STARBUCKS CORP
Form 10-K
December 14, 2006

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549
Form 10-K

þ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For The Fiscal Year Ended October 1, 2006

OR

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

For the transition period from to .
Commission File Number: 0-20322
Starbucks Corporation
(Exact Name of Registrant as Specified in Its Charter)

WASHINGTON	**91-1325671**
(State or other jurisdiction of incorporation or organization)	*(IRS Employer Identification No.)*

2401 Utah Avenue South
Seattle, Washington 98134
(Address of principal executive offices, zip code)

(REGISTRANT S TELEPHONE NUMBER, INCLUDING AREA CODE):
(206) 447-1575

SECURITIES REGISTERED PURSUANT TO SECTION 12(G) OF THE ACT:
Common Stock, $0.001 Par Value Per Share

SECURITIES REGISTERED PURSUANT TO SECTION 12(B) OF THE ACT:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes þ No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No þ

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation of S-K is not contained herein, and will not be contained, to the best of the registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. þ

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one)

Large Accelerated Filer þ Accelerated Filer o Non-Accelerated Filer o

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

The aggregate market value of the voting stock held by non-affiliates of the registrant as of the last business day of the registrant s most recently completed second fiscal quarter, based upon the closing sale price of the registrant s common stock on March 31, 2006 as reported on the National Market tier of The NASDAQ Stock Market, Inc. was $28.2 billion.

As of December 8, 2006, there were 754,857,728 shares of the registrant s Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement for the registrant s Annual Meeting of Shareholders to be held on March 21, 2007 have been incorporated by reference into Part III of this Annual Report on Form 10-K.

STARBUCKS CORPORATION

FORM 10-K
For the Fiscal Year Ended October 1, 2006

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PART I

Item 1. Business

GENERAL

Starbucks Corporation (together with its subsidiaries, Starbucks or the Company) was formed in 1985. Starbucks purchases and roasts high-quality whole bean coffees and sells them, along with fresh, rich-brewed coffees, Italian-style espresso beverages, cold blended beverages, a variety of complementary food items, coffee-related accessories and equipment, a selection of premium teas and a line of compact discs, primarily through Company-operated retail stores. Starbucks also sells coffee and tea products and licenses its trademark through other channels and, through certain of its equity investees, Starbucks produces and sells ready-to-drink beverages which include, among others, bottled Frappuccino® coffee drinks and Starbucks DoubleShot® espresso drinks, and a line of superpremium ice creams. All channels outside the Company-operated retail stores are collectively known as Specialty Operations. The Company s objective is to establish Starbucks as one of the most recognized and respected brands in the world. To achieve this goal, the Company plans to continue rapid expansion of its retail operations, to grow its Specialty Operations and to selectively pursue other opportunities to leverage the Starbucks brand through the introduction of new products and the development of new channels of distribution. The Company s brand portfolio includes superpremium Tazo® teas, Starbucks Hear Music® compact discs, Seattle s Best Coffee® and Torrefazione Italia® coffee.

SEGMENT FINANCIAL INFORMATION

Beginning in the fiscal fourth quarter of 2006, the Company increased its reporting segments from two to three to include a Global Consumer Products Group (CPG) segment in addition to the United States and International segments. This additional operating segment reflects the culmination of internal management realignments in fiscal 2006, and the successful development and launch of certain branded products in the United States and internationally commencing in fiscal 2005 and continuing throughout fiscal 2006. Additionally, with the 100% acquisition of the Company s operations in Hawaii in fiscal 2006 and the shift in internal management of this market to the United States, these operations have been moved from the International segment into the United States segment. Segment information for all prior periods presented has been revised to reflect these changes.

The United States and International segments both include Company-operated retail stores and certain components of Specialty Operations. Specialty operations within the United States include licensed retail stores, foodservice accounts and other initiatives related to the Company s core business. International specialty operations primarily include retail store licensing operations in more than 25 countries and foodservice accounts in Canada and the United Kingdom. The CPG segment includes the Company s grocery and warehouse club business as well as branded products operations worldwide. Information about Starbucks revenues, earnings before income taxes, depreciation and amortization, income from equity investees, equity method investments, identifiable assets, net impairment and disposition losses and capital expenditures by segment is included in Note 19 Segment Reporting to the consolidated financial statements included in Item 8 of this Annual Report on Form 10-K (Form 10-K or Report).

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REVENUE COMPONENTS

The following table shows the Company s revenue components for the fiscal year ended October 1, 2006:

REVENUES	% of Total Net Revenues	% of Specialty Revenues
Company-operated retail	85%	
Specialty:		
Licensing:		
Retail stores	7%	45%
Grocery and warehouse club	4%	24%
Branded products	<1%	2%
Total licensing	11%	71%
Foodservice and other:		
Foodservice	4%	27%
Other initiatives	<1%	2%
Total foodservice and other	4%	29%
Total specialty	15%	100%
Total net revenues	100%	

COMPANY-OPERATED RETAIL STORES

The Company s retail goal is to become the leading retailer and brand of coffee in each of its target markets by selling the finest quality coffee and related products and by providing each customer a unique *Starbucks Experience.* The *Starbucks Experience*, or third place after home and work, is built upon superior customer service as well as clean and well-maintained Company-operated retail stores that reflect the personalities of the communities in which they operate, thereby building a high degree of customer loyalty. Starbucks strategy for expanding its retail business is to increase its market share primarily by opening additional stores in existing markets and to open stores in new markets where the opportunity exists to become the leading specialty coffee retailer. In support of this strategy, Starbucks opened 1,040 new Company-operated stores during the fiscal year ended October 1, 2006 (fiscal 2006). Starbucks Company-operated retail stores, including 11 Seattle s Best Coffee® (SBC) stores and 4 Hear Music retail stores, accounted for 85% of total net revenues during fiscal 2006.

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The following table summarizes total Company-operated retail store data for the periods indicated:

	Net Stores Opened During the Fiscal Year Ended		Stores Open as of	
	Oct 1, 2006	Oct 2, 2005	Oct 1, 2006	Oct 2, 2005
United States (1)	810	580	5,728	4,918
International:				
United Kingdom	47	45	514	467
Canada	74	62	508	434
Thailand	22	14	85	63
Australia	25	14	83	58
Germany	24	9	68	44
China	14	18	38	24
Singapore	5	(3)	37	32
Puerto Rico (1)	6	5	17	11
Chile	6	1	16	10
Ireland	7	1	8	1
Total International	230	166	1,374	1,144
Total Company-operated	1,040	746	7,102	6,062

(1) International store data has been adjusted for the acquisitions of the Puerto Rico and Hawaii operations by reclassifying historical information from Licensed stores to Company-operated stores. United States store data was also adjusted to align with the Hawaii operations segment change by reclassifying historical information from International Company-operated stores to the United States.

Starbucks retail stores are typically located in high-traffic, high-visibility locations. Because the Company can vary the size and format, its stores are located in or near a variety of settings, including downtown and suburban retail centers, office buildings and university campuses. While the Company selectively locates stores in shopping malls, it focuses on locations that provide convenient access for both pedestrians and drivers. With the flexibility in store size and format, the Company also locates retail stores in select rural and off-highway locations to serve a broader array of customers outside major metropolitan markets and further expand brand awareness. To provide a greater degree of access and convenience for nonpedestrian customers, the Company has increased development of Drive-Thru retail stores. At the end of fiscal 2006, the Company operated approximately 1,600 Drive-Thru locations.

All Starbucks stores offer a choice of regular and decaffeinated coffee beverages, a broad selection of Italian-style espresso beverages, cold blended beverages, iced shaken refreshment beverages, a selection of teas and distinctively packaged roasted whole bean coffees. Starbucks stores also offer a selection of fresh pastries and other food items, sodas, juices, bottled water, coffee-making equipment and accessories, a selection of compact discs, games and seasonal novelty items. Each Starbucks store varies its product mix depending upon the size of the store and its location. Larger stores carry a broad selection of the Company s whole bean coffees in various sizes and types of packaging, as well as an assortment of coffee and espresso-making equipment and accessories such as coffee grinders, coffee filters, storage containers, travel tumblers and mugs. Smaller Starbucks stores and kiosks typically sell a full line of coffee beverages, a limited selection of whole bean coffees and a few accessories such as travel tumblers and logo mugs. In the United States and in International markets, approximately 3,800 stores and 1,300 stores, respectively, carry a selection of prepared sandwiches and salads. Starbucks continues to expand its food warming program in select markets in the United States, with approximately 640 stores as of October 1, 2006 providing warm food items including breakfast sandwiches.

