

BusinessWeek

SALES & MARKETING July 18, 2008, 2:00PM EST

Vying with Starbucks: A Love-Hate Thing

As Starbucks' expansion loses steam, independent coffee shops reveal the subtle ways they compete with the coffee powerhouse

by [Ricky McRoskey](#)

In July 2004, Kinley Pon was throwing his annual block party at his El Paso (Tex.) coffee shop, Kinley's House, on the same day that a Starbucks ([SBUX](#)) across the street was having its grand opening. Pon, 51, says he had planned the party for months—a day-long event with musicians, belly dancers, and local law enforcement intended both to promote his business and to raise awareness about drunk driving. Pon was surprised when an employee from the new Starbucks store walked across the street and started passing out Starbucks promotional cards to customers—on Pon's own patio. A spokesperson for Starbucks couldn't cite a specific policy regarding the distribution of promotions on a competitor's premises. "They did it for a week," says Pon. "But I allowed it to occur, because my reasoning was that they were going to pass them out anyways."

There's a love-hate relationship between Starbucks and the thousands of independent coffee shop owners in the U.S. For years, the Seattle-based chain has brought coffee drinking into the mainstream and revitalized the business of java, yet its ubiquity has also made survival more difficult for mom-and-pop coffee houses. In 2007, there were roughly 26,300 coffee cafés, kiosks, and carts across the U.S., and about 60% of those were independent, according to Mike Ferguson, the marketing communications director at the Specialty Coffee Association of America. On July 1, Starbucks announced it would be [shuttering 600 locations](#) (BusinessWeek.com, 7/1/08). On July 17, it listed the names and locations of the [600 specific stores it was planning to close](#) of its roughly 11,000 U.S. stores. The closures prompted the question: What have independent coffee shops been doing to compete with the \$9.4 billion company, the largest coffee retailer in the world?

Many cafes have survived by serving coffee differently from Starbucks. Skip DuCharme, who has run his 27-employee Lakota Coffee Co. in Missouri since 1992, says that the store's most popular drink is a latte served in a signature large green bowl that requires two hands to hold. A Starbucks opened down the street from DuCharme's place in January 2006, and since then, DuCharme says, his tactics have helped his business create a more at-home atmosphere than his competitor's.

"In Starbucks, everything is based on 'to-go,'" he says. "We give [our customers] real latte mugs."

POWER OF FREEBIES

Other stores give customers free refills on coffee—a strategy Starbucks tested in select stores in January. "A free cup of coffee goes a long way," says Theresa Tocio, co-owner of Tocio's Sunburst Café in Naples, Fla., that offers customers unlimited refills for the \$1.50 they pay for a 12-ounce coffee. When a Starbucks opened inside a Target ([TGT](#)) next to her shop, Tocio and her husband offered free coffees to Target employees on break, since she says the workers weren't offered Starbucks discounts.

"The independents that are successful are really serving a different type of product," says Andrew Hetzel, a coffee

industry consultant. "They have their own unique style and brand." For some, that means selling food or drinks that Starbucks doesn't have. Many stores that begin as coffee-and-pastry shops evolve into full-scale food cafés, giving customers more choice than chains can offer. At Jammin' Java, a coffee house based in Fayetteville, Ark., customers can buy everything from breakfast burritos to turkey sandwiches along with their coffee. "I started to see that I was doing almost as much business at lunch as I was doing coffee in the morning," says owner Brandon Karn, who launched the store in 2002. Since a Starbucks opened nearby several years ago, Karn has also expanded the menu to include beer and wine. "That has taken off real well," he says.

Having a nimble management team enables cafés to implement changes more quickly than bureaucratic corporations, says Jean Bernstein, owner of 21-year-old Albuquerque-based Flying Star Café and Satellite Coffee, which started up in 1998. "We keep changing things to constantly offer something fun and unique," says Bernstein, who first started competing against Starbucks when one opened near the Flying Star in 1996. She says she picked up on several of Starbucks' shortcomings ("their tea drinks were weak") and responded by offering blended concoctions to complement her store's coffee drinks. One is a homemade lemonade mixed with ginger, and another is a blend of herbal teas, cranberry juice, and mint.

CHANGE THE SETTINGS

Independent coffee shop owners say that Starbucks has gradually drifted away from the high-quality coffee that first made it successful, focusing instead on swank marketing campaigns or coffee drinks blended with milk or caramel. "They've basically become a sugar-and-dairy company," says Arne Holt, owner of Caffè Calabria in San Diego. Says coffee consultant Hetzel: "Starbucks decisions aren't coffee decisions, they are big public-business decisions." That's why many entrepreneurs can differentiate their coffee shops by paying meticulous detail to the coffee itself. Holt, for instance, grinds coffee beans at different settings, based on the amount of moisture in the air, since water passes through the grounds differently when the humidity is higher. Starbucks and other big chains rarely change the grinding settings on their automatic espresso machines, he says. "It's like McDonald's," he says. "It's not the best hamburger, but it's consistent."

The roughly 11,000 Starbucks stores across the country get their beans from the company's three major U.S. roasting facilities—in Nevada, Washington, and Pennsylvania. Smaller roasters can deliver a fresher cup of coffee, says Gina Nasson, who owns the Farfalle Italian Market in Concord, Mass., with her husband. Nasson's café gets its beans from a roastery about 11 miles away, she says. "When we order coffee, we don't order tons."

Smaller coffee stores also work to create loyal customer bases by emphasizing local ties. Karen Anderson, whose husband's family was among the first English settlers in Concord centuries ago, says their Main Street's Market & Café resonates with the town's historic atmosphere. "If you sit here and have a cup of coffee," she says, "you'll hear guys in their 80s and 90s just reminiscing." Red brick walls, pickle barrels, and 1930s-era photographs give the store a different feel from the surrounding [Dunkin' Donuts](#) and Starbucks stores. Mary Allen Lindemann and her husband, who run Coffee by Design in Portland, Me., sponsor local arts organizations and offer a grant each year to a Maine artist (last year's grant was \$2,800). It has given the store a unique following among local artists.

CREATE A DIFFERENT EXPERIENCE

The bottom line? The relationship between boutique coffee shops and Starbucks has helped bolster the overall coffee market and cultivate unique ways to serve customers. For local coffee shops, many of which are worried that a Starbucks slowdown could curtail overall coffee spending, competing against Starbucks simply means taking an approach that Starbucks hasn't.

"Focus on making your product, your brand, and your experience as good as it can possibly be," says consultant

Andrew Hetzel. "You can't look to what Starbucks is doing as your barometer."

For a look at sales and marketing techniques that a handful of independent coffee shops use to compete with chains such as Starbucks, flip through this [slide show](#).

[McRoskey](#) is an intern at *BusinessWeek.com*.

Xerox Color. It makes business sense.

Copyright 2000-2008 by The McGraw-Hill Companies Inc. All rights reserved.

The McGraw-Hill Companies