Panera Bread Company

Submitted to Dr. Desmarais
December 17, 2011

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Executive Summary:

Our consulting team completed an analysis of Panera Bread Company mainly focusing on the opportunities and threats within the industry, Panera’s competitive capabilities, and the company’s strengths and weaknesses. The following recommendations contain the opportunity or threat within the industry, the strength or weakness that allows Panera to pursue or defend against the critical issues and the tools needed to take immediate action.

We recommend that Panera Bread Company:

1. **Open cafés in untapped markets, and focus on utilizing franchising to achieve the desired 1:160,000 café: person ratio by 2010.** We found that the restaurant industry life cycle is still in growth. This growth coupled with Panera’s strong franchising capability offers a significant opportunity for Panera to pursue. To achieve this Panera must first use the current site selection and market analysis processes to choose ideal locations for new cafés in untapped markets. Panera should also utilize this process to assess the logistics necessary to support the potential locations. Next, Panera needs to utilize the established, stringent franchisee selection criteria to identify candidates that are a good fit, and then work with the selected franchisees using the existing franchise assistance programs to educate and train franchisees in Panera’s unique brand, vision and culture. Once Panera sets up franchising systems in new markets, the company should measure success by whether or not the 1 café per 160,000 people per location by 2010. Panera also must assess the new franchisees based on the historical areas of success.

2. **Bolster the current promotional strategy to a more aggressive soft-sell promotional strategy while still utilizing word-of-mouth tactics to increase first-time customer traffic.** We found that customers are prone to give newly opened eating establishments a trial. Panera has underutilized potential in its promotional strategy to allow customers to know of newly opened cafés. Panera can pursue the opportunity within the industry if it strengthens the current promotional strategy to promote awareness. This helps Panera promote brand awareness to become a dominant leader in the bakery-café industry. To do this, the company must begin expanding to untapped and low-penetrated markets where customers will not know much about the company. The company must then increase excitement about these new cafés before opening by using guerilla marketing. An example of this is hiring plain-clothed personnel to circulate future and current development sites and engage potential consumers by drumming up interest in café openings. The next implementation step is to distribute coded coupons with a two-week expiration period, and an
additional coupon to be given to a friend. Success can be measured by tracking new customer foot traffic in the specific cafés and the new café’s sales volume in the first six months.

3. Implement the “Oven Fresh, To Go” program that will increase customers switching costs and reward buyer loyalty through progressive discounts based on levels of return patronage. Our analysis revealed that the restaurant industry is threatened by low switching costs and low customer loyalty. Our analysis revealed that Panera had strengths in buyer loyalty. Panera should first begin steps one month prior to the start of this service using signage and promotion. Next Panera should print menus that displaying the oven fresh option and distribute them at the point of sale. Panera should cross train employees on the oven fresh operational procedures of taking orders and bringing orders to customer’s cars. Next Panera should purchase or lease 2 to 3 parking spots per location in close proximity to the door with signs for designated parking. Last Panera should place a pre-paid post card with survey questions inside to-go packaging and place customer loyalty punch card in packaging that rewards returning loyal customers. Panera should track the discounts given by customers. Because of the progressive nature of the discounts, Panera can identify its most loyal clientele based on the level of the discount rate.

4. Broaden the product scope and service offering to include a wider array of light entrees, dinner fare, and beer and wine available after 4:30 at select locations nationwide. The new offerings will be paired with community events such as wine-tastings and fundraisers to bolster the perceived dinner atmosphere. Our analysis of the restaurant industry led us to determine that there were a large number of buyers available to firms providing an opportunity for increased market share. Our analysis of the competitive capabilities showed that Panera had an internal strength in research and development. Panera needs to utilize the extensive research and development skills to determine ideal menu offerings, portions, price, and locations suitable for beer and wine. The new product offerings will be introduced to a limited number of stores to determine customer response and verify the scalability to ensure quality. The successful food and alcohol items will be introduced to pre-determined ideal locations along with marketing and training support. The final implementation step will be a market survey question at the point-of-sales system that will determine the number of new dinner customers. The ultimate goal of this recommendation is to increase market share for Panera.
Macro-Environment:

The United States saw 3.0% growth in the overall economy for the year 2006. Additionally, real disposable income increased by 2.1% from the third quarter of 2005 until the end of 2006. The unemployment rate continued on a downward trend from a high of 6.0% in 2003. Unemployment was 4.65% in 2006. According to the Bureau of Labor Statistics, consumer expenditures were $48,398 and $2,794 was spent on food away from home per household. Because there was overall economic growth, consumer expenditures were high, and unemployment was on a downward trend, the economy at large was in a healthy state. When economic conditions were perceived as good, consumers were more willing to spend excess income, as opposed to saving or investing. Therefore, consumers were more likely to spend money on eating out for various meals; this was an opportunity for the restaurant industry.

The legal, regulatory and political environment was relatively stable in 2006. Because there was a stable regulatory and political environment, business owners were able to operate at a more functional level. Companies were not worried about significant changes to regulations which hinder business growth. Therefore, this stable environment was an opportunity for the industry.

The population demographics for the U.S. consumer in 2006 were as follows. The population was 49.27% male and 50.37% female; the median age was 36.4. About 15.07% of the population was over 62 years old. The median income was $46,326 for a single earner household and $67,348 for a dual earner household. Of the total 299,398,484 consumers, 36.43% lived in the South Region, 18.28% in the Northeast Region, 22.12% in the Midwest Region and 23.16% lived in the West Region. In the U.S. 31.7% of persons over the age of 25 were a high school graduate; 18.3% held a Bachelor’s degree, and 9.7% held an advanced degree. Because of the large number of variables and the diversity of the U.S. population across all descriptors, the restaurants industry’s target market was large and the individual buyers were small and numerous. This caused decreased competition over potential buyers, and therefore was an opportunity in the restaurant industry.