The Company s retail sales mix by product type during fiscal 2006 was as follows: 77% beverages, 15% food, 3% whole bean coffees and 5% coffee-making equipment and other merchandise.

SPECIALTY OPERATIONS

Specialty Operations strive to develop the Company s brands outside the Company-operated retail store environment through a number of channels. Starbucks strategy is to reach customers where they work, travel, shop and dine by

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establishing relationships with prominent third parties that share the Company s values and commitment to quality. These relationships take various forms, including licensing arrangements, foodservice accounts and other initiatives related to the Company s core businesses. In certain situations, Starbucks has an equity ownership interest in licensee operations. During fiscal 2006, specialty revenues (which include royalties and fees from licensees, as well as product sales derived from Specialty Operations) accounted for 15% of total net revenues.

Licensing Retail stores

In its licensed retail store operations, the Company leverages the expertise of its local partners and shares Starbucks operating and store development experience. Licensee partners are typically master concessionaires, which can provide improved access to desirable retail space, or prominent retailers with in-depth market knowledge and access. As part of these arrangements, Starbucks receives license fees and royalties and sells coffee, tea, compact discs and related products for resale in licensed locations. Employees working in licensed retail locations are required to follow Starbucks detailed store operating procedures and attend training classes similar to those given to employees in Company-operated stores.

During fiscal 2006, 733 new Starbucks licensed retail stores were opened in the United States and, as of October 1, 2006, the Company s licensees operated 3,168 stores. During fiscal 2006, 426 new International licensed stores were opened. At October 1, 2006, the Company s International operating segment had a total of 2,170 licensed retail stores. Product sales to and royalty and license fee revenues from U.S. and International licensed retail stores accounted for 45% of specialty revenues in fiscal 2006.

At fiscal year end 2006, Starbucks total licensed retail stores by region and specific location were as follows:

Asia Pacific		Europe/Middle East/Africa		Americas	
Japan	650	Spain	55	United States	3,168
China	223	Turkey	51	Canada	178
Taiwan	175	Greece	50	Mexico	101
South Korea	174	Saudi Arabia	46	Peru	9
Philippines	98	United Arab Emirates	44	The Bahamas	5
Malaysia	71	Kuwait	36		
New Zealand	45	Switzerland	27		
Indonesia	45	France	26		
		Austria	11		
		Lebanon	11		
		Bahrain	8		
		Qatar	8		
		Cyprus	7		
		UK	6		
		Jordan	5		
		Oman	4		
		Ireland	1		
Total	1,481	Total	396	Total	3,461

Licensing Grocery and warehouse club

In grocery and warehouse club stores throughout the United States, the Company sells a selection of Starbucks® whole bean and ground coffees, as well as Seattle s Best Coffee and Torrefazione Italia branded coffees and a selection of premium Tazo® teas through a licensing relationship with Kraft Foods Inc. (Kraft). Kraft manages all distribution, marketing, advertising and promotion of these products. In International markets, Starbucks also has licensing arrangements with other grocery and warehouse club stores. By the end of fiscal 2006, the Company s coffees and teas were available in approximately 31,900 grocery and warehouse club stores, with 30,000 in the United States and 1,900 in International markets. Revenues from this category comprised 24% of specialty revenues in fiscal 2006.

Licensing Branded products

The Company has licensed the rights to produce and distribute Starbucks branded products to two partnerships in which the Company holds 50% equity interests. The North American Coffee Partnership with the Pepsi-Cola Company develops and distributes ready-to-drink beverages which include, among others, bottled Frappuccino® coffee drinks and Starbucks DoubleShot® espresso drinks. The Starbucks Ice Cream Partnership with Dreyer s Grand Ice Cream, Inc., develops and distributes superpremium ice creams.

Starbucks and Jim Beam Brands Co., a unit of Fortune Brands, Inc., manufacture and market Starbucks-branded premium coffee liqueur products in the United States and Canada. The Company introduced a coffee liqueur product nationally during the fiscal second quarter of 2005, and launched a coffee and cream liqueur product in the second quarter of fiscal 2006 in restaurants, bars and retail outlets where premium distilled spirits are sold. During the fiscal fourth quarter of 2006, the Company launched Starbucks™ Coffee Liqueur and Cream Liqueur in Canada. The Company does not and will not sell the liqueur products in its Company-operated or licensed retail stores.

In September 2005, the Company launched Starbucks Discoveries™, a ready-to-drink chilled cup coffee beverage in refrigerated cases of convenience stores in Japan, through a manufacturing and distribution agreement with Suntory Limited, and in Taiwan, through separate co-packing and distribution agreements with Uni-President Enterprises Corporation and the Company s equity investee, President Starbucks Coffee Taiwan Ltd. In fiscal 2006, the Company entered the ready-to-drink coffee category in South Korea through a licensing agreement with Dong Suh Foods Corporation to import bottled Starbucks Frappuccino® coffee drinks produced in the United States.

Collectively, the revenues from these branded products accounted for 2% of specialty revenues in fiscal 2006.

Foodservice

The Company sells whole bean and ground coffees, including the Starbucks, Seattle s Best Coffee and Torrefazione Italia brands, as well as a selection of premium Tazo® teas, to institutional foodservice companies that service business, industry, education and healthcare accounts, office coffee distributors, hotels, restaurants, airlines and other retailers. The majority of the Company s direct distribution accounts are with SYSCO Corporation s and U.S. Foodservice ™ national broadline distribution networks and Starbucks foodservice sales, customer service and support resources are aligned with those of SYSCO Corporation and U.S. Foodservice. Starbucks and Seattle s Best Coffee are the only superpremium national-brand coffees actively promoted by SYSCO Corporation. The Company s total worldwide foodservice operations had approximately 16,200 accounts at fiscal year end 2006, and revenues from these accounts comprised 27% of total specialty revenues.

Other Initiatives

Included in this category is the Company s emerging entertainment business, which encompasses multiple music and technology based initiatives designed to appeal to new and existing Starbucks customers. Among these initiatives are strategic marketing and co-branding arrangements, such as the 24-hour Starbucks Hear Music™ digital music channel 75 available to all XM Satellite Radio subscribers, and the availability of wireless broadband Internet service in Company-operated retail stores located in the United States and Canada. Additionally, the entertainment business includes the innovative partnerships of Starbucks Hear Music with other music labels for the production, marketing and distribution of both exclusive and nonexclusive music, music programming for Starbucks stores worldwide, and CD sales through the Company s website at Starbucks.com/hearmusic. In the first quarter of fiscal 2007, Starbucks and Apple® announced the availability of the Starbucks Hear Music catalog on the iTunes® Store, giving iTunes users the ability to preview, buy and download a wide variety of popular Starbucks Hear Music® titles.

The Company has a strategic agreement with Chase Bank USA, N.A. and Visa to issue the Starbucks Card Duetto™ Visa® (the Duetto Card) in the United States, and a similar arrangement with Royal Bank of Canada and Visa Canada Association to issue the Duetto Card in Canada. The Duetto Card is a first-of-its-kind card, combining the functionality

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of a credit card with the convenience of a reloadable Starbucks Card. Through these arrangements, Starbucks primarily receives commissions for each activated customer account and payments based on credit card usage.

Collectively, the operations of these other initiatives accounted for 2% of specialty revenues in fiscal 2006.

PRODUCT SUPPLY

Starbucks is committed to selling only the finest whole bean coffees and coffee beverages. To ensure compliance with its rigorous coffee standards, Starbucks controls its coffee purchasing, roasting and packaging, and the distribution of coffee used in its operations.

The Company purchases green coffee beans from coffee-producing regions around the world and custom roasts them to its exacting standards for its many blends and single origin coffees.

The supply and price of coffee are subject to significant volatility. Although most coffee trades in the commodity market, coffee of the quality sought by the Company tends to trade on a negotiated basis at a substantial premium above commodity coffee prices, depending upon the supply and demand at the time of purchase. Supply and price can be affected by multiple factors in the producing countries, including weather, political and economic conditions. In addition, green coffee prices have been affected in the past, and may be affected in the future, by the actions of certain organizations and associations that have historically attempted to influence prices of green coffee through agreements establishing export quotas or by restricting coffee supplies.

