

# Thesis proposal on ethical outsourcing for starbucks coffee company

[Business](#), [Company](#)



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## **How will Starbucks maintain it?**

### **Abstract**

This thesis presents a critical analysis of the business situations faced by Starbucks Corporation over the years. It briefly analyses its business practices and the causes of its decline in sales. It argues how the company's move to outsource some processes is ethical. This paper also looks at the sensitive side of outsourcing and argues how even the offshore outsourcing is ethical in today's world of globalization. In order to present the arguments in favour of ethical outsourcing the paper also touches upon concepts in business economics that were present as early as 18th century and were highly publicised by the economist, Adam Smith. Finally, the paper concludes by showing methods of practicing and maintaining ethical outsourcing.

Outsourcing is a very sensitive topic and when you talk about ethical outsourcing it is more of a paradox. Can outsourcing be really ethical? This can be answered only when both the pros and cons are weighed together. Let us first start with understanding the basics – what is outsourcing?

When a business obtains the services of a function or a part of that function, from a vendor outside the company, instead of getting it done in-house, it is called outsourcing. For e. g., if business A gets its database managed from a vendor B instead of managing it in-house by employing staff, business A is said to be outsourcing a part of its IT function to the vendor B. Similarly many other support functions such as manufacturing, marketing and customer service can also be outsourced. Outsourcing is usually done to

leverage upon the cheaper labour costs and direct the resources available to the company for concentrating on improving the core competency of its business.

Outsourcing per se is a very old concept. We can find its roots in economic principles as early as 1776 when the distinguished economist, Adam Smith made a theory about competitive advantage in *The Wealth of Nations*. He propagated that companies can be more productive if they cut costs and use cheaper labour. He also insisted on the rationale of how self-interest in a free-market economy leads to economic well-being. Smith also argued that acts of charity alone cannot bring prosperity, but it is the self-interest that can. When a labourer earns for his services, he has to create and show value in his services to be able to command income on it. This by itself creates competition and propels creation of wealth and better standards of living which the society endeavours for.

The onset of globalization has left no such function which the companies cannot outsource. In fact, globalization has opened the gates for offshore outsourcing and which is why the question of ethics arises so fervently. When the outsourcing vendor is in a different country the outsourcing is termed as offshore outsourcing and the jobs are directly transferred to another country. But the very core of globalization is connecting the free-market economies across the globe for cost-effective production and increasing the consumption of better value-added products and services for achieving higher standards of living around the globe. Drawing from Adam Smith's tenets for business economics, companies will seek to maximize

profitability out of self-interest for generating higher value to their shareholders in the wake of fierce competition which ensues as a result of globalization. If there are benefits associated with the globalization then those will come at a cost albeit just for some time when there is a transition i. e. from the time when a company declares its plans to outsource one of its functions to the point when the outsourcing is implemented.

Starbucks Corporation, one of the best known brands in the United States of America and the largest coffeehouse in the world, too has outsourced some of its functions such as IT, customer service and growing coffee beans at some parts of the world. It is one of the Fortune 500 companies known for its impeccable customer service, for treating its employees as its partners and for implementing some of the best ethical business practices. Starbucks was the first company to offer health insurance to its part-time employees also. Starbucks has been known for its ethical sourcing of highest quality of Arabica coffee beans in the world and for its unwavering commitment to excellence in providing the Starbucks experience to its customers. But Starbucks also could not escape the wrath of the fierce home-grown competition and other hurdles of expanding internationally.

To maximise profits every company has to figure out ways to maximise return on investment (ROI) in various departments or functional units. If the companies reduce costs and still get the benefits by implementing the fundamentals of ‘division of labour’, guided through globalization then they can maximize their shareholders value. This is so because division of labour improves the productive power of labours or employees situated elsewhere

on the globe where they can perform the organized and streamlined processes. To this extent, when tasks in the support functions are outsourced because they can be performed more efficiently because of their repetitive nature at a lower cost, and as long as the companies engage in ethical business practices, outsourcing is ethical.

