

Fitch Rates Starbucks' Proposed \$750MM Notes Issuance 'A-'

Written by Australian Business

CHICAGO--([BUSINESS WIRE](#))--Fitch Ratings has assigned an 'A-' rating to Starbucks Corporation's (Starbucks) (NASDAQ:SBUX) proposed \$750 million aggregate issuance of fixed-rate three-year and five-year senior unsecured notes. The Rating Outlook is Stable. At Sept. 29, 2013, Starbucks had approximately \$1.3 billion of total debt.

The notes will be issued under Starbucks' Aug. 23, 2007 indenture and will rank equally with Starbucks' existing senior unsecured debt. Terms include a change of control triggering event provision. Proceeds will be used for general corporate purposes, including helping to fund Starbucks' \$2.8 billion settlement with Kraft Foods Global, Inc. (KRAFT).

Key Rating Drivers:

Low Financial Leverage

For the LTM period ending Sept. 29, 2013, total debt-to-operating EBITDA and total adjusted debt-to-operating EBITDAR (or rent-adjusted leverage by capitalizing leases at 8x gross rents) were 0.4x and 2.2x, respectively. Operating EBITDAR-to-gross interest expense plus gross rents was 4.2x and funds from operations (FFO) fixed-charge coverage was 3.9x. Starbucks' total debt pro forma for the above mentioned debt issuance is \$2.1 billion. Pro forma total debt-to-operating EBITDA is 0.7x and rent-adjusted leverage is 2.4x.

Ratings reflect Fitch's expectations that Starbucks will maintain rent-adjusted leverage in the low 2.0x range over the near- to intermediate-term due to its strong operating EBITDA and cash flow from operations growth. Starbucks' capital structure framework is guided by its desire to maintain an 'A-' credit rating.

Significant and Growing Cash Flow

Cash flow from operations has grown at an 18% compound annual growth rate since

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2008 to \$2.9 billion in 2013, exceeding Fitch's expectations. Annual free cash flow (FCF - defined as cash flow from operations less capital expenditures and dividends) has averaged \$752 million over the same period. Starbucks' cash flow priorities include investing in the business and returning cash to shareholders via dividends and share buybacks. The firm is targeting a dividend payout of 35%-45% and share repurchases will be mainly opportunistic.

Strong Operating Performance

Starbucks' record operating performance is being driven by mid-single digit same store sales (SSS) growth, new unit development, channel development, and a favorable coffee cost environment. Fitch views Starbucks' long-term annual revenue growth target of at least 10% as achievable, given multiple platforms for growth. Global SSS have increased 6% or more for 15 consecutive quarters, due to transaction growth and modest increases in average check, and net new unit development is progressing at a mid-single-digit rate or higher.

During fiscal 2013, revenue grew 12% to \$14.9 billion and consolidated operating income, excluding the \$2.8 billion litigation charge associated with the Kraft Foods Group, Inc. settlement, increased approximately 25% to \$2.5 billion. Consolidated operating margin expanded to 16.5% from approximately 15% in 2012. Results were the by-product of 7% global SSS growth, new unit development, and lower commodity coffee prices which will continue to benefit the company in fiscal 2014.

Market Leadership, Brand Equity

With 19,767 units globally at Sept. 29, 2013, Starbucks is a leader in the U.S. restaurant industry and the fast-growing U.S. beverage-snack category. Starbucks' well-respected brand, additional food, tea and juice sales layers, and ability to engage customers with its rewards program and mobile payment systems should help sustain SSS growth. Moreover, expanding points of distribution via grocery and other retail outlets is additive to sales and helps strengthen Starbucks' overall brand equity and customer loyalty.

Liquidity and Debt Structure

Starbucks' liquidity is supported by its good cash flow generation and ready access to capital markets. At Sept. 29, 2013, liquidity totaled \$3.3 billion. Starbucks had approximately \$2.6 billion of cash and equivalents, of which a significant portion will be used to fund the firm's settlement with Kraft. Starbucks also had \$729 million of availability, excluding \$21 million of letters of credit, under a committed \$750 million revolver that serves as backup for commercial paper and expires Feb. 5, 2018.

The firm's financial flexibility is complemented by a \$729 million borrowing limit under its \$1 billion commercial paper program. At Sept. 29, 2013, there was no CP outstanding. Upcoming maturities are limited to \$550 million 6.25% notes due Aug. 15, 2017 and \$750 million 3.85% notes due Oct. 1, 2023.

Ratings Sensitivities

Future developments that may, individually or collectively, lead to a positive rating action include:

--An upgrade of Starbucks' ratings is not anticipated in the near- to intermediate-term due to significant levels of off-balance-sheet lease obligations and the potential for additional debt issuances over the intermediate term.

Future developments that may, individually or collectively, lead to a negative rating action include:

--Rent-adjusted leverage sustained at the mid-2.0x or higher level as a result of higher debt and a weakening of operating trends would trigger a downgrade. SSS declines, margin contraction, and materially lower FCF would be viewed negatively.

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Fitch currently rates Starbucks' debt as follows:

--Long-term Issuer Default rating (IDR) 'A-';

--Bank Credit facility 'A-';

--6.25% Senior Unsecured Notes 'A-';

--Short-term IDR 'F2';

--Commercial Paper 'F2'.

The Rating Outlook is Stable.

Additional information is available at 'www.fitchratings.com'.

Applicable Criteria and Related Research:

--'Corporate Rating Methodology' (Aug. 5 2013);

--'2014 Outlook: U.S. Restaurants - Shareholder Demands to Rise, Even as Market Share Battle and Cost Pressures Continue (Dec. 2, 2013).

Applicable Criteria and Related Research:

Corporate Rating Methodology: Including Short-Term Ratings and Parent and Subsidiary Linkage

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=715139

Additional Disclosure

Solicitation Status

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