The Company depends upon its relationships with coffee producers, outside trading companies and exporters for its supply of green coffee. With green coffee commodity prices at relatively low levels in recent years, the Company has used fixed-price purchase commitments in order to secure an adequate supply of quality green coffee, bring greater certainty to the cost of sales in future periods, and promote sustainability by paying a fair price to coffee producers. As of October 1, 2006, the Company had $546 million in fixed-price purchase commitments which, together with existing inventory, is expected to provide an adequate supply of green coffee through fiscal 2007. The Company believes, based on relationships established with its suppliers, the risk of non-delivery on such purchase commitments is remote. During the first few months of fiscal 2006, green coffee commodity prices increased moderately. Since then, commodity prices have stabilized but still remain above the historically low levels experienced in recent years. Based on its market experience, the Company believes that fixed-price purchase commitments are less likely to be available on favorable terms when commodity prices are high. If prices were to move higher during fiscal 2007, Starbucks would likely return to its previous practice of entering into price-to-be-fixed purchase contracts to meet a large part of its demand. These types of contracts state the quality, quantity and delivery periods but allow the price of green coffee over a market index to be established after contract signing. The Company believes that, through a combination of fixed-price and price-to-be-fixed contracts it will be able to secure an adequate supply of quality green coffee. However, an increased use of price-to-be-fixed contracts instead of fixed-price contracts would decrease the predictability of coffee costs in future periods.

During fiscal 2004, Starbucks established the Starbucks Coffee Agronomy Company S.R.L., a wholly owned subsidiary located in Costa Rica, to reinforce the Company s leadership role in the coffee industry and to help ensure sustainability and future supply of high-quality green coffees from Central America. Staffed with agronomists and sustainability experts, this first-of-its-kind Farmer Support Center is designed to proactively respond to changes in coffee producing countries that impact farmers and the supply of green coffee.

In addition to coffee, the Company also purchases significant amounts of dairy products to support the needs of its Company-operated retail stores. Dairy prices in the United States, which closely follow the monthly Class I fluid milk base price as calculated by the U.S. Department of Agriculture, rose in both fiscal 2004 and 2005, then declined in

2006. Should prices rise significantly in the future, Starbucks profitability could be adversely affected. In the United States, the Company purchases substantially all of its fluid milk requirements from two dairy suppliers. The Company believes, based on relationships established with these suppliers, that the risk of non-delivery of enough fluid milk to support its U.S. retail business is remote.

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The Company also purchases a broad range of paper and plastic products, such as cups, lids, napkins, straws, shopping bags and corrugated paper boxes from several companies to support the needs of its retail stores as well as its manufacturing and distribution operations. The cost of these materials is dependent in part upon commodity paper and plastic resin costs, but the Company believes it mitigates the effect of short-term raw material price fluctuations through strategic relationships with key suppliers. In the United States, the Company is contractually required to purchase all of its cups, lids, straws and cutlery from a single supplier. Any material interruption in the supply of these products to the Company, if not offset by sufficient purchases from other suppliers, could materially adversely affect the Company s supply chain and its ability to serve its U.S. retail customers. The Company believes, based on its relationship with this supplier, that the risk of non-delivery of enough of these products to support its U.S. retail business is remote.

Products other than whole bean coffees and coffee beverages sold in Starbucks retail stores are obtained through a number of different channels. Beverage ingredients, other than coffee and milk, including leaf teas and the Company s menu of ready-to-drink beverages, are purchased from several specialty manufacturers, usually under long-term supply contracts. Food products, such as fresh pastries and lunch items, are generally purchased from both regional and local sources. Coffee-making equipment, such as drip and French press coffeemakers, espresso machines and coffee grinders, are generally purchased directly from their manufacturers. Coffee-related accessories, including items bearing the Company s logos and trademarks, are produced and distributed through contracts with a number of different suppliers.

COMPETITION

The Company s primary competitors for coffee beverage sales are restaurants, specialty coffee shops and doughnut shops. In almost all markets in which the Company does business, there are numerous competitors in the specialty coffee beverage business, and management expects this situation to continue. Although competition in the beverage market is currently fragmented, competition is increasing, particularly from competitors in the quick-service restaurant sector who are focusing on growing the specialty coffee part of their business. A major competitor with substantially greater financial, marketing and operating resources than the Company could enter this market at any time and compete directly against Starbucks.

The Company s whole bean coffees compete directly against specialty coffees sold through supermarkets, specialty retailers and a growing number of specialty coffee stores. Both the Company s whole bean coffees and its coffee beverages compete indirectly against all other coffees on the market. The Company believes that its customers choose among retailers primarily on the basis of product quality, service and convenience, and, to a lesser extent, on price.

Starbucks believes that supermarkets are the most competitive distribution channel for specialty whole bean coffee, in part because supermarkets offer customers a variety of choices without having to make a separate trip to a specialty coffee store. A number of coffee manufacturers are distributing premium coffee products in supermarkets. Regional specialty coffee companies also sell whole bean coffees in supermarkets.

In addition to the competition generated by supermarket sales of coffee, Starbucks competes for whole bean coffee sales with franchise operators and independent specialty coffee stores. In virtually every major metropolitan area where Starbucks operates and expects to expand, there are local or regional competitors with substantial market presence in the specialty coffee business. Starbucks Specialty Operations also face significant competition from established wholesale and mail order suppliers, some of whom have greater financial and marketing resources than the Company.

Starbucks faces intense competition from both restaurants and other specialty retailers for suitable sites for new stores and qualified personnel to operate both new and existing stores. There can be no assurance that Starbucks will be able to continue to secure adequate sites at acceptable rent levels or that the Company will be able to attract a sufficient number of qualified personnel.

PATENTS, TRADEMARKS, COPYRIGHTS AND DOMAIN NAMES

The Company owns and/or has applied to register numerous trademarks and service marks in the United States and in nearly 180 additional countries throughout the world. Rights to the trademarks and service marks in the United

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States are generally held by a wholly owned affiliate of the Company and are used by the Company under license. Some of the Company s trademarks, including Starbucks®, the Starbucks logo, Frappuccino®, Seattle s Best Coffee® and Tazo® are of material importance to the Company. The duration of trademark registrations varies from country to country. However, trademarks are generally valid and may be renewed indefinitely as long as they are in use and/or their registrations are properly maintained.

The Company owns numerous copyrights for items such as product packaging, promotional materials, in-store graphics and training materials. The Company also holds patents on certain products, systems and designs. In addition, the Company has registered and maintains numerous Internet domain names, including Starbucks.com and Starbucks.net.

RESEARCH AND DEVELOPMENT

Starbucks research and development efforts are led by food scientists, engineers, chemists and culinarians in the Research and Development department. This team is responsible for the technical development of food and beverage products and new equipment. The Company spent approximately $6.5 million, $6.2 million and $4.7 million during fiscal 2006, 2005 and 2004, respectively, on technical research and development activities, in addition to customary product testing and product and process improvements in all areas of its business.

SEASONALITY AND QUARTERLY RESULTS

Starbucks business is subject to seasonal fluctuations. Significant portions of the Company s net revenues and profits are realized during the first quarter of the fiscal year, which includes the holiday season. In addition, quarterly results are affected by the timing of the opening of new stores, and the Company s rapid growth may conceal the impact of other seasonal influences. Because of the seasonality of the business, results for any quarter are not necessarily indicative of the results that may be achieved for the full fiscal year.

EMPLOYEES

As of October 1, 2006, the Company employed approximately 145,800 people worldwide. In the United States, Starbucks employed approximately 123,600 people, with 116,100 in Company-operated retail stores and the remainder in the Company s administrative and regional offices, and store development, roasting and warehousing operations. Approximately 22,200 employees were employed in International, with 21,200 in Company-operated retail stores and the remainder in the Company s regional support facilities and roasting and warehousing operations. At fiscal year end, employees at nine of the Company s Canadian stores were represented by a union. Starbucks believes its current relations with its employees are good.

AVAILABLE INFORMATION

Starbucks Form 10-K reports, along with all other reports and amendments filed with or furnished to the Securities and Exchange Commission (SEC), are publicly available free of charge on the Investor Relations section of Starbucks website at http://investor.starbucks.com or at www.sec.gov as soon as reasonably practicable after these materials are filed with or furnished to the SEC. The Company s corporate governance policies, ethics code and Board of Directors committee charters are also posted within this section of the website. The information on the Company s website is not part of this or any other report Starbucks files with, or furnishes to, the SEC.

