

Last Price	Fair Value Estimate	Price/FVE	Market Cap	Economic Moat™	Equity Style Box	Uncertainty	Capital Allocation	ESG Risk Rating Assessment¹
84.17 USD	87.00 USD	0.97	95.90 USD Bil	Wide	Large Value	Medium	Exemplary	
29 Oct 2025	11 Feb 2025 21:39, UTC		30 Oct 2025					3 Sep 2025 05:00, UTC

Fair Value: 87.00
11 Feb 2025 21:39, UTC

Last Close: 84.17

Overvalued
Undervalued

Year	YTD	Price/Fair Value	Total Return %
2020	1.07	23.59	
2021	1.07	11.06	
2022	0.94	-13.48	
2023	0.91	-1.04	
2024	1.06	-2.54	
YTD	0.97	-5.75	

Morningstar Rating

★★★★★
★★★★
★★★
★★
★

MORNINGSTAR

Starbucks Corp SBUX ★★★

29 Oct 2025 21:31, UTC

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Sector	Industry
Consumer Cyclical	Restaurants

Business Description

Starbucks is one of the most widely recognized restaurant brands in the world, operating more than 40,000 stores across more than 80 countries at the end of March 2025. The firm operates in three segments: North America, international markets, and channel development (grocery and ready-to-drink beverage). The coffee chain generates revenue from company-operated stores, royalties, sales of equipment and products to license partners, ready-to-drink beverages, packaged coffee sales, and single-serve products.

in the near future, in addition to developing new stores that cost less to build. Internationally, we expect the firm to open more regular and flagship stores to drive growth.

- Despite ongoing challenges, we expect a sharper consumer focus to reinforce Starbucks' brand strength and fuel a traffic recovery in the medium term. This, coupled with better investment discipline and cost savings, should drive low-teens operating profit growth annually.

Business Strategy & Outlook Dan Su, CFA, Equity Analyst, 4 Aug 2025

Starbucks' business strategy will likely change materially, consistent with new CEO Brian Niccol's "Back to Starbucks" plan. The firm continues to play in a global category of one, with its \$36 billion in 2024 revenue outpacing its closest global competitor, Inspire Brands' Dunkin', by a factor of 3 globally and by a factor of 2 in the firm's home US market. Recent strategic missteps, however, have stalled the firm's momentum, with global comparable store sales declining 2% in fiscal 2024 due to consumer price sensitivity, macroeconomic weakness, and a deteriorating value perception. Traffic fell by a brutal 10% in its core North American markets in the fourth quarter of 2024, but the decline narrowed to low single digits by the third quarter of 2025.

The firm's new approach involves upfront investments in store renovation, labor hours, brand marketing, and everyday value in menu price architecture, although it prudently slowed deployment of costly automated equipment. Porting successful ideas from his time at Taco Bell and at wide-moat Chipotle, Niccol's emphasis appears to center on providing guests with quality, handcrafted, coffee-forward products, to recapture the firm's third-place attraction and simultaneously eliminate operational bottlenecks that had resulted in order delays during peak hours. Under the new plan, menu pricing and product assortment will be simplified, the brand will be marketed outside of its Starbucks Rewards customer base, and brand-dilutive discounts and promotions will be quickly eliminated.

The approach is the right one for this current moment in Starbucks' history, given that issues appear to run deeper than we'd initially contemplated. To fund the required capital and operational investment, Starbucks plans to redeploy savings from its supply chain initiatives, savings from the wind down of promotional activity, and capital conserved by slowing its store expansion in 2025. On balance, we expect substantial near-term pain for the brand, followed by more defensible traffic-led growth as initiatives take hold.

Bulls Say Dan Su, CFA, Equity Analyst, 4 Aug 2025

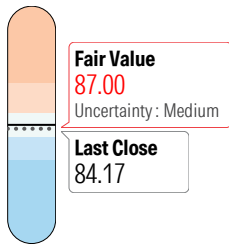
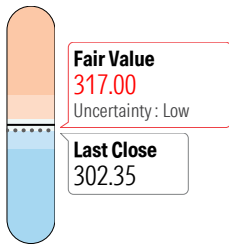
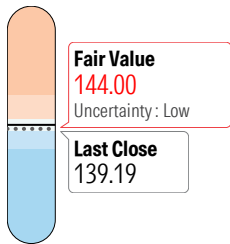
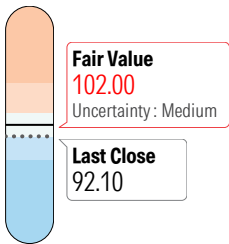
- Starbucks' "Connect" initiative should drive continued adoption of the firm's loyalty program, materially increasing customer lifetime value and helping drive new user acquisition.
- An emphasis on throughput and providing value for customers on every purchase occasion could drive defensible transaction share gains in a competitive global coffee category.
- Starbucks' scale-driven cost advantage should defend its return profile even as it invests heavily to turn

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Competitors

	Starbucks Corp SBUX	McDonald's Corp MCD	Yum Brands Inc YUM	Restaurant Bra...ernational Inc QSR
				
Economic Moat	Wide	Wide	Wide	Narrow
Currency	USD	USD	USD	CAD
Fair Value	87.00 11 Feb 2025 21:39, UTC	317.00 4 Sep 2025 19:59, UTC	144.00 19 Aug 2025 13:34, UTC	102.00 21 Aug 2025 17:39, UTC
1-Star Price	117.45	396.25	180.00	137.70
5-Star Price	60.90	253.60	115.20	71.40
Assessment	Fairly Valued 29 Oct 2025	Fairly Valued 29 Oct 2025	Fairly Valued 29 Oct 2025	Fairly Valued 29 Oct 2025
Morningstar Rating	★★★ 29 Oct 2025 21:31, UTC	★★★ 29 Oct 2025 21:26, UTC	★★★ 29 Oct 2025 21:31, UTC	★★★ 29 Oct 2025 22:16, UTC
Analyst	Dan Su, Equity Analyst	Kristoffer Inton, Senior Equity Analyst	David Swartz, Senior Equity Analyst	David Swartz, Senior Equity Analyst
Capital Allocation	Exemplary	Standard	Standard	Standard
Price/Fair Value	0.97	0.95	0.97	0.90
Price/Sales	2.58	8.34	4.98	3.30
Price/Book	—	—	—	6.65
Price/Earning	38.09	25.28	27.81	21.74
Dividend Yield	2.90%	2.34%	2.01%	3.71%
Market Cap	95.68 Bil	215.76 Bil	38.63 Bil	30.19 Bil
52-Week Range	75.50—117.46	276.53—326.32	122.13—163.30	83.32—101.52
Investment Style	Large Value	Large Value	Mid Blend	Large Blend

around its struggling business.

Bears Say Dan Su, CFA, Equity Analyst, 4 Aug 2025

- Challenges attracting lapsed customers could diminish the expected return on investment for Brian Niccol's "Back to Starbucks" strategic initiative.
- We expect substantially softer—if still attractive—cash on cash returns in China moving forward rather than the 50%-70% that Starbucks has historically enjoyed, as competition in that country remains extreme.
- Shrinking arabica growing regions could drive structurally higher green coffee prices, threatening gross margins (if swallowed by Starbucks) or driving consumer switching toward cheaper caffeinated alternatives.

Economic Moat Dan Su, CFA, Equity Analyst, 10 Jun 2025

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Low barriers to entry and minimal switching costs render the restaurant industry very competitive, making it difficult for most operators to develop an economic moat. In our view, firms that are able to do so generally lean into a brand intangible asset or a scale-driven cost advantage, with those sources often arising in tandem. While brand intangible assets are often difficult to definitively quantify, we assess brands based on their ability to generate comparable store sales growth (price, mix, and traffic) in excess of category inflation, carry a banner to international markets, and create value for franchisees where relevant, while cost advantages often materialize through lower general and administrative costs as a percentage of systemwide sales and superior restaurant-level margins.

In our view, Starbucks is one of the few operators in our coverage that boasts a wide economic moat, with brand strength—evidenced by pricing power, attractive unit-level economics, successful international replication, and strong results in the retail channel underpinning a durable brand intangible asset. The firm's ability to generate excitement and traffic, evidenced by impressive comparable sales growth in the core US market, while spending less on marketing than category peers, reinforces the importance of the brand and its impact on results. Moreover, though we view it as a secondary moat source, we also believe that Starbucks benefits from an durable cost advantage, with its global scale allowing it to procure commoditized food and paper items at favorable prices. The firm's scale allows it to leverage technology spending across a larger store base, generating efficiency improvements and cost savings through automated inventory management, scheduling, and a robust omnichannel ordering platform, while a strong loyalty program increases its affinity with core customers. Our wide moat rating implies the assumption that the firm can continue to earn positive economic returns for the next 20 years—a view embodied by our 10-year forecast adjusted ROICs of 25%, healthily outstripping our WACC estimate of 8.3%.