There were two significant societal trends that emerged among restaurant industry stakeholders in 2006. First, the issues surrounding trans-fats in restaurants were coming to a head after a 2003 court case. Consumers called for a ban on trans-fats in restaurant food in many different states. Since this made restaurants appear to be the culprit, it decreased customer
satisfaction with local restaurant establishments. This decrease was a treat to the industry. Second, the baby boomer generation was aging, and the children of the baby boomers were moving out. This increased the number of empty nesters in the U.S. With no children at home and both husband and wife working, the couple was less likely to arrive home and feel the need to cook dinner. This phenomenon led to more dinner outings and consumers looking for an establishment to eat a quick and quality meal. Because this increased the numbers of consumers looking to dine out, the aging baby boomer population increased the number of meal occasions and therefore was an opportunity for the industry.

**Industry Analysis:**

**i. Industry Drivers:**

The market size of the industry was quite large. “Commercial eating places accounted for about $345 billion… The U.S. restaurant industry … served about 70 billion meals and snack occasions, and was growing about 5% annually.” Based on unit sales of $345 billion, sales volume of 70 billion and a growth rate of 5% annually, we conclude that the market size of the restaurant industry was quite large and growing. Because when the market size of the competing industry was growing, rivalry among competitors decreased, we conclude that decreased rivalry was a threat for the restaurant industry.

The scope of the competitive rivalry was broad. Restaurant chains competed on regional, national and global levels. The product scope was also broad. The industry served breakfast, lunch, dinner and snack covering many ethnic tastes. Because geographic and product scope were wide, industry members competed in many geographic areas and over a wide array of product lines. Because competition was increased, we conclude that the scope of competitive rivalry was a threat for the industry.

Market growth rate and position in the business cycle was in the growth stage. “The U.S. restaurant industry… served about 70 billion meals and snack occasions, and was growing about 5% annually.” Because the industry was growing at a rate of 5% annually we conclude that the industry was still in the growth stage. Because no indication was given that growth rate was declining, we conclude that the rate was not increasing at a decreased rate and therefore not approaching maturity. Because expanding buyer demand produced enough new business for all industry members to grow without using volume-boosting sales tactics to draw customers away
from rival enterprises, rivalry in the industry was decreased when the life cycle was in growth. Because rivalry decreased when the industry was in growth, we conclude that the growth rate was an opportunity for the industry.

The number of buyers and their relative size in 2006 were as follows. “On a typical day, about 130 million U.S. consumers were food service patrons at an eating establishment – sales at commercial eating places averaged close to $1 billion daily.” Since 130 million consumers spent $1 billion daily, we conclude that on average, each consumer spent $7.69 per day. Based on our analysis, we conclude that the number of buyers was large and their relative size was small. Because buyers have more power when they are large and few in number, we conclude that many small buyers was an opportunity for the industry.

The pace of technological innovation in product introduction was fast. “Most restaurants were quick to adapt their menu offerings to changing consumer tastes and eating preferences, frequently featuring heart-healthy, vegetarian, organic, low-calorie, and/or low-carb items on their menus. It was the norm at many restaurants to rotate some menu selections seasonally and to periodically introduce creative dishes in an effort to keep regular patrons coming back, attract more patrons, and remain competitive.” The constant change in consumer tastes and habits and the rate at which most competitors stayed on top of the changes made product competition very fierce. To stay competitive, establishments needed similar commitment to constant revision of menu items. We conclude that the fast pace of innovation in product introduction was a threat for the industry.

Product differentiation in the industry was common. “Industry members pursued differentiation strategies of one variety or another, seeking to set themselves apart from rivals via pricing, food quality, menu theme, signature menu selections, dining ambiance and atmosphere, service, convenience, and location.” Despite attempts to differentiate products, the restaurant industry operated in a pure competition environment where switching costs were low and there were many competitors. Because the industry products by nature were weakly differentiated, we conclude that the extent to which rivals differentiate their products was a threat to the industry.

The learning and experience curve for the restaurant industry was low. “Just over 7 out of 10 eating and drinking places in the United States were independent single-unit establishments with fewer than 20 employees.” Because 70% of competitors were restaurants who could open and close at any time, new entrants did not need large corporate backing and were free to open
anywhere. The ability of so many small competitors to enter and compete in the industry indicated a steep learning curve. The steep learning curve and low capital requirement was threat to the industry because of the ease of rivals to enter the industry.

ii. Five Forces:

Our analysis revealed that there were about 624,511 commercial eating locations in the industry. Because rivalry intensifies as the numbers of competitors increase and as competitors become more equal in size and competitive strength, we conclude that the high number of competitors was a threat for the industry.

Based on industry sales of $345 billion, the leading competitor Starbucks had less than two percent of the market share. This fact coupled with the above mentioned 70% single unit establishments characterized the industry as having many competitors with very small market share. Because rivalry tends to be stronger when competitors are numerous or are of roughly equal size and in competitive strength, we conclude that the small relative size based on market share was a threat for the industry.

Switching costs and buyer loyalty were low for the industry. “Consumers (especially those who ate out often) were prone to give newly opened eating establishments a trial…loyalty to existing restaurants was low when consumers perceived there were better dining alternatives.” Because low switching costs and low buyer loyalty increase rivalry among competitors, we conclude that low switching costs and buyer loyalty were a threat to the industry.

