CASE 16

Panera Bread Company (2010): Still Rising Fortunes?

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BREAD—ESSENTIAL AND BASIC, but nonetheless special—has transcended millennia. A master baker combined simple ingredients to create what has been an integral part of society and culture for over 6000 years. Sourdough bread, a uniquely American creation, was made from a "culture" or "starter." Sourdough starter contained natural yeasts, flour, and water and was the medium that made bread rise. In order to survive, a starter had to be cultured, fed, and tended to by attentive hands in the right environment. Without proper care and maintenance, the yeast, or the growth factor, would slow down and die. Without a strong starter, bread would no longer rise.

Ronald Shaich, CEO and Chairman of Panera Bread Company, created the company's "starter." Shaich, the master baker, combined the ingredients and cultivated the leavening agent that catalyzed the company's phenomenal growth. Under Shaich's guidance, Panera's total systemwide (both company and franchisee) revenues rose from US$350.8 million in 2000 to US$1,353.5 million in 2009, consisting of US$1,153.3 million from company-owned bakery-café sales, US$78.4 million from franchise royalties and fees, and US$121.9 million from fresh dough sales to franchisees. Franchise-operated bakery-café sales, as reported by franchisees, were US$1,640.3 million in fiscal 2009.[1] Panera shares have outperformed every major restaurant stock over the last 10 years.[2] Panera's share price has risen over 1600% from US$3.88 a share on December 31, 1999, to US$67.95 a share on December 28, 2009.[3] Along the way, Panera largely led the evolution of what became known as the "fast casual" restaurant category.

~~Ronald Shaich~~ had clearly nurtured the company's "starter" and had been the vision and driving force behind Panera's success from the company's beginnings until his resignation as CEO and Chairman effective May 13, 2010. For Panera to continue to rise, the company's new CEO, William Moreton, would need to continue to feed and maintain Panera's "starter." In addition to new unit growth, new strategies and initiatives must be folded into the mix.

History

Panera Bread grew out of the company that could be considered the grandfather of the fast casual concept: Au Bon Pain. In 1976, French oven manufacturer Pavailler opened the first Au Bon Pain (a French colloquialism for "where good bread is") in Boston's Faneuil Hall as a demonstration bakery. Struck by its growth potential, Louis Kane, a veteran venture capitalist, purchased the business in 1978.[4] Between 1978 and 1981, Au Bon Pain opened 13, and subsequently closed 10, stores in the Boston area and piled up US$3 million in debt.[5] Kane was ready to declare bankruptcy when he gained a new business partner in Ronald Shaich.[6]

Shortly after opening the Cookie Jar bakery in Cambridge, Massachusetts, in 1980, Shaich, a recent Harvard Business graduate, befriended Louis Kane. Shaich was interested in adding bread and croissants to his menu to stimulate morning sales. He recalled that "50,000 people a day were going past my store, and I had nothing to sell them in the morning."[7] In February 1981, the two merged the Au Bon Pain bakeries and the cookie store to form one business, Au Bon Pain Co. Inc. The two served as co-CEOs until Kane's retirement in 1994. They had a synergistic relationship that made Au Bon Pain successful: Shaich was the hard-driving, analytical strategist focused on operations, and Kane was the seasoned businessperson with a wealth of real estate and finance connections.[8] Between 1981 and 1984, the team expanded the business, worked to decrease the company's debt, and centralized facilities for dough production.[9]

In 1985, the partners added sandwiches to bolster daytime sales as they noticed a pattern in customer behavior—that is, customers were buying sliced baguettes and making their own sandwiches. It was a "eureka" moment, and the birth of the fast casual restaurant category.[10] According to Shaich, Au Bon Pain was the "first place that gave white collar folks a choice between fast food and fine dining."[11] Au Bon Pain became a lunchtime alternative for urban dwellers who were tired of burgers and fast food. Differentiated from other fast-food competitors by its commitment to fresh, quality sandwiches, bread, and coffee, Au Bon Pain attracted customers who were happy to pay more money (US$5 per sandwich) than they would have paid for fast food.[12]

In 1991, Kane and Shaich took the company public. By that time, the company had US$68 million in sales and was a leader in the quick service bakery segment. By 1994, the company had 200 stores and US$183 million in sales, but that growth masked a problem. The company was built on a limited growth concept, what Shaich called, "high density urban feeding."[13] The main customers of the company were office workers in locations like New York, Boston, and Washington, DC. The real estate in such areas was expensive and hard to come by. This strategic factor limited expansion possibilities.[14]

Au Bon Pain acquired the Saint Louis Bread Company in 1993 for US$24 million. Shaich saw this as the company's "gateway into the suburban marketplace."[15] The acquired company, founded in 1987 by Ken Rosenthal, consisted of a 19-store bakery-café chain located in the Saint Louis, Missouri, area. The concept of the café was based on San Francisco sourdough bread bakeries. The acquired company would eventually become the platform for what is now Panera.

Au Bon Pain management spent two years studying Saint Louis Bread Co., looking for the ideal concept that would unite Au Bon Pain's operational abilities and quality food with the broader suburban growth appeal of Saint Louis Bread. The management team understood that a growing number of consumers wanted a unique expression of tastes and styles, and were tired of the commoditization of fast-food service. Shaich and his team wrote a manifesto that spelled out what Saint Louis Bread would be, from the type of food it would serve, to the kind of people behind the counters, and to the look and feel of the physical space.[16]

Au Bon Pain began pouring capital into the chain when Shaich had another "eureka" moment in 1995. He entered a Saint Louis Bread store and noticed a group of business people meeting in a corner. The customers explained that they had no other place to talk.[17] This experience helped Shaich realize that the potential of the neighborhood bakery-café concept was greater than that of Au Bon Pain's urban store concept. The bakery-café concept capitalized on a confluence of current trends: the welcoming atmosphere of coffee shops, the food of sandwich shops, and the quick service of fast food.[18]

While Au Bon Pain was focusing on making Saint Louis Bread a viable national brand, the company's namesake unit was faltering. Rapid expansion of its urban outlets had resulted in operational problems, bad real estate deals,[19] debt over US$65 million,[20] and declining operating margins.[21] Stiff competition from bagel shops and coffee chains such as Starbucks compounded operational difficulties. Au Bon Pain's fast-food ambiance was not appealing to customers who wanted to sit and enjoy a meal or a cup of coffee. At the same time, the café style atmosphere of Saint Louis Bread, known as Panera (Latin for "time for bread") outside the Saint Louis area, was proving to be successful. In 1996, comparable sales at Au Bon Pain locations declined 3% while same-store sales of the Panera unit were up 10%.[22]

Lacking the capital to overhaul the ambiance of the Au Bon Pain segment, the company decided to sell the unit. This allowed the company to strategically focus its time and resources on the more successful Panera chain. Unlike Au Bon Pain, Panera was not confined to a small urban niche and had greater growth potential. On May 16, 1999, Shaich sold the Au Bon Pain unit to investment firm Bruckman, Sherrill, and Co. for US$73 million. At the time of the divestiture, the company changed its corporate name to Panera Bread Company. The sale left Panera Bread Company debt-free, and the cash allowed for the immediate expansion of its bakery-café stores.[23]

Throughout the 2000s, Panera grew through franchise agreements, acquisitions (including the purchase of Paradise Bakery & Café, Inc.), and new company-owned bakery-cafés. By 2009, Panera had become a national bakery-café concept with 1380 company-owned and franchise-operated bakery-café locations in 40 states and in Ontario, Canada. Panera had grown from serving approximately 60 customers a day at its first bakery-café to serving nearly six million customers a week systemwide, becoming one of the largest food-service companies in the United States. The company believed its success was rooted in its ability to create long-term dining concept differentiation.[24] The company operated under the Panera, Panera Bread, Saint Louis Bread Co., Via Panera, You Pick Two, Mother Bread, and Paradise Bakery & Café design trademark names registered in the United States. Others were pending. Panera also had some of its marks registered in foreign countries.[25]

May 13, 2010, marked a significant change in the history of Panera Bread Company. After 28 years, Ronald Shaich stepped down as CEO and Chairman effective immediately following the Annual Stockholders Meeting, and William Moreton, previously the Executive Vice President and co-Chief Operating Officer, assumed the role of CEO. Shaich planned to remain as the company's Executive Chairman. He announced that he expected to focus his time and energy within Panera on a range of strategic and innovation projects and mentoring the senior team. In typical Panera fashion, the transition had been planned for one-and-a-half years to ensure its success.

