

STARBUCKS CORP
Form 10-Q
May 02, 2012
[Table of Contents](#)

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Quarterly Period Ended April 1, 2012

OR

.. **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to .

Commission File Number: 0-20322

STARBUCKS CORPORATION

(Exact Name of Registrant as Specified in its Charter)

Edgar Filing: STARBUCKS CORP - Form 10-Q

Washington
(State or Other Jurisdiction of

91-1325671
(IRS Employer

Incorporation or Organization)

Identification No.)

2401 Utah Avenue South, Seattle, Washington 98134

(Address of principal executive offices)

(206) 447-1575

(Registrant's Telephone Number, including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act): Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Title	Shares Outstanding as of April 25, 2012
Common Stock, par value \$0.001 per share	758.5 million

Table of Contents

STARBUCKS CORPORATION

FORM 10-Q

For the Quarterly Period Ended April 1, 2012

Table of Contents

	Page
PART I. FINANCIAL INFORMATION	
Item 1	3
<u>Financial Statements (Unaudited):</u>	
<u>Condensed Consolidated Statements of Earnings</u>	3
<u>Condensed Consolidated Balance Sheets</u>	4
<u>Condensed Consolidated Statements of Cash Flows</u>	5
<u>Notes to Condensed Consolidated Financial Statements</u>	6
Item 2	16
<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	
Item 3	29
<u>Quantitative and Qualitative Disclosures About Market Risk</u>	
Item 4	29
<u>Controls and Procedures</u>	
PART II. OTHER INFORMATION	
Item 1	29
<u>Legal Proceedings</u>	
Item 1A	30
<u>Risk Factors</u>	
Item 2	30
<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	
Item 6	32
<u>Exhibits</u>	
<u>Signatures</u>	33
Index to Exhibits	

Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****STARBUCKS CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS***(in millions, except per share data)**(unaudited)*

	Quarter Ended		Two Quarters Ended	
	Apr 1, 2012	Apr 3, 2011	Apr 1, 2012	Apr 3, 2011
Net revenues:				
Company-operated stores	\$ 2,521.2	\$ 2,293.5	\$ 5,253.0	\$ 4,744.8
Licensed stores	290.3	237.8	596.9	491.9
CPG, foodservice and other	384.4	254.4	781.9	499.8
Total net revenues	3,195.9	2,785.7	6,631.8	5,736.5
Cost of sales including occupancy costs	1,411.9	1,171.2	2,908.0	2,363.5
Store operating expenses	956.5	867.2	1,952.2	1,755.2
Other operating expenses	105.3	98.9	212.0	189.0
Depreciation and amortization expenses	137.1	129.0	271.9	256.7
General and administrative expenses	206.9	181.6	398.4	366.8
Total operating expenses	2,817.7	2,447.9	5,742.5	4,931.2
Income from equity investees	52.2	38.3	97.1	72.7
Operating income	430.4	376.1	986.4	878.0
Interest income and other, net	35.3	19.9	58.5	34.2
Interest expense	(8.8)	(7.1)	(17.4)	(15.0)
Earnings before income taxes	456.9	388.9	1,027.5	897.2
Income taxes	146.8	126.5	335.2	287.3
Net earnings including noncontrolling interests	310.1	262.4	692.3	609.9
Net earnings attributable to noncontrolling interests	0.2	0.8	0.4	1.8
Net earnings attributable to Starbucks	\$ 309.9	\$ 261.6	\$ 691.9	\$ 608.1
Earnings per share - basic	\$ 0.41	\$ 0.35	\$ 0.92	\$ 0.81
Earnings per share - diluted	\$ 0.40	\$ 0.34	\$ 0.90	\$ 0.79
Weighted average shares outstanding:				
Basic	754.6	750.3	751.3	748.0
Diluted	773.3	771.8	770.9	769.3
Cash dividends declared per share	\$ 0.17	\$ 0.13	\$ 0.34	\$ 0.26

See Notes to Condensed Consolidated Financial Statements

Table of Contents

STARBUCKS CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

(in millions, except per share data)

(unaudited)

