BARRON'S

CEO SPOTLIGHT

Panera Bread's Ron Shaich: "Flour on His Shoes"

Like Starbucks' Howard Schultz, Shaich came out of retirement to remake the company he helped launch. Doing good, eating well.

By
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"The world doesn't need me to read yesterday's research," says Ron Shaich, founder and chief executive of Panera Bread, the bakery-cafe chain. "It needs me to make sure Panera is arriving where the world is going."

For many years, Panera (ticker: PNRA) got there first, with high-quality food served in a pleasantly casual setting. Shaich (pronounced "shake"), 61, is considered a pioneer in the lucrative space between fast food and fine dining. He was the first "fast casual" restaurateur to serve antibiotic- and cage-free chicken, and among the first to drop transfats and MSG. And, along with Howard Schultz, longtime CEO of Starbucks (SBUX), he was a leader in envisioning a third place—neither work nor home—where people could gather comfortably.

Shaich's epiphanies have included artisanal bread and pay-what-you-can cafes. *Photo: Shawn Henry for Barron's*

The Panera formula worked like a charm for the company's first 15 years but hit a roadblock in 2013. Shaich, who ran the St. Louis–based company from 1993 to 2010, came out of retirement to take the reins again—much like Schultz did at Starbucks—and embarked on an ambitious turnaround. Things haven't gone smoothly of late: Panera reported two weeks ago that per-share profit fell 7% in the fourth quarter, and warned that year-to-year earnings will be flat to lower in 2015. The stock lost 11% on the news, to $157.33, and now trades for $158.

But betting against Shaich could be a big mistake. Panera's shares have returned nearly 1,700% since 1991, when the company was known as Au Bon Pain, against a gain of 450% in the Standard & Poor's 500 index. While the fast-casual market has become a lot more crowded in recent years, given the explosive growth ofChipotle Mexican Grill (CMG), Buffalo Wild Wings (BWLD), and other chains, he is arguably better-equipped than anyone to get Panera back on track.
"Shaich is a rare visionary who consistently understands how modern American life is evolving," says Thomas Lynch, founder of Mill Road Capital, in Greenwich, Conn., and a member of Panera's board.

PANERA'S LATEST ISSUES relate to higher costs—for food, labor, and an ambitious technology overhaul spearheaded by the CEO. Panera, which owns, operates, or franchises 1,880 cafes, has been spending about $65,000 per company store, and millions more at the corporate level, to streamline the ordering and delivery of meals, launch a new advertising campaign, and expand its $300 million business-to-business catering division. Dubbed Panera 2.0, the restaging is painful but essential if the chain is to maintain a competitive advantage in the fast-casual arena. Many Wall Street analysts who cover Panera are unimpressed, but Jeffrey Bernstein of Barclays has an Overweight rating on the stock and a price target of $200, based on his view that the Panera 2.0 initiative will succeed. Paul Westra, an analyst at Stifel, has a Hold on the stock, but says, "It is going to get done because Ron is leading it."

By the end of 2015, 400 Panera cafes will have been converted to an easy-order/fast-delivery format, whereby customers place orders at iPad-equipped kiosks and await delivery at tables. The hope is that this system will cut down on order errors and the long lines that so aggravated diners.

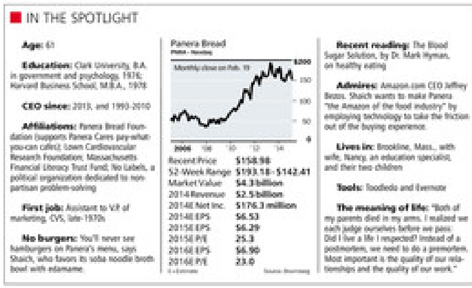
Shaich predicts it will take at least three quarters to see improved sales, although the potential results seem worth the wait. Sales have risen by more than 10% a year at the first cafes to be converted, three years ago. "I completely get it," he says of the stock market's negative reaction. "People are voting on what they see today."

Shaich insists on taking the longer view, which is more challenging for a publicly traded company. "Let me do my job," he says.

SHAICH GREW UP in Livingston, N.J. His father was an accountant, and his mother, a homemaker. During his college years at Clark University in Worcester, Mass., he was wrongly accused of shoplifting while visiting a convenience store unfriendly to students. He decided to start his own store, using his position as the school's student-body treasurer to raise money for the cause.
Running the business was hugely gratifying, although he thought mostly about working in politics, especially after a stint with Sen. George McGovern's 1972 presidential campaign. Yet, when a friend suggested he apply to Harvard Business School and write his admission essay about the convenience-store experience, he did so, and was accepted.

After graduating from business school in 1978, Shaich worked briefly for CVS and another retailer, before joining the Original Cookie Company (later known as Mrs. Fields Cookies) in Ohio. He returned to Boston in 1980 to open his own Cookie Jar store, backed by a $75,000 loan from his father and another $25,000 in savings. When he noticed that no one bought cookies before noon, he added baguettes and croissants purchased from Au Bon Pain, a chain of stores started by Louis Kane, a venture capitalist.