Concept and Strategy[26]

Concept

At the time when Panera was created, the fast-food industry was described as featuring low-grade burgers, greasy fries, and sugared colas. Shaich decided to create a casual but comfortable place where customers could eat fresh-baked artisan breads and fresh sandwiches, soups, and salads without worrying about whether it was nutritious.[27]

Panera's restaurant concept focused on the specialty bread/bakery-café category. Bread was Panera's platform and entry point to the Panera experience at its bakery-cafés. It was the symbol of Panera quality and a reminder of "Panera Warmth," the totality of the experience the customer received and could take home to share with friends and family. The company endeavored to offer a memorable experience with superior customer service. The company's associates were passionate about sharing their expertise and commitment with Panera customers. The company strove to achieve what Shaich termed "Concept Essence," Panera's blueprint for attracting targeted customers that the company believed differentiated it from competitors. Concept Essence included a focus on artisan bread, quality products, and a warm, friendly, and comfortable environment. It called for each of the company's bakery-cafés to be a place customers could trust to serve high-quality food. Bread was Panera's passion, soul, expertise, and the platform that made all of the company's other food items special.

The company's bakery-cafés were principally located in suburban, strip mall, and regional mall locations and featured relaxing décor and free Internet access. Panera's bakery-cafés were designed to visually reinforce the distinctive difference between its bakery-cafés and those of its competititors.

Panera extended its strong values and concept of fresh food in an unpretentious, welcoming atmosphere to the nonprofit community. The company's bakery-cafés routinely donated bread and baked goods to community organizations in need. Panera's boldest step was the May 2010 opening of the Panera Cares bakery-café in Missouri, which had no set prices; instead, customers were asked to pay what they wanted.[28]

Panera's success in achieving its concept was often acknowledged through customer surveys and awards from the press. From *Advertising Age*[29] to *Zagat*,[30] Panera was touted as one of America's hottest brands and most popular chains. Customers rated Panera fifth overall in the restaurant industry in 2008 and highest among fast casual eateries in an annual customer satisfaction and quality survey conducted by Dandelman & Associates, a restaurant market research firm.[31] In 2009, Panera also was named number one on the "Healthiest for Eating on the Go" list by *Health* magazine for its variety of health menu options, whole grain breads, and half-sized items. Numerous other national and local awards had been received each year for the company's sandwiches, breads, lunches, soups, vegetarian offerings, cleanliness, Wi-Fi, community responsibility, workplace quality, and kids' menu.[32] Panera's own consumer panel testing of 1000 customers showed consistently high value perceptions of the company's products.[33]

Strategy

Panera operated in three business segments: company-owned bakery-café operations, franchise operations, and fresh dough operations. As of December 29, 2009, the company-owned bakery-café segment consisted of 585 bakery-cafés, all located in the United States, and the franchised operations segment consisted of 795 franchise-operated bakery-cafés, located throughout the United States and in Ontario, Canada. The company anticipated 80 to 90 systemwide bakery-cafés opening in 2010 with average weekly sales for company-owned new units of US$36,000 to US$38,000.[34] **Exhibit 1** shows the total number of systemwide

EXHIBIT 1 Company-Owned and Franchise-Operated Bakery-Cafés: Panera Bread Company

	For the Fiscal Year Ended				
	December 29, 2009	December 30, 2008	December 25, 2007	December 26, 2006	December 27, 2005
Number of bakery-cafés					
company-owned					
Beginning of period	562	532	391	311	226
Bakery-cafés opened	30	35	89	70	66
Bakery-cafés closed	(7)	(5)	(5)	(3)	(2)
Bakery-cafés acquired from franchisees (1)	—	—	36	13	21
Bakery-cafés acquired (2)	—	—	22	—	—
Bakery-cafés sold to a franchisees (3)	—	—	(1)	—	—
End of period	585	562	532	391	311
Franchise-operated					
Beginning of period	763	698	636	566	515
Bakery-cafés opened	39	67	80	85	73
Bakery-cafés closed	(7)	(2)	(5)	(2)	(1)
Bakery-cafés sold to company (1)	—	—	(36)	(13)	(21)
Bakery-cafés acquired (2)	—	—	22	—	—
Bakery-cafés purchased from company (3)	—	—	1	—	—
End of period	795	763	698	636	566
Systemwide					
Beginning of period	1,325	1,230	1,027	877	741
Bakery-cafés opened	69	102	169	155	139
Bakery-cafés closed	(14)	(7)	(10)	(5)	(3)
Bakery-cafés acquired (2)	—	—	44	—	—
End of period	1,380	1,325	1,230	1,027	877

Notes:

(1) In June 2007, Panera acquired 32 bakery-cafés and the area development rights from franchisees in certain markets in Illinois and Minnesota. In February 2007, the company acquired four bakery-cafés, as well as two bakery-cafés still under construction, and the area development rights from a franchisee in certain markets in California.

In October 2006, Panera acquired 13 bakery-cafés (one of which was under construction) and the area development rights from a franchisee in certain markets in Iowa, Nebraska, and South Dakota. In September 2006, the company acquired one bakery-café in Pennsylvania from a franchisee. In November 2005, Panera acquired 23 bakery-cafés (two of which were under construction) and the area development rights from a franchisee in certain markets in Indiana.

(2) In February 2007, Panera acquired 51% of the outstanding capital stock of Paradise Bakery & Café Inc., which then owned and operated 22 bakery-cafés and franchised 22 bakery-cafés, principally in certain markets in Arizona and Colorado.

(3) In June 2007, Panera sold one bakery-café and the area development rights for certain markets in Southern California to a new area developer.

SOURCES: Panera Bread Company Inc., *2009 Form 10-K*, p. 25 and *2006 Form 10-K*, p. 20.

bakery-cafés for the last five years. As of December 29, 2009, the company's fresh dough operations segment, which supplied fresh dough items daily to most company-owned and franchise-operated bakery-cafés, consisted of 23 fresh dough facilities. Company-owned bakery-café operations accounted for 85.2% of revenues in 2009, up from 78% in 2005. Royalties and fees from franchise operations made up 5.8% of revenues in 2009, down from 8.5% in 2005, and fresh dough operations accounted for 9% of total revenues in 2009, down from 13.5% in 2005.[35]

In addition to the dine-in and take-out business, the company offered Via Panera, a nationwide catering service that provided breakfast assortments, sandwiches, salads, and soups using the same high-quality ingredients offered in the company's bakery-cafés. Via Panera was supported by a national sales infrastructure. The company believed that Via Panera would be a key component of long-term growth.

The key initiatives of Panera's growth strategy focused on growing store profit, increasing transactions and gross profit per transaction, using its capital smartly, and putting in place drivers for concept differentiation and competitive advantage.[36] The company paid careful attention to the development of new markets and further penetration of existing markets by both company-owned and franchised bakery-cafés, including the selection of sites that would achieve targeted returns on invested capital.[37] Panera's strategy in 2009 was different from many of its competitors. When many restaurant companies were focused on surviving the economic meltdown by downsizing employees, discounting prices, and lowering quality, Panera chose to stay the course and continued to execute its long-term strategy of investing in the business to benefit the customer. The result, according to Shaich: "Panera zigged while others zagged."[38]

During the economic downturn, Panera stuck to a simple recipe: Get more cash out of each customer, rather than just more customers. While other recession-wracked restaurant chains discounted and offered meals for as little as US$5 to attract customers, Panera bucked conventional industry wisdom by eschewing discounts and instead targeted customers who could afford to shell out an average of about US$8.50 for lunch. While many of its competitors offered less expensive meals, Panera added a lobster sandwich for US$16.99 at some of its locations. Panera was able to persuade customers to pay premiums because it had been improving the quality of its food.[39] "Most of the world seems to be focused on the Americans who are unemployed," said CEO Ronald Shaich. "We're focused on the 90 percent that are still employed."[40]

Panera's positive financial results contrasted with those of many other casual dining chains, which had posted negative same-store sales due partly to declining traffic and lower-priced food. Some chains found that discounting not only hurt margins but also failed to lure as many customers as hoped. Shaich seemed to thrive on doing the opposite of his competition. During 2009, instead of slashing prices, he raised them twice, one on bagels and once on soup. "We're contrarians to the core," said Shaich. "We don't offer a lower-end strategy. In a world where everyone is cutting back, we want to give more not less."[41] "This is the time to increase the food experience," insisted Shaich, "that is, when consumers least expect it."[42]

Also crucial to Panera's success in 2009 was the company's approach to operations during the recession. Over the years, many restaurant companies told investors they were able to improve labor productivity while running negative comparable store sales. Panera believed that reducing labor in a restaurant taxed the customer by creating longer waits, slower service, and more frazzled team members. Panera took the approach of keeping labor consistent with sales and continuing to invest in its employees as a way to better serve its customers.[43]

The results for 2009 showed that Panera's strategy of zigging while others were zagging paid off. Panera met or exceeded its earnings targets in each quarter of 2009. Panera delivered 25% earnings per share (EPS) growth in 2009 on top of 24% EPS growth in 2008. Panera's stock price increased 115% from December 31, 2007, to March 30, 2010.