	Apr 1, 2012	Oct 2, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 1,432.2	\$ 1,148.1
Short-term investments	802.1	902.6
Accounts receivable, net	437.4	386.5
Inventories	1,205.0	965.8
Prepaid expenses and other current assets	259.6	161.5
Deferred income taxes, net	215.2	230.4
Total current assets	4,351.5	3,794.9
Long-term investments	145.9	107.0
Equity and cost investments	393.8	372.3
Property, plant and equipment, net	2,382.5	2,355.0
Other assets	392.1	409.6
Goodwill	340.7	321.6
TOTAL ASSETS	\$ 8,006.5	\$ 7,360.4
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	\$ 388.3	\$ 540.0
Accrued liabilities	896.3	940.9
Insurance reserves	155.9	145.6
Deferred revenue	530.9	449.3
Total current liabilities	1,971.4	2,075.8
Long-term debt	549.6	549.5
Other long-term liabilities	348.8	347.8
Total liabilities	2,869.8	2,973.1
Shareholders' equity:		
Common stock (\$0.001 par value) authorized, 1,200.0 shares; issued and outstanding, 757.9 and 744.8 shares, respectively (includes 3.4 common stock units in both periods)	0.8	0.7
Additional paid-in capital	359.3	40.5
Retained earnings	4,732.1	4,297.4
Accumulated other comprehensive income	41.7	46.3
Total shareholders' equity	5,133.9	4,384.9
Noncontrolling interests	2.8	2.4
Total equity	5,136.7	4,387.3
TOTAL LIABILITIES AND EQUITY	\$ 8,006.5	\$ 7,360.4

Edgar Filing: STARBUCKS CORP - Form 10-Q

See Notes to Condensed Consolidated Financial Statements

Table of Contents**STARBUCKS CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS***(in millions, unaudited)*

	Two Quarters Ended	
	Apr 1, 2012	Apr 3, 2011
OPERATING ACTIVITIES:		
Net earnings including noncontrolling interests	\$ 692.3	\$ 609.9
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	287.9	271.6
Deferred income taxes, net	44.6	49.1
Income earned from equity method investees, net of distributions	(18.2)	(7.4)
Stock-based compensation	76.0	71.2
Other	(0.8)	21.1
Cash provided/(used) by changes in operating assets and liabilities:		
Inventories	(236.5)	(226.2)
Accounts payable	(159.3)	46.1
Accrued liabilities	(34.2)	(107.5)
Deferred revenue	81.6	70.7
Prepaid expenses, other current assets and other assets	(157.8)	(129.1)
Net cash provided by operating activities	575.6	669.5
INVESTING ACTIVITIES:		
Purchase of investments	(1,240.9)	(105.0)
Maturities and calls of investments	1,306.9	214.6
Acquisitions, net of cash acquired	(29.7)	0.0
Additions to property, plant and equipment, net	(313.8)	(239.1)
Other	(9.5)	(9.6)
Net cash used by investing activities	(287.0)	(139.1)
FINANCING ACTIVITIES:		
Proceeds from issuance of common stock	123.8	126.4
Excess tax benefit from exercise of stock options	135.2	67.6
Cash dividends paid	(255.0)	(194.3)
Repurchase of common stock	(15.7)	(60.5)
Other	(0.2)	(0.5)
Net cash used by financing activities	(11.9)	(61.3)
Effect of exchange rate changes on cash and cash equivalents	7.4	12.1
Net increase in cash and cash equivalents	284.1	481.2
CASH AND CASH EQUIVALENTS:		
Beginning of period	1,148.1	1,164.0
End of period	\$ 1,432.2	\$ 1,645.2
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest, net of capitalized interest	\$ 17.2	\$ 17.2
Income taxes	\$ 271.2	\$ 267.2

See Notes to Condensed Consolidated Financial Statements

Table of Contents

STARBUCKS CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

Note 1: Summary of Significant Accounting Policies

Financial Statement Preparation

The unaudited condensed consolidated financial statements as of April 1, 2012, and for the quarter and two quarters ended April 1, 2012 and April 3, 2011, have been prepared by Starbucks Corporation under the rules and regulations of the Securities and Exchange Commission (SEC). In the opinion of management, the financial information for the quarter and two quarters ended April 1, 2012 and April 3, 2011 reflects all adjustments and accruals, which are of a normal recurring nature, necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods. In this Quarterly Report on Form 10-Q (10-Q) Starbucks Corporation is referred to as Starbucks, the Company, we, us or our .

The financial information as of October 2, 2011 is derived from our audited consolidated financial statements and notes for the fiscal year ended October 2, 2011 (fiscal 2011), included in Item 8 in the Fiscal 2011 Annual Report on Form 10-K (the 10-K). The information included in this 10-Q should be read in conjunction with the footnotes and management s discussion and analysis of the financial statements in the 10-K.

In the second quarter of fiscal 2012, we renamed our Global Consumer Products Group (CPG) segment Channel Development.

The results of operations for the quarter and two quarters ended April 1, 2012 are not necessarily indicative of the results of operations that may be achieved for the entire fiscal year ending September 30, 2012 (fiscal 2012).