Considering the firm's brand intangible asset, we highlight five points that would suggest a strong brand—the firm's pricing power, restaurant-level profitability, successful international replication, strength in the retail channel, and lower marketing spending relative to peers. Starbucks' position as a premium vendor of coffee, tea, and refresher beverages is widely recognized, as it has historically managed its positioning to avoid finding itself caught between discount competitors like Dunkin' and McDonald's McCafé platform on the low end and specialty independent shops on the high end of the market. Strong increases in average check, up 8.2% per year in the US market over the last five years, attest to the firm's ability to continue to push menu price increases, larger drink sizes, and premium customized beverages without alienating customers (exempting a brutal fiscal 2024). Modifiers like an extra pump of syrup or shot of espresso have purportedly grown to a \$1 billion platform on their own, to this effect. Further, a US average ticket of \$8.99 in 2023, based on Morningstar estimates and Euromonitor data, comfortably outpaced peers like Dunkin' (\$4.39), Tim Hortons (\$5.16), and Caribou (\$6.88), corroborating our thesis. While pricing power is generally less pronounced in the grocery channel, we note that narrow-moat Kroger's management has identified Starbucks' packaged coffee

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and other premium offerings as bellwethers for consumer health in the past, implying that the firm operates at higher price points than other category players, such as Folgers, Maxwell House, and JDE Peet's.

Pivoting to unit economics, Starbucks' cash-on-cash returns offer one of the highest returns on investment in our coverage for franchisees, with management historically estimating 50% cash-on-cash returns in the US and close to 70% in China (though closer to 50% in China today). The firm's restaurant margins oscillate meaningfully, but with median North America restaurant margins in the midteens over the past five years and with average unit sales north of \$2.2 million at company-owned stores, we back into roughly \$370,000 in average restaurant-level operating profit at midcycle margins—and considering competitive buildout costs (probably around \$1 million), given the lack of a full kitchenette at the coffee chain's units, we believe that management's historical estimates are in the appropriate ballpark. We'd estimate a payback figure just shy of three years in the US today, which stacks up remarkably against a QSR industry average of 4-6 years, suggesting that multibrand license partners are more likely to funnel discretionary capital into new Starbucks units than competitive brands with a lower ROI, and generally permits that Starbucks is able to seek out the most reputable and best capitalized license partners in the markets in which it operates—an important undertaking as the firm seeks to maintain its premium positioning and global brand cachet.

Turning to that global positioning, we view international replication as another pillar of our restaurant intangible asset framework, with strong international uptake and concept portability indicating brand recognition, strength, and product quality. Starbucks operated or licensed more than 21,700 international stores at the end of fiscal 2024, featuring operations in more than 80 global markets. The brand's reach is matched only by McDonald's and KFC among chained restaurants worldwide, and potential expansion through the global coffee alliance partnership with wide-moat Nestlé could result in further international opportunities as the consumer packaged goods behemoth has a 190-country footprint. Considering this channel, we appreciate Starbucks' ability to amplify its brand with premium offerings such as packaged coffees, ready-to-drink beverages, single-serve products such Nespresso pods, instant coffee, and a variety of related items. While the firm has recently seen sales pressure in those channels as competition has extended into the grocery aisle, we continue to take a positive view of Starbucks' position, and believe that the firm's long-standing bottling partnership with PepsiCo increases its distribution and manufacturing capability, while the global coffee alliance joint venture has allowed Starbucks to quickly expand into new international markets by leveraging the European firm's unrivaled network of distribution touch points globally. With distribution and shelf space representing the biggest bottlenecks in the grocery channel, we believe that Nestlé's entrenched distribution relationships, role as a channel captain, and ability to operate with lower costs as it delivers larger case sizes to retail partners (due to cross-selling) are extremely attractive, while premium shelf placement should see inventories turn faster and in turn become more alluring to retail partners.

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Finally, while lower marketing costs as a percentage of sales (averaging 1.1% of sales over the last five years, relative to McDonald's 4% marketing royalty rate and Dunkin's 5%) could be construed as a cost advantage, we believe that it more accurately reflects brand strength, as Starbucks has been able to generate buzz and sales volume despite a tighter marketing budget—corroborating our thesis that the firm's cost advantage is a secondary moat source, subordinate to the strength of its brand intangible asset. As a separate proof point of lesser maintenance marketing requirements, Starbucks disclosed that discounted sales comprised 14% of total revenue during the third fiscal quarter of 2024, against an industry average of 29% during the period. Moving forward, we'd expect the firm's marketing outlay to increase modestly and its promotional activity to decline, consistent with recently appointed CEO Brian Niccol's "Back to Starbucks" strategic plan—but not to the extent that this gap to industry average spending is completely erased.

While brand intangibles are undoubtedly the firm's stronger moat source, we believe that Starbucks features a durable and stand-alone cost advantage, with the company's global scale and strong unit volumes allowing it to benefit from procurement discounts, while strong systemwide sales provide natural operating leverage over fixed investments in technology and product research and development. With revenue of \$29.8 billion through company-owned stores around the world in fiscal 2024 (and an undisclosed amount through more than 19,100 licensed stores), Starbucks is one of the largest global restaurant chains, with systemwide sales likely falling somewhere between Restaurant Brands International and Yum Brands. Only McDonald's, with more than \$131 billion in 2024 systemwide sales handily outpaces Starbucks' global reach. As a result, we believe that centralized purchasing allows the firm to take advantage of volume discounts on everything from Mastrena espresso machines to commoditized staples like milk, eggs, syrups, and pastry items, which are subsequently distributed across the company-operated and licensed footprint. We believe that higher unit volumes and proportionately larger drop sizes lower the cost of servicing Starbucks' stores, allowing the firm to benefit from volume discounts with food distributors and underpinning a durable cost advantage in a category that derives more than one third of sales from independent restaurants. As a final proof point, we consider our estimated \$3.8 billion of capital expenditures per year through 2027, against a backdrop that has seen sluggish restaurant traffic and persistent margin pressure—an attestation, in our view, that Starbucks' scale permits investments in moat-accretive investment opportunities through the cycle, ossifying the firm's position as the global category leader during a period in which peers are widely pulling back on nonessential spending.

Further, Starbucks' scale allows the firm to leverage large technological investments across the store footprint, with a recent focus on artificial intelligence-driven efficiency, yielding a new cold beverage station, a plug-and-play cloud-deployed retail technology stack for US licensed partners, and new equipment for brewing hot and cold brew coffees. Other technological investments, including omnichannel ordering capabilities and the expansion of the firm's loyalty program have proven fruitful,

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with more than 34 million active members in the US utilizing the loyalty program and driving roughly 60% of North American sales volume. The firm believes that loyalty program members spend as much as 2-3 times that of non-loyalty program participants, and storing ordering data on a proprietary platform affords the firm an invaluable database of popular item pairings, promotion efficacy, and even ordering tendencies across geographies, dayparts, and weather patterns. With an estimated domestic customer base in the neighborhood of 75 million (implying penetration of more than 40%), we believe that Starbucks has one of the most widely adopted platforms in our coverage and see strong upside in China and the Asia-Pacific region, where technology savvy customers have more widely embraced mobile order and payment options.

The importance of these technological investments is difficult to overstate. Targeted promotional activity allows the firm to charge consumers different prices without cheapening the brand, while limited-time offers and promotional activity can help drive volumes across dayparts and toward underutilized days of the week or times of day. Marketing campaigns can be measured, adjusted, and deployed in real time, while consumer ordering preferences can quickly offer insights into popular menu categories that garner line extensions and further attention. Proximity to and relationship with customers represents one of the key links in the food-service value chain that cannot be commoditized, and a heightened attention to shifting demand—few would have foreseen cold drinks representing nearly three quarters of the beverage mix, for example—offers a tremendous competitive edge.

Fair Value and Profit Drivers Dan Su, CFA, Equity Analyst, 4 Aug 2025

We are maintaining our fair value estimate at \$87 after digesting the results from the third quarter of fiscal 2025. Sales rose 4%, as global comp store sales decline of 2% was more than offset by store expansion. Operating profits dropped 38% as margins fell 680 basis points to 9.9%. Even as consumer belt-tightening in the core US market continued to pressure transactions (down 4%), the firm remains steadfast in its investments in in-store service, innovation and marketing to reinforce consumer connection for the longer term. Its customer service commitment is evidenced by the decision to roll out the Green Apron Service nationwide this August to boost barista hospitality. We expect part of the \$500 million in labor hours budgeted for this project over the next year will be funded by cost savings. The 2% comp sales lift in China improved sequentially from flat, which we attribute to effective digital marketing and successful zero-sugar offerings. This should boost the firm's position as it continues to screen for local partners to drive store base expansion in the coming years. We expect the coffee chain to refrain from price increases in the coming quarters, but to leverage zero-based budgeting, procurement savings, and productivity initiatives to offset green coffee cost inflation and higher store investments.