Panera's objectives for 2010 included a target of 17%–20% EPS growth through the execution of its key initiatives. To further build transactions, Panera planned to focus on differentiation through innovative salads utilizing new procedures to further improve quality. Panera also planned to test a new way to make paninis using newly designed grills. The company expected to roll out improved versions of several Panera classics while continuing to focus on improving operations, speed of service, and accuracy.[44]

In early 2010, to increase gross profit per transaction and further improve margins while still providing overall value to customers, Panera introduced an initiative called the Meal Upgrade Program. With this program, a customer who ordered an entrée and a beverage was offered the opportunity to purchase a baked good to complete their meal at a "special" price point. Panera intended to test other impulse add-on initiatives, bulk baked goods, and bread as a gift.[45]

"I worry about keeping the concept special," said Shaich. "Is it worth walking across the street to? It doesn't matter how cheap it is. If it isn't special, there's no reason the business needs to exist."[46]

The Fast Casual Segment

Panera's predecessor, Au Bon Pain, was a pioneer of the fast casual restaurant category. Dining trends caused fast casual to emerge as a legitimate trend in the restaurant industry as it bridged the gap between the burgers-and-fries fast-food industry and full service, sitdown, casual dining restaurants.

Technomic Information Services, a food-service industry consultant, coined the term to describe restaurants that offered the speed, efficiency, and inexpensiveness of fast food with the hospitality, quality, and ambiance of a full-service restaurant. Technomic defined a fast casual restaurant by whether or not the restaurant met the following four criteria: (1) The restaurant had to offer a limited service or self-service format. (2) The average check had to be between US$6 and US$9, whereas fast-food checks averaged less than US$5. This pricing scheme placed fast casual between fast food and casual dining. (3) The food had to be made-to-order, as consumers perceived newly prepared, made-to-order foods as fresh. Fast casual menus usually also had more robust and complex flavor profiles than the standard fare at fast-food restaurants. (4) The décor had to be upscale or highly developed. Décor inspired a more enjoyable experience for the customer as the environment of fast casual restaurants was more akin to a neighborhood bistro or casual restaurant. The décor also created a generally higher perception of quality.[47]

The fast casual market was divided into three categories: bread-based chains, traditional chains, and ethnic chains. According to a Mintel 2008 report, bread-based chains, such as Panera, and ethnic chains, such as Chipotle Mexican Grill, had sales momentum and were predicted to grow at the expense of traditional chains such as Steak 'n Shake, Boston Market, Fuddruckers, and Fazoli's, which were weighted down by older concepts. The report also suggested that bread-based and ethnic chains had an edge with respect to consumer perceptions about food healthfulness.[48] Most fast casual brands did not compete in all dayparts (breakfast, lunch, dinner, late-night), but instead focused on one or two. While almost all competitors in this segment had a presence at lunch, many grappled with the question of whether and how to participate in other dayparts.[49] In addition, unlike fast-food restaurants that constructed stand-alone stores, fast casual chains were typically located in strip malls, small-town main streets, and preexisting properties.

According to Technomic, by offering high-quality food with fast service, fast casual chains had experienced increased traffic in 2009 as diners "traded-down" from casual dining chains and "traded-up" from fast-food restaurants to lower-priced but still higher-quality fresh food.[50] In other words, the desire to eat out did not diminish; only the destination changed. Sales in 2009 for the top 100 fast casual chains reached US$17.5 billion, a 4.5% increase over 2008; and units grew by 4.3% to 14,777 locations,[51] compared to a 3.2% sales decline in the overall restaurant industry.[52] The growth in the fast casual segment was also due to the maturation of two large segments of the U.S. population: baby boomers and their children. Both age groups had little time for cooking and were tired of fast food.

Bakery-café/bagel remained the largest of the fast casual restaurant clusters and the largest menu category, generating US$4.8 billion in U.S. sales in 2009 and jumping from 17% to 21% of the top 100 fast casual restaurants. In 2009, Mexican, with total sales of US$3.8 billion, was the second-largest fast casual cluster of restaurants.[53] Technomic's 2009 Top 100 Fast-Casual Restaurant Report noted that besides burgers (up 16.7%), the fastest growing menu categories reflected the growing interest of consumers in international flavors: Asian/noodle (up 6.4%) and Mexican (up 6.3%).[54]

Exhibit 2 provides a list of the 20 largest fast casual franchises in 2010. Even though Chipotle Mexican Grill was one of Panera's key competitors, it was not included on this list because it did not franchise.

EXHIBIT 2
2010's Twenty Largest Fast Casual Franchises

	2009 United States Sales
1. Panera Bread	$2,796,500
2. Zaxby's	718,250
3. El Pollo Loco	582,000
4. Boston Market	545,000
5. Jason's Deli	475,870
6. Five Guys Burgers and Fries	453,500
7. Qdoba Mexican Grill	436,500
8. Einstein Bros. Bagels	378,444
9. Moe's Southwestern Grill	358,000
10. McAlister's Deli	351,960
11. Fuddruckers	320,500
12. Wingstop	306,606
13. Baja Fresh Mexican Grill	300,000
14. Schlotzky's	248,000
15. Corner Bakery Café	235,029
16. Fazoli's	235,000
17. Noodles & Company	230,000
18. Bruegger's Bagel Bakery	196,000
19. Donatos Pizza	185,000
20. Cosi	168,500

Note:
(a) Not all key fast casual competitors are franchised restaurants.

SOURCES: Technomic's 2010 Top 100 Fast-Casual Chain Restaurant Report, www.bluemaumau.cor/9057/2010's-top-twenty-largest-fastcausual-franchises.

Competition

Panera experienced competition from numerous sources in its trade areas. The company's bakery-cafés competed with specialty food, casual dining and quick service cafés, bakeries, and restaurant retailers, including national, regional, and locally owned cafés, bakeries, and restaurants. The bakery-cafés competed in several segments of the restaurant business based on customers' needs for breakfast, AM "chill," lunch, PM "chill," dinner, and take-home through both on-premise sales and Via Panera catering. The competitive factors included location, environment, customer service, price, and quality of products. The company competed for leased space in desirable locations and also for hourly employees. Certain competitors or potential competitors had capital resources that exceeded those available to Panera.[55]

Panera's 2009 sales of nearly US$2.8 billion ranked as the largest of the fast casual chains. The company saw an increase in sales of 7.1% and an increase in units of 4.3% to 1380 stores over 2008. Chipotle Mexican Grill held on to the number two spot, growing U.S. sales 13.9% to US$1.5 billion, and units by 14.2% to 955 locations in 2009.[56]

Panera and Chipotle Mexican Grill, which together made up more than 25% of the fast casual segment, posted double-digit percentage increases in first-quarter 2010 sales over the same period in 2009, driven by opening new outlets and robust increases in same-store sales. By contrast, United States revenues at McDonald's suffered in 2009, and for the first five months of 2010, same-store sales were up 3% over the same period in 2009. Burger King struggled during the same period with revenues in the United States and Canada down 4% for the first three months of 2010.[57] Established restaurant chains were beginning to take notice of the opportunities in the fast casual segment and were considering options. For example, Subway started testing an upscale design in the Washington, DC, market in 2008. New competitors, such as Otarian, were also entering the fast casual segment and testing new concepts, many having a health and wellness or sustainability component to them.

Although Panera continued to learn from its competitors, none of its competitors had yet figured out the formula to Panera's success. While McDonald's had rival Burger King, and Applebee's had T.G.I. Friday's, there was no direct national competitor that replicated Panera's business model. Like Panera, Chipotle sold high-quality food made with fine ingredients—but it was Mexican. Cosi sold quality sandwiches and salads, but lacked pastries and gourmet coffees. Starbucks had fine coffee and pastries but not Panera's extensive food menu. According to Shaich, the reason is that "this is hard to do, . . . what seems simple can be tough. It is not so easy to knock us off."[58]

Corporate Governance

Panera was a Delaware corporation and its corporate headquarters were located in Saint Louis, Missouri.