Starbucks demonstrates its commitment to corporate social responsibility (CSR) by conducting its business in ways that produce social, environmental and economic benefits to the communities in which Starbucks operates. The Company aligns its principles for social responsibility with its overall strategy and business operations. As a result, Starbucks believes it delivers benefits to the Company and its stakeholders partners, customers, suppliers, shareholders, community members and others while distinguishing Starbucks as a leader within the coffee industry. Providing open communication and transparency helps the Company be accountable to its stakeholders. To support this goal, Starbucks publishes a CSR Annual Report. Starbucks fiscal 2006 CSR Annual Report will be available online at

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www.starbucks.com/csr beginning March 14, 2007. To request a printed copy of the report, which will be available in late March 2007, please call 1-800-23-LATTE (1-800-235-2883) or email your request to info@starbucks.com.

Item 1A. Risk Factors

This Annual Report on Form 10-K includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements generally are identified by words such as believe , expect , anticipate , estimate , intend , strategy , may , will likely and similar words or phrases. A forward-look statement is neither a prediction nor a guarantee of future events or circumstances, and those future events or circumstances may not occur. Investors should not place undue reliance on the forward-looking statements, which speak only as of the date of this Report. Starbucks is under no obligation to update or alter any forward-looking statements, whether as a result of new information, future events or otherwise. These forward-looking statements are all based on currently available operating, financial and competitive information and are subject to various risks and uncertainties. The Company s actual future results and trends may differ materially depending on a variety of factors including, but not limited to, the risks and uncertainties discussed below. The risks below are not the only ones the Company faces. Additional risks and risks that management currently considers immaterial may also have an adverse effect on the Company.

A regional or global health pandemic could severely affect Starbucks business.

A health pandemic is a disease that spreads rapidly and widely by infection and affects many individuals in an area or population at the same time. If a regional or global health pandemic were to occur, depending upon its duration and severity, the Company s business could be severely affected. Starbucks has positioned itself as a third place between home and work where people can gather together for human connection. Customers might avoid public gathering places in the event of a health pandemic, and local, regional or national governments might limit or ban public gatherings to halt or delay the spread of disease. A regional or global health pandemic might also adversely impact the Company s business by disrupting or delaying production and delivery of materials and products in its supply chain and by causing staffing shortages in its stores. The impact of a health pandemic on Starbucks might be disproportionately greater than on other companies that depend less on the gathering of people together for the sale, use or license of their products and services.

Market expectations for Starbucks financial performance are high.

Management believes the price of Starbucks stock reflects high market expectations for its future operating results. In particular, any failure to meet the market s high expectations for Starbucks comparable store sales growth rates, earnings per share and new store openings could cause the market price of Starbucks stock to drop rapidly and sharply.

Starbucks is subject to a number of significant risks that might cause the Company s actual results to vary materially from its forecasts, targets, or projections, including:

- declines in actual or estimated comparable store sales growth rates and expectations;

- failing to meet annual targets for store openings, as a result of delays in store openings or failing to identify and secure sufficient real estate locations;

- negative trends in operating expenses or failing to continue to increase net revenues and operating income in any or all of Starbucks United States, International and CPG operating segments;

failing to penetrate and expand into emerging International markets, such as China;

opening less productive stores and cannibalizing existing stores with new stores;

higher costs associated with maintaining and refurbishing the Company s existing base of Company-operated retail stores;

failing to anticipate, appropriately invest in and effectively manage the human, information technology and logistical resources necessary to support the growth of its business, including managing the costs associated with such resources;

failing to integrate, leverage and generate expected rates of return on investments, including expansion of existing businesses and expansion through domestic and foreign acquisitions;

failing to generate sufficient future positive operating cash flows and, if necessary, secure adequate external financing to fund its growth;

declines in general consumer demand for specialty coffee products;

failing to meet customer demand efficiently during peak periods;

lack of customer acceptance of new products;

lack of customer acceptance of Starbucks products in new markets;

failing to consistently provide high quality products and innovate new products and business processes to retain the Company s existing customer base and attract new customers;

increases in the price of high quality *arabica* coffee, dairy products, fuel, energy or other consumables, and the Company s inability to obtain a sufficient supply of such commodities and consumables as its business grows;

failing to manage the impact of any adverse publicity regarding the Company s business practices or the health effects of consuming its products;

increased labor costs, including significant increases in health care benefits and worker s compensation insurance costs;

litigation against Starbucks, particularly any class action litigation;

unfavorable general economic conditions in the markets in which Starbucks operates, including, but not limited to, changes in interest rates, unemployment rates, disposable income and other events or factors that adversely affect consumer spending;

unanticipated changes in executive management;

any material interruption in the Company s supply chain, such as material interruption of roasted coffee supply due to the casualty loss of any of the Company s roasting plants, or material interruption in the supply of fluid milk or paper and plastic products such as cups, lids, napkins, straws, shopping bags and corrugated paper boxes, in each case due to the inability of one or more key suppliers to fulfill the Company s requirements;

the impact of initiatives by competitors and increased competition generally;

failing to manage the impact on Starbucks business of factors such as labor discord, war, terrorism, political instability in certain markets and natural disasters; and interruptions in service by common carriers that ship goods within the Company s distribution channels.

The Company s success depends substantially on the value of the Starbucks brand.

Starbucks believes it has built an excellent reputation globally for the quality of its products, for delivery of a consistently positive consumer experience and for its corporate social responsibility programs. The Starbucks brand has been highly rated in several global brand value studies. Management believes it must preserve and grow the value of the Starbucks brand to be successful in the future, particularly outside of North America, where the Starbucks brand is less well known. Brand value is based in part on consumer perceptions as to a variety of subjective qualities, and can be damaged badly even by isolated business incidents that degrade consumer trust, particularly if the incidents receive considerable publicity or result in litigation. Consumer demand for the Company s products and its brand equity could diminish significantly if

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Starbucks fails to preserve the quality of its products, is perceived to act in an unethical or socially irresponsible manner or fails to deliver a consistently positive consumer experience in each of its markets.

Starbucks is highly dependent on the financial performance of its United States operating segment.

The Company s financial performance is highly dependent on its United States operating segment, which comprised 79% of consolidated total net revenues in fiscal 2006. Any substantial or sustained decline in these operations, if not offset by increased financial performance elsewhere, could materially adversely affect the Company s business and financial results.

Starbucks is increasingly dependent on the success of its International operating segment in order to achieve its growth targets.

The Company s future growth depends increasingly on the growth and operations of its International operating segment. Some or all of the Company s International market business units (MBUs), which Starbucks generally defines by the countries or regions in which they operate, may not be successful in their operations or in achieving expected growth. Starbucks may find business partners who do not share its cultural, marketing or operating philosophies or who are unable to operate the MBU profitably. Some factors that will be critical to the success of International MBUs are different than those affecting the Company s U.S. stores and licensees. Tastes naturally vary by region, and consumers in new international markets into which Starbucks and its licensees expand may not embrace Starbucks products to the same extent as consumers in the Company s existing markets. Occupancy costs and store operating expenses are also sometimes higher internationally than in the United States due to higher rents for prime store locations or costs of compliance with country-specific regulatory requirements. Because many of the Company s International operations are in an early phase of development, operating expenses as a percentage of related revenues are often higher, compared to U.S. operations. The Company s International operations are also subject to additional inherent risks of conducting business abroad, such as:

- foreign currency exchange rate fluctuations;
- changes or uncertainties in economic, social and political conditions in the Company s markets;
- interpretation and application of laws and regulations;
- restrictive actions of foreign or United States governmental authorities affecting trade and foreign investment, including protective measures such as export and customs duties and tariffs and restrictions on the level of foreign ownership;
- import or other business licensing requirements;
- the enforceability of intellectual property and contract rights;
- limitations on the repatriation of funds and foreign currency exchange restrictions;
- lower levels of consumer spending on a *per capita* basis than in the United States;
- difficulty in staffing, developing and managing foreign operations due to distance, language and cultural differences; and
- local laws that make it more expensive and complex to negotiate with, retain or terminate employees.

The China market is important to the Company s long-term growth prospects doing business there and in other developing countries can be challenging.

Starbucks expects the People s Republic of China to be its largest market outside of the United States. Any significant or prolonged deterioration in U.S.-China relations might adversely affect the Company s China business. The Company s growing investments in its China operations will increase the Company s exposure in this market.