Recent Accounting Pronouncements

In September 2011, the Financial Accounting Standards Board (FASB) issued guidance that revises the requirements around how entities test goodwill for impairment. The guidance allows companies to perform a qualitative assessment before calculating the fair value of the reporting unit. If entities determine, on the basis of qualitative factors, that the fair value of the reporting unit is more likely than not greater than the carrying amount, a quantitative calculation would not be needed. We plan to early adopt this guidance effective for our fiscal 2012 annual goodwill impairment test. The adoption of this guidance will result in a change in how we perform our goodwill impairment assessment; however, it will not have a material impact on our financial statements.

In June 2011, the FASB issued guidance that revises the manner in which entities present comprehensive income in their financial statements. The guidance requires entities to report the components of comprehensive income in either a single, continuous statement or two separate but consecutive statements. The guidance will become effective for us at the beginning of our first quarter of fiscal 2013. The adoption of this new guidance will result in a change in how we present the components of comprehensive income, which is currently presented within our consolidated statements of equity.

In May 2011, the FASB issued guidance to amend the fair value measurement and disclosure requirements. The guidance requires the disclosure of quantitative information about unobservable inputs used, a description of the valuation processes used, and a qualitative discussion around the sensitivity of the measurements. The guidance became effective for us at the beginning of our second quarter of fiscal 2012. The adoption of this new guidance did not have a material impact on our financial statements.

Reclassifications

Change in shared service allocations

Effective at the beginning of fiscal 2012, we implemented the previously announced strategic realignment of our organizational structure designed to accelerate our global growth strategy. A president for each region, reporting directly to our chief executive officer, now oversees the company-operated retail business working closely with both the licensed and joint-venture business partners in each market. The regional presidents also work closely with our Channel Development team to continue building out our brands and channels in each region.

Table of Contents

In connection with the changes to our organizational structure and reporting, we have changed the accountability for, and reporting of, certain indirect overhead costs. Certain indirect merchandising, manufacturing costs and back-office shared service costs, which were previously allocated to segment level costs of sales and operating expenses, are now managed at a corporate level and will be reported within unallocated corporate expenses. These expenses have therefore been removed from the segment level financial results. In order to conform prior period classifications with the new alignment, the historical consolidated financial statements have been recast with the following adjustments to previously reported amounts:

	Quarter Ended Apr 3, 2011			Two Quarters Ended Apr 3, 2011		
	As Filed	Reclass	As Adjusted	As Filed	Reclass	As Adjusted
Total net revenues	\$ 2,785.7	\$ 0.0	\$ 2,785.7	\$ 5,736.5	\$ 0.0	\$ 5,736.5
Cost of sales including occupancy costs	1,180.1	(8.9)	1,171.2	2,380.9	(17.4)	2,363.5
Store operating expenses	885.4	(18.2)	867.2	1,791.0	(35.8)	1,755.2
Other operating expenses	101.1	(2.2)	98.9	193.7	(4.7)	189.0
Depreciation and amortization expenses	129.0	0.0	129.0	256.7	0.0	256.7
General and administrative expenses	152.3	29.3	181.6	308.9	57.9	366.8
Total operating expenses	2,447.9	0.0	2,447.9	4,931.2	0.0	4,931.2
Income from equity investees	38.3	0.0	38.3	72.7	0.0	72.7
Operating income	\$ 376.1	\$ 0.0	\$ 376.1	\$ 878.0	\$ 0.0	\$ 878.0

There was no impact to consolidated net revenues, total operating expenses, operating income, or net earnings as a result of this change. Additional discussion regarding the change in our organizational structure and segment results is included at Note 12.

Note 2: Acquisition

On November 10, 2011, we acquired the outstanding shares of Evolution Fresh, Inc., a super-premium juice company, to expand our portfolio of product offerings and enter into the super-premium juice market. We acquired Evolution Fresh for a purchase price of \$30 million in cash. The fair value of the net assets acquired on the acquisition date included \$18 million of goodwill.

Evolution Fresh is its own operating segment and is reported in Other along with our Seattle's Best Coffee operating segment, our Digital Ventures business, and unallocated corporate expenses.

Note 3: Derivative Financial Instruments**Cash Flow Hedges**

Net derivative losses of \$23.1 million and \$11.1 million, net of taxes, were included in accumulated other comprehensive income as of April 1, 2012 and October 2, 2011, respectively, related to cash flow hedges. Included in the net derivative losses for the quarter was the impact of cash flow derivative instruments entered into during the period to hedge portions of our future coffee purchases. Of the net derivative losses accumulated as of April 1, 2012, \$5.7 million pertains to hedging instruments that will be dedesignated within 12 months and will also continue to experience fair value changes before affecting earnings. Ineffectiveness from hedges during the year-to-date periods in fiscal 2012 and 2011 was not material. Outstanding contracts will expire within 18 months.

Net Investment Hedges

Net derivative losses of \$27.8 million and \$34.2 million, net of taxes, were included in accumulated other comprehensive income as of April 1, 2012 and October 2, 2011, respectively, related to investment derivative hedges. Outstanding contracts will expire within 36 months.