To understand why Starbucks went the outsourcing way and whether it was an ethical outsourcing, it is important to look at the beginning when Howard Schultz joined Starbucks in 1981; how over the years its business has grown and how the market forces led to its declining sales. Howard Schultz wanted Starbucks coffee bars to provide great experience and not just be any other retail store. He wanted to provide customized coffee to his customers and made sure that some of the best coffee beans were procured from around the world. Strong aroma of roasted coffee beans would fill the Starbucks cafes where the baristas would hand-grind coffee beans specific to customers' orders. Customers would flock the cafes and could associate it with an urbane place to hang around. All of the appeal could only be possible when the core of the product i. e. the coffee beans were of the highest quality. Moreover they were procured from the third world countries where the coffee farmers were paid above market price for those premium coffee beans. Not only this, Starbucks would also participate in environment friendly methods to procure coffee beans. Such an ethical sourcing would make customers want to associate themselves with Starbucks.

Later, in order to standardize the experience Starbucks replaced the process of hand-creating of a cup of coffee by barista by automated espresso

machines and vacuum-packed ground coffee. The Starbucks 'experience' drove its growth over many years. The stocks saw a phenomenal growth rate of nearly 5800% from initial public offering in 1992 to its peak in 2006.

But rapid expansion slowed down by 2007 and the increasing cost of expansion showed in the weakening financial ratios. Increasing oil prices added to the company's woes. The oil prices rose from \$30 a barrel to about \$65 a barrel by 2007. This directly translated into the increase in price of goods sold. Starbucks found that the price of buying coffee beans rose about 20% over the 2005- 2007 period. There was also an increase in minimum wages by 14% in July 2007. Still at the end of the year 2007 Starbucks reported an increase of 9% in the net income. But still Starbucks' stocks went down by 20% between 2006 and 2007. Analysts attribute this mainly to the rapid expansion policy which Starbucks had announced. It was not received positively by the market. The other factors which led to the decline in sales were the cheaper version of coffee options at competitors such as Dunkin Donuts and McDonalds.

In July 2007 Starbucks signed an outsourcing contract with Convergys to provide global human resources business process services. This followed with offshore outsourcing in 2009, when Starbucks outsourced its data center services to Unisys in China in order to support continued expansion of Starbucks globally and to simplify and standardize its IT management. Earlier Starbucks had outsourced its end-user support services, including service desk and nationwide infrastructure support services to Unisys in 2006. The latest outsourcing deal came in January 2010, when Starbucks announced

that it will close down its Seattle customer service center and outsource it to a third party in New Mexico. The main reason behind such a move was to better manage the customer complaints and ramp the vendor's services up or down as the need may be.

Ever since Howard Schultz came back as a CEO in 2008, Starbucks stock price has quadrupled. When Howard Schultz came back as the CEO, he came with a transformational agenda which had priority for cutting costs and rekindling the erstwhile emotional attachment that his customers used to experience. Starbucks did what it should have done – it cut costs drastically and focussed strategically on introducing new beverage products based on market survey reports and invested in advertising, which it had never done before. With launch of Via, a new product, Starbucks regained its growing sales numbers.

In future too when the market forces guide a company to outsource some processes, there are ways that the ethical outsourcing can be maintained. It can be maintained by following some of the methods listed here:

### **Announce the outsourcing plans well in advance**

Offer severance packages commensurate with the years that an employee has spent at the company and based on how his/her performance has been

### **Offer other job roles to the employees or offer to relocate them to other sites**

Moderate growth plans so as to take black-swan like events into account such as that faced by Starbucks in Israel and the drop in sales due to

recession that followed the global financial meltdown. Hence avoid retrenching employees due to exploding overheads.

Expand to new markets after carefully studying experiences of other players in the food and beverages industry, such as those of McDonalds.

As Howard Schultz was quoted in a special report in the U. S. News, “ The art of leadership is making sure we don't allow the scale and size of the company to change the methodology of how we conduct ourselves. We have to be careful not to let our values be compromised by an ambition to grow.”

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