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Many of the risks and uncertainties of doing business in China are solely within the control of the Chinese government. China s government regulates the business conducted by Starbucks through its subsidiaries, joint ventures and authorized licensees by restricting the scope of the Company s foreign investments within China and the food and beverage, retail, wholesale and distribution business conducted within China. Although management believes it has structured the Company s China operations to comply with local laws, there are substantial uncertainties regarding the interpretation and application of laws and regulations and the enforceability of intellectual property and contract rights in China. If China s governmental authorities were ultimately to conclude that Starbucks has not complied with one or more existing or future laws or regulations, or if their interpretations of those laws or regulations were to change over time, the Company s affiliates could be subject to fines and other financial penalties or forced to cease operations entirely. Moreover, it could adversely affect the Company s business if it is unable to enforce its intellectual property and contract rights in China s courts.

Additionally, Starbucks plans to enter selected markets in other developing countries (such as Russia and India) as an important part of the projected growth of the International operating segment. Some of those markets pose legal and business challenges similar to the China market, such as substantial uncertainty regarding the interpretation and application of laws and regulations and the enforceability of intellectual property and contract rights.

Effectively managing the Company s rapid growth is challenging.

The Company s long-term goal is to open approximately 20,000 Starbucks stores in the United States and at least 20,000 stores in International markets. Starbucks expects annual total net revenue growth of approximately 20% and annual earnings per share growth of approximately 20-25% for the next three to five year period. Effectively managing growth on this scale is challenging, particularly as Starbucks expands into new markets internationally, and it becomes increasingly difficult to ensure a consistent supply of high quality raw materials, to hire sufficient numbers of key employees to meet the Company s growth targets, to maintain an effective system of internal controls for a globally dispersed enterprise and to train employees worldwide to deliver a consistently high quality product and customer experience. Achieving the Company s growth targets is also dependent on its ability to open more new stores in the current year as well as future years than it opened in prior years.

The loss of key personnel or difficulties recruiting and retaining qualified personnel could jeopardize the Company s ability to meet its growth targets.

The success of the Company s efforts to grow its business depends on the contributions and abilities of key executive and operating officers and other personnel. Starbucks must continue to recruit, retain and motivate management and operating personnel sufficient to maintain its current business and support its projected growth. A shortage or loss of these key employees might jeopardize the Company s ability to meet its growth targets.

Starbucks faces intense competition in the specialty coffee market.

There are numerous competitors in almost every market in which Starbucks operates and in which it expects to expand in both the specialty coffee beverage business and the specialty whole bean coffee business. This is especially true in the major metropolitan areas where Starbucks operates and expects to expand, in virtually all of which there are local or regional competitors with substantial collective market presence. Although competition in the specialty coffee beverage market is currently fragmented, competition is increasing, particularly from competitors in the quick-service restaurant sector who are focusing on growing the specialty coffee beverage part of their businesses. A major competitor with substantially greater financial, marketing and operating resources than Starbucks could enter this market at any time and compete directly against Starbucks. The Company s whole bean coffees compete directly against specialty coffees sold through supermarkets, specialty retailers and a growing number of specialty coffee stores. Some of the Company s competitors in these whole bean specialty coffee distribution channels have greater financial and marketing resources than Starbucks. Both the Company s whole bean coffees and its coffee beverages compete indirectly against all other coffees on the market. Starbucks also faces well-established competitors in many international markets. If Starbucks fails to maintain and build market share in the specialty coffee market and the coffee market generally, it could harm the Company s business and financial results.

Adverse public or medical opinions about the health effects of consuming the Company s products could harm its business.

Some of the Company s products contain caffeine, dairy products, sugar and other active compounds, the health effects of which are the subject of increasing public scrutiny, including the suggestion that excessive consumption of caffeine, dairy products, sugar and other active compounds can lead to a variety of adverse health effects. There has also been greater public awareness that sedentary lifestyles, combined with excessive consumption of high-calorie foods, have led to a rapidly rising rate of obesity. Particularly in the United States, there is increasing consumer awareness of health risks, including obesity, due in part to increasing publicity and attention from health organizations, as well as increased consumer litigation based on alleged adverse health impacts of consumption of various food products. While Starbucks has a variety of beverage and food items that are low in caffeine and calories, an unfavorable report on the health effects of caffeine or other compounds present in the Company s products, or negative publicity or litigation arising from other health risks such as obesity, could significantly reduce the demand for the Company s beverages and food products.

Significant increases in the market price or decreases in availability of high quality arabica coffee could harm the Company s business and financial results.

The supply and price of coffee are subject to significant volatility. Although most coffee trades in the commodity market, high-altitude *arabica* coffee of the quality sought by Starbucks tends to trade on a negotiated basis at a substantial premium above commodity coffee prices, depending on the supply and demand at the time of purchase. Supply and price can be affected by multiple factors in the producing countries, including weather, political and economic conditions. In addition, green coffee prices have been affected in the past, and may be affected in the future, by the actions of certain organizations and associations that have historically attempted to influence prices of green coffee through agreements establishing export quotas or restricting coffee supplies. Any significant increase in the market price or any significant decrease in the availability of high quality *arabica* coffee could adversely affect the Company s business and financial results. Starbucks also purchases large quantities of dairy products particularly milk. Any significant increase in the market price or decrease in availability of dairy products could harm the Company s business and financial results.

Failure of the Company s internal control over financial reporting could harm its business and financial results.

The management of Starbucks is responsible for establishing and maintaining effective internal control over financial reporting. Internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of financial reporting for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes maintaining records that in reasonable detail accurately and fairly reflect the Company s transactions; providing reasonable assurance that transactions are recorded as necessary for preparation of the financial statements; providing reasonable assurance that receipts and expenditures are made in accordance with management authorization; and providing reasonable assurance that unauthorized acquisition, use or disposition of the Company assets that could have a material effect on the financial statements would be prevented or detected on a timely basis. Because of its inherent limitations, internal control over financial reporting is not intended to provide absolute assurance that a misstatement of the Company s financial statements would be prevented or detected. The Company s rapid growth and entry into new, globally dispersed markets will place significant additional pressure on the Company s system of internal control over financial reporting. Any failure to maintain an effective system of internal control over financial reporting could limit the Company s ability to report its financial results accurately and timely or to detect and prevent fraud.

Item 1B. Unresolved Staff Comments

Not applicable.

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Item 2. Properties

The following table shows properties used by Starbucks in connection with its roasting and distribution operations:

Location	Approximate Size in Square Feet	Owned or Leased	Purpose
Kent, WA	332,000	Owned	Roasting and distribution
Kent, WA	402,000	Leased	Warehouse
Renton, WA	125,000	Leased	Warehouse
York County, PA	365,000	Owned	Roasting and distribution
York County, PA	297,000	Owned	Warehouse
York County, PA	42,000	Leased	Warehouse
Carson Valley, NV	360,000	Owned	Roasting and distribution
Portland, OR	80,000	Leased	Warehouse
Basildon, United Kingdom	141,000	Leased	Warehouse and distribution
Amsterdam, Netherlands	94,000	Leased	Roasting and distribution

The Company leases approximately 1,000,000 square feet of office space and owns a 200,000 square foot office building in Seattle, Washington for corporate administrative purposes.

As of October 1, 2006, Starbucks had more than 7,100 Company-operated retail stores, of which nearly all are located in leased premises. The Company also leases space in approximately 120 additional locations for regional, district and other administrative offices, training facilities and storage, not including certain seasonal retail storage locations.

Item 3. Legal Proceedings

See discussion of Legal Proceedings in Note 18 to the consolidated financial statements included in Item 8 of this Report.

Item 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of security holders during the fiscal fourth quarter of 2006.

EXECUTIVE OFFICERS OF THE REGISTRANT

The executive officers of the Company are as follows:

Name	Age	Position
Howard Schultz	53	chairman of the Board of Directors
James L. Donald	52	president, chief executive officer and director
James C. Alling	45	president, Starbucks Coffee U.S.
Martin Coles	51	president, Starbucks Coffee International
Gerardo I. Lopez	47	senior vice president; president, Global Consumer Products
Michael Casey	61	executive vice president, chief financial officer and chief administrative officer
Paula E. Boggs	47	executive vice president, general counsel and secretary
Dorothy J. Kim	44	executive vice president, Supply Chain Operations
David A. Pace	47	executive vice president, Partner Resources

Howard Schultz is the founder of the Company and the chairman of the board. From the Company s inception in 1985 to June 2000, he served as chairman of the board and chief executive officer. From June 2000 to February 2005, Mr. Schultz also held the title of chief global strategist. From 1985 to June 1994, Mr. Schultz was the Company s president. From January 1986 to July 1987, Mr. Schultz was the chairman of the board, chief executive officer and president of Il Giornale Coffee Company, a predecessor to the Company. From September 1982 to December 1985, Mr. Schultz was the director

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of retail operations and marketing for Starbucks Coffee Company, a predecessor to the Company. Mr. Schultz also serves on the board of directors of DreamWorks Animation SKG, Inc.