We maintain our 3.5% sales growth forecast for fiscal 2025, largely driven by net new stores, with comparable sales performance likely to remain muted as the firm tweaks its menu price architecture to

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provide better value for guests amid weak store traffic trends. Our EPS estimate for 2025 comes down to \$2.73 from \$2.76 as we incorporate slightly higher expenses.

Longer term, the company's prospects look salient. Still, the firm will find it challenging to reverse declining traffic trends, and we don't view its current slate of initiatives as likely to buck industry traffic trends for a few quarters. The ability to invest through the cycle distinguishes Starbucks from smaller peers as the firm should be able to drive growth in systemwide sales despite material pressure on store-level sales, setting it up for long-term market share capture.

Key sensitivities, consistent with the remainder of our restaurant coverage, include growth in transaction volume, price increases, and new unit openings on the top line, with cost inflation, operating leverage, and tenancy costs playing into operating margins.

Our model includes 8% average annual top-line growth through 2034, with adjusted EPS growing at a 14% annual clip. Growth in the more mature North America segment favors comparable store sales, with 4.2% annual comparable sales growth outpacing 2.2% projected unit growth over that period. We expect the international segment, heavily skewed toward China, to generate 14% annual revenue growth, driven primarily by new unit openings (8%) as Starbucks continues to expand its reach into those markets.

Our forecast sees Starbucks continue to outgrow the global coffee market, reaching its goal of 55,000 stores in 2030 (in line with its 2020 investor day forecast). We view expectations for long-term market share gains as justified on a global basis, considering both the firm's historical dominance in the global coffee category, market share gains over the last 10 years and its ability to continue to invest through the cycle against a backdrop where the lion's share of its peers are pulling back on nonessential investments.

On the cost side, we forecast substantial gross margin expansion through 2034 (improving 190 basis points from 2024) as restaurant margins approach prepandemic levels over the next few years. Our 2034 non-GAAP operating margin estimate of 15.9% also hangs on modest leverage over overhead expenses and wages, with a slight skew toward proportionately headcount-light international markets.

Risk and Uncertainty Dan Su, CFA, Equity Analyst, 4 Aug 2025

We assign Starbucks a Medium Uncertainty Rating. The firm remains sensitive to consumer caution, particularly at the lower end of the income spectrum (as seen in 2007-09), but its position as an affordable luxury may insulate it from minor downturns. Other key uncertainties include input cost inflation and operational risks.

Wage inflation remains a concern, with the firm raising its partner wages to an average of \$17 per hour in the summer of 2022. The pace of change remains unprecedented—Starbucks' announcement of \$15

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average wages in 2020 was a landmark event just four years ago—and the labor market remains relatively tight across the restaurant industry. Broader traction of unionization efforts remains a tail-end risk, with the firm continuing to negotiate a union contract with approximately 500 of its domestic stores—a mid-single-digit percentage of its company-owned footprint in the US. Elsewhere, eyes turn to California, where legislators mandated a \$20 minimum wage in the restaurant space effective in April 2024—perhaps a harbinger of similar changes in more politically liberal states like Oregon and Illinois.

Further, we view execution risks as substantial, with the firm remaining in the early innings of CEO Brian Niccol's "Back to Starbucks" strategic plan. Market prices suggest a return to high-single-digit revenue growth, and our own cash flow projections hang on the firm's ability to drive traffic back into its stores after an extremely challenging fiscal 2024.

On environmental, social, and governance risks, the procurement of green coffee is the firm's largest sensitivity (albeit a long-term one) in our view, with climate change threatening sensitive arabica coffee growing regions. The firm will need to continue to invest in farmer education in new regions as climate conditions evolve, and green coffee prices may increase in the long term as a result (historically about 10% of the firm's cost of sales).

Capital Allocation Dan Su, CFA, Equity Analyst, 4 Aug 2025

We assess Starbucks' Morningstar Capital Allocation Rating as Exemplary, with a sound balance sheet, strong investment strategy, and appropriate shareholder distributions properly aligned with the firm's strategy and core competencies. We maintain this rating despite the firm's current spell of pressure, with the firm's "Back to Starbucks" plan setting the stage for a return to defensible, transaction-led growth.

Our sound balance sheet rating is underpinned by a manageable debt load, with our forecasts calling for the firm to remain below its prudent long-term lease adjusted debt/EBITDAR target of less than 3 turns in every forecast year but fiscal 2025 (3.3 turns during an investment cycle). Concerns are further alleviated by a highly free cash flow generative business model, with our estimates calling for average annual free cash flow to the firm to average 7% to 8% of sales over the next five years, affording Starbucks a substantial degree of investment flexibility.

Considering the firm's investment decisions, we have assigned management an Exemplary rating, with moat-accretive investments like Starbucks connect, proprietary brewing systems, and streamlined cold beverage stations helping the firm adapt to changing customer demands, increasing average unit volumes, and potentially allowing partners to spend more time engaging in customer-facing activities. While the firm's struggles to defend its customer value perception and provide attractive in-store and digital order experiences simultaneously have resulted in recent traffic weakness, we believe that CEO Brian Niccol's remedial measures outlined in his "Back to Starbucks" plan look like the appropriate, if painful remedy. Sensible limits to digital order customization, a more streamlined menu that favors the

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coffee-forward beverage core, a more separate store experience for different customer groups, and consistent fulfillment times should address most of the customer complaints we've heard during recent challenging quarters. Our view is supported by a generally positive returns on invested capital trajectory.

While we award Starbucks an excellent investment rating in aggregate, we do note that management's acquisition record is spotty, with Teavana, Evolution Fresh, and recently divested Seattle's Best struggling to gain traction. The firm paid \$620 million for Teavana in 2012, later shuttering the brand's nearly 400 brick-and-mortar outlets, with Evolution Fresh (\$50 million, four stores) and Seattle's Best (\$72 million) representing much smaller financial outlays.

Finally, we take a positive stance toward management's newfound openness to pursuing a strategic partnership in the China market. To be clear, we remain believers in that market's long-term prospects, with the firm generating self-reported 50% cash-on-cash returns despite absolutely brutal declines in store-level sales--a strong return on invested capital. Nevertheless, as seen with wide-moat Yum China and with wide-moat McDonald's CITIC partnership, a license partner can substantially reduce operating profit volatility while accelerating store development, addressing a core market concern and potentially slowing or even reversing recent market share losses. We believe that this could would be a positive move both from a return on capital perspective and from a shareholder return perspective if structured appropriately.

Last, we believe that shareholder distributions are appropriate, with management intending to split free cash flow between capital expenditures, dividends, and share buybacks. With our forecast for average net new unit growth of nearly 6% per year through 2034, we believe that Starbucks is striking a good balance between establishing critical mass in new markets and maintaining the proper corporate and supply chain resources to ensure their success. Given low build-out costs due to the lack of a conventional kitchen, Starbucks can maintain strong unit growth without compromising on store remodeling or technological investments, all within a capital expenditure budget in the mid to high-single-digit percentage of sales. Our forecast anticipates shareholder returns of \$22.2 billion over the next five years, with a projected dividend payout ratio of 55% in the long run.

Analyst Notes Archive

Starbucks Earnings: Focus on Services and Cost-Cutting to Fuel Turnaround; Shares Not Cheap
Dan Su, CFA,Equity Analyst,30 Jul 2025

Starbucks' sales grew by 4% in the third quarter of fiscal 2025 as a global comparable store sales decline of 2% was more than offset by store expansion. Operating profit dropped 38% as operating margin fell 680 basis points to 9.9%. Why it matters: Even as consumer belt-tightening in the core US market pressured transactions (down 4%), the firm remains steadfast in its investments in service,

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Starbucks Corp **SBUX** ★★★

29 Oct 2025 21:31, UTC

Last Price	Fair Value Estimate	Price/FVE	Market Cap	Economic Moat™	Equity Style Box	Uncertainty	Capital Allocation	ESG Risk Rating Assessment¹
84.17 USD 29 Oct 2025	87.00 USD 11 Feb 2025 21:39, UTC	0.97	95.90 USD Bil 30 Oct 2025	Wide	Large Value	Medium	Exemplary	3 Sep 2025 05:00, UTC

innovation, and marketing to reinforce long-term consumer connections. Starbucks' customer service commitment is evidenced by the rollout of the Green Apron Service to boost barista hospitality nationwide in August. We expect part of the \$500 million in labor cost budgeted for this project over the next year will be funded by savings. The 2% comparable sales lift in China was a sequential improvement from flat, which we attribute to effective digital marketing and successful zero-sugar offerings. These efforts should boost the firm's position as it screens for local partners to drive store base expansion. The bottom line: We don't plan any material changes to our \$87 per share fair value estimate for wide-moat Starbucks, or to our 10-year forecasts for 8% annual sales growth and a 15% average operating margin, both of which are consistent with the respective averages achieved in the past decade. Following a 4% pop in after-hours trading on July 29, 2025, shares don't strike us as particularly attractive. We'd wait for a better entry point as the stock may come under pressure amid economic or competitive headwinds. Despite ongoing challenges, we expect a sharper focus on consumer engagement will bolster Starbucks' brand strength and fuel a traffic recovery in the midterm, thereby driving low-teens operating profit growth annually. Coming up: We think Starbucks remains on track to expand its store base by 70% over the next decade, from 2024's level (a 6% increase annually), but expect efforts to rightsize the US footprint will slow the pace of expansion in the near term.