Board of Directors

Panera's Board was divided into three classes of membership. The terms of service of the three classes of directors were staggered so that only one class expired at each annual meeting. At the time of the May 2010 annual meeting, the Board consisted of six members. Class I consisted of Ronald M. Shaich and Fred K. Foulkes, with terms expiring in 2011; Class II consisted of Domenic Colasacco and Thomas E. Lynch, with terms expiring in 2012; and Class III consisted of Larry J. Franklin and Charles J. Chapmann III, with terms ending in 2010. Mr. Franklin and Mr. Chapman were both nominated for reelection with terms ending in 2013, if elected.[59]

The biographical sketches for the board members are shown next.[60]

Ronald M. Shaich (age 56) was a Director since 1981, co-founder, Chairman of the Board since May 1999, Co-Chairman of the Board from January 1988 to May 1999, Chief Executive Officer since May 1994, and Co-Chief Executive Officer from January 1988 to May 1994. Shaich served as a Director of Lown Cardiovascular Research Foundation, as a trustee of the nonprofit Rashi School, as Chairman of the Board of Trustees of Clark University, and as Treasurer of the Massachusetts Democratic Party. He had a Bachelor of Arts degree from Clark University and an MBA from Harvard Business School. Immediately following the 2010 Annual Meeting, Mr. Shaich planned to resign as Chief Executive Officer and the Board intended to elect him as Executive Chairman of the Board.

Larry J. Franklin (age 61) was a Director since June 2001. Franklin had been the President and Chief Executive Officer of Franklin Sports Inc., a leading branded sporting goods manufacturer and marketer, since 1986. Franklin joined Franklin Sports Inc. in 1970 and served as its Executive Vice President from 1981 to 1986. Franklin served on the Board of Directors of Bradford Soap International Inc. and the Sporting Goods Manufacturers Association (Chairman of the Board and member of the Executive Committee).

Fred K. Foulkes (age 68) was a Director since June 2003. Dr. Foulkes had been a Professor of Organizational Behavior and had been the Director (and founder) of the Human Resources Policy Institute at Boston University School of Management since 1981. He had taught courses in human resource management and strategic management at Boston University since 1980. From 1968 to 1980, Foulkes had been a member of the Harvard Business School faculty. Foulkes wrote numerous books, articles, and case studies. He served on the Board of Directors of Bright Horizons Family Solutions and the Society for Human Resource Management Foundation.

Domenic Colasacco (age 61) was a Director since March 2000, and Lead Independent Director since 2008. Colasacco had been President and Chief Executive Officer of Boston Trust & Investment Management, a banking and trust company, since 1992. He also served as Chairman of its Board of Directors. He joined Boston Trust in 1974 after beginning his career in the research division of Merrill Lynch & Co. in New York City.

Charles J. Chapman III (age 47) was a Director since 2008. Chapman had been the Chief Operating Officer and a Director of the American Dairy Queen Corporation since October 2005. From 2001 to October 2005, Chapman held a number of senior positions at American Dairy Queen. Prior to joining American Dairy Queen, Chapman served as Chief Operating Officer at Bruegger's Bagel's Inc., where he was also President and co-owner of a franchise. He also held marketing and operations positions with Darden Restaurants and served as a consultant with Bain & Company.

Thomas E. Lynch (age 50) was a Director since March 2010 and previous Director from 2003–2006. Lynch served as Senior Managing Director of Mill Road Capital, a private equity firm, since 2005. From 2000 to 2004, Lynch served as Senior Managing Director of Mill Road Associates, a financial advisory firm that he founded in 2000. From 1997 through 2000, Lynch was the founder and Managing Director of Lazàrd Capital Partners. From 1990 to 1997, Lynch was a Managing Director of the Blackstone Group, where he was a senior investment professional for Blackstone Capital Partners. Prior to Blackstone, Lynch was a senior consultant at the Monitor Company. He also had previously served on the Board of Directors of Galaxy Nutritional Foods Inc.

The Board had established three standing committees, each of which operated under a charter approved by the Board. The *Compensation and Management Development Committee* included Foulkes (Chair), Franklin, and Colasacco. The *Committee on Nominations and*

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Corporate Governance included Franklin (Chair), Chapman, and Foulkes. The *Audit Committee* included Colasacco (Chair), Foulkes, and Franklin.[61]

The compensation package of non-employee directors consisted of cash payments and stock and option awards. Total non-employee director compensation ranged from US$29,724 to US$124,851 in fiscal 2009 depending on services rendered.[62]

Top Management

The biographical sketches for some of the key executive officers follow.[63]

Ronald Shaich (age 56) planned to resign as Chief Executive Officer immediately following the May 2010 Annual Meeting. The Board of Directors announced its intentions to elect him as Executive Chairman of the Board at that time. The Board intended to appoint William W. Moreton to succeed Mr. Shaich as Chief Executive Officer and President and to elect him to the Board of Directors.[64]

William M. Moreton (age 50) re-joined Panera in November 2008 as Executive Vice President and Co-Chief Operating Officer. He previously served as Executive Vice President and Chief Financial Officer from 1998 to 2003. From 2005 to 2007, Moreton served as President and Chief Financial Officer of Potbelly Sandwich Works, and from 2004–2005 as Executive Vice President-Subsidiary Brands, and Chief Executive Officer of Baja Fresh, a subsidiary of Wendy's International Inc. Immediately following the conclusion of the 2010 Annual Meeting, upon the resignation of Mr. Shaich, the Board planned for Mr. Moreton to succeed Mr. Shaich as Chief Executive Officer, and the Board intended to appoint him as President and elect him to the Board.

John M. Maguire (age 44) had been Chief Operating Officer and subsequently Co-Chief Operating Officer since March 2008 and Executive Vice President since April 2006. He previously served as Senior Vice President, Chief Company, and Joint Venture Operations Officer from August 2001 to April 2006. From April 2000 to July 2001, Maguire served as Vice President, Bakery Operations, and from November 1998 to March 2000, as Vice President, Commissary Operations. Maguire joined the company in April 1993; from 1993 to October 1998, he was a Manager and Director of Au Bon Pain/Panera Bread/St. Louis Bread.

Cedric J. Vanzura (age 46) had been Executive Vice President and Co-Chief Operating Officer since November 2008 and Executive Vice President and Chief Administrative Officer from March to November 2008. Prior to joining the company, Vanzura held a variety of roles at Borders International from 2003 to 2007.

Mark A. Borland (age 57) had been Senior Vice President and Chief Supply Chain Officer since August 2002. Borland joined the company in 1986 and held management positions within Au Bon Pain and Panera Bread divisions until 2000, including Executive Vice President, Vice President of Retail Operations, Chief Operating Officer, and President of Manufacturing Services. From 2000 to 2001, Borland served as Senior Vice President of Operations at RetailDNA, and then rejoined Panera as a consultant in the summer of 2001.

Jeffrey W. Kip (age 42) had been Senior Vice President and Chief Financial Officer since May 2006. He previously served as Vice President, Finance and Planning, and Vice President, Corporate Development, from 2003 to 2006. Prior to joining Panera, Mr. Kip was an Associate Director and then Director at UBS from 2002 to 2003 and an Associate at Goldman Sachs from 1999 to 2002.

Michael J. Nolan (age 50) had been Senior Vice President and Chief Development Officer since he joined the company in August 2001. From December 1997 to March 2001, Nolan served as Executive Vice President and Director for John Harvard's Brew House, L.L.C., and Senior Vice President, Development, for American Hospitality Concepts Inc. From March 1996 to December 1997, Nolan was Vice President of Real Estate and Development for Apple South Incorporated, a chain restaurant operator, and from July 1989 to March 1996, Nolan was Vice President of Real Estate and Development for Morrison Restaurants Inc. Prior to 1989, Nolan served in various real estate and development capacities for Cardinal Industries Inc. and Nolan Development and Investment.