James L. Donald joined Starbucks in October 2002 and has been president and chief executive officer and a director of the Company since April 2005. From October 2004 to April 2005, Mr. Donald served as ceo designate. Prior to that, Mr. Donald served as president, North America from the time he joined the Company in October 2002. From October 1996 to October 2002, Mr. Donald served as chairman, president and ceo of Pathmark Stores, Inc. and prior to that time he held a variety of senior management positions with Albertson s, Inc., Safeway, Inc., and Wal-Mart Stores, Inc.

James C. Alling joined Starbucks in September 1997 as senior vice president, Grocery and was promoted to president, Starbucks Coffee U.S. in October 2004. Mr. Alling held a number of positions as senior vice president from September 1997 until November 2003, when he was promoted to executive vice president, Business and Operations United States. Prior to joining Starbucks, Mr. Alling held several senior positions at Nestlé from 1985 to 1997 and served as vice president and general manager of several divisions, including ground coffee.

Martin Coles joined Starbucks in April 2004 as president, Starbucks Coffee International. Prior to joining Starbucks, Mr. Coles served as an executive vice president of Reebok International, Ltd. from December 2001 to February 2004, including as president and chief executive officer of the Reebok® brand from June 2002 to February 2004 and executive vice president of Global Operating Units from December 2001 to May 2002. From February 2001 to December 2001, Mr. Coles was senior vice president, International Operations for Gateway, Inc. From February 2000 to January 2001, Mr. Coles was president and chief executive officer of Letsbuyit.com. From September 1992 to February 2000, Mr. Coles held several executive level general management, sales and operations positions for NIKE Inc. s Global and European operations.

Gerardo I. Lopez joined Starbucks in October 2004 as senior vice president; president, Global Consumer Products. Prior to joining Starbucks, Mr. Lopez was an executive with the Handleman Entertainment Resources division of Handleman Company, serving as president from November 2001 to September 2004 and as senior vice president and general manager from May 2000 to November 2001. From April 1997 to May 2000, Mr. Lopez was an executive with International Home Foods, Inc. serving as president of its International division from April 1999 to May 2000 and as senior vice president and general manager of its SouthWest Brands division from April 1997 to April 1999. Previously, Mr. Lopez held positions of increasing responsibility with Frito-Lay, Inc., Pepsi-Cola Company and The Procter & Gamble Company. Mr. Lopez serves on the board of directors of TXU Corp.

Michael Casey joined Starbucks in August 1995 as senior vice president and chief financial officer and was promoted to executive vice president, chief financial officer and chief administrative officer in September 1997. Prior to joining Starbucks, Mr. Casey served as executive vice president and chief financial officer of Family Restaurants, Inc. from its inception in 1986. During his tenure there, he also served as a director from 1986 to 1993, and as president and chief executive officer of its El Torito Restaurants, Inc. subsidiary from 1988 to 1993. Mr. Casey serves on the board of directors of The Nasdaq Stock Market, Inc.

Paula E. Boggs joined Starbucks in September 2002 as executive vice president, general counsel and secretary. Prior to joining Starbucks, Ms. Boggs served as vice president, legal, for products, operations and information technology at Dell Computer Corporation from 1997 to 2002. From 1995 to 1997, Ms. Boggs was a partner with the law firm of Preston Gates & Ellis. Ms. Boggs served in several roles at the Pentagon, White House and U.S. Department of Justice between 1984 and 1995.

Dorothy J. Kim joined Starbucks in November 1995 and was promoted to executive vice president, Supply Chain Operations in December 2004. From April 2003 to December 2004, Ms. Kim was senior vice president, Global

Logistics, Planning and Procurement. From April 2002 to April 2003, Ms. Kim was vice president, Supply Chain and Coffee Operations, Logistics, and from October 2000 to April 2002, Ms. Kim was vice president, Supply Chain and Coffee Operations, Finance and Systems. Prior to becoming a vice president, Ms. Kim held several positions in retail planning and operations.

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David A. Pace joined Starbucks in July 2002 as executive vice president of Partner Resources. From 2000 to 2002, Mr. Pace was the president of i2 Technologies. From 1999 to 2000 Mr. Pace served as the chief human resources officer for HomeGrocer.com. From 1995 to 1999, he served as senior vice president of human resources for Tricon Restaurants International (now YUM! Brands, Inc.).

There are no family relationships between any directors or executive officers of the Company.

PART II

Item 5. Market for the Registrant s Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities

SHAREHOLDER INFORMATION

MARKET INFORMATION AND DIVIDEND POLICY

The Company s common stock is traded on the Global Select Market of The NASDAQ Stock Market, Inc. (NASDAQ), under the symbol SBUX. The following table shows the quarterly high and low closing sale prices per share of the Company s common stock as reported by NASDAQ for each quarter during the last two fiscal years:

	High	Low
October 1, 2006:		
Fourth Quarter	$ 38.02	$ 29.55
Third Quarter	39.63	34.93
Second Quarter	37.63	30.24
First Quarter	31.96	24.91
October 2, 2005:		
Fourth Quarter	$ 26.35	$ 23.08
Third Quarter	28.13	22.78
Second Quarter	30.80	24.79
First Quarter	31.94	23.53

As of December 8, 2006, the Company had approximately 16,653 shareholders of record. Starbucks has never paid any dividends on its common stock. The Company presently intends to retain earnings for use in its business and to repurchase shares of common stock and, therefore, does not anticipate paying a cash dividend in the near future.

The following table provides information regarding repurchases by the Company of its common stock during the 13-week period ended October 1, 2006:

ISSUER PURCHASES OF EQUITY SECURITIES

	Total Number of Shares	Maximum Number of

Period (1)	Total Number of Shares Purchased	Average Price Paid per Share	Purchased as Part of Publicly Announced Plans or Programs (2)	Shares that May Yet Be Purchased Under the Plans or Programs (2)
July 3, 2006 July 30, 2006	6,601,624	$ 34.54	6,601,624	29,440,530
July 31, 2006 August 27, 2006	7,262,404	30.87	7,262,404	22,178,126
August 28, 2006 October 1, 2006	690,000	31.48	690,000	21,488,126
Total	14,554,028	32.57	14,554,028	

(1) Monthly information is presented by reference to the Company s fiscal months during the fourth quarter of fiscal 2006.

(2) The Company s share repurchase program is conducted under authorizations made from time to time by the Company s Board of Directors. The shares reported in the table are covered by Board authorizations to repurchase shares of common stock, as follows: 20 million shares publicly announced on May 5, 2005, 10 million shares publicly announced on September 22, 2005 and 25 million shares publicly announced August 2, 2006. Shares remaining for repurchase relate to the August 2, 2006 authorization, which has no expiration date.

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Item 6. Selected Financial Data

In thousands, except earnings per share and store operating data

The following selected financial data are derived from the consolidated financial statements of the Company. The data below should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations, Risk Factors, and the Company s consolidated financial statements and notes. In particular, see Note 1 to the consolidated financial statements included in Item 8 of this Report for a description of accounting changes that materially affect the comparability of the data presented below.