Starbucks Earnings: Turnaround in Early Stage as Q2 Disappoints; Shares Slightly Undervalued Dan Su, CFA, Equity Analyst, 30 Apr 2025

Starbucks grew sales by 2% in the second quarter as its global comparable sales decline of 1% was more than offset by store expansion. Adjusted operating margin fell 450 basis points to 8.2%. Why it matters: Despite higher marketing and labor spending, weak traffic drove same-store sales down 2% in the core US market. Flat comp sales in China improved sequentially on more effective brand messaging, but demand headwinds persisted. Management is prudent to focus on staff hospitality and a streamlined consumer experience (including shorter wait times), but we expect Starbucks' planned switch to higher store staffing (versus equipment automation) to achieve its goals will drive choppy profits in the coming quarters. We expect the coffee chain to refrain from price increases in 2025 but to leverage zero-based budgeting, procurement savings, and productivity initiatives to offset green coffee cost inflation and higher store investments. The bottom line: We don't plan any material changes to our \$87 per share fair value estimate for wide-moat Starbucks. Shares look undervalued after a 6% fall in after-hours trading as the market prices in prolonged weakness versus our forecast for comparable sales and margins to rebound in 2026. While we plan to trim our 2025 estimates following two soft quarters, our 10-year forecast for 8% annual sales growth and a 15% average operating margin remains in place. Both metrics are consistent with averages achieved over the past decade. Despite current challenges, we think stepped-up investments in consumer experience should reinforce Starbucks' brand strength and drive a traffic turnaround in the medium term, fueling low-teens annual growth in operating profits. Coming up: We expect Starbucks to slow the pace of store openings and focus instead

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on store renovation and operational enhancement. Over the next decade, however, we think Starbucks remains on track to grow its store base by 70% from 2024, a 6% annual increase.

Starbucks: Cathy Smith Named New Finance Chief; No Change to Our Exemplary Capital Allocation Rating

Dan Su, CFA, Equity Analyst, 4 Mar 2025

Wide-moat Starbucks announced the appointment of Cathy Smith as the new chief financial officer. Smith, who is currently the finance chief at the soon-to-go-private department store chain no-moat Nordstrom, will likely join over the next month. She will replace Rachel Ruggeri, who is leaving the firm after having served as the finance chief since 2021. We are maintaining our \$87 per share fair value estimate, leaving shares rich. While we remain constructive about management's efforts to right the ship, we posit investors are overly optimistic about the firm's near-term recovery amid industrywide traffic challenges, promotional activity, and competition from at-home coffee. We see Smith as a strong finance leader to partner with CEO Brian Niccol and steer the coffee chain through turnaround efforts to revive store traffic growth and reinforce its competitive edge. We expect Smith to leverage her experience as the finance chief at large retail companies including Nordstrom, Target, and Walmart (international division), to help shape and implement investment strategies. Moreover, as Starbucks reviews its growth prospects in international markets, including in China where the firm is rumored to be evaluating refranchising options amid intense local competition, Smith's international experience could prove helpful. We don't expect the new CFO appointment to bring any material changes to Starbucks' long-term growth and capital allocation priorities, and our Exemplary Capital Allocation Rating remains in place. With Brian Niccol at the helm, we expect Starbucks to remain focused on the "Back to Starbucks" plan unveiled in September. The plan aims to provide quality, handcrafted, and coffee-forward products to restore the firm's appeal as a third place, and simultaneously reduce operational complexity. We continue to expect the firm to expend 7% of sales in capital expenditure and another 7% in selling, marketing, and payroll expenses over the 10-year forecast period.

Starbucks Earnings: Initiatives Support Gradual Sequential Traffic Improvement Amid Tough Landscape

David Swartz, Senior Equity Analyst, 29 Jan 2025

Given that wide-moat Starbucks' turnaround is in its early stages amid a challenging restaurant landscape, expectations were tempered going into its fiscal 2025 first-quarter report. Although its sales of \$9.4 billion were flat and exceeded our \$9.3 billion estimate, its earnings per share of \$0.69 fell \$0.03 short. We don't anticipate making a material change to our \$86 fair value estimate, leaving shares as rich. While we remain optimistic about management's efforts to bolster its brand positioning through in-store investments, process improvements, and menu innovation, we posit investors are overly optimistic about the firm's near-term recovery amid industrywide traffic challenges, heightened promotional activity, and competition from the grocery channel. Domestically, Starbucks' 4% comparable sales decline aligned with our expectation as traffic declines sequentially moderated to 8%

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in the quarter (from 10%). We surmise a milder decline was supported by strategic initiatives (like eliminating fees for nondairy milk customizations) following prior challenges in engaging its core consumer base. Additionally, nonloyalty member traffic increased, which we attribute to the early impact of a shift toward external advertising, and discounted transactions declined 40% year over year. We view this shift toward brand positioning over discounting as a prudent strategy that reinforces Starbucks' premium positioning. Alongside efforts to reduce wait times, streamline the menu by eliminating 30% of its offerings, and enhance store environments with renovations (among others), we continue to expect US comparable sales growth to average around 4% over the next decade. In the quarter, growth initiatives pressured profitability, with the operating margin down 380 basis points to 11.9%, below our 12.6% estimate. While investments to maximize efficiency will likely weigh on near-term margin performance, we continue to see expansion to around 18% in 2034 from 15% in 2024.

Starbucks Earnings: We Expect to Lower Fair Value Estimate on Poor Medium-Term Outlook Sean Dunlop, CFA, Director, 31 Oct 2024

Wide-moat Starbucks is headed in the right direction, but it looks like it will take a substantial amount of time and capital to get there. Consistent with the views expressed in our Oct. 22 note after the firm previewed its fourth-quarter earnings, we are disappointed to see that US traffic fell by a striking 10% and expect costly remedial measures as we move into fiscal 2025. We expect to lower our \$95 fair value estimate by a high-single-digit percentage, leaving shares looking slightly expensive as reported results aligned with the earnings preview. While we're encouraged by CEO Brian Niccol's efforts to port best practices from his time at Taco Bell and wide-moat Chipotle to the beleaguered coffee chain, it's challenging not to see those priorities in terms of dollars and cents. During the earnings call, Niccol mentioned an increase in marketing to non-Starbucks Rewards members, store remodels to prioritize the in-cafe experience, the rollout of Clover Vertica machines to all stores by fiscal year-end 2025, an acceleration of the rollout of Siren equipment and processes, an increase in barista hours during peak hours, investments in order sequencing for mobile orders, and a manager conference in 2025. While these will be partially funded by targeted operational savings, the rollback of brand-dilutive and ineffective promotional activity, and a pullback on store development, we envision a large step-up in capital and operating expenditure in the medium term that is unlikely to be offset by comparable-store sales growth for a handful of years. Ultimately, we expect this approach to pay dividends slowly in the form of a return to more maintainable, traffic-led growth by fiscal 2026, but it has become clear that we had underestimated the scope of Starbucks' operational and store estate issues. Consistent with our earlier note, we expect margins to trough in fiscal 2025 around 12% before gradually recovering as stores return to transaction-led growth.

Starbucks: Early Earnings Numbers Are Weak as Traffic Pressure Persists; Shares Fairly Priced Sean Dunlop, CFA, Director, 23 Oct 2024