Other key Senior Vice Presidents included Scott Davis, Chief Concept Officer; Scott Blair, Chief Legal Officer; Rebecca Fine, Chief People Officer; Thomas Kish, Chief Information Officer; Michael Kupstas, Chief Franchise Officer; Michael Simon, Chief Marketing Officer; and William Simpson, Chief Company and Joint Venture Operations Officer. In 2009, the total compensation for the top five highest-paid executive officers ranged from US$939,919 to US$3,354,708.[65]

At year-end 2009, there were two classes of stock: (1) Class A common stock with 30,491,278 shares outstanding and one vote per share, and (2) Class B common stock with 1,392,107 shares outstanding and three votes per share.[66] Class A common stock was traded on NASDAQ under the symbol PNRA. As of March 15, 2010, all directors, director nominees, and executive officers as a group (20 persons) held 1,994,642 shares or 6.22% of Class A common stock and 1,311,690 shares or 94.22% of Class B common stock with a combined voting percentage of 13.23%. Ronald Shaich owned 5.5% of Class A common stock and 94.22% of Class B common stock for a combined voting percentage of 12.42%.[67] In November 2009, Panera's Board of Directors approved a three-year share repurchase program of up to US$600 million of Class A common stock.[68]

Menu[69]

Panera's value-oriented menu was designed to provide the company's target customers with affordably priced products built on the strength of the company's bakery expertise. The Panera menu featured proprietary items prepared with high-quality fresh ingredients as well as unique recipes and toppings. The key menu groups were fresh-baked goods, including a variety of freshly baked bagels, breads, muffins, scones, rolls, and sweet goods; made-to-order sandwiches; hearty and unique soups; hand-tossed salads; and café beverages including custom-roasted coffees, hot or cold espresso, cappuccino drinks, and smoothies.

The company regularly reviewed and updated its menu offerings to satisfy changing customer preferences, to improve its products, and to maintain customer interest. To give its customers a reason to return, Panera had been rolling out new products with fresher ingredients such as antibiotic-free chicken (Panera is the nation's largest buyer[70]). The roots of most new Panera dishes could be traced to its R&D team's twice-yearly retreats to the Adirondacks, where staffers took turns trying to out-do each other in the kitchen. "We start with: What do we think tastes good," said Scott Davis. "We're food people, and if we're not working on something that gets us really excited, it's kind of not worth working on."[71] Panera did not have test kitchens and instead tested all new menu items directly in its cafés.

Panera integrated new product rollouts into the company's periodic or seasonal menu rotations, referred to as "Celebrations." Examples of products introduced in fiscal 2009 included the Chopped Cobb Salad and Barbeque Chicken Chopped Salad, introduced during the 2009 summer salad celebration. Other menu changes in 2009 included a reformulated French baguette, a new line of smoothies, new coffee, a new Napa Almond Chicken Salad sandwich, a new Strawberry Granola Parfait, the Breakfast Power Sandwich, and a new line of brownies and blondies. Three new salmon options, five years in the making, were introduced in early 2010 along with a new Low-Fat Garden Vegetable Soup and a new Asiago Bagel

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Breakfast Sandwich. New chili offerings were in the planning stages. During this time Shaich had also been busy tweaking things he wanted Panera to do better, such as improving the freshness of Panera's lettuce by cutting the time from field to plate in half. He also improved the freshness of the company's breads by opting to bake all day long, not just in the early morning hours. Panera's changes and improvements were all designed to build competitive advantage by strengthening value. Value, according to the company, meant offering guests an even better "total experience."

In 2008, Panera introduced the antithesis to the microwaved, processed breakfast sandwich, by introducing a made-to-order grilled breakfast sandwich. The new line of breakfast sandwiches were made fresh daily with quality ingredients—a combination of all-natural eggs, Vermont white cheddar cheese, Applewood-smoked bacon or all natural sausage, grilled between two slices of fresh baked ciabatta. Many of the company's competitors had also moved to more protein-based breakfast sandwich offerings because of the growth opportunities in this segment of the market. In order to be competitive, Panera needed to be different.

Not all of Panera's menu innovations had been successful with customers or had added much to the bottom line. Panera redesigned its menu boards in 2009 to draw the customers' eyes toward meals with higher margins, like the soup and salad combo, rather than pricier items, like a strawberry poppy-seed salad, that did not bring as much to the bottom line. The Crispani pizza was discontinued in 2008 after it failed to drive business during evening hours.

To improve margins, Panera was able to anticipate and react to changes in food and supply costs including, among other things, fuel, proteins, dairy, wheat, tuna, and cream cheese costs through increased menu prices and to use its strength at purchasing to limit cost inflation in efforts to drive gross profit per transaction.

Panera believe in being transparent with regard to the ingredients it used. They were one of the first restaurants to serve antibiotic-free chicken even though it was more expensive. Panera chose to be ahead of the curve again when it announced in early 2010 that it would post calorie information on all systemwide bakery-café menu boards by the end of 2010. Panera had for a number of years provided a nutritional calculator on its website so customers could find nutritional information for individual products or build a meal according to their dietetic specifications. Recognizing the health risks associated with transfats, Panera had completely removed all transfat from its menu by 2006.[72] Panera also offered a wide range of organic food products including cookies, milk, and yogurt, which were incorporated into the company's children's menu, Panera Kids, in 2006. Because of its healthy choices, Panera was named "One of the 10 Best Fast-Casual Family Restaurants" by *Parents* magazine in its July 2009 issue.[73]

Site Selection and Company-Owned Bakery-Cafés[74]

As of December 29, 2009, the company-owned bakery-café segment consisted of 585 company-owned bakery-cafés, all located in the United States. During 2009, Panera focused on using its cash to build new high-ROI bakery-cafés and executed a disciplined development process that took advantage of the recession to drive down costs while selecting locations that delivered strong sales volume. In 2009, Panera believed the best use of its capital was to invest in its core business, either through the development of new bakery-cafés or through the acquisition of existing bakery-cafés from franchisees or other similar restaurant or bakery-café concepts, such as the acquisition of Paradise Bakery & Café Inc.

All company-owned bakery-cafés were in leased premises. Lease terms were typically 10 years with one, two, or three 5-year renewal option periods thereafter. Leases typically had charges for a proportionate share of building and common area operating expenses and real estate taxes, and a contingent percentage rent based on sales above a stipulated sales level. Because Panera was considered desirable as a tenant due to its profitable balance sheet and national reputation, the company enjoyed a favorable leasing environment in lease terms and the availability of desirable locations.

The average size of a company-owned bakery-café was approximately 4600 square feet as of December 29, 2009. The average construction, equipment, furniture and fixtures, and signage costs for the 30 company-owned bakery-cafés opened in fiscal 2009 was approximately US$750,000 per bakery-café after landlord allowances and excluding capitalized development overhead. The company expected that future bakery-cafés would require, on average, an investment per bakery-café of approximately US$850,000.

In evaluating potential new locations for both company-owned and franchised bakery-cafés, Panera studied the surrounding trade area, demographic information within the most recent year, and publicly available information on competitors. Based on this analysis and utilizing predictive modeling techniques, Panera estimated projected sales and a targeted return on investment. Panera also employed a disciplined capital expenditure process focused on occupancy and development costs in relation to the market, designed to ensure the right-sized bakery-café and costs in the right market. Panera's methods had proven successful in choosing a number of different types of locations, such as in-line or end-cap locations in strip or power centers, regional malls, drive-through, and freestanding units.

Bakery S

Franchises[75]

Franchising was a key component of Panera's growth strategy. Expansion through franchise partners enabled the company to grow more rapidly as the franchisees contributed the resources and capabilities necessary to implement the concepts and strategies developed by Panera.

The company began a broad-based franchising program in 1996, when the company actively began seeking to extend its franchise relationships. As of December 29, 2009, there were 795 franchise-operated bakery-cafés open throughout the United States and in Ontario, Canada, and commitments to open 240 additional franchise-operated bakery-cafés. At this time, 57.6% of the company's bakery-cafés were owned by franchises comprised of 48 franchise groups. The company was selective in granting franchises, and applicants had to meet specific criteria in order to gain consideration for a franchise. Generally, the franchisees had to be well capitalized to open bakery-cafés, with a minimum net worth of US$7.5 million and meet liquidity requirements (liquid assets of US$3 million),[76] have the infrastructure and resources to meet a negotiated development schedule, have a proven track record as multi-unit restaurant operators, and have a commitment to the development of the Panera brand. A number of markets were still available for franchise development.

