BOSS TALK

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Panera Bread Co. chief Ron Shaich on staying recharged and why the company opened pay-what-you-can cafes.

The fast-casual dining segment is getting crowded. While chains like Panera Bread Co. PNRA -0.64% and Chipotle Mexican Grill Inc. CMG -0.12% continue to log rapid expansion, even fast-food operators like Wendy's are going upscale, adding items like flatbread sandwiches and remodeling their interiors.

Bakery-cafe chain Panera Bread, based in a St. Louis suburb, rang up a 28% increase in profit for fiscal 2012, outpacing the sector as a whole, but the company's customer-traffic growth slowed in the first quarter.

Amid increasing competition, Panera's co-Chief Executive Ron Shaich has stepped up spending on marketing, added new menu categories like pasta and developed a vast loyalty program.

Ramsay de Give for The Wall Street Journal

Panera Bread's Ron Shaich has stepped up spending on marketing, added new menu categories like pasta and developed a vast loyalty program.

But perhaps the chain's biggest recent innovation was opening pay-what-you-can cafes—there are no set prices, just suggested donations—in markets that are struggling economically, such as Detroit and St. Louis. Three years into the experiment, the company now is testing one pay-what-you-can item—turkey chili in a bread bowl—at for-profit St. Louis stores, in hopes the idea will expand to all of its 1,700 outlets.

The 59-year-old Mr. Shaich, who becomes the sole CEO in August, recently talked with The Wall Street Journal about potential acquisitions and why pay-what-you-can is catching on. Edited excerpts:

1Q Revenue, in millions		1Q Profit, in millions		Employees	
2013	2012	2013	2012	end 2012	end 2011
$561.8	$498.6	$48.1	$41.2	20,800	18,000

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Panera Bread Co.

WSJ: How has the competitive landscape changed in the fast-casual area?

Mr. Shaich: We were clearly the first people out there in the space. For at least five years, in the mid '90s, my stock was flat. I couldn't get anybody to see a place that existed between fast food and fine dining.

Basically, fast casual is us, Chipotle and Starbucks SBUX -0.21% . Probably between the three of us, we represent 95% of the sales that are considered fast casual.

WSJ: Do you expect a shakeout in the industry?

Mr. Shaich: There's always a continual shakeout going on; this is a dynamic industry. The reality is, what was good enough yesterday will not be good enough tomorrow.

WSJ: Panera was born out of an acquisition. What are your thoughts on making other acquisitions, maybe of smaller chains like Così Inc., COSI +3.63% a cafe and sandwich shop that has struggled recently?

Mr. Shaich: We come from very different places, we're in very different businesses, we have very different focuses...We are continually looking at all options. [But] the bottom line is we certainly aren't out there actively looking.

WSJ: You operate five pay-what-you-can stores. How do they work?

Mr. Shaich: Opening the first Panera Cares store was a roller coaster of an experience. People came up to me and began talking about the fact that they had been customers for 5-10 years and had lost their jobs. And how appreciated it was. There were occasionally people who tried to beat it, or game it. So ultimately it was a test of human nature.

This year we'll service over 1 million people in these cafes. And 20% of customers leave more than the suggested donation, 60% leave the suggested donation, and 20% leave what they can, but often significantly less.

WSJ: Panera's loyalty program, launched in 2010, now has 14 million members, and represents roughly 45% of customer transactions. You have had to tweak the program to make it more beneficial to Panera. How are you using that customer data now?

Mr. Shaich: This was a major commitment. It cost tens of millions of dollars to get it up. There's great benefit to a loyalty program; there is great benefit to being able to talk to your customer individually, but it requires a great deal of scale.

So many people's loyalty programs are 'buy 10 sandwiches, get the 11th one free.' That's a discount program; that's not a loyalty program. To me, the loyalty program is about being able to talk to you individually, and it's about being able to get the information so I can understand what you're doing individually. I'm not for discounting; I'm for learning.

WSJ: Panera is a suburban brand, but you recently opened Manhattan locations. How have you had to change operations for an urban environment?

Mr. Shaich: What we need to do to succeed here, is we have to have the capabilities to meet the demand. It's no surprise, the volumes are extraordinary.

We have the capabilities of producing two to three times more per hour in certain locations in Manhattan than we do in Manhattan, Kansas. And I think as we continue to open more stores in Manhattan, you'll start to see more of that.

WSJ: Some think your experience with urban stores in Manhattan could be a launching pad for you going abroad, to European cities that look more like New York. What are your plans for that?

Mr. Shaich: I don't believe there is such a thing as a global strategy. There are only markets. We're now essentially playing throughout the U.S. and parts of Canada. We will not announce someday that we're going global. We will continue to grow and expand, market by market.

WSJ: The Affordable Care Act is putting a lot of pressure on the restaurant industry. How are you preparing for it?

Mr. Shaich: We see it as a very modest element of cost inflation. It isn't going to drive our business one way or the other in a material way. We already have many of our team members on health insurance. [About 4,500 employees in Panera's cafes have elected medical coverage, which represents about 16% of those who are eligible.]

We aren't going to let the tail wag the dog....If this is a cost that we're all going to pay, then we're all going to pay it.

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