Enterprise Value) is a measure of a company's value, often used as an alternative to straightforward market capitalisation. It is calculated as (market cap + debt + minority interest + preferred shares) − total cash − cash equivalents.

FCF (Free Cash Flow): represents the difference between operating cash flow and capital expenditures.

FFO (Funds from Operations): measures a REIT's operating performance. It is net income plus gains (minus losses) from property sale and purchase. FFO per share is often used in place of earnings per share when analysing REITs.

FY0: Realised year, **FY1**: Current unrealised year, **FY2**: next year, **FY18E:** Fiscal year 2018 estimation

GOODWILL: is an intangible asset that arises as a result of the acquisition of one company by another company for a premium value.

GROSS INCOME: gross profit calculated as a company's total sales minus its cost of goods sold (COGS) that corresponds to labour and production costs.

GROSS MARGIN: expresses gross income as a percentage of total sales.

LIKE FOR LIKE (LFL) GROWTH: is a measure of growth in sales, adjusted for new or divested businesses.

Loan-to-deposit (L/D) ratio: Loans/Deposits. This helps in assessing a bank's liquidity, lending capacity and balance sheet quality.

LTV (Loan-To-Value Ratio): is a financial term used to express the ratio of a loan to the value of an asset purchased.

NAV (Net Asset Value): is similar to book value and is also called per investment unit. NAV is the marked-to-market value of the company's property investments less liabilities.

ND (Net Debt): is calculated as a company's total debt minus cash and other similar liquid assets.

NET MARGIN: is a financial ratio which measures the profitability of the net income of a company.

NI (Net Income or Bottom Line): represents a company's total earnings (or profit) which is calculated by adjusting revenues for the costs, depreciation, interest, taxes and other expenses.

NIM: Net Interest Margin

NON-PERFORMING LOANS (NPL) RATIO: NPLs/Loans. This indicates the percentage of the loans that are non-performing or are in stressed segments.

OPERATING MARGIN: See definition of EBIT Margin.

ORGANIC GROWTH: is the growth rate that a company can achieve by increasing its output and enhancing sales, excluding any profits or growth from takeovers or M&A activities.

P/E or PER (Price Earnings Ratio): reflects the trading price of a share in relation to the expected earnings.

P/BV (Price To Book Value): expresses the share price with regard to the accounting value of the company.

PAYOUT RATIO: is the proportion of earnings paid out as dividends to shareholders and typically expressed as a percentage.

PROFIT WARNING: is the announcement made by the company before its earnings release indicating the investors that its earnings would not meet the analysts' expectations.

RWA (Risk Weighted Assets): is a measure of the bank's assets, weighted according to their risk. It involves the risk weighting of both on and off-balance-sheet exposures.

REVENUE GROWTH: Illustrates the growth of sales over a given period.

ROA (Return on assets): a financial ratio that is calculated as net income divided by total assets and shows how profitable a company is relative to its total assets.

ROC (Return on invested capital): a profitability ratio which is calculated as net income minus dividends divided by total invested capital.

ROE (Return On Equity): The amount of net income returned as a percentage of shareholders' equity. Return on equity measures a corporation's profitability by disclosing how much profit a company generates with the money shareholders have invested.

TBV (Tangible Book Value): is the book value excluding intangible assets.

TBV/S (Tangible Book Value Per Share): allows to estimate the accounting value of a company by measuring its stockholders' equity per share. Formula: Re-valued Net Assets/Total Shares of Company.

WACC (Weighted Average Cost of Capital): also referred to as the firm's cost of capital, it is the rate that a company is expected to pay on an average to all its security holders to finance its assets.

WORKING CAPITAL: is the difference between a company's current assets and current liabilities and shows whether the company has sufficient short-term assets to cover its short-term debts.

Appendix

Investment Rating Definitions:

Buy Stock that is expected to outperform its MSCI sector index over a 12-month investment horizon.

Neutral Stock that is expected to perform in line with its MSCI sector index over a 12-month investment horizon.

Sell Stock that is expected to underperform its MSCI sector index over a 12-month investment horizon.

Restricted Covered stock that is not rated or assigned a target price as the Societe Generale group has a capital market transaction with that company.

Termination Stock is subject to be deleted from the SGPB recommended universe and will no longer be followed. In this case, a coverage termination alert is issued.

Recommended Universe Principle:

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Product Risk Rating:

The product category of single equity, stock, share is rated at '4'.

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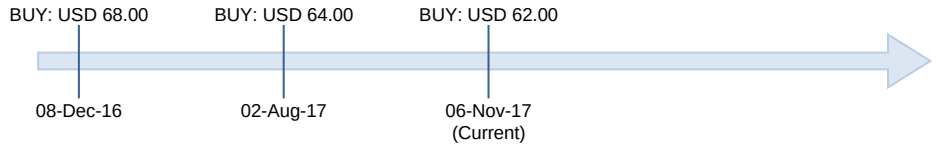
Risk Levels	Losses
0 - Lowest Risk	There is a 95% probability that the product will not depreciate in value in one year.
1 - Low Risk	There is a 95% probability that the product will not lose more than 5% of its value in one year.
2 - Medium Risk	There is a 95% probability that the product will not lose more than 15% of its value in one year.
3 - High Risk	There is a 95% probability that the product will not lose more than 30% of its value in one year.
4 - Highest Risk	There is a minimum of 5% probability that the product will lose more than 30% of its value in one year.

1Y Target Price:



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SG acted as passive bookrunner in the Mcdonald's senior bond issue.

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Risk Classification:

R0: Lowest Risk
R1: Low Risk
R2: Medium Risk
R3: High Risk
R4: Highest Risk

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