Panera did not sell single-unit franchises. Instead, they chose to develop by selling market areas using Area Development Agreements, referred to as ADAs, which required the franchise developer to open a number of units, typically 15 bakery-cafés, in a period of four to six years. If franchisees failed to develop bakery-cafés on schedule or defaulted in complying with the company's operating or brand standards, the company had the right to terminate the ADA and to develop company-owned locations or develop locations through new area developers in that market.

The franchise agreement typically required the payment of an up-front franchise fee of US$35,000 (broken down into US$5000 at the signing of the area development agreement and US$30,000 at or before the bakery-café opens) and continued royalties of 4%–5% on sales from each bakery-café. The company's franchise-operated bakery-cafés followed the same protocol for in-store operating standards, product quality, menu, site selection, and bakery-café construction as did company-owned bakery-cafés. Generally, the franchisees were required to purchase all of their dough products from sources approved by the company.

The company did not generally finance franchise construction or area development agreement purchases. In addition, the company did not hold an equity interest in any of the franchise-operated bakery-cafés. However, in fiscal 2008, to facilitate expansion into Ontario, Canada, the company entered into a credit facility with the Canadian franchisee. By March 2010, Panera had repurchased the three franchises in Toronto in order to be more directly involved in the Canadian market. While the company thought the geographic market represented a good growth opportunity, Panera decided to study and learn from other U.S. firms that had expanded successfully in Canada.[77]

Bakery Supply Chain[78]

According to Ronald Shaich, "Panera has a commitment to doing the best bread in America."[79] Freshly baked bread made with fresh dough was integral to honoring this commitment. System-wide bakery-cafés used fresh dough for sourdough and artisan breads and bagels.

Panera believed its fresh dough facility system and supply chain function provided competitive advantage and helped to ensure consistent quality at its bakery-cafés. The company had a unique supply-chain operation in which dough was supplied daily from one of the company's regional fresh dough facilities to substantially all company-owned and franchise-operated bakery-cafés. Panera bakers then worked through the night shaping, scoring, and glazing the dough by hand to bring customers fresh-baked loaves every morning and throughout the day. In 2009, the company began baking loaves later in the morning to ensure freshness throughout the day and altered the fermentation cycle of its baguettes to make them sweeter.

As of December 29, 2009, Panera had 23 fresh dough facilities, 21 of which were company-owned, including a limited production facility that was co-located with one of the company's franchised bakery-cafés in Ontario, Canada, to support the franchise-operated bakery-cafés located in that market (2 of the fresh dough facilities were franchise operated). All fresh dough facilities were leased. In fiscal 2009, there was an average of 62.5 bakery-cafés per fresh dough facility compared to an average of 62.0 in fiscal 2008.[80]

Distribution of the fresh dough to bakery-cafés took place daily through a leased fleet of 184 temperature-controlled trucks driven by Panera employees. The optimal maximum distribution range for each truck was approximately 300 miles; however, when necessary, the distribution ranges might be up to 500 miles. An average distribution route delivered dough to seven bakery-cafés.

The company focused its expansion in areas served by the fresh dough facilities in order to continue to gain efficiencies through leveraging the fixed cost of its fresh dough facility structure. Panera expected to enter selectively new markets that required the construction of additional facilities until a sufficient number of bakery-cafés could be opened that permitted efficient distribution of the fresh dough.

In addition to its need for fresh dough, the company contracted externally for the manufacture of the remaining baked goods in the bakery-cafés, referred to as sweet goods. Sweet goods products were completed at each bakery-café by professionally trained bakers. Completion included finishing with fresh toppings and other ingredients and baking to established artisan standards utilizing unique recipes.

With the exception of products supplied directly by the fresh dough facilities, virtually all other food products and supplies for the bakery-cafés, including paper goods, coffee, and smallwares, were contracted externally by the company and delivered by vendors to an independent distributor for delivery to the bakery-cafés. In order to assure high-quality food and supplies from reliable sources, Panera and its franchisees were required to select from a list of approved suppliers and distributors. The company leveraged its size and scale to improve the quality of its ingredients, effect better purchasing efficiency, and negotiate purchase agreements with most approved suppliers to achieve cost reduction for both the company and its customers. One company delivered the majority of Panera's ingredients and other products to the bakery-cafés two or three times weekly. In addition, company-owned bakery-cafés and franchisees relied on a network of local and national suppliers for the delivery of fresh produce (three to six times per week).

Marketing[81]

Panera focused on customer research to plan its marketing and brand-building initiatives. According to Panera executives, "everything we do at Panera goes through the customer filter first."[82] Panera's target customers were between 25 and 50 years old, earned US$40,000 to US$100,000 a year, and were seeking fresh ingredients and high-quality choices.[83] The company's customers spent an average of US$8.50 per visit.[84]

Panera was committed to improving the customer experience in ways the company believed rare in the industry. The company leveraged its nationwide presence as part of a broader marketing strategy of building name recognition and awareness. As much as possible, the company used its store locations to market its brand image. When choosing a location to open a new store, Panera carefully selected the geographic area. Better locations needed less marketing, and the bakery-café concept relied on a substantial volume of repeat business.

In 2009, Panera executed a more aggressive marketing strategy than most of its competitors. While many competitors discounted to lure customers back through 2009, Panera focused on offering guests an even better "total experience." Improvements to the "total experience" included new coffee and breakfast items, new salads, new china, smoothies, and mac and cheese. The company focused on improving store profit by increasing transactions as well as increasing gross profit per transaction through the innovation and sales of higher gross profit items. Panera also had a successful initiative to drive add-on sales through the Meal Upgrade program.[85]

In 2010, Panera began modest increases in advertising and additional investments in its marketing infrastructure because the company recognized the importance of marketing as a driver of earnings and sales increases.[86] In spite of these increases, Panera remained very cautious about its marketing investments and focused on the appropriate mix for each market. Panera primarily used radio and billboard advertising, with some television, social networking, and in-store sampling days. Panera found that it benefited when other companies advertised products that Panera also carried, such as McDonald's early 2010 promotion of smoothies. Panera was testing additional television advertising in 20 markets but considered any significant growth in this medium to be a few years away.[87]

Panera's franchise agreements required franchisees to pay the company advertising fees based on a percentage of sales. In fiscal 2009, franchise-operated bakery-cafés contributed 0.7% of their sales to a company-run national advertising fund, paid a marketing administration fee of 0.4% of sales, and were required to spend 2.0% of their sales on advertising in their respective local markets. The company contributed the same sales percentages from company-owned bakery-cafés toward the national advertising fund and marketing administration fee. For fiscal 2010, the company increased the contribution rate to the national advertising fund to 1.1% of sales.[88]

Panera invested in cause-related marketing efforts and community activities through its Operation Dough-Nation program. These programs included sponsoring runs and walks, helping nonprofits raise funds, and the Day-End Dough-Nation program through which unsold bakery products were packaged at the end of each day and donated to local food banks and charities.[89]

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Management Information Systems[90]

Each company-operated bakery-café had programmed point-of-sale registers to collect transaction data used to generate pertinent information, including transaction counts, product mix, and average check. All company-owned bakery-café product prices were programmed into the system from the company's corporate headquarters. The company allowed franchisees to have access to certain proprietary bakery-café systems and systems support. The fresh dough facilities had information systems that accepted electronic orders from the bakery-cafés and monitored delivery of the ordered product. The company also used proprietary online tools such as eLearning to provide online training for retail associates and online baking instructions for its bakers.

Panera's intranet site, The Harvest, allowed the company to monitor important analytics and provide support to its bakery-cafés. For example, Panera used a weather application on its intranet that tied a bakery-café's historic local weather to the store's historic sales, allowing managers to forecast sales based on weather for any given day. "That helps in staffing and how you're going to allocate labor and what you need in terms of materials," said Greg Rhoades, Panera's senior manager in information services. He called The Harvest "our single source of information." Panera shared news with its employees about food safety and customer satisfaction websites and provided information on daily sales, hourly sales, staffing, product sales, labor costs, and ingredient costs.[91]

The company began offering Wi-Fi in its bakery-cafés in 2003. By 2010, most bakery-cafés provided customers with free Internet access through a managed Wi-Fi network. As a result, Panera hosted one of the largest free public Wi-Fi networks in the country.[92]

In 2010, Panera began to pilot test a loyalty program, "My Panera," in 23 stores. Rather than just a food-discounting program, "My Panera" was intended to provide a deeper relationship with the customer by including participants in events such as the food tasting of new products. The company expected to complete the pilot by year-end 2010 and hoped to begin leveraging the data to better understand its high-frequency customers and to "surprise and delight" them in a way that was tailored to the customers' buying habits.[93]

Human Resources[94]

From the beginning, Panera realized that the key ingredients to the successful development of the Panera brand ranged from the type of food it served to the kind of people behind the counters. The company placed a priority on staffing its bakery-cafés, fresh dough facilities, and support center operations with skilled associates and invested in training programs to ensure the quality of its operations. As of December 29, 2009, the company employed approximately 12,000 full-time associates (defined as associates who average 25 hours or more per week), of whom approximately 600 were employed in general or administrative functions, principally in the company's support centers; approximately 1200 were employed in the company's fresh dough facility operations; and approximately 10,300 were employed in the company's bakery-café operations as bakers, managers, and associates. The company also had approximately 13,200 part-time hourly associates at the bakery-cafés. There were no collective bargaining agreements. The company considered its employee relations to be good.