It was not more costly to exit the industry than continue to participate. “Many restaurants had fairly short lives.” Based on our previous analysis of market share, we determined competitors were small in size and can enter and exit with little capital requirements. Assets were sold easily and the workers in the industry were not entitled to significant job protection. Because rivals had low barriers to exit they did not resort to deep discounts to remain in business. Continuous new entrants increased rivalry. We conclude that the ease of entry was a threat and ease of exit was an opportunity for the industry.

The industry's products were discretionary purchases. “The average U.S. consumer ate 76% of meals at home.” The fact that consumers could eat at home for less characterized the discretionary nature of the eating out option. Because discretionary spending was not necessary and represent consumers’ first costs to cut in economic difficulty, we conclude that the discretionary nature of the purchase was a threat to the industry.
iii. Changes to the Industry Structure and Competitive Environment:

As of 2006, the restaurant industry was growing by 5% a year. Due to this growth rate there was room for more firms to enter the industry. This changed the industry structure in the coming years by introducing more competitors. However, since the market was not saturated, firms entering were in a business environment that allowed them to obtain new market share. Since the long-term growth rate was increasing there was an opportunity for new firms to gain the growing market share.

The average U.S. consumer ate 76% of their meals at home. The average person in 2004 had $974 of income to spend on food purchases away from home. Customers were less likely to be loyal to a restaurant if they perceived a better option available to them. Patrons also used restaurants for more than just eating. Restaurants served as places where people could catch up on work, meet friends, and read the paper. The fact that majority of meals were eaten in the home and that restaurant spending was discretionary, coupled with the fickle and specific nature of the customer created strong competition among rivals, and resulted in a threat to firms.

Marketing innovation in product and promotion was especially strong in the restaurant industry. Firms constantly updated their menus to accommodate new trends such as low calorie, organic, vegetarian, and heart healthy foods. Restaurants also utilized Wi-Fi and large television screens in order to enhance the experience for customers. Happy hours and other events served as promotion to attract new customers. The constant marketing pressures created complex rivalries between firms and resulted in an altered industry structure. The industry structure resulted in a business environment where firms diligently adapted and changed with updated marketing mixes. This constant change was a threat within the industry.

Entry into the restaurant industry was marked by just over 7 of 10 eating and drinking places being independent, single-unit establishments with fewer than 20 employees. Exit from the industry was frequent and often firms were limited to short lives. The easy entry and exit of firms to and from the industry created a business environment that was fiercely competitive. The ease of new rivals entering and the large failure rate was a threat for firms within the industry.

iv. Existing Rivals Competitive Capabilities Analysis:

The case did not provide specific information about rivals’ resources and strategic goals to formulate conclusive competitive capabilities.
v. Key Success Factors:

The key success factors in the restaurant industry were dictated by what consumers deemed necessary attributes to have and what allowed the business to profit. Consumers did not dine at particular places that did not possess these qualities because they lost value in their purchase. Also, there were many substitutes that offered the key factors to patrons instead. The particular key success factors related to the restaurant industry were: low-cost production efficiency, customer service, breadth of product line and selection, ability to respond quickly to shifting market conditions, overall consumer experience, image and reputation, and high consumer volume.

The first key success factor was low-cost production efficiency, which was crucial in lowering prices for the consumer. When a restaurant could not keep costs low, the high costs were passed through to the consumer with a higher price. If customers did not believe the value in what they were buying was worth that high price, they did not pay for it. Since there were many competitors in the restaurant industry, the consumer shopped around for similar food at a lower price. Restaurants needed to keep these costs low to stay competitive and not risk bankruptcy.

Customer service was another key success factor because it added value to the meal. The consumer was not just purchasing food; they were paying for the entire experience. A component of this was having pleasant employees in all customer contact positions. Good customer service skills that made the customer feel comfortable in the restaurant helped to keep customers coming back. When a waitress went above and beyond her normal duties to please a customer, the patron was likely to return because of the great experience offered. Exceeding customer expectations was crucial in attracting loyal customers who returned to the establishment.

Another factor for success was having a wide breadth of product line and selection. Restaurants needed to offer many different kinds of dishes to attract a broad group of buyers. Some examples were serving chicken, beef, seafood, and vegetarian. If there were ten dishes or so within each of those categories, the restaurant was offering a large selection and a customer could find a meal they craved. Offering various types of dishes helped widen the breadth of what was offered, such as: breakfast, lunch, dinner, soups, salads, pasta, and sides. There were also various styles of food offered such as Mexican, bland, Cajun, Irish, Italian, Mediterranean,
and more. Such a broad selection ensured that customers found what they were looking for. If the consumer saw multiple meals he or she as interested in, he or she returned.

The fourth key success factor within the restaurant industry was the ability to respond quickly to shifting market conditions. Customers were constantly changing what they wanted, and restaurants needed to keep up with those changes. If a restaurant had an inability to change its menu, it could not compete with its rivals. Recently, consumers changed their needs to heart healthy, vegetarian, organic, low calorie, and low-carb. This also took into consideration seasonal changes. Soups became more prevalent in the winter than the summer. Certain seasonal soups like pumpkin, squash, and others were craved around the holidays, but not as much during other times in the year. Desserts and specialty beverages followed similar patterns. Restaurants needed to change their menus to satisfy customers’ cravings and remain competitive within the industry.

Having a good overall consumer experience was extremely important in the restaurant industry. This was crucial in building a loyal clientele that could promote the business through word-of-mouth tactics and regularly dined at the establishment. The overall experience took into consideration more than just food and customer service because it encompassed the entire value perceived by the consumer. This included price, food quality, quality of service, ambience and atmosphere, and having a variety of offerings. Without that great experience, a customer would not return and they could verbally damage the restaurant’s reputation when they told friends about their poor experience. This factor was important to build loyal customers and increase brand awareness.