Other Derivatives

To mitigate the translation risk of certain balance sheet items, we enter into foreign currency forward contracts that are not designated as hedging instruments. These contracts are recorded at fair value, with the changes in fair value recognized in net interest income and other on the consolidated statements of earnings. Gains and losses from these instruments are largely offset by the financial impact of translating foreign

Edgar Filing: STARBUCKS CORP - Form 10-Q

currency denominated payables and receivables, which is also recognized in net interest income and other.

We also enter into swap and futures contracts that are not designated as hedging instruments, to mitigate the price uncertainty of a portion of our future purchases of dairy products and diesel fuel. These contracts are recorded at fair value, with the changes in fair value recognized in net interest income and other on the consolidated statements of earnings.

Table of Contents

The following table presents the pretax effect of derivative instruments on earnings and other comprehensive income for the quarter and two quarters ended (in millions):

	Cash Flow Hedges		Net Investment Hedges		Other Derivatives	
	Apr 1, 2012	Apr 3, 2011	Apr 1, 2012	Apr 3, 2011	Apr 1, 2012	Apr 3, 2011
<i>Quarter Ended:</i>						
Gain/(Loss) recognized in earnings	\$ (2.8)	\$ (3.3)	\$ 0.0	\$ 0.0	\$ (5.7)	\$ (1.2)
Gain/(Loss) recognized in OCI	\$ (15.2)	\$ 0.2	\$ 10.3	\$ 3.7		

	Cash Flow Hedges		Net Investment Hedges		Other Derivatives	
	Apr 1, 2012	Apr 3, 2011	Apr 1, 2012	Apr 3, 2011	Apr 1, 2012	Apr 3, 2011
<i>Two Quarters Ended:</i>						
Gain/(Loss) recognized in earnings	\$ (5.9)	\$ (6.2)	\$ 0.0	\$ 0.0	\$ 4.0	\$ 0.5
Gain/(Loss) recognized in OCI	\$ (16.5)	\$ (8.1)	\$ 10.3	\$ 0.1		

The amounts shown as recognized in earnings for cash flow and net investment hedges represent the realized gains/(losses) transferred out of other comprehensive income (OCI) to earnings during the year. The amounts shown as recognized in OCI are prior to these transfers of realized gains/(losses) to earnings.

Notional amounts of outstanding derivative contracts as of April 1, 2012:

\$416 million in foreign exchange contracts

\$200 million in coffee contracts

\$31 million in dairy contracts

\$16 million in diesel contracts

Note 4: Fair Value Measurements

Assets and Liabilities Measured at Fair Value on a Recurring Basis (in millions):

	Fair Value Measurements at Reporting Date Using			
	Balance at April 1, 2012	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Short-term investments:				
Available-for-sale securities				
Agency obligations	\$ 70.0	\$ 0.0	\$ 70.0	\$ 0.0
Commercial paper	137.9	0.0	137.9	0.0
Corporate debt securities	67.4	0.0	67.4	0.0

Edgar Filing: STARBUCKS CORP - Form 10-Q

Government treasury securities	399.7	399.7	0.0	0.0
Certificates of deposit	68.4	0.0	68.4	0.0
Total available-for-sale securities	743.4	399.7	343.7	0.0
Trading securities	58.7	58.7	0.0	0.0
Total short-term investments	802.1	458.4	343.7	0.0
Long-term investments:				
Agency obligations	14.0	0.0	14.0	0.0
Corporate debt securities	72.0	0.0	72.0	0.0
State and local government obligations	28.3	0.0	0.0	28.3
Certificates of deposit	31.6	0.0	31.6	0.0
Total long-term investments	145.9	0.0	117.6	28.3
Total	\$ 948.0	\$ 458.4	\$ 461.3	\$ 28.3
Liabilities:				
Derivatives	\$ 22.9	\$ 0.0	\$ 22.9	\$ 0.0

Table of Contents

	Fair Value Measurements at Reporting Date Using			
	Balance at October 2, 2011	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Short-term investments:				
Available-for-sale securities				
Agency obligations	\$ 20.0	\$ 0.0	\$ 20.0	\$ 0.0
Commercial paper	87.0	0.0	87.0	0.0
Corporate debt securities	78.0	0.0	78.0	0.0
Government treasury securities	606.0	606.0	0.0	0.0
Certificates of deposit	64.0	0.0	64.0	0.0
Total available-for-sale securities	855.0	606.0	249.0	0.0
Trading securities	47.6	47.6	0.0	0.0
Total short-term investments	902.6	653.6	249.0	0.0
Long-term investments:				
Corporate debt securities	67.0	0.0	67.0	0.0
State and local government obligations	28.0	0.0	0.0	28.0