Panera believed that providing bakery-café operators the opportunity to participate in the success of the bakery-cafés enabled the company to attract and retain experienced and highly motivated personnel, which resulted in a better customer experience. Through a Joint Venture Program, the company provided selected general managers and multi-unit managers with a multi-year bonus program based upon a percentage of the cash flows of the bakery-café they operated. The intent of the program's five-year period was to create team stability, generally resulting in a higher level of stability for that bakery-café and thus lead to stronger associate engagement and customer loyalty. In December 2009, approximately 50% of company-owned bakery-café operators participated in the Joint Venture program.[95]

Finance

Panera reported a 48% increase in net income of US$25,845 million, or US$0.82 per diluted share, during the first quarter of 2010, compared to US$17,432 million, or US$0.57 per diluted share, during the first quarter of 2009. For this same period, Panera reported revenues of US$364,210 million, a 14% gain over revenues of US$320,709 for the same period in 2009.[96] Company-owned comparable bakery-café sales in the first quarter of fiscal 2010 increased 10.0%, due to transaction growth of 3.5% and average check growth of 6.5% over the comparable period in 2009. Franchise-operated comparable bakery-café sales increased 9.2% in the first quarter of 2010 compared to the same period in 2009. As a result, total comparable bakery-café sales increased 9.5% in the first quarter of fiscal 2010 compared to the comparable period in 2009.[97] In addition, average weekly sales (AWS) for newly opened company-owned bakery-cafés during the first quarter of 2010 were US$56,111 compared to US$41,922 in the first quarter of 2009. During the first quarter of 2010, Panera and its franchises opened eight new bakery-cafés systemwide. No bakery-cafés were closed during this period.[98]

Exhibits 3 to **5** provide Panera's consolidated statement of operations, common size income statements, and consolidated balance sheets, respectively, for the company for the fiscal years ended 2005 through 2009.

In fiscal 2009, during an uncertain economic environment, Panera bucked industrywide trends and increased performance on the following key metrics: (1) systemwide comparable bakery-café sales growth of 0.5% (0.7% for company-owned bakery-cafés and 0.5% for franchise-operated bakery-cafés); (2) systemwide average weekly sales increased 1.8% to US$39,926 (US$39,050 for company-owned bakery-cafés and US$40,566 for franchise-operated bakery-cafés); and (3) 69 new bakery-cafés opened systemwide (7 company-owned bakery-cafés and 39 franchise-operated bakery-cafés). In fiscal 2009, Panera earned US$2.7[illegible] per diluted share.[99] In addition, average weekly sales (AWS) for newly opened company-owned bakery-cafés in 2009 reached a six-year high for new units.[100] **Exhibit 6** provides 2005–2009 selected financial information about Panera.

Total company revenue in fiscal 2009 increased 4.2% to US$1,353.5 million from US$1,298.9 million in fiscal 2008. This growth was primarily due to the opening of 69 new bakery-cafés systemwide in fiscal 2009 (and the closure of 14 bakery-cafés) and, to a lesser extent, the 0.5% increase in systemwide comparable bakery sales.

Company-owned bakery-café sales increased 4.2% in fiscal 2009 to US$1,153.3 million compared to US$1,106.3 million in fiscal 2008. This increase was due to the opening of 30 new company-owned bakery-cafés and to the 0.7% increase in comparable company-owned bakery-café sales in 2009. Company-owned bakery-café sales as a percentage of revenue remained consistent at 85.2% in both fiscal 2009 and fiscal 2008. In addition, the increase in average weekly sales for company-owned bakery-cafés in fiscal 2009 compared to the prior fiscal year was primarily due to the average check growth that resulted from the company's initiative to drive add-on sales. Franchise royalties and fees in fiscal 2009 were up 4.8% to US$78.4 million, or 5.8% of total revenues, up from US$74.8 million in 2008. Fresh dough sales to franchises increased 3.5% in fiscal 2009 to US$121.9 million compared to US$117.8 million in fiscal 2008.[101]

Panera believed that its primary capital resource was cash generated by operations. The company's principal requirements for cash have resulted from the company's capital expenditures for the development of new company-owned bakery-cafés; for maintaining

EXHIBIT 3 Consolidated Statement of Operations: Panera Bread Company

	(Dollar amounts in thousands, except per share information) For the Fiscal Year Ended (1)				
	December 29, 2009	**December 30, 2008**	**December 25, 2007**	**December 26, 2006**	**December 27, 2005**
Revenues					
Bakery-café sales	$ 1,153,255	$ 1,106,295	$ 894,902	$ 666,141	$ 499,422
Franchise royalties and fees	78,367	74,800	67,188	61,531	54,309
Fresh dough sales to franchisee	121,872	117,758	104,601	101,299	86,544
Total revenue	1,353,494	1,298,853	1,066,691	828,971	640,275
Costs and expenses					
Bakery-café expenses					
Cost of food and paper products	$ 337,599	$ 332,697	$271,442	$ 196,849	$ 143,057
Labor	370,595	352,462	286,238	204,956	151,524
Occupancy	95,996	90,390	70,398	48,602	35,558
Other operating expenses	155,396	147,033	121,325	92,176	70,003
Total bakery-café expenses	959,586	922,582	749,403	542,583	400,142
Fresh dough cost of sales to franchisees	100,229	108,573	92,852	85,951	74,654
Depreciation and amortization	67,162	67,225	57,903	44,166	33,011
General and administrative expenses	83,169	84,393	68,966	59,306	46,301
Pre-opening expenses	2,451	3,374	8,289	6,173	5,072
Total costs and expenses	1,212,597	1,186,147	977,413	738,179	559,180
Operating profit	140,897	112,706	89,278	90,792	81,095
Interest expense	700	1,606	483	92	50
Other (income) expense, net	273	883	333	(1,976)	(1,133)
Income before income taxes	139,924	110,217	88,462	92,676	82,178
Income taxes	53,073	41,272	31,434	33,827	29,995
Net income	86,851	68,945	57,028	58,849	52,183
Less: income (loss) attributable to noncontrolling interest	801	1,509	(428)		
Net income attributable to Panera Bread	$ 86,050	$ 67,436	$ 57,456	$ 58,849	$ 52,183
Per share data					
Earnings per common share attributable to Panera Bread Company					
Basic	$ 2.81	$ 2.24	$ 1.81	$ 1.88	$ 1.69
Diluted	$ 2.78	$ 2.22	$ 1.79	$ 1.84	$ 1.65
Weighted average shares of common and common equivalent shares outstanding					
Basic	30,667	30,059	31,708	31,313	30,871
Diluted	30,979	30,422	32,178	32,044	31,651

Notes:

(1) Fiscal 2008 was a 53-week year consisting of 371 days. All other fiscal years presented contained 52 weeks consisting of 364 days with the exception of fiscal 2005. In fiscal 2005, the company's fiscal week was changed to end on Tuesday rather than Saturday. As a result, the 2005 fiscal year ended on December 27, 2005, instead of December 31, 2005, and, therefore, consisted of 52 and a half weeks rather than the 53 week year that would have resulted without the calender change.

SOURCES: Panera Bread Company Inc., *2009 Form 10-K*, pp. 20–21.