OF AND FOR THE FISCAL YEAR ENDED [1]	Oct 1, 2006 (52 Wks)	Oct 2, 2005 (52 Wks)	Oct 3, 2004 (53 Wks)	Sept 28, 2003 (52 Wks)	Sept 29, 2002 (52 Wks)
SULTS OF OPERATIONS					
t revenues:					
mpany-operated retail	$ 6,583,098	$ 5,391,927	$ 4,457,378	$ 3,449,624	$ 2,792,904
ecialty:					
ensing	860,676	673,015	565,798	409,551	311,932
odservice and other	343,168	304,358	271,071	216,347	184,072
al specialty	1,203,844	977,373	836,869	625,898	496,004
al net revenues	7,786,942	6,369,300	5,294,247	4,075,522	3,288,908
erating income	893,952	780,518	606,494	420,672	313,301
n on sale of investment [2]					13,361
nings before cumulative effect of change in ounting principle	581,473	494,370	388,880	265,177	210,460
mulative effect of accounting change for FIN 47, of taxes [3]	17,214				
t earnings	$ 564,259	$ 494,370	$ 388,880	$ 265,177	$ 210,460
nings per common share before cumulative effect change in accounting principle diluted	$ 0.73	$ 0.61	$ 0.47	$ 0.33	$ 0.26
mulative effect of accounting change for FIN 47, of taxes per common share	0.02				
t earnings per common share diluted	$ 0.71	$ 0.61	$ 0.47	$ 0.33	$ 0.26
sh dividends per share					
LANCE SHEET					
rking capital [4]	$ (405,832)	$ (17,662)	$ 604,636	$ 335,767	$ 328,777
al assets	4,428,941	3,513,693	3,386,266	2,775,931	2,249,432
ort-term borrowings [5]	700,000	277,000			
ng-term debt (including current portion)	2,720	3,618	4,353	5,076	5,786

areholders equity	$ 2,228,506	$ 2,090,262	$ 2,469,936	$ 2,068,507	$ 1,712,453
ORE INFORMATION					
centage change in comparable store sales [6]					
ited States	7%	9%	11%	9%	7
ernational	8%	6%	6%	7%	1
nsolidated	7%	8%	10%	8%	6
res opened during the year: [7][8]					
ited States					
mpany-operated stores	810	580	521	514	507
ensed stores	733	596	417	315	264
ernational					
mpany-operated stores	230	166	144	126	118
ensed stores	426	330	262	246	288
al	2,199	1,672	1,344	1,201	1,177

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AS OF AND FOR THE FISCAL YEAR ENDED (1)	Oct 1, 2006 (52 Wks)	Oct 2, 2005 (52 Wks)	Oct 3, 2004 (53 Wks)	Sept 28, 2003 (52 Wks)	Sept 29, 2002 (52 Wks)
Stores open at year end:(8)					
United States					
Company-operated stores	5,728	4,918	4,338	3,817	3,239
Licensed stores	3,168	2,435	1,839	1,422	1,033
International					
Company-operated stores	1,374	1,144	978	834	708
Licensed stores	2,170	1,744	1,414	1,152	906
Total	12,440	10,241	8,569	7,225	5,886

(1) The Company s fiscal year ends on the Sunday closest to September 30.

(2) On October 10, 2001, the Company sold 30,000 of its shares of Starbucks Coffee Japan, Ltd. at approximately $495 per share, net of related costs, which resulted in a gain of $13.4 million.

(3) As discussed in Note 1 Asset Retirement Obligations under the Notes to Consolidated Financial Statements included in Item 8, Financial Statements and Supplementary Data of this Form 10-K, Starbucks adopted FASB Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations an interpretation of FASB Statement No. 143 at the end of the fourth fiscal quarter of 2006.

(4) Working capital deficit as of October 1, 2006 was primarily due to increased current liabilities from short term borrowings under the revolving credit facility. See (5) below.

(5) In August 2006, the Company increased its borrowing capacity under the five-year revolving credit facility to $1 billion and had borrowings of $700 million outstanding as of October 1, 2006.

(6) Includes only Starbucks Company-operated retail stores open 13 months or longer. Comparable store sales percentage for fiscal 2004 excludes the extra sales week.

(7) Store openings are reported net of closures.

(8) International store information has been adjusted for the fiscal 2006 acquisitions of Hawaii and Puerto Rico and fiscal 2005 acquisitions of Germany, Southern China and Chile licensed operations by reclassifying historical information from Licensed stores to Company-operated stores. United States store information was also adjusted to align with the Hawaii operations segment change by reclassifying historical information from International Company-operated stores to the United States.

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations

GENERAL

Starbucks Corporation s fiscal year ends on the Sunday closest to September 30. The fiscal years ended on October 1, 2006 and October 2, 2005, included 52 weeks. The fiscal year ended October 3, 2004, included 53 weeks, with the 53rd week falling in the fiscal fourth quarter.

MANAGEMENT OVERVIEW

During the fiscal year ended October 1, 2006, the Company s focus on execution in all areas of its business, from U.S. and International Company-operated retail operations to the Company s specialty businesses, delivered strong financial performance. Management believes that its ability to achieve the balance between growing the core business and building the foundation for future growth is the key to increasing long-term shareholder value. Starbucks fiscal 2006 performance reflects the Company s continuing commitment to achieving this balance.

The primary driver of the Company s revenue growth continues to be the opening of new retail stores, both Company-operated and licensed, in pursuit of the Company s objective to establish Starbucks as one of the most recognized and respected brands in the world. Starbucks opened 2,199 new stores in fiscal 2006 and plans to open approximately 2,400 in fiscal 2007. With a presence in 37 countries, serving customers more than 40 million times per week, management

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continues to believe that the Company s long-term goal of approximately 20,000 Starbucks retail locations throughout the United States and at least 20,000 stores in International markets is achievable.

In addition to opening new retail stores, Starbucks works to increase revenues generated at new and existing Company-operated stores by attracting new customers and increasing the frequency of visits by current customers. The strategy is to increase comparable store sales by continuously improving the level of customer service, introducing innovative products and improving speed with service through training, technology and process improvement.

Global comparable store sales for Company-operated markets increased by 7%, making fiscal 2006 the 15th consecutive year with comparable store sales growth of 5% or greater. Comparable store sales growth for fiscal 2007 is expected to be in the range of 3% to 7%.

In licensed retail operations, Starbucks shares operating and store development experience to help licensees improve the profitability of existing stores and build new stores. Internationally, the Company s strategy is to selectively increase its equity stake in licensed international operations as these markets develop. In January 2006, the Company increased its equity ownership from 5% to 100% in its operations in Hawaii and Puerto Rico, and subsequent to the end of fiscal 2006 purchased a 90% stake in its previously-licensed operations in Beijing, China.

The combination of more retail stores, comparable store sales growth of 7% and growth in other business channels in the U.S., International, and CPG operating segments resulted in a 22% increase in total net revenues for fiscal 2006, compared to fiscal 2005. The Company expects revenue growth of approximately 20% in fiscal 2007, consistent with its three to five year revenue growth target.

Operating income as a percentage of total net revenues decreased to 11.5% in fiscal 2006 from 12.3% in fiscal 2005, due to the recognition of stock-based compensation. Net earnings increased by 14% in fiscal 2006, compared to fiscal 2005. Reported operating margin and net earnings include the effects of stock-based compensation in fiscal 2006, while stock-based compensation expense was not included in the Company s consolidated financial results in fiscal 2005.

ACQUISITIONS

In January 2006, Starbucks increased its equity ownership to 100% in its operations in Hawaii and Puerto Rico and applied the consolidation method of accounting from the acquisition date. Previously the Company owned 5% of both Coffee Partners Hawaii and Café del Caribe in Puerto Rico. Because Coffee Partners Hawaii was a general partnership, the equity method of accounting was previously applied. Retroactive application of the equity method of accounting for the Puerto Rico investment, which was previously accounted for under the cost method, resulted in a reduction of retained earnings of $0.5 million as of April 2, 2006. The cumulative effect of the accounting change for financial results previously reported under the cost method and as restated in this report under the equity method reduced net earnings by $97 thousand for the fiscal year ended October 2, 2005 and $93 thousand for the fiscal year ended October 2, 2004. Previously reported earnings per share amounts were not impacted.

On October 18, 2006, the Company acquired 90% equity ownership of the licensed operations of 61 Starbucks retail stores in Beijing and Tianjin, China (See Note 20 Subsequent Event).

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RESULTS OF OPERATIONS   FISCAL 2006 COMPARED TO FISCAL 2005

The following table presents the consolidated statement of earnings as well as the percentage relationship to total net revenues, unless otherwise indicated, of items included in the Company s consolidated statements of earnings (*amounts in thousands*):

FISCAL YEAR ENDED	Oct 1, 2006 (52 Wks)	% of Revenues	Oct 2, 2005 (52 Wks)	% of Revenues	Oct 3, 2004 (53 Wks)	% of Revenues
STATEMENTS OF EARNINGS DATA						
Net revenues:						
Company-operated retail	$ 6,583,098	84.5%	$ 5,391,927	84.7%	$ 4,457,378	84.2%
Specialty:						
Licensing	860,676	11.1	673,015	10.5	565,798	10.7
Foodservice and other	343,168	4.4	304,358	4.8	271,071	5.1
Total specialty	1,203,844	15.5	977,373	15.3	836,869	15.8
Total net revenues	7,786,942	100.0	6,369,300	100.0	5,294,247	100.0
Cost of sales including occupancy costs	3,178,791	40.8	2,605,212	40.9	2,191,440	41.4
Store operating expenses	2,687,815	40.8 (1)	2,165,911	40.2 (1)	1,790,168	40.2 (1)
Other operating expenses	260,087	21.6 (2)	197,024	20.2 (2)	171,648	20.5 (2)
Depreciation and amortization expenses	387,211	5.0	340,169	5.3	289,182	5.5
General and administrative expenses	473,023	6.1	357,114	5.6	304,293	5.7
Subtotal operating expenses	6,986,927	89.7	5,665,430	88.9	4,746,731	89.7
Income from equity investees	93,937	1.2	76,648	1.2	58,978	1.1
Operating income	893,952	11.5	780,518	12.3	606,494	11.5
Interest and other income, net	12,291	0.1	15,829	0.2	14,140	0.2
Earnings before income taxes	906,243	11.6	796,347	12.5	620,634	11.7
Income taxes	324,770	4.1	301,977	4.7	231,754	4.4
Earnings before cumulative effect of change in accounting principle	581,473	7.5%	494,370	7.8%	388,880	7.3%
Cumulative effect of accounting change for FIN 47, net of taxes	17,214	0.3				

Net earnings	$	564,259	7.2%	$	494,370	7.8%	$	388,880	7.3%

(1) Shown as a percentage of related Company-operated retail revenues.