Image and reputation was another key success factor because this was what attracted customers to the establishment. This also created word-of-mouth advertising for a restaurant. When something happened to tarnish a restaurant’s reputation, patrons no longer dined there, which led the company to go out of business. Image and reputation was how consumers perceived the company, which could add value for the customer when it was extremely good.

Another key success factor was having high consumer volume. No matter what type of eating establishment, having high customer foot traffic was essential for success. This increased brand recognition, word-of-mouth advertising, and sales. This factor was essential to success in the industry, without it, a restaurant was unable to grow, or even survive.
These seven key success factors dictated the industry and how restaurants needed to perform in order to remain competitive in the industry. The restaurant industry was purely competitive and extremely risky due to the large number of rivals. The seven factors were areas to focus on because that was what consumers deemed important.

**Critical Issues the Industry Faces:**

Our analysis led us to the following critical issues faced by the restaurant industry. There were many opportunities in the industry for businesses to capitalize on. According to the analysis of the industry drivers, we concluded that the business life cycle was still in growth and there was a capacity shortage in the industry. This was an opportunity for the industry. Based on our analysis of the five forces model, we concluded that there were many buyers in the industry with many choices in selection of products. This was also an opportunity for the industry. Based on our analysis of the industry drivers, five forces model, and the changes to the industry structure, we concluded that there were untapped markets and consumers were prone to give newly opened eating establishments a trial. Based on our analysis of the changes to the industry structure and the competitive environment and the five forces model, we concluded there was a threat to the industry in that there was low customer switching costs and low customer loyalty.

**Panera Bread Company’s Competitive Capabilities:**

**i. Business Strategy:**

Panera Bread Company’s strategic intent was “to make Panera Bread a nationally recognized brand name and to be the dominant restaurant operator in the specialty bakery-café segment.” Panera intended to achieve this by “being better than the guy across the street” and implementing a successful business model. Panera’s business model satisfied customers’ needs through providing quality food in a casual setting that continued to bring customers in for the ambiance as well as the food. Panera achieved sufficient profits to cover the costs of providing this value to the customers by selling food in the cafés and by collecting franchising fees and a percentage of franchisee sales. Management intended to grow the number of Panera Bread locations by 17% annually and expand further into suburban markets. Panera focused on achieving a 1 café per 160,000 people per location ratio by 2010 through effective use of franchising. Panera intended to build a loyal clientele by employing a superior business model
and offering artisan breads as a base of a high quality menu that changed to reflect evolving consumer tastes.

The prevailing market in which Panera operated experienced 5% growth in 2006. Thus Panera’s strategy of growth was in sync with market conditions. Furthermore, by focusing on building a loyal clientele through quality breads and a menu that suits customers tastes, Panera tailored the strategy to strengths the company already possessed. Panera’s ability to create well-crafted, predictive strategies and adapt well to changing conditions with reactive strategies indicated that Panera’s strategy was a dynamic fit to the company and market. Therefore, Panera’s strategy was a good fit for the company.

Operating in an almost pure competition environment, Panera faced threats from low cost and differentiated products. Panera employed a best cost provider strategy to take advantage of the large amount of value-conscious buyers who want a good meal and pleasant dining experience at an affordable price. Taking a position as best cost provider, in conjunction with a commitment to “providing crave-able food that people trust, served in a warm, community gathering place by associates who make guests feel comfortable” helped Panera achieve a strong strategy, but the competitive nature of the industry does not permit the strength of Panera’s strategy to become a competitive advantage.

Panera had 0.5409% market share of the $345 billion annual sales in the restaurant industry. Though Panera was not a dominant operator, this was a relatively big market share, given the nurture of the industry. The company’s profits and number of locations grew from 2002 to 2006. Panera’s strategy led to a strong financial position and a sizable market share.

Because Panera’s strategy was a good fit for the company, was strong in the competitive industry, and was financially successful, we concluded that Panera’s strategy was working very well and gave the company a competitive position in the industry. Therefore we feel Panera’s overall strategy, as well as its strategy to grow the business and build a loyal clientele was a strength.

ii. Functional Area Strategies:

Panera’s marketing strategy contained three distinct initiatives. The first aimed to raise the quality of awareness about Panera by focusing on quality crave-able food the consumer can trust, and by enhancing the appeal of its bakery-cafés as gathering places. The second initiative focused on boosting awareness and trials of Panera at multiple meal times. The third initiative
was to increase consumers’ perception of Panera as a dinner option. Throughout the entire marketing strategy Panera avoided hard-sell, in-your-face advertising. Panera preferred consumers “gently collide” with and discover the brand. As Panera performed well financially in past years, this marketing strategy was successful. However our analysis led us to conclude there was an untapped potential in the soft-sell marketing technique. This was a weakness that Panera must bolster to pursue industry opportunities.

Panera’s production and distribution strategy was to use economies of scale and centralize operations for the dough making process. There were 17 regional fresh dough facilities to service the 1,027 Panera bakery-café locations. By controlling the process at central locations Panera was able to ensure consistent quality and dough making efficiency. Panera’s production strategy supports the overall strategic intent of being better than the guy across the street and ensures quality to keep customers coming back. Because Panera’s production strategy supported the company’s overarching strategic goals, we concluded that the strategy was working well and was a strength for Panera.

Panera had a unique franchise system. Each franchise license was for a multi unit deal, usually for 15 bakery-cafés to be opened over six years. Panera only granted licenses to applicants who met stringent criteria. These criteria included a net worth of $7.5 million or more, access to resources that would allow for the expansion of 15 locations, real estate and multi unit restaurant operator experience and commitment to Panera’s brand, culture and passion. Historically, Panera’s ambitious franchising model was a success. Franchisees indicated a high level of satisfaction with Panera Bread Company’s concept, support and leadership. Likewise, Panera reported satisfaction with the quality and pace of franchisee openings and the franchisees’ operations. Panera committed limited fiscal resources to franchising; the company did not “finance franchisee construction of area development payment, or hold any equity in any of the franchise-operated bakery-cafés.” Because the franchising model supported the company’s intent to grow to a dominant restaurant operator, we concluded Panera’s franchising system was a strength.