Shaich soon learned that the local Au Bon Pain stores were struggling and the owners wanted to sell. He approached Kane with an interest in running the chain, and was hired, he says, because Kane said he had “flour on his shoes.” The two became partners, and Shaich merged his cookie store with Au Bon Pain.



The Au Bon Pain stores had been poorly managed. Among other things, Shaich saw the bakers doing cocaine and stealing from the registers. When he fired them, they chased him through the parking lot.

The menu was limited, as well. Shaich added sandwiches, and aggressively shopped for real estate in strip malls to tap into America’s lunch crowd. By the time the company sold stock to the public in 1991, it was operating 125 stores.

Two years later, Au Bon Pain bought St. Louis Bread, a regional chain, for $23 million. St. Louis baked its own bread, emphasizing fresh ingredients, and sought to create an inviting environment that could serve as a gathering place. The concept intrigued Shaich, who wanted the company to focus on the new chain instead of Au Bon Pain, and a fight with the board ensued. Shaich prevailed, and Au Bon Pain was sold to a private-equity firm in 1999 for $73 million. St. Louis changed its name to Panera, Latin for bread basket, and hit the $1 billion mark in sales in 2007.

IN THE ENSUING YEARS, Panera posted some of the strongest same-store sales gains in its industry. Sales at stores open at least a year continued to grow by single digits even through the Great Recession, which derailed many competitors. Thanks to stellar financial results, the company became a stock market darling. Shaich was named executive chairman in 2010, and handed the CEO job to William Moreton, his executive vice president and co-chief operating officer. “I learned so much at Panera,” Shaich says. “I wanted to take all I learned to make a difference in the world.”
Within a year, however, he was restless. He also feared the company was losing its competitive edge. In a move reminiscent of Starbucks’ Schultz, another memo writer whose retirement also didn’t last long, Shaich wrote an eight-page “vision document” code-named Amazon, about how Panera could employ technology to “change the customer experience.” By 2012 he was back in the saddle, working 80-hour weeks and serving as Moreton’s co-CEO. The following year, when Moreton had to curtail his travel, Shaich became the sole CEO.

“I realized the best contribution I could make to the world was through Panera,” he says.

Tucking into a Thai chicken salad at a Panera store in Braintree, Mass., near his Brookline home, Shaich says he can trace the “aha!” moments of his professional life to time spent on Caribbean beaches. His first aha! occurred in 1994, when he recognized a market opportunity in fast-casual dining. He sensed there would be a reaction to fast-food joints, or “self-serve gas stations for the human body,” and a preference among a portion of the public for the “de-commodification” of dining.

Specifically, he thought customers would pay more for artisanal breads and other specialty foods in a quick-service setting. “Everyone thought I was nuts,” he says.

SHAICH’S SECOND beach epiphany occurred in 1998, when he realized that Panera, then a regional brand, had the potential to become a dominant national player. “It had scalability,” he recalls thinking.
The third occurred during his hiatus from corporate life, and related to “having an impact.” During this restless period, Shaich started an initiative to help reduce hunger called Panera Cares. The Panera Bread Foundation, a charitable organization, has since opened and operates Panera Cares community cafes in Clayton, Mo.; Dearborn, Mich.; Boston; and Portland, Ore., based on a pay-what-you-can model.

The stores break even on 25% fewer sales than conventional cafes. Many customers pay a suggested donation, 15% leave more, and 25% pay less. “People are fundamentally good,” Shaich says. “It’s like a handicapped parking spot. Few take advantage of the situation.”

Shaich signed on to take the SNAP challenge in 2013, named for the Supplemental Nutrition Assistance Program, aka food stamps. Like a food-stamp recipient, he ate on $4.15 a day for a week.

“It’s no big deal for a rich guy to go on diet,” he says, but the SNAP challenge was another matter. It sensitized him to “the emotional toll” of poverty. He recalls feeling humiliated at a grocery-store counter when he ran out of money and had to put a carton of eggs back on the shelf. Worrying about food, he soon realized, could become such a preoccupation that there wasn’t much room to think about anything else.

AT AROUND THE same time the Foundation launched the Panera Cares cafes, Shaich helped start No Labels, a nonpartisan nonprofit aimed at getting Congress to stop bickering and start working on problems. Among other things, he advocates open primary elections, in which voters don’t have to be registered with either major party, to reduce the influence of what he calls ultrapartisanship.
“I blame us,” he says, noting that elections are won by the most engaged and often more extreme interest groups that manage to wrest control of the vote at the primary level. The result is candidates beholden to groups that represent relatively few people. “Our real election isn’t in the general election but in the primary,” he says.

Shaich’s nonprofit work currently is taking a backseat to Panera, as he tries to restart growth. “We are transitioning the business, which isn’t the same as it was five years ago, when building stores was easy because we already had done it a thousand times,” he says.

Based on Wall Street’s consensus estimate, Panera will earn $6.29 a share this year, down about 4% from 2014, on revenue of $2.7 billion. For next year, analysts are penciling in earnings of $176.7 million, or $6.90 a share, on revenue of $2.9 billion. Thereafter, the optimists expect the numbers to head higher.

“It’s not a question of whether Ron can do it again,” says Lynch, the Panera board member, “He’s done it continuously.”