EXHIBIT 4 Common Size Statement: Panera Bread Company

(Percentages are in relation to total revenues except where otherwise indicated)
For the Fiscal Year Ended

	December 29, 2009	December 30, 2008	December 25, 2007	December 26, 2006	December 27, 2005
Revenues					
Bakery-café sales	85.2%	85.2%	83.9%	80.4%	78.0%
Franchise royalties and fees	5.8	5.8	6.3	7.4	8.5
Fresh dough sales to franchisee	9.0	9.1	9.8	12.2	13.5
Total revenue	100.0%	100.0%	100.0%	100.0%	100.0%
Costs and expenses					
Bakery-café expense (1)					
Cost of food and paper products	29.3%	30.1%	30.3%	29.6%	28.6%
Labor	32.1	31.9	32.0	30.8	30.3
Occupancy	8.3	8.2	7.9	7.3	7.1
Other operating expenses	13.5	13.3	13.6	13.8	14.0
Total bakery-café expenses	83.2	83.4	83.7	81.5	80.0
Fresh dough cost of sales to franchisees (2)	82.2	92.2	88.8	84.5	86.7
Depreciation and amortization	5.0	5.2	5.4	5.3	5.2
General and administrative expenses	6.1	6.5	6.5	7.2	7.2
Pre-opening expenses	0.2	0.3	0.8	0.7	0.8
Total costs and expenses	**89.6**	**91.3**	**91.6**	**89.0**	**87.3**
Operating profit	10.4	8.7	8.4	11.0	12.7
Interest expense	0.1	0.1	0.1	—	—
Other (income) expense, net	—	0.1	—	-0.2	-0.2
Income before income taxes	10.3	8.5	8.3	11.2	12.8
Income taxes	3.9	3.2	2.9	4.1	4.7
Net income	**6.4**	**5.3**	**5.4**	**7.1**	**8.2**
Less: net income attributable to noncontrolling interest	0.1	0.1	—	—	—
Net income attributable to Panera Bread Company	**6.4%**	**5.2%**	**5.4%**	**7.1%**	**8.2%**

Notes:
(1) As a percentage of bakery-café sales.
(2) As a percentage of fresh dough facility sales to franchisees.

SOURCES: Panera Bread Company, Inc. *2009 Form 10-K*, p. 24 and *2006 Form 10-K*, p. 19.

EXHIBIT 5 Conso

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Class B,
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in 2009;
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in 2006

EXHIBIT 5 Consolidated Balance Sheets: Panera Bread Company

	(Dollar amounts in thousands, except share and per share information) For the Fiscal Year Ended				
	December 29, 2009	December 30, 2008	December 25, 2007	December 26, 2006	December 27, 2005
Assets					
Current assets					
Cash and cash equivalents	$ 246,400	$ 74,710	$ 68,242	$ 52,097	$ 24,451
Short-term investments	—	2,400	23,198	20,025	36,200
Trade accounts receivable, net	17,317	15,198	25,122	19,041	18,229
Other accounts receivable	11,176	9,944	11,640	11,878	6,929
Inventories	12,295	11,959	11,394	8,714	7,358
Prepaid expenses	16,211	14,265	5,299	12,036	5,736
Deferred income taxes	18,685	9,937	7,199	3,827	3,871
Total current assets	322,084	138,413	152,124	127,618	102,774
Property and equipment, net	403,784	417,006	429,992	345,977	268,809
Other assets					
Goodwill	87,481	87,334	87,092	57,192	48,540
Other intangible assets, net	19,195	20,475	21,827	6,604	3,219
Long-term investments	—	1,726	—	—	10,108
Deposits and other	4,621	8,963	7,717	5,218	4,217
Total other assets	111,297	118,498	116,636	69,014	66,084
Total assets	$ 837,165	$ 673,917	$ 698.752	$ 542,609	$ 437,667
Liabilities and stockholders' equity					
Current liabilities					
Accounts payable	6,417	4,036	6,326	5,800	4,422
Accrued expenses	135,842	109,978	121,440	102,718	81,559
Deferred revenue	—	—	—	1,092	884
Total current liabilities	142,259	114,014	127,766	109,610	86,865
Long-term debt	—	—	75,000	—	—
Deferred rent	43,371	39,780	33,569	27,684	23,935
Deferred income taxes	28,813	—	—	—	5,022
Other long-term liabilities	25,686	21,437	14,238	7,649	4,867
Total liabilities	240,129	175,231	250,573	144,943	120,689
Stockholders' equity					
Common stock, $.0001 par value:					
Class A, 75,000,000 shares authorized: 30,364,915 issued and 30,196,808 outstanding in 2009; 29,557,849 issued and 29,421,877 outstanding in 2008; 30,213,869 issued and 30,098,275 outstanding in 2007.	3	3	3	3	3
Class B, 10,000,000 shares authorized; 1,392,107 issued and outstanding in 2009; 1,398,242 in 2008; 1,398,588 in 2007; 1,400,031 in 2006 and 1,400,621 in 2005.	—	—	—	—	—

(cont

EXHIBIT 5 (Continued)

Treasury stock, carried at cost;	(3,928)	(2,204)	(1,188)	(900)	(900)
Additional paid-in capital	168,288	151,358	168,386	176,241	154,402
Accumulated other comprehensive income (loss)	224	(394)	—	—	—
Retained earnings	432,449	346,399	278,963	222,322	163,473
Total stockholders' equity	597,036	495,162	446,164	397,666	316,978
Noncontrolling interest	—	3,524	2,015	—	—
Total equity	$ 597,036	$ 498,686	$ 446,164	$ 397,666	$ 316,978
Total equity and liabilities	$ 837,165	$ 673,917	$ 698,752	$ 542,609	$ 437,667

SOURCES: Panera Bread Company, Inc., *2009 Form 10-K*, p. 45; *2008 Form 10-K*, p. 43; and *2006 Form 10-K*, p. 36.

EXHIBIT 6 Selected Financial Information: Panera Bread Company

(Dollar amounts in thousands)

A. Year to Year Comparable Sales Growth (not adjusted for differing number of weeks)

	For the Fiscal Year Ended				
	December 29, 2009 (52 weeks)	**December 30, 2008 (53 weeks)**	**December 25, 2007 (52 weeks)**	**December 26, 2006 (52 weeks)**	**December 27, 2005 (52-1/2 weeks)**
Company-owned	0.7%	5.8%	1.9%	3.9%	7.4%
Franchise-operated	0.5%	5.3%	1.5%	4.1%	8.0%
Systemwide	0.5%	5.5%	1.6%	4.1%	7.8%

B. System Wide Average Weekly Sales

	For the Fiscal Year Ended				
	December 29, 2009	**December 30, 2008**	**December 25, 2007**	**December 26, 2006**	**December 27, 2005**
Systemwide average weekly sales	$ 39,926	$ 39,239	$ 38,668	$ 39,150	$ 38,318

C. Company-owned Bakery-Café Average Weekly Sales

	For the Fiscal Year Ended				
	December 29, 2009	**December 30, 2008**	**December 25, 2007**	**December 26, 2006**	**December 27, 2005**
Company-owned average weekly sales	39,050	38,066	37,548	37,833	37,348
Company-owned number of operating weeks	29,533	29,062	23,834	176,077	13,280

D. Franchise-owned Bakery-Café Average Weekly Sales

	For the Fiscal Year Ended				
	December 29, 2009	**December 30, 2008**	**December 25, 2007**	**December 26, 2006**	**December 27, 2005**
Franchise average weekly sales	40,566	40,126	39,433	39,894	38,777
Franchise number of operating weeks	40,436	38,449	34,905	31,220	28,090

SOURCES: Panera Bread Company, Inc., *2009 Form 10-K*, pp. 26–30; *2008 Form 10-K*, pp. 25–27; and *2006 Form 10-K*, pp. 20–23.

(900)
154,402

163,473
316,978

$ 316,978
$ 437,667

December 27, 2005 (52-1/2 weeks)
7.4%
8.0%
7.8%

December 27, 2005
$ 38,318

December 27, 2005
37,348
13,280

December 27, 2005
38,777
28,090

0-K, pp. 20–23.

or remodeling existing company-owned bakery-cafés; for purchasing existing franchis operated bakery-cafés or ownership interests in other restaurant or bakery-café concepts; f developing, maintaining, or remodeling fresh dough facilities; and for other capital nee such as enhancements to information systems and infrastructure. The company had access a US$250 million credit facility which, as of December 29, 2009, had no borrowings outstan ing. Panera believed its cash flow from operations and available borrowings under its existi credit facility to be sufficient to fund its capital requirements for the foreseeable future.[102]

According to Nicole Miller Regan, an analyst at Piper Jaffray, "the key to Panera's su cess during the recessionary period lies in what the company hasn't done. . . . It hasn't tried change."[103] "For us, the recession has been the best of times," said CEO Shaich.[104]

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