Starbucks Corp

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29 Oct 2025 21:31, UTC

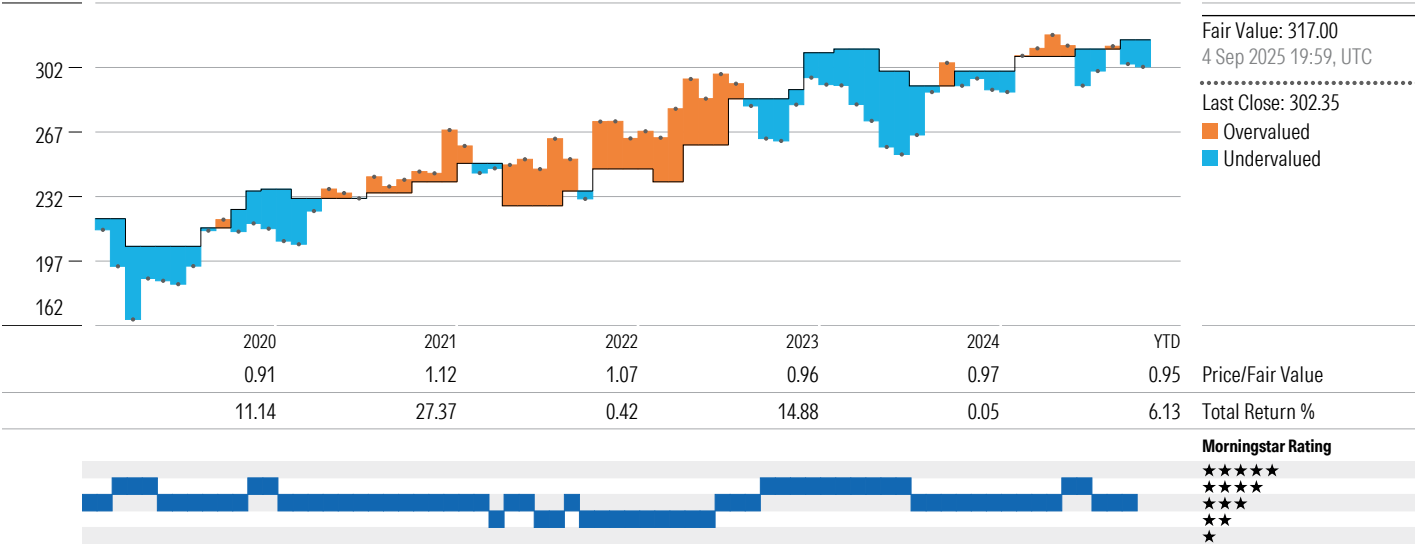
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Wide-moat Starbucks' forgettable year continued with its fiscal fourth-quarter early earnings release. Weak traffic and commensurate margin deleverage saw the firm's \$9.1 billion in sales and \$0.80 in diluted earnings per share fall well short of our \$9.4 billion and \$1.05 per share estimates. Traffic weakness was concerning, with a 10% traffic decline in the US driving the firm's 6% comparable-store sales drop in its flagship market, lagging our expectation for a 3% drawdown. Our key takeaway: the Starbucks brand isn't impaired, but all the fixes outlined in newly christened CEO Brian Niccol's preliminary "Back to Starbucks" plan point in the direction of higher near-term operational and capital investment—and lower near-term earnings power for the largest global coffee restaurateur. Those initiatives look likely to take place against a backdrop of softer than desired consumer spending through the third quarter of calendar 2025 (Starbucks' entire fiscal year), suggesting another tough year awaits. Shares fell 4%-5% on the release, consistent with our anticipated update to our \$96 fair value estimate. We'll be keen to hear Niccol's thoughts on early results and the firm's investment priorities. Still, it looks likely that his blueprint involves an increase in barista hours, a pull-forward of operational investments like the firm's Siren System cold bar, and a re-emphasis on the coffeehouse ambiance that long distinguished the brand experience for guests. Menu simplification and fixing the menu price architecture should prove accretive but also likely to carry immediate costs. We expect to sharpen our pencils on fiscal 2025 growth and margin prospects, now anticipating low-single-digit revenue growth in 2025 (from 5.3%) and the firm's weakest operating margin performance since the covid-19 period in the year to come (down from 14.5%)—although investments look cogent and moat strengthening over the long term. ■■■

Starbucks Corp SBUX ★★★ 29 Oct 2025 21:31, UTC

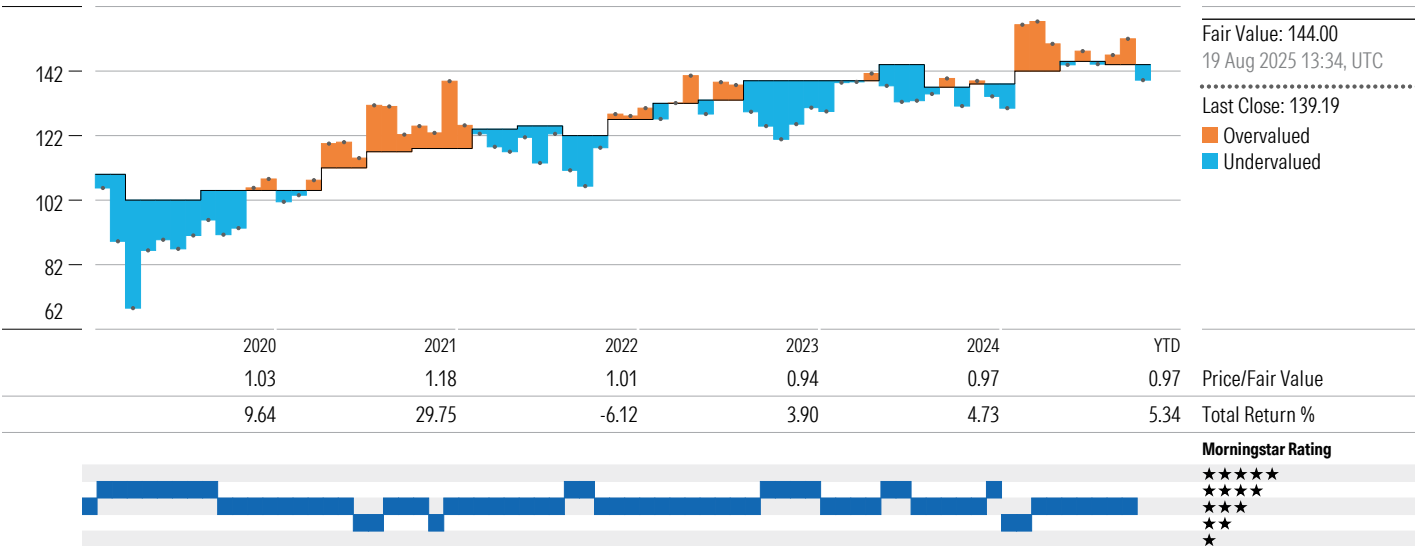
Competitors Price vs. Fair Value

McDonald's Corp MCD



Total Return % as of 29 Oct 2025. Last Close as of 29 Oct 2025. Fair Value as of 4 Sep 2025 19:59, UTC.

Yum Brands Inc YUM



Total Return % as of 29 Oct 2025. Last Close as of 29 Oct 2025. Fair Value as of 19 Aug 2025 13:34, UTC.

Starbucks Corp

SBUX

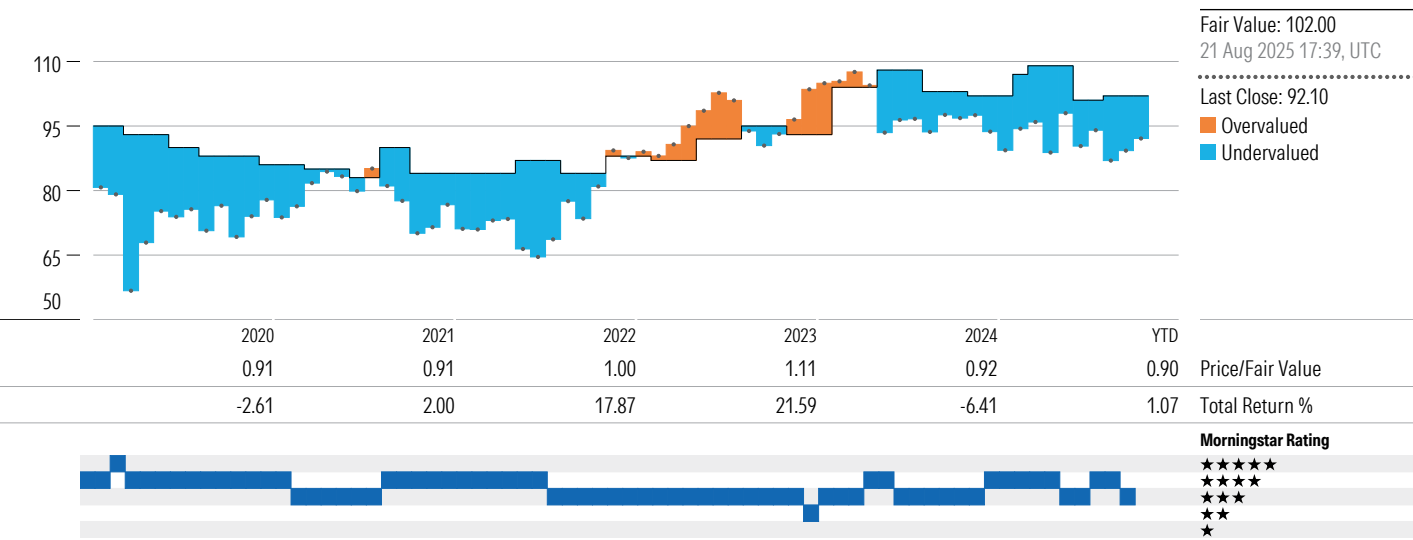
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29 Oct 2025 21:31, UTC

Competitors Price vs. Fair Value

Restaurant Brands International Inc

QSR



Total Return % as of 29 Oct 2025. Last Close as of 29 Oct 2025. Fair Value as of 21 Aug 2025 17:39, UTC.

