

All the coffee in China

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Starbucks is taking another major step forward in its march to dominate the Chinese coffee market by stepping up coffee bean cultivation efforts in Yunnan Province.

The American coffee company plans on enlarging its bean cultivating operations in Baoshan, Yunnan Province in 2010 in order to supply its nearly 700 stores in China, the company said Thursday.

"Ultimately I'd love to see our coffee from China feature on the shelves of every one of our stores in 49 countries around the world," Martin Coles, president of Starbucks International, said in January when the company launched its Yunnan-grown "South of the Clouds" bean line.

The company spent almost three years conducting investigations and tests on the Yunnan beans before it decided to make them available for their stores. The beans will be grown in Yunnan and then shipped to America or the Netherlands to be roasted before being shipped back to China. The company said that it has no plans to set up a bean roasting facility anytime in the near future. China has become a more important market for Starbucks over recent years, and the company's domestic profits doubled in 2009 over the previous fiscal year, and the coffee giant expects that the country could support as many as 10,000 stores, equal to the number currently operating in the US.

Problems in Shangri-la

Baoshan is located in a remote part of China's Southwest also known as Shangri-la, surrounded by mountains and the Salween and Mekong Rivers. Patrick Chovanec, a professor at Tsinghua University's School of Economics and Management, wrote on his blog after the announcement that "[t]he challenge facing Shangri-La, as always, is transportation."

However, Starbucks said that the region is seeing large trade infrastructure development due to its proximity to Myanmar and Vietnam and already boasts an airport capable of supporting airplanes as large as Boeing 737s.

Not everyone is positive on Starbucks' growth prospects in China. When Wang Jinlong, the company's head for the Greater China region, said that China will be Starbucks' number two market after the United States, critics balked at the proposition.

Daniel Gross wrote in Slate magazine that Starbucks has struggled to "foist American-style consumerism on to China's rising masses" who have "no coffee culture to speak of." But Gross' critics seem to be ignoring one of the key factors to Starbucks' success so far in the Middle Kingdom: it's not about the coffee. When the company opened its first shop in China in 1999, it focused on making itself more than a place to buy coffee and rather built spacious cafes where people could stay for long periods of time.

From the beginning CEO Howard Schultz has promoted "the idea of Starbucks becoming the third place between home and work in [Asian] countries." According to the company's research, 90 percent of people who order food or beverages stay on the premises to consume them. Only 20 percent of Americans going to Starbucks do the same. And drinking coffee is not even one of the top five reasons why Chinese go to Starbucks (It's No. 6). After surveying customers, Starbucks China discovered that the main reason people go to their shops is to have a place to hang out.

And Kristin Graham, former financial analyst for The Motley Fool, also opined the company would have trouble expanding in China due to the fact "that Starbucks in China may be a daily ritual for expats, but not locals." This has remained a common misperception among people looking at the company, even experts who, like Graham, are based in China.

Research from the University of Florida showed that locals had already eclipsed foreigners in Shanghai Starbucks four years ago. Non-Chinese only accounted for around 40 percent of total customers in several branches located in areas of Shanghai with heavy concentrations of expats.

Li Jing, a communications manager with Starbucks Corporation in Shanghai, confirmed the University of Florida's findings, saying that expats were the company's mainstay when branches first opened up, but locals now make up the majority of their customers around the country.

She declined to give exact figures but was confident that the proportion of Chinese going to Starbucks would continue to grow.

Tea country

Graham's and Gross's criticisms are nothing new for Starbucks in China. When the company first declared it would move into the market, analysts were skeptical that Chinese, steeped in millennia of tea culture, would be unlikely to embrace coffee.

After several years of testing and market research, Starbucks came out with a multi-pronged attack that built on Schultz's idea of creating "third places" that would give Chinese consumers a spot to relax and meet up with friends away from home and work.

Thanks to its real estate know-how and analyses of pedestrian traffic flows, Starbucks has been able to open up branches in the best locations where its most likely customers live and work.

And Starbucks in China has also benefited from the burgeoning Chinese middle class' propensity towards conspicuous consumption. To many Chinese, Starbucks appears as a somewhat upscale coffee chain where well-off hipsters go to hang out.

"To be perfectly honest," said Zhang Liang, a frequent Starbucks-goer in Beijing, "I like to go to Starbucks simply because it's a cool place to be. I'm not actually a huge fan of the coffee."

As long as Starbucks can continue to bring in people like Zhang, its China gamble most likely will pay off no matter where the beans are coming from.

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