Panera committed to constantly staying in tune with consumers’ changing tastes for the base of the research and development strategy. Panera regularly reviewed the menu and revised the options to sustain customer interest. When developing new products, Panera first made the menu items in test kitchens before introducing them in a select few bakery-cafés. Panera used the
test kitchens and select rollouts to determine customer response and ensure that the products could be produced in mass quantities and still maintain the high quality standards associated with the Panera brand. The successful products were then introduced in all the chain locations and integrated into menus. Because it helped keep up the Panera standard for quality food that customers craved, the research and development aspect of Panera’s strategy supported the marketing strategy. Furthermore, by ensuring consistently high quality food that consumers depended on, Panera’s extensive research and development supported the company’s strategic goal of becoming a dominant operator in the restaurant industry.

iii. Assessment of Panera Bread Company’s Strategic Performance:

- Business Strategy Performance

The strategic intent of Panera was to become a nationally recognized brand and dominant operator in the specialty bakery-café segment. In 2005 Panera Bread was the highest rated for the fourth year in a row among competitors in the Sandleman & Associates national customer satisfaction survey. Panera had also won “best of” awards in 36 states and across a range of markets. In addition, “J. D. Power and Associates’ 2004 restaurant satisfaction study of 55,000 customers ranked Panera Bread highest among quick-service restaurants in the Midwest and Northeast regions of the United States in all categories, which included environment, meal, service, and cost.” Panera created this nationwide renown through the successful implementation of the company’s business model.

In 2006 Panera opened 155 company and franchise owned cafés bringing the total units to 1,027 in 36 states. The continued expansion of cafés in new markets showed that Panera was operating successfully within the framework of the intended strategy. However, Panera managed to open only 1 café per 330,000 by 2006. So, although Panera had begun the process of increased penetration into markets, the benchmark given of 1 café per 160,000 people in 2010 at the time of the case had not been reached. Therefore a complete analysis of the success of the growth strategy was not possible.

Panera differentiated the bakery-cafés by implementing several important menu changes that addressed the targeted consumer needs and trends. The addition of “good carb” breads, antibiotic-free chicken, and an artisan line of sweet goods were employed as part of a differentiation strategy. In 2005-2006 Panera introduced the G2 concept in an attempt to bolster
the dining environment, thus providing more value for the customer. There was no data to support or deny the effectiveness of these strategic moves.

**Functional Area Strategic Performance**

Due to fact that the Panera won considerable accolades in consumer satisfaction, we determined that its marketing initiative of developing customer awareness of the quality and trust-worthiness of the company’s food was working. The second initiative of boosting awareness and trial of dining at Panera Bread at multiple meal times had not been shown operationally. Therefore, we were not able to determine the performance of this strategy. The marketing data showed that, “85% of consumers who were aware that there was a Panera Bread bakery-café in their community or neighborhood had dined at Panera on at least one occasion.” From this data, we concluded that the strategy was sound to pursue and specifically implement. The third initiative of increasing consumers’ perception of Panera as a dinner option had not yet been implemented with specific steps. The marketing research showed that 81% of consumers indicated a “considerable willingness” to try Panera at other meal times which supported following this strategy into the implementation phase.

Panera’s production and distribution goal was to ensure lowered costs and quality control with a strategy of centralized locations taking advantage of economies of scale. The quality of the product was evidenced by the many “best of” awards and other consumer satisfaction accolades. The lowered costs due to economies of scale and the high quality of the products indicate that Panera’s production and distribution strategy was successfully implemented and executed.

Panera pursued a unique franchising model based on multi-unit, multi-year deals with franchisees who were selected based on stringent criteria. The franchised cafés performed better in return on equity investments and average weekly and annual sales than company-owned cafés and were also equally or slightly more profitable. The measured success of the franchisee owned stores showed that the franchising model strategy was performing well.

The research and development strategy was to stay in tune with customers’ changing tastes. The implementation consisted of regularly reviewing and revising the menus, and the use of test kitchens for exploring new products and determining customer response. In 2003 Panera scored the highest level of customer loyalty among quick-casual restaurants, according to a study
conducted by TNS Intersearch. This customer loyalty indicated the success of Panera in anticipating customer needs through the company’s research and development strategy.

**iv. Resources:**

Panera had skills and expertise in sight selection and café environment. They chose sights and café environment by the following method. “Based on analysis of this information, including the use of predictive modeling using proprietary software, Panera developed projections of sales and return on investment for candidate sites.” This recourse was difficult but not impossible to copy. The length of time it would last depended on how hard competitors chose to work to develop similar technology. This resource was really competitively superior because no other competitors had it. It could not be trumped by rival’s resources because the same software had to be developed before competitors could use it. Because this resource was hard to copy, competitively superior, potentially long lasting and could not be trumped by rivals’ resources, the site selection and café environment was a competitive capability. This competitive capability was a strength that gave Panera a competitive advantage.