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Morningstar Valuation Model Summary

Financials as of 01 Aug 2025

Fiscal Year, ends 30 Sep	Actual			Forecast				
	2022	2023	2024	2025	2026	2027	2028	2029
Revenue (USD Mil)	32,250	35,976	36,176	37,433	41,496	46,652	50,567	55,138
Operating Income (USD Mil)	4,430	5,503	5,107	4,020	4,945	6,050	7,094	8,114
EBITDA (USD Mil)	6,147	7,321	7,001	6,115	7,114	8,520	9,814	11,124
Adjusted EBITDA (USD Mil)	6,147	7,321	7,001	6,115	7,114	8,520	9,814	11,124
Net Income (USD Mil)	3,282	5,062	3,762	3,054	3,639	4,469	5,263	6,013
Adjusted Net Income (USD Mil)	3,282	5,062	3,762	3,054	3,639	4,469	5,263	6,013
Free Cash Flow To The Firm (USD Mil)	3,380	5,303	4,726	1,504	2,291	3,300	4,964	5,821
Weighted Average Diluted Shares Outstanding (Mil)	1,159	1,151	1,137	1,119	1,100	1,102	1,073	1,053
Earnings Per Share (Diluted) (USD)	2.83	4.40	3.31	2.73	3.31	4.05	4.91	5.71
Adjusted Earnings Per Share (Diluted) (USD)	2.83	4.40	3.31	2.73	3.31	4.05	4.91	5.71
Dividends Per Share (USD)	1.96	2.16	2.32	2.44	2.25	2.43	2.82	3.14

Margins & Returns as of 01 Aug 2025

	3 Year Avg	Actual			Forecast					5 Year Avg
		2022	2023	2024	2025	2026	2027	2028	2029	
Operating Margin %	15.2	13.7	15.3	14.1	10.7	11.9	13.0	14.0	14.7	13.5
EBITDA Margin %	—	19.1	20.3	19.4	16.3	17.1	18.3	19.4	20.2	—
Adjusted EBITDA Margin %	—	19.1	20.3	19.4	16.3	17.1	18.3	19.4	20.2	18.3
Net Margin %	11.6	10.2	14.1	10.4	8.2	8.8	9.6	10.4	10.9	9.6
Adjusted Net Margin %	11.6	10.2	14.1	10.4	8.2	8.8	9.6	10.4	10.9	9.6
Free Cash Flow To The Firm Margin %	12.8	10.5	14.7	13.1	4.0	5.5	7.1	9.8	10.6	7.4

Growth & Ratios as of 01 Aug 2025

	3 Year CAGR	Actual			Forecast					5 Year CAGR
		2022	2023	2024	2025	2026	2027	2028	2029	
Revenue Growth %	7.6	11.0	11.6	0.6	3.5	10.9	12.4	8.4	9.0	8.8
Operating Income Growth %	3.1	-4.9	24.2	-7.2	-21.3	23.0	22.4	17.3	14.4	9.7
EBITDA Growth %	3.6	-3.9	19.1	-4.4	-12.7	16.4	19.8	15.2	13.4	10.4
Adjusted EBITDA Growth %	3.1	-3.9	19.1	-4.4	-12.7	16.4	19.8	15.2	13.4	9.7
Earnings Per Share Growth %	-2.3	-20.0	55.2	-24.8	-17.5	21.2	22.6	21.0	16.4	11.5
Adjusted Earnings Per Share Growth %	-2.3	-20.0	55.2	-24.8	-17.5	21.2	22.6	21.0	16.4	11.5

Valuation as of 01 Aug 2025

	Actual			Forecast				
	2022	2023	2024	2025	2026	2027	2028	2029
Price/Earning	29.8	20.7	29.5	30.8	25.4	20.8	17.1	14.7
Price/Sales	3.0	2.9	3.1	2.6	2.3	2.1	1.9	1.7
Price/Book	-11.2	-13.2	-14.9	-12.4	-13.3	-14.7	-14.2	-12.2
Price/Cash Flow	—	—	—	—	—	—	—	—
EV/EBITDA	19.1	17.1	18.9	19.5	16.7	14.0	12.1	10.7
EV/EBIT	26.5	22.8	25.9	29.6	24.1	19.7	16.8	14.7
Dividend Yield %	2.3	2.4	2.4	2.9	2.7	2.9	3.4	3.7
Dividend Payout %	69.2	49.1	70.1	89.4	68.0	60.0	57.5	55.0
Free Cash Flow Yield %	—	—	—	—	—	—	—	—

Operating Performance / Profitability as of 01 Aug 2025

Fiscal Year, ends 30 Sep	Actual			Forecast				
	2022	2023	2024	2025	2026	2027	2028	2029
ROA %	11.7	17.2	12.0	9.5	10.1	10.9	11.9	12.7
ROE %	-37.7	-63.4	-50.6	-40.1	-52.2	-71.1	-82.9	-82.8
ROIC %	22.6	27.2	24.5	18.0	19.6	21.6	23.1	24.7

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Financial Leverage (Reporting Currency)

Fiscal Year, ends 30 Sep	Actual			Forecast				
	2022	2023	2024	2025	2026	2027	2028	2029
Debt/Capital %	19.8	19.1	18.9	13.9	14.1	14.6	15.1	15.6
Assets/Equity	-3.2	-3.7	-4.2	-4.2	-5.2	-6.5	-7.0	-6.5
Net Debt/EBITDA	3.4	2.8	3.2	2.3	2.1	1.8	1.6	1.5
Total Debt/EBITDA	3.9	3.4	3.7	2.6	2.4	2.2	2.0	2.0
EBITDA/ Net Interest Expense	15.9	-15.6	15.9	14.2	16.1	17.7	19.4	19.8

Forecast Revisions as of 4 Aug 2025

Prior data as of 10 Jun 2025	2025		2026		2027	
	Current	Prior	Current	Prior	Current	Prior
Fair Value Estimate Change (Trading Currency)	87.00	87.24	—	—	—	—
Revenue (USD Mil)	37,433	37,431	41,496	41,509	46,652	46,684
Operating Income (USD Mil)	4,020	4,171	4,945	5,257	6,050	6,390
EBITDA (USD Mil)	6,115	6,058	7,114	7,369	8,520	8,802
Net Income (USD Mil)	3,054	3,084	3,639	3,924	4,469	4,779
Earnings Per Share (Diluted) (USD)	2.73	2.76	3.31	3.57	4.05	4.34
Adjusted Earnings Per Share (Diluted) (USD)	2.73	2.76	3.31	3.57	4.05	4.34
Dividends Per Share (USD)	2.44	2.44	2.25	2.42	2.43	2.60

Key Valuation Drivers as of 01 Aug 2025

Cost of Equity %	9.0
Pre-Tax Cost of Debt %	5.5
Weighted Average Cost of Capital %	8.3
Long-Run Tax Rate %	22.9
Stage II EBI Growth Rate %	6.0
Stage II Investment Rate %	32.0
Perpetuity Year	20

Additional estimates and scenarios available for download at <https://pitchbook.com/>.

Discounted Cash Flow Valuation as of 01 Aug 2025

	USD Mil
Present Value Stage I	33,556
Present Value Stage II	27,142
Present Value Stage III	45,916
Total Firm Value	106,615
Cash and Equivalents	3,286
Debt	15,568
Other Adjustments	-766
Equity Value	93,567
Projected Diluted Shares	1,132
Fair Value per Share (USD)	87.00

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ESG Risk Rating Breakdown

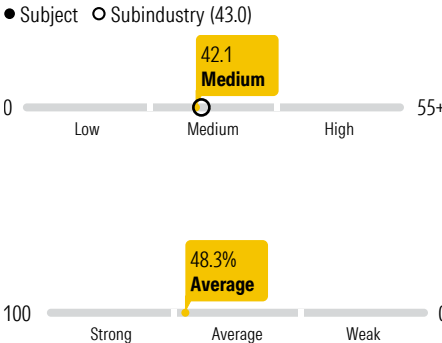
Exposure

Company Exposure¹	42.1
- Manageable Risk	39.2
Unmanageable Risk²	2.9

Management

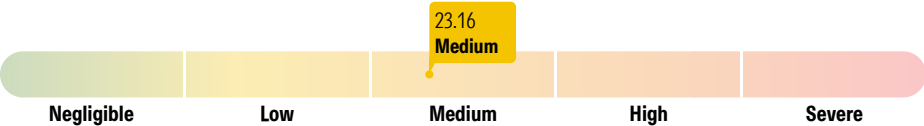
Manageable Risk	39.2
- Managed Risk³	18.9
Management Gap⁴	20.3

Overall Unmanaged Risk 23.2



- Exposure represents a company's vulnerability to ESG risks driven by their business model
- Exposure is assessed at the Subindustry level and then specified at the company level
- Scoring ranges from 0-55+ with categories of low, medium, and high-risk exposure
- Management measures a company's ability to manage ESG risks through its commitments and actions
- Management assesses a company's efficiency on ESG programs, practices, and policies
- Management score ranges from 0-100% showing how much manageable risk a company is managing

ESG Risk Rating



ESG Risk Ratings measure the degree to which a company's value is impacted by environmental, social, and governance risks, by evaluating the company's ability to manage the ESG risks it faces.

