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BUSINESS THE END OF LUNCH?

How Panera Solved Its 'Mosh Pit' Problem

By Julie Jargon
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Sandwich-and-soup chain cut wait time to order from eight minutes to one, thanks to in-store touch screens, a mobile app and an army of delivery drivers

Self-order kiosks are one of the tools Panera used to cut lines.

Long lines at lunch should make restaurant chains happy. But not at Panera Bread Co.

Seven years ago, customers at the popular sandwich-and-soup chain had to wait in line for up to eight minutes to place an order. Then they had to stand in what Chief Executive Ron Shaich called a "mosh pit" of people waiting for their food. Ten percent of the time, the orders were wrong, the company said.

The St. Louis-based chain of more than 2,000 restaurants realized it had to rethink its service model—and found online ordering was the answer.

It took more than six years to get the process right, testing the patience of store managers, company management and Wall Street analysts—and even attracting an activist shareholder.

Today, online orders make up more than a quarter of its company-owned restaurant sales, and the average time customers spend waiting in line to order food has shrunk to one minute. Panera is widely cited by analysts as one of the most technologically savvy, best-performing chains in the industry.

European investment fund JAB Holding Co. in April offered a 20% premium to take Panera private, in a deal that will keep Mr. Shaich at the helm of the fast-casual chain. The transaction is expected to close in the third quarter.

In 2010, as he started the overhaul of Panera's ordering process, Mr. Shaich drew on his own frustration as a customer.

"By the time I'd get there, find a parking space, go in and wait for the food, it's 30 minutes. I'd just as soon go to my fridge and look for leftovers," he recalled thinking.

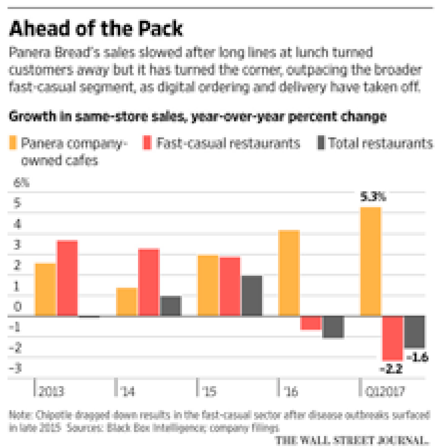
Blaine Hurst, left, and Ronald Shaich spent about 100 hours a week in a prototype Panera during tests in 2012, observing what would work. PHOTO: BRITTANY SOWACKE FOR THE WALL STREET JOURNAL

At the time, Mr. Shaich had retired as CEO but was still the company's chairman. He tapped Blaine Hurst, a former Papa John's International Inc. executive, to help with the overhaul.

Mr. Shaich eventually returned as CEO in 2012, and the chain opened a prototype Panera in Braintree, Mass., to test all elements of "Panera 2.0": self-order kiosks, delivery, digital ordering and a new practice of bringing food to customers' tables.
Messrs. Shaich and Hurst spent about 100 hours a week in that Braintree cafe observing what would work.

Easing the ordering bottleneck by taking orders online, instead of at the counter, wasn’t enough: The kitchen had to be able to handle the volume. Allowing customers to place orders themselves led to more customization, but also more staff mistakes. The company revamped the way employees process orders in an effort to minimize errors by simplifying the kitchen display systems.

“It was literally hundreds of these little things that we did,” said Mr. Hurst, who became company president last year after holding several other executive positions with Panera.



Other restaurant chains are going through similar struggles as they try to adapt their business models to the way consumers want to order and receive their food. Starbucks Corp. has suffered growing pains as customers have migrated to its mobile order and pay app, shifting the congestion that used to occur at the counter to an area in the cafes where the mobile orders are handed off.

Starbucks is currently working on ways to solve the bottleneck, including texting customers when their orders are ready.

Many other chains, such as McDonald’s Corp., are just now starting to roll out mobile ordering and delivery.

Panera began rolling out its rapid pickup system nationwide in 2014. But the results didn’t come overnight. In the fourth quarter of 2014, the chain reported that per-share profit had fallen 7%, in part because of the investment in technology, and warned that earnings growth would be flat or negative in 2015.

New York investment firm Luxor Capital Group LP took a roughly 4% stake in Panera in 2015 and encouraged the restaurant chain to cut costs and take on debt to buy back more shares. Noah Elbogen, an investment analyst at Luxor at the time, said the firm believed that digital ordering and delivery were the right things to do, but pushed the company to find other cost-cutting to help offset the investment in technology, which he pegs at well over $100 million. Panera wouldn’t disclose the cost of the upgrades.

“I took three years of flat earnings and a lot of heat as we made these bets,” Mr. Shaich said. While he agreed to buy back shares and cut costs unrelated to the technology effort, Mr. Shaich told employees to press ahead.

In addition to ordering at the counter or the drive-thru, many Panera locations have added a rapid pickup option.

Panera turned the corner last year as digital orders and delivery gained traction. In the first quarter of 2016, it posted its best traffic and same-store sales growth in four years, outperforming the industry by 6.5 percentage points—the widest margin it had ever recorded.

The company continued to post strong growth throughout 2016, raising its full-year earnings per share guidance each quarter. It ended the year with earnings per share up 7% and same-store sales up 4.2% versus the prior year, far outpacing the industry.

Catherine Rhinehart, of Kingsport, Tenn., says Panera’s online ordering has been a “life-saver.”

“It saves me from standing in line and taking half my lunch hour to get the food,” said the 68-year-old marketer, who remembers the time when the lines inside Panera were long.

Mr. Elbogen, now chief executive of Misada Capital Group LLC, a New Jersey-based investment manager, said he wasn’t surprised by Panera’s success. He recalls seeing lines out the door at Panera, which convinced him that demand wasn’t the company’s problem, but rather its ability to handle it. By implementing digital ordering, he said, “They were really solving a problem.”

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