(2) Shown as a percentage of related total specialty revenues.

CONSOLIDATED RESULTS OF OPERATIONS

Net revenues for the fiscal year ended 2006 increased 22% to $7.8 billion from $6.4 billion for fiscal 2005, driven by increases in both Company-operated retail revenues and specialty operations. Net revenues are expected to grow approximately 20% in fiscal 2007 compared to fiscal 2006.

During the fiscal year ended 2006, Starbucks derived 85% of total net revenues from its Company-operated retail stores. Company-operated retail revenues increased 22% to $6.6 billion for the fiscal year ended 2006, from $5.4 billion for fiscal 2005. This increase was primarily due to the opening of 1,040 new Company-operated retail stores in the last 12 months and comparable store sales growth of 7% in fiscal 2006. The increase in comparable store sales was due to a 5% increase in the number of customer transactions and a 2% increase in the average value per transaction. Management believes increased customer traffic continues to be driven by sustained popularity of core products, new product innovation and a high level of customer satisfaction.

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The Company derived the remaining 15% of total net revenues from channels outside the Company-operated retail stores, collectively known as Specialty Operations. Specialty revenues, which include licensing revenues and foodservice and other revenues, increased 23% to $1.2 billion for the fiscal year ended 2006, from $977 million for fiscal 2005.

Licensing revenues, which are derived from retail store licensing arrangements, as well as grocery, warehouse club and certain other branded product operations, increased 28% to $861 million for fiscal 2006, from $673 million for fiscal 2005. The increase is primarily due to higher product sales and royalty revenues from the opening of 1,159 new licensed retail stores in the last 12 months and, to a lesser extent, growth in the licensed grocery and warehouse club business.

Foodservice and other revenues increased 13% to $343 million for fiscal 2006, from $304 million for fiscal 2005. Foodservice and other revenues increased primarily due to growth in new and existing U.S. foodservice accounts.

Cost of sales including occupancy costs decreased slightly to 40.8% of total net revenues for fiscal 2006, from 40.9% in fiscal 2005. The decrease was primarily due to fixed rent costs in fiscal 2006 being distributed over an expanded revenue base, as well as increased occupancy costs in fiscal 2005 resulting from intensified store maintenance activities. These favorable items, combined with lower dairy costs, offset higher green coffee costs for fiscal 2006.

Store operating expenses as a percentage of Company-operated retail revenues increased to 40.8% for fiscal 2006 from 40.2% for fiscal 2005. The increase was due to the recognition of stock-based compensation expense and to higher provisions for incentive compensation.

Other operating expenses, which are expenses associated with the Company s Specialty Operations, increased to 21.6% of specialty revenues in fiscal 2006, compared to 20.2% in fiscal 2005. The increase was primarily due to the recognition of stock-based compensation expense as well as higher payroll-related expenditures to support the expanding licensed store operations, both in the U.S. and in existing and new international markets.

Depreciation and amortization expenses increased to $387 million in fiscal 2006, from $340 million in fiscal 2005. The increase of $47 million was due to the opening of 1,040 new Company-operated retail stores in the last 12 months. As a percentage of total net revenues, depreciation and amortization decreased to 5.0% for fiscal 2006, from 5.3% for fiscal 2005.

General and administrative expenses increased to $473 million in fiscal 2006, compared to $357 million in fiscal 2005. The increase was due to higher payroll-related expenditures from the recognition of stock-based compensation expense, additional employees to support continued global growth, and higher professional fees in support of global systems infrastructure development. As a percentage of total net revenues, general and administrative expenses increased to 6.1% for fiscal 2006, from 5.6% for fiscal 2005.

Income from equity investees increased to $94 million in fiscal 2006, compared to $77 million in fiscal 2005. The increase was primarily due to favorable volume-driven operating results for The North American Coffee Partnership, which produces ready-to-drink beverages which include, among others, bottled Frappuccino® coffee drinks and Starbucks DoubleShot® espresso drinks, as well as improved operating results from international investees, including Korea and Japan, mainly as a result of new store openings.

Operating income increased 15% to $894 million in fiscal 2006, from $781 million in fiscal 2005. The operating margin decreased to 11.5% of total net revenues in fiscal 2006, compared to 12.3% in fiscal 2005, due to the recognition of stock-based compensation expense.

Net interest and other income, which primarily consists of interest income, decreased to $12 million in fiscal 2006, from $16 million in fiscal 2005. The decrease was primarily due to higher interest expense on the Company s revolving credit facility, as well as lower interest income earned due to lower average investment balances, offset in part by the recognition of $4.4 million of income on unredeemed stored value card balances in fiscal 2006. There was no income recognized on unredeemed stored value card balances in fiscal 2005.

Income taxes for fiscal 2006 resulted in an effective tax rate of 35.8%, compared to 37.9% in fiscal 2005. The decline in the effective tax rate was due to the reversal of a valuation allowance in fiscal 2006 that had been established in fiscal 2005,

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the settlement in the third quarter of fiscal 2006 of a multi-year income tax audit in a foreign jurisdiction for which the Company had established a contingent liability, and to increased effectiveness of the Company s long-term tax planning strategies. The effective tax rate for fiscal 2007 is expected to be approximately 38%, with quarterly variations.

OPERATING SEGMENTS

Segment information is prepared on the same basis that the Company s management reviews financial information for operational decision-making purposes. Beginning in the fiscal fourth quarter of 2006, the Company increased its reporting segments from two to three to include a Global CPG segment in addition to the United States and International segments. This additional operating segment reflects the culmination of internal management realignments in fiscal 2006, and the successful development and launch of certain branded products in the United States and internationally commencing in fiscal 2005 and continuing throughout fiscal 2006. Additionally, with the 100% acquisition of the Company s operations in Hawaii in fiscal 2006 and the shift in internal management of this market to the United States, these operations have been moved from the International segment into the United States segment. Segment information for all prior periods presented has been revised to reflect these changes.

The following tables summarize the Company s results of operations by segment for fiscal 2006 and 2005 (*in thousands*):

	52 Weeks Ended			52 Weeks Ended	
	Oct 1, 2006	Oct 2, 2005	% Change	Oct 1, 2006	Oct 2, 2005
UNITED STATES				As a % of U.S. Total Net Revenues	
Net revenues:					
Company-operated retail	$ 5,495,240	$ 4,539,455	21.1%	88.9%	89.1%
Specialty:					
Licensing	369,155	277,987	32.8	6.0	5.4
Foodservice and other	314,162	280,073	12.2	5.1	5.5
Total specialty	683,317	558,060	22.4	11.1	10.9
Total net revenues	6,178,557	5,097,515	21.2	100.0	100.0
Cost of sales including occupancy costs	2,374,485	1,944,356		38.4	38.1
Store operating expenses	2,280,044	1,848,836		41.5 (1)	40.7 (1)
Other operating expenses	190,624	150,712		27.9 (2)	27.0 (2)
Depreciation and amortization expenses	284,625	250,339		4.6	4.9
General and administrative expenses	93,754	85,362		1.5	1.7
Income from equity investees	151	592			

Operating income	$ 955,176	$ 818,502	16.7%	15.5%	16.1%

(1) Shown as a percentage of related Company-operated retail revenues.

(2) Shown as a percentage of related total specialty revenues.

	52 Weeks Ended	52 Weeks Ended
	Oct 1, 2006	Oct 2, 2005