1. A company's Exposure to material ESG issues 2. Unmanageable Risk refers to risks that are inherent to a particular business model that cannot be managed by programs or initiatives 3. Managed Risk = Manageable Risk multiplied by a Management score of 48.3% 4. Management Gap assesses risks that are not managed, but are considered manageable 5. ESG Risk Rating Assessment = Overall Unmanaged Risk = Management Gap plus Unmanageable Risk

ESG Risk Rating Assessment⁵



ESG Risk Rating is of Sep 03, 2025. Highest Controversy Level is as of Oct 08, 2025. Sustainability Subindustry: Restaurants. Sustainability provides Morningstar with company ESG ratings and metrics on a monthly basis and as such, the ratings in Morningstar may not necessarily reflect current Sustainability scores for the company. For the most up to date rating and more information, please visit: sustainalytics.com/esg-ratings/.

Peer Analysis 03 Sep 2025

Company Name	Exposure	Management	ESG Risk Rating
Starbucks Corp	42.1 Medium 0 —●— 55+	48.3 Average 100 —●— 0	23.2 Medium 0 —●— 40+
McDonald's Corp	43.6 Medium 0 —●— 55+	37.6 Average 100 —●— 0	28.3 Medium 0 —●— 40+
Yum Brands Inc	41.3 Medium 0 —●— 55+	47.8 Average 100 —●— 0	22.9 Medium 0 —●— 40+
First Watch Restaurant Group Inc	42.1 Medium 0 —●— 55+	25.3 Average 100 —●— 0	32.2 High 0 —●— 40+
Restaurant Brands International Inc	44.5 Medium 0 —●— 55+	44.8 Average 100 —●— 0	25.9 Medium 0 —●— 40+

Appendix

Historical Morningstar Rating

Starbucks Corp SBUX 29 Oct 2025 21:31, UTC

Dec 2025 —	Nov 2025 —	Oct 2025 ★★★	Sep 2025 ★★★	Aug 2025 ★★★	Jul 2025 ★★★	Jun 2025 ★★★	May 2025 ★★★	Apr 2025 ★★★	Mar 2025 ★★	Feb 2025 ★★	Jan 2025 ★★
Dec 2024 ★★★	Nov 2024 ★★	Oct 2024 ★★★	Sep 2024 ★★★	Aug 2024 ★★★	Jul 2024 ★★★★	Jun 2024 ★★★★	May 2024 ★★★★	Apr 2024 ★★★★	Mar 2024 ★★★★	Feb 2024 ★★★★	Jan 2024 ★★★★
Dec 2023 ★★★	Nov 2023 ★★★	Oct 2023 ★★★★	Sep 2023 ★★★	Aug 2023 ★★★	Jul 2023 ★★★	Jun 2023 ★★★	May 2023 ★★★	Apr 2023 ★★★	Mar 2023 ★★★	Feb 2023 ★★★	Jan 2023 ★★★
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McDonald's Corp MCD 29 Oct 2025 21:26, UTC

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Yum Brands Inc YUM 29 Oct 2025 21:31, UTC

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Restaurant Brands International Inc QSR 29 Oct 2025 22:16, UTC

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Research Methodology for Valuing Companies

Overview

At the heart of our valuation system is a detailed projection of a company's future cash flows, resulting from our analysts' research. Analysts create custom industry and company assumptions to feed income statement, balance sheet, and capital investment assumptions into our globally standardized, proprietary discounted cash flow, or DCF, modeling templates. We use scenario analysis, in-depth competitive advantage analysis, and a variety of other analytical tools to augment this process. Moreover, we think analyzing valuation through discounted cash flows presents a better lens for viewing cyclical companies, high-growth firms, businesses with finite lives (e.g., mines), or companies expected to generate negative earnings over the next few years. That said, we don't dismiss multiples altogether but rather use them as supporting cross-checks for our DCF-based fair value estimates. We also acknowledge that DCF models offer their own challenges (including a potential proliferation of estimated inputs and the possibility that the method may miss short-term market-price movements), but we believe these negatives are mitigated by deep analysis and our long-term approach.

Morningstar's equity research group ("we," "our") believes that a company's intrinsic worth results from the future cash flows it can generate. The Morningstar Rating for stocks identifies stocks trading at a discount or premium to their intrinsic worth—or fair value estimate, in Morningstar terminology. Five-star stocks sell for the biggest risk adjusted discount to their fair values, whereas 1-star stocks trade at premiums to their intrinsic worth.

Four key components drive the Morningstar rating: (1) our assessment of the firm's economic moat, (2) our estimate of the stock's fair value, (3) our uncertainty around that fair value estimate and (4) the current market price. This process ultimately culminates in our single-point star rating.

1. Economic Moat

The concept of an economic moat plays a vital role not only in our qualitative assessment of a firm's long-term investment potential, but also in the actual calculation of our fair value estimates. An economic moat is a structural feature that allows a firm to sustain excess profits over a

long period of time. We define economic profits as returns on invested capital (or ROIC) over and above our estimate of a firm's cost of capital, or weighted average cost of capital (or WACC). Without a moat, profits are more susceptible to competition. We have identified five sources of economic moats: intangible assets, switching costs, network effect, cost advantage, and efficient scale.

Companies with a narrow moat are those we believe are more likely than not to achieve normalized excess returns for at least the next 10 years. Wide-moat companies are those in which we have very high confidence that excess returns will remain for 10 years, with excess returns more likely than not to remain for at least 20 years. The longer a firm generates economic profits, the higher its intrinsic value. We believe low-quality, no-moat companies will see their normalized returns gravitate toward the firm's cost of capital more quickly than companies with moats.

When considering a company's moat, we also assess whether there is a substantial threat of value destruction, stemming from risks related to ESG, industry disruption, financial health, or other idiosyncratic issues. In this context, a risk is considered potentially value destructive if its occurrence would eliminate a firm's economic profit on a cumulative or midcycle basis. If we deem the probability of occurrence sufficiently high, we would not characterize the company as possessing an economic moat.

2. Estimated Fair Value

Combining our analysts' financial forecasts with the firm's economic moat helps us assess how long returns on invested capital are likely to exceed the firm's cost of capital. Returns of firms with a wide economic moat rating are assumed to fade to the perpetuity period over a longer period of time than the returns of narrow-moat firms, and both will fade slower than no-moat firms, increasing our estimate of their intrinsic value.

Our model is divided into three distinct stages:

Stage I: Explicit Forecast

In this stage, which can last five to 10 years, analysts make full financial statement forecasts, including items such as revenue, profit margins, tax rates, changes in working capital accounts, and capital spending. Based on these projections, we calculate earnings before interest,

after taxes (EBI) and the net new investment (NNI) to derive our annual free cash flow forecast.

Stage II: Fade

The second stage of our model is the period it will take the company's return on new invested capital—the return on capital of the next dollar invested ("RONIC")—to decline (or rise) to its cost of capital. During the Stage II period, we use a formula to approximate cash flows in lieu of explicitly modeling the income statement, balance sheet, and cash flow statement as we do in Stage I. The length of the second stage depends on the strength of the company's economic moat. We forecast this period to last anywhere from one year (for companies with no economic moat) to 10–15 years or more (for wide-moat companies). During this period, cash flows are forecast using four assumptions: an average growth rate for EBI over the period, a normalized investment rate, average return on new invested capital (RONIC), and the number of years until perpetuity, when excess returns cease. The investment rate and return on new invested capital decline until a perpetuity value is calculated. In the case of firms that do not earn their cost of capital, we assume marginal ROICs rise to the firm's cost of capital (usually attributable to less reinvestment), and we may truncate the second stage.

Stage III: Perpetuity

Once a company's marginal ROIC hits its cost of capital, we calculate a continuing value, using a standard perpetuity formula. At perpetuity, we assume that any growth or decline or investment in the business neither creates nor destroys value and that any new investment provides a return in line with estimated WACC.

Because a dollar earned today is worth more than a dollar earned tomorrow, we discount our projections of cash flows in stages I, II, and III to arrive at a total present value of expected future cash flows. Because we are modeling free cash flow to the firm—representing cash available to provide a return to all capital providers—we discount future cash flows using the WACC, which is a weighted average of the costs of equity, debt, and preferred stock (and any other funding sources), using expected future proportionate long-term, market-value weights.

3. Uncertainty Around That Fair Value Estimate

Morningstar's Uncertainty Rating is designed to capture the range of potential outcomes for a company's intrinsic value. This rating is used to assign the margin of safety required before investing, which in turn explicitly drives our stock star rating system. The Uncertainty Rating is aimed at identifying the confidence we should have in assigning a fair value estimate for a given stock.