Our analysis revealed that Panera’s advertising and promotion strategy was too weak. They had underutilized promotion potential. Panera’s strategy was to raise the quality of awareness by the “caliber and appeal of its breads and baked goods, by hammering the theme “food you crave, food you can trust.” Panera also aimed to “raise awareness and boost trial of dining at Panera Bread at multiple meal times (breakfast, lunch, “chill out” times, and dinner.)” Panera avoided hard-sell approaches, preferring “instead to employ a range of ways to softly drop the Panera Bread name into the midst of consumers as they moved through their lives and let them ‘gently collide’ with the brand; the idea was to let consumers ‘discover’ Panera Bread and then convert them into loyal customers by providing a very satisfying dining experience.” This approach was a great concept and successful to an extent, however we conclude that because many of Panera’s competitors were using more aggressive promotion, the current strategy was not aggressive enough.

“Management claimed that the company’s fresh- dough-making capability provided a competitive advantage by ensuring consistent quality and dough-making efficiency.” Because this dough making capability allowed Panera to maximize the production capacity, used no preservatives, did not freeze the product and control the quality of the dough by making it themselves, this recourse was hard to copy. How long it would last depended on strengthening
competitor capabilities and their interest in the dough making market. Based on the first two tests, we conclude that this capability was really competitively superior and could not be trumped by rivals’ capabilities and therefore a competitive advantage. Panera’s franchise system used superior intellectual capital with the use experienced and capable workforce. The success of the franchise system was an example of proven managerial know-how. The site selection software granted the franchises cutting-edge knowledge in technology to choose locations and café environments. The stringent franchisee requirements employed only the most dedicated, well capitalized and capable franchisees as managers. The franchise system was hard to copy because of the stringent requirements for the franchisees, managerial know-how and the proprietary site selection software. Site selection system would tend to last because of how difficult it was to copy and could not be trumped by rivals because it was so rare, and was characterized by a gradual learning curve. This analysis led us to the conclusion that Panera’s franchise system was a distinct competitive capability and therefore gave Panera a competitive advantage.

The product research and development program was also an example of Panera’s superior intellectual capital. “Product development was focused on providing food that customers would crave and trust to be tasty. New menu items were developed in test kitchens and then introduced in a limited number of the bakery-cafés to determine customer response and verify that preparation and operating procedures resulted in product consistency and high quality standards. If successful, they were then rolled out system wide.” The research and development system was hard to copy because of the gradual learning curve and constant need for revision. Because every competitor was also engaged in tactics to improve product development, we conclude that this intellectual capital was only hard to copy in Panera’s specific product line. Because it was not generally hard to copy we do not conclude that it was competitively superior. Based on our analysis, we conclude that Panera’s product research and development was a resource capability and therefore strength, but it was not a competitive advantage because many competitors have the same resources.

Panera’s financial position was an important resource. Panera had a low debt to equity ratio. In 1998 this strategy began with the sale of Au Bon Pain for 73 million in cash. This strategy was well served by the franchise system. “Panera did not finance franchisee construction or area development agreement payments or hold an equity interest in any of the franchise-
The franchise system allowed Panera to keep long term levels debt low. This allowed Panera to use cash reserves and or take on long term debt at lower costs when capital was necessary to seize opportunities. Panera’s financial position was a resource capability because it was hard to copy. The resource tended to last long because the franchise system kept debt low. It was not really competitively superior because other competitors could have had similar financial positions. Because this capability was hard to copy but it was not competitively superior, we conclude that it was a capability and there for strength, but not a competitive advantage because others may have a similar financial position.

v. Value Chain:

- Inbound Logistics

The case does not provide enough information to comment on the inbound logistics that Panera has with suppliers. However, each franchisee purchased dough directly from Panera Bread. Panera had an interest in each of the franchised stores succeeding because the company received 4%-5% royalties from sales continually. This meant Panera as the supplier had an interest to keep prices of dough as low as possible to maintain viable franchise operations.

- Operations

Panera provided and required comprehensive front and back of house training, market analysis, and bakery-café certification. This corporate level tactic impacted the company’s franchised and company owned stores by enabling Panera to develop systems used by all the cafés thus applying economies of scale to operations. Since each café-bakery did not have to develop its own operations structure this reduced costs for each store. In addition, the methods Panera introduced to each store had proven historically successful, thus increased the learning curve for a new café and lowered costs.

Panera had a policy to not finance new franchisees, area development payment agreements, or hold any equity in the new cafés. This operational model resulted in minimal long-term debt and low capital intensity to expand the Panera brand.

All the cafés offered an assortment of 20-plus varieties of bread baked daily and as of 2006 at least 22 types of sandwiches. Each of these breads and sandwiches were regularly reviewed to determine whether the products matched regular customer needs, new consumer trends, and seasonal relevance. The complexity of the product line enabled Panera to match
menu items with a variety of customer needs. This process ensured that weak selling items would be removed limited excess inventory.

-Outbound logistics

Each franchisee purchased dough directly from Panera Bread. Each dough making facility was able to produce dough for six bakeries. The fresh dough was sold to both company-owned and franchised bakery-cafés at a delivered cost not to exceed 27% of the retail value of the product. These costs margins were achieved by producing the dough at central locations employing economies of scale.

-Sales and Marketing

Panera used focus groups to determine customer food and drink preferences, and price points. This work was done by only a few individuals at the corporate level and scaled to the rest of the cafés. The existing company and franchise owned cafés would be able to take advantage of this market information and reduce costs associated with sales and marketing information.

The franchising model Panera used required the franchisee to pay 0.7% of total sales to a national advertising fund and 0.4 % of total sales as a marketing administration fee. Franchisees were also required to spend 2.0 % of total sales on advertising in local markets. Panera contributed similar amounts of capital from the company owned stores. Requiring the franchise owned cafés to pay a significant portion of marketing costs allowed Panera Bread to lower the company’s capital contribution.

