HBR Blog Network

When Growth is Deceiving

by Ron Shaich | 3, 2013

Although the economy is finally improving, growth is still hard to come by. As the founder and co-chief executive of Panera Bread, I can safely report that the growth challenge looms even larger in the brutally combative restaurant industry, where four out of five new concepts fail. After all, it's not like the country is clamoring for another restaurant.

But not so long ago, I happened upon another reason why growth comes hard: even when you think you're growing, you're probably not.

Let me explain. Like most retailers, restaurants have just two ways to drive customer transactions: get new customers to come through the door or get existing customers to return more often. A couple of years ago, Panera was growing new customer transactions from zero to a paltry one percent. That modest performance took me aback. After all, we had increased investments to improve the customer experience and thereby attract new guests. Why hadn't those investments produced better results?

Only after a deep dive into the data did I discover, to my surprise, that we were operating under the wrong assumption. We thought we were working from a baseline that was zero. In fact, the baseline was *negative* three or four percent transaction growth. Based on our investments, we should have hit about five percent growth. Instead, our so-called positive growth was mostly negative.

Why? Because most food-service companies compete in a bloody, shark-infested red ocean. The big fish are always looking to make a quick meal out of a laggard; schools of hungry new entrants are always anxious to tear into you. Thanks to the competition, it's not hard to lose more customers than you're gaining, for a net decrease.

To thrive in those hyper-competitive seas, a company must continually unleash value-creating innovations. If you've got a mature retail concept, and you simply continue with what worked in the past, plus a little more, competitors will take a bite out of your customer transactions. The size of the loss will vary by company and market. But rest assured, in our industry, failing to create game-changing products and services will likely lead to a significant drop in customer transactions. With that, the steep descent into the red begins.

Here's another way to think about it. My father was a CPA and amateur poker player. When he retired, he played professional poker in Las Vegas for eighteen months. At the end of that stretch he felt duty bound, as a CPA, to calculate his performance. Lo and

behold, he discovered he won about three cents an hour. I was amazed that such a modest result left him ecstatic. But he understood that his nearly imperceptible winnings came only after he offset the House vigorish — the five-to-ten percent commission that the casino extracts from the pot.

In business as in poker, we must all figure out how to beat the vig.

Especially in a challenging business environment, we must continually re-examine our assumptions about how to get real growth. Though it doesn't show up on a spreadsheet, we must still account for the vigorish — the constant round of cuts our competitors extract. Even if we're investing enough to increase transactions by three percent annually, but we're paying a competitive vig of five percent, we're in the hole.

That's why, more frequently than we realize, simply relying on incremental improvements, which is tantamount to defending the status quo, often results in negative growth — even when you think you're getting a modest gain. With market and competitive conditions more punishing than ever, a strategy based on playing it safe is often more risky than betting on an unconventional idea. The better course of action (and the one with the lesser risk) is to innovate break-the-mold products while at the same time calculating the vig to understand your real growth.

True, that once-beloved buzzword, "innovation," has become a little ho-hum, as many executives focus on "running the business" and "execution." But it still bears repeating: Growth is deceiving, especially if we're not factoring in the cost that competitors take. To get the real growth we want to create, we must continually examine our assumptions. Otherwise, the House vig will quickly take its toll.