Our Uncertainty Rating is meant to take into account anything that can increase the potential dispersion of future

Morningstar Equity Research Star Rating Methodology



Research Methodology for Valuing Companies

outcomes for the intrinsic value of a company, and anything that can affect our ability to accurately predict these outcomes. The rating begins with a suggested rating produced by a quantitative process based on the trailing 12-month standard deviation of daily stock returns. An analyst overlay is then applied, with analysts using the suggested rating, historical rating data, and their own knowledge of the company to inform them as they make the final Uncertainty Rating decision. Ultimately, the rating decision rests with the analyst. Analysts take into account many characteristics when making their final decision, including cyclical factors, operational and financial factors such as leverage, company-specific events, ESG risks, and anything else that might increase the potential dispersion of future outcomes and our ability to estimate those outcomes.

Our recommended margin of safety—the discount to fair value demanded before we'd recommend buying or selling the stock—widens as our uncertainty of the estimated value of the equity increases. The more uncertain we are about the potential dispersion of outcomes, the greater the discount we require relative to our estimate of the value of the firm before we would recommend the purchase of the shares. In addition, the Uncertainty Rating provides guidance in portfolio construction based on risk tolerance.

Our Uncertainty Ratings are: Low, Medium, High, Very High, and Extreme.

Qualitative Analysis Uncertainty Ratings	Margin of Safety	
	★★★★★ Rating	★ Rating
Low	20% Discount	25% Premium
Medium	30% Discount	35% Premium
High	40% Discount	55% Premium
Very High	50% Discount	75% Premium
Extreme	75% Discount	300% Premium

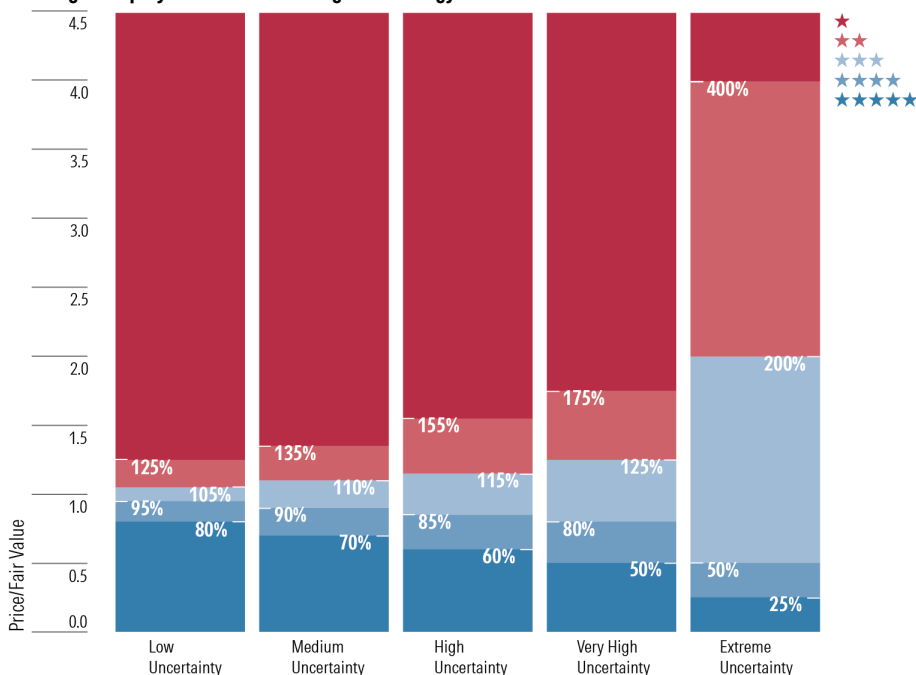
Our uncertainty rating is based on the interquartile range, or the middle 50% of potential outcomes, covering the 25th percentile–75th percentile. This means that when a stock hits 5 stars, we expect there is a 75% chance that the intrinsic value of that stock lies above the current market price. Similarly, when a stock hits 1 star, we expect there is a 75% chance that the intrinsic value of that stock lies below the current market price.

4. Market Price

The market prices used in this analysis and noted in the report come from exchange on which the stock is listed which we believe is a reliable source.

For more details about our methodology, please go to <https://shareholders.morningstar.com>

Morningstar Equity Research Star Rating Methodology



Morningstar Star Rating for Stocks

Once we determine the fair value estimate of a stock, we compare it with the stock's current market price on a daily basis, and the star rating is automatically re-calculated at the market close on every day the market on which the stock is listed is open. Our analysts keep close tabs on the companies they follow, and, based on thorough and ongoing analysis, raise or lower their fair value estimates as warranted.

Please note, there is no predefined distribution of stars. That is, the percentage of stocks that earn 5 stars can fluctuate daily, so the star ratings, in the aggregate, can serve as a gauge of the broader market's valuation. When there are many 5-star stocks, the stock market as a whole is more undervalued, in our opinion, than when very few companies garner our highest rating.

We expect that if our base-case assumptions are true the market price will converge on our fair value estimate over time generally within three years (although it is impossible to predict the exact time frame in which market prices may adjust).

Our star ratings are guideposts to a broad audience and individuals must consider their own specific investment goals, risk tolerance, tax situation, time horizon, income needs, and complete investment portfolio, among other factors.

The Morningstar Star Ratings for stocks are defined below:

★★★★★ We believe appreciation beyond a fair risk-adjusted return is highly likely over a multiyear time frame. Scenario analysis developed by our analysts indicates that the current market price represents an excessively pessimistic outlook, limiting downside risk and maximizing upside potential.

★★★★ We believe appreciation beyond a fair risk-adjusted return is likely.

★★★ Indicates our belief that investors are likely to receive a fair risk-adjusted return (approximately cost of equity).

★★ We believe investors are likely to receive a less than fair risk-adjusted return.

★ Indicates a high probability of undesirable risk-adjusted returns from the current market price over a multi-year time frame, based on our analysis. Scenario analysis by our analysts indicates that the market is pricing in an excessively optimistic outlook, limiting upside potential and leaving the investor exposed to Capital loss.

Other Definitions

Last Price: Price of the stock as of the close of the market of the last trading day before date of the report.

Capital Allocation Rating: Our Capital Allocation (or Stewardship) Rating represents our assessment of the quality of management's capital allocation, with particular emphasis on the firm's balance sheet, investments,

Research Methodology for Valuing Companies

and shareholder distributions. Analysts consider companies' investment strategy and valuation, balance sheet management, and dividend and share buyback policies. Corporate governance factors are only considered if they are likely to materially impact shareholder value, though either the balance sheet, investment, or shareholder distributions. Analysts assign one of three ratings: "Exemplary", "Standard", or "Poor". Analysts judge Capital Allocation from an equity holder's perspective. Ratings are determined on a forward looking and absolute basis. The Standard rating is most common as most managers will exhibit neither exceptionally strong nor poor capital allocation.

Capital Allocation (or Stewardship) analysis published prior to Dec. 9, 2020, was determined using a different process. Beyond investment strategy, financial leverage, and dividend and share buyback policies, analysts also considered execution, compensation, related party transactions, and accounting practices in the rating.

Capital Allocation Rating: Our Capital Allocation (or Stewardship) Rating represents our assessment of the quality of management's capital allocation, with particular emphasis on the firm's balance sheet, investments, and shareholder distributions. Analysts consider companies' investment strategy and valuation, balance sheet management, and dividend and share buyback policies. Corporate governance factors are only considered if they are likely to materially impact shareholder value, though either the balance sheet, investment, or shareholder distributions. Analysts assign one of three ratings: "Exemplary", "Standard", or "Poor". Analysts judge Capital Allocation from an equity holder's perspective. Ratings are determined on a forward looking and absolute basis. The Standard rating is most common as most managers will exhibit neither exceptionally strong nor poor capital allocation.

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Sustainalytics ESG Risk Rating Assessment: The ESG Risk Rating Assessment is provided by Sustainalytics; a Morningstar company.

Sustainalytics' ESG Risk Ratings measure the degree to which company's economic value at risk is driven by environment, social and governance (ESG) factors.

Sustainalytics analyzes over 1,300 data points to assess a company's exposure to and management of ESG risks. In other words, ESG Risk Ratings measures a company's unmanaged ESG Risks represented as a quantitative score.

Unmanaged Risk is measured on an open-ended scale starting at zero (no risk) with lower scores representing less unmanaged risk and, for 95% of cases, the unmanaged ESG Risk score is below 50.

Based on their quantitative scores, companies are grouped into one of five Risk Categories (negligible, low, medium, high, severe). These risk categories are absolute, meaning that a 'high risk' assessment reflects a comparable degree of unmanaged ESG risk across all subindustries covered.

The ESG Risk Rating Assessment is a visual representation of Sustainalytics ESG Risk Categories on a 1 to 5 scale. Companies with Negligible Risk = 5 Globes, Low Risk = 4, Medium Risk = 3 Globes, High Risk = 2 Globes, Severe Risk = 1 Globe. For more information, please visit sustainalytics.com/esg-ratings/

Ratings should not be used as the sole basis in evaluating a company or security. Ratings involve unknown risks and uncertainties which may cause our expectations not to occur or to differ significantly from what was expected and should not be considered an offer or solicitation to buy or sell a security.

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Research Methodology for Valuing Companies

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