-Research and Development

New menu items were rolled out in limited cafés and developed in test kitchens prior to nationwide release. This process addressed two cost drivers. First, by employing economies of scale individual cafés will not have to spend resources and capital investing in the development of new menu items. Second, through the expertise of the advanced research and development department Panera ensured both quality of product and process. This resulted in less product waste and increased customer satisfaction and in turn lowered costs.

-Integrated Value Chain Effect

Panera Bread utilized both structural and executional cost drivers to lower costs on the value chain particularly in inbound logistics, operations, outbound logistics, sales and marketing, and research and development. The cost reduction across the value chain gave Panera a strong capability.
vi. Assessment of Panera Bread Company’s Financial Performance and Capabilities:

Panera Bread Company showed growth in its profitability from 2002 to 2006, but there were no industry standards presented to compare the numbers in relation to the industry and individual competitors. Panera Bread Company stated a desired growth rate of 17% each year, and the sustainable growth rates from 2003 to 2006 were all above this desired rate (See Financial Ratios Section), but the internal growth rates were slightly lower for these years (See Financial Ratios Sections). For the most part, Panera Bread Company showed consistent results for the profitability financial ratios calculated. Therefore the company maintained management’s objectives and values each year. Panera’s ability to maintain cash reserves allowed the company to expand and open new cafés while maintaining management’s goal of not taking on large amounts of long-term debt. Panera Bread Company showed increased revenues as the number of cafés increased, which shows company growth (See Financial Trend Graphs Section). Also, Panera’s current ratio was 1.16 in 2006, which shows the company was able to satisfy all current obligations from operating activities without the need for long-term financing. Since Panera strives to decrease long-term debt, the cash reserves could be used for expansion without the need to restrict assets for future obligations. The company presented low total debt and debt-to-equity ratios which allowed the company to avoid overleveraging itself. This also left some capacity for the company to take on long-term debt if deemed necessary during expansion. The company created a strong financial position for itself by having available cash reserves and diminishing the amount of long-term debt assumed. This created an opportunity for expansion.

vii. Strategic Issues Panera Bread Company Faces:

The strategic issues that Panera faced were as follows. Our first strategic issue was Panera’s potential to use its internal franchising capabilities to take advantage of the fact that the industry life cycle remained in its growth phase. The second strategic issue Panera faced was how to alter its existing promotion strategy in untapped markets in order to take advantage of the opportunity presented by customer’s willingness to try new restaurants. The third strategic issue was how Panera could use its internal capability to build loyal clientele to defend against the threat of low switching costs and low customer loyalty. The final strategic issue was how Panera could use its internal capability of advanced research and development skills to take advantage of the large number of buyers within the industry.
viii. Management’s Values:

Management valued the enthusiasm Panera Bread cafés showed for the quality and value of the products offered. The main example was in the company’s dough making capabilities. Panera believed that actions spoke louder than words, so the company needed to show the high quality of its food to the customers. Management believed that the “attractive menu and the dining ambience of its bakery-cafés provided significant growth opportunity, despite the fiercely competitive nature of the restaurant industry”. Management strived to become the dominant operator within the bakery-café segment as well as a leader in the specialty bread segment while making its brand name nationally recognized. Another key value within Panera’s management was maintaining a debt-free balance sheet. The ability to uphold this value came from the company’s franchising model because the franchisees financed the majority of the café building expenses. Management stressed the quality of the food and service offered and knew that all other goals, such as expansion, recognition, and holding a higher market share, would simply fall into place as a result.

ix. Organizational Culture:

Panera Bread Company’s organizational culture began with the overall company and the dough-making facilities and spread out to the bakery cafés, whether company owned or franchised. Panera Bread Company was centered on its dough-making capabilities. The company guaranteed freshness and high quality in each dough it created. The dough was then passed to the cafés, where it was baked fresh and delivered to the customer. The quality controls within the company were maintained through the entire process to ensure that the customer would be pleased with his purchase. Quality was the basis for success, and quality was what the company relied on to generate loyal customers. Franchising was also a crucial aspect to Panera’s organizational culture because cafés were where the majority of customer contact occurred, and it was the basis for some of management’s values. Panera’s franchising model was extremely stringent, so only certain individuals were able to have cafés. There were eight criteria that had to be met in order to be considered, and a passion for fresh bread was one of them. Panera ensured that each franchisee had the capital and prior knowledge necessary to succeed. The stringent criteria and Panera’s site selection technology provided a strong basis for café success, which in turn led to a strong and satisfying organizational culture. Although Panera did not own the franchised cafés, the company dictated where supplies could be obtained to ensure quality.
Panera also trained the franchisees so they could operate on their own successfully, but turn to the company for guidance when necessary. The open environment was helpful without it being too overbearing. The strength in the organizational culture was a contributing factor to Panera’s success and continued growth.
Appendices

i. SWOT Matrix
ii. Stakeholder Matrix
iii. Financial Ratios (See attached Excel file)
iv. Financial Trend Graphs
v. Responses to Questions Not Answered in the Presentation
### i. SWOT Matrix

<table>
<thead>
<tr>
<th><strong>STRENGTHS:</strong></th>
<th><strong>WEAKNESSES:</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>- Strong and attainable growth strategy</td>
<td>- Under utilized potential in promotion strategy</td>
</tr>
<tr>
<td>- Ability to build a loyal clientele</td>
<td>- Frequent diners only come at one meal time per day</td>
</tr>
<tr>
<td>- The business model</td>
<td>- Only located regionally</td>
</tr>
<tr>
<td>- Franchising system &amp; site selection and proprietary software</td>
<td></td>
</tr>
<tr>
<td>- Research and Development &amp; Product Innovation</td>
<td></td>
</tr>
<tr>
<td>- Financial position – lack of long term debt</td>
<td></td>
</tr>
<tr>
<td>- 81% of frequent and moderately frequent customers indicated a willingness to try Panera for multiple meal times</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>OPPORTUNITIES:</strong></th>
<th><strong>THREATS:</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>- The industry life cycle is still in growth</td>
<td>- Low switching costs/low customer loyalty</td>
</tr>
<tr>
<td>- Low cost substitutes viewed as lower quality &amp; value</td>
<td>- Product is a discretionary purchase</td>
</tr>
<tr>
<td>- Large number of small buyers in the industry (Lack of buyer bargaining power)</td>
<td>- Substitutes are convenient and lower priced</td>
</tr>
<tr>
<td>- Buyers are characterized as likely to give new restaurants a try</td>
<td>- Wide breadth of competitive rivalry</td>
</tr>
<tr>
<td></td>
<td>- Steep learning curve</td>
</tr>
</tbody>
</table>
## Stakeholder Matrix

<table>
<thead>
<tr>
<th>Stakeholders</th>
<th>Companies, Groups, And Individuals</th>
<th>Type/Nature of the Relationship/ What We Do For Each of Them</th>
<th>Needs</th>
<th>How We Satisfy Those Needs</th>
</tr>
</thead>
</table>
| Customers    | -U.S. Consumers                    | -A chain of cafés perceived as a neighborhood bakery- café which can be found in various locations around the U.S. and quality is consistent in all locations | -A quality food option which is perceived as a good value  
-A pleasant dining experience with good service and a warm ambiance | -By providing quality food in a casual setting that continued to bring customers in for the ambiance and the food  
-Creating food consumers crave and can trust at all locations |
| Competitors  | -Independent single-unit establishments with fewer than 20 employees  
-Fast-casual restaurants  
-Commercial eating institutions | -Competed on a local level, as Panera desired to be seen as the local, neighborhood café and gathering place  
-Competed on inviting dining environment, quality of food and enticing menus  
-Competed on price, service, ambiance, overall experience and convenience | | |
| Employees    | -Franchisees                        | -Provide a successful franchising model to be pursued by highly | -Preopening assistance with market | -Provided market analysis and site selection assistance, lease review, |
capitalized, experienced and passionate individuals

analysis and site selection, training programs, leadership

new store opening assistance, a comprehensive initial training program, and a program for hourly employees, benchmarking data regarding costs and profit margins, company developed marketing and advertising programs, neighborhood marketing assistance

<table>
<thead>
<tr>
<th>Shareholders</th>
<th>Owners of the 31,313 shares outstanding</th>
<th>Provided a stable company to invest in</th>
<th>Do not pay dividends</th>
</tr>
</thead>
<tbody>
<tr>
<td>Community</td>
<td>The community of the regional markets of company and franchised café</td>
<td>Provide a gathering place for locals and visitors and support the community the locations operate in</td>
<td>A food option and company that adds value to its product and the community at large</td>
</tr>
</tbody>
</table>
iv. Financial Trend Graphs:

This figure shows the net income for Panera Bread Company from 2002-2006. It depicts a steady increase in net income each year.

This figure depicts the net cash provided by operating activities for Panera Bread Company from 2002 to 2006. It shows an increase over time, except from 2005 to 2006.
This figure shows the number of cafés opened at the end of each year. It depicts growth within the company. It also shows that franchise-owned cafés are more prevalent than company-owned ones, which shows success in the company’s franchising model.

This graph shows a steady increase in revenues for each café over time.
v. Responses to Questions Not Answered in the Presentation:

Alterations to Opening Cafés in Untapped and Low Penetrated Markets Recommendation:

Our recommendation needed to be altered to provide a separate action plan from recommendation to pursue a more aggressive soft-sell promotion strategy. We altered this recommendation by moving Panera’s focus when opening new bakery-cafés using the superior franchising model to solely untapped markets. These untapped markets would allow for sufficient growth to achieve the desired 1:160,000 ratio.

Alterations to the More Aggressive Soft-Sell Promotional Strategy Recommendation:

Recommendation two needed to be altered from a marketing strategy to a purely promotional strategy. Panera needed to promote its quality menu by implementing the suggested promotional strategies in its bakery cafés. The purpose of the promotional campaign was to bring new customers into the cafés. This satisfied the opportunity within the industry that customers are prone to try newly opened eating establishments in their community. The campaign needed to be implemented in untapped and low-penetrated markets in order to develop brand awareness by attracting new patrons. Though it may help, it will not be as successful in the highly-penetrated markets because Panera is already an established company with high brand awareness and loyal customers.

Alterations to Implementation of “Oven Fresh, To Go” Program Recommendation:

In response to your concerns regarding recommendation three, we agree that our implementation of “Oven Fresh, To Go” did not specifically address the low switching cost threat by rewarding return customers for their loyalty. To resolve this issue, we altered the implementation steps to include a punch card in the to-go packaging that would reward existing “Oven Fresh, To Go” customers for their loyalty and raze their switching costs with progressive discounts based on their level of return patronage.

Alterations to Broaden Product Scope Recommendation:

During the presentation of the recommendations there was concern that recommendation 4 did not adequately address the goal of increasing market share. The primary concern was that offering an expanded dinner menu after 430 pm would not be incentive enough to overcome
factors of image, location, and substitutes for Panera to obtain a relevant increase in market share. To bolster the strength of our recommendation and overcome the aforementioned hurdles to success we have amended our recommendation to include the addition of beer and wine at select Panera locations. A Panera site will qualify for alcohol consideration if the area demographics and local legal and regulatory environment are ideal. Selected locations will participate in wine-tasting and other events to engage the surrounding community. The combination of new menu items and select sites serving alcohol will create a new and lively experience for dining at Panera.