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HEDGEYE

PANERA BREAD COMPANY

FLASH CALL: THE ACTIVIST PLAYBOOK

APRIL 17, 2015

LEGAL

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PLEASE SUBMIT QUESTIONS* TO

QA@HEDGEYE.COM

*ANSWERED AT THE END OF THE CALL

HEDGEYE RESTAURANTS IDEA LIST

LONG LIST		TRADE	TREND	TAIL
LONG				
YUM	Yum! Brands*	-	✓	✓
ZOES	Zoe's Kitchen*	✓	-	✓
WEN	The Wendy's Company	-	✓	✓
CMG	Chipotle Mexican Grill	✓	✓	✓
PNRA	Panera Bread Company	-	✓	✓
LONG BENCH				
LONG				
JACK	Jack In The Box	-	✓	✓
PLKI	Popeyes Louisiana Kitchen	-	✓	✓

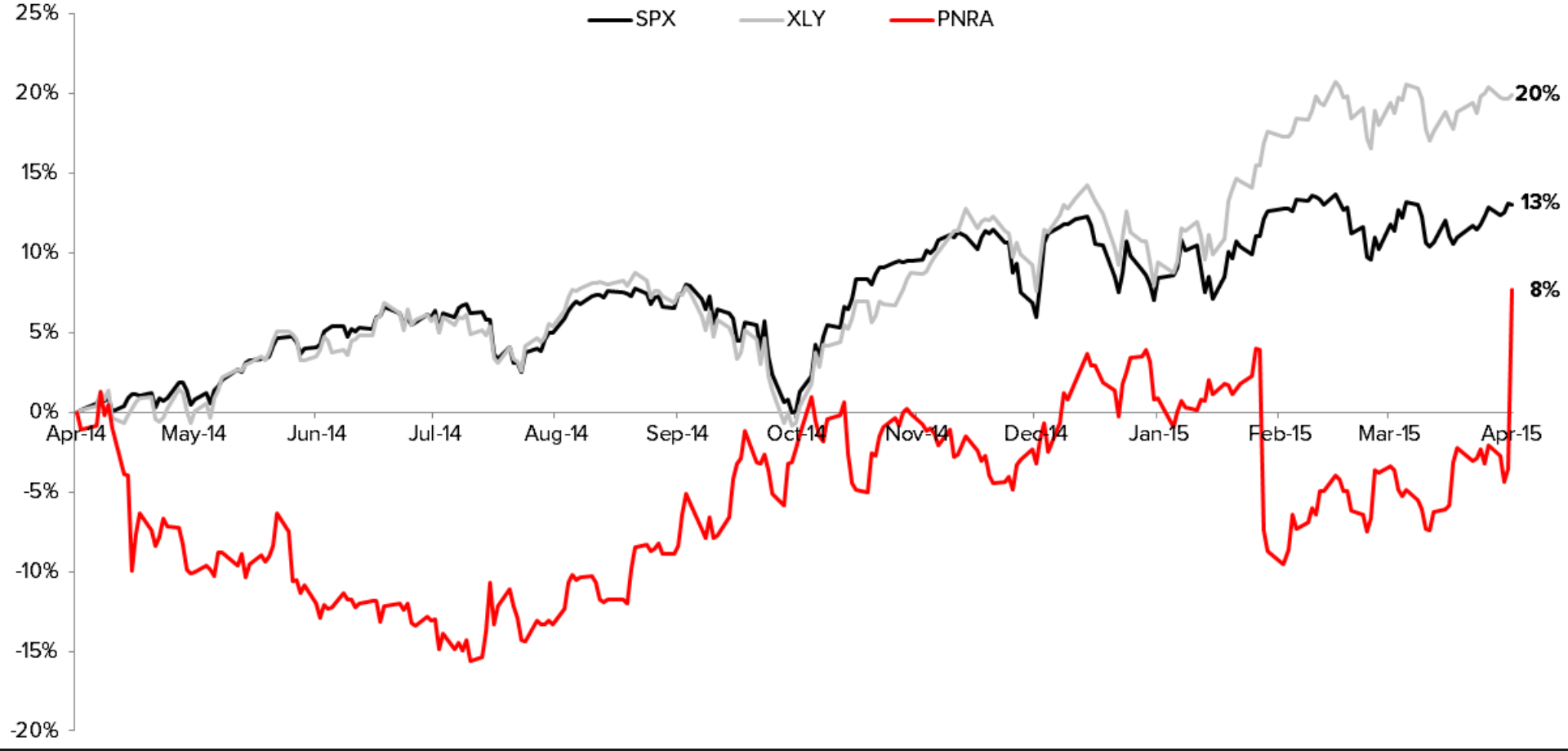
SHORT LIST		TRADE	TREND	TAIL
SHORT				
SHAK	Shake Shack*	-	X	X
DFRG	Del Frisco's Rest. Group	X	X	X
NDLS	Noodles & Co.	X	X	-
CHUY	Chuy's Holdings	X	X	-
SHORT BENCH				
SHORT				
PLAY	Dave & Busters Ent.	-	X	-
HABT	Habit Restaurants	-	X	-
CBRL	Cracker Barrel	X	X	✓
CAKE	The Cheesecake Factory	-	X	-
EAT	Brinker International	X	X	✓
DRI	Darden Restaurants	X	X	-

*Denotes Hedgeye Best Idea

Bench = timing is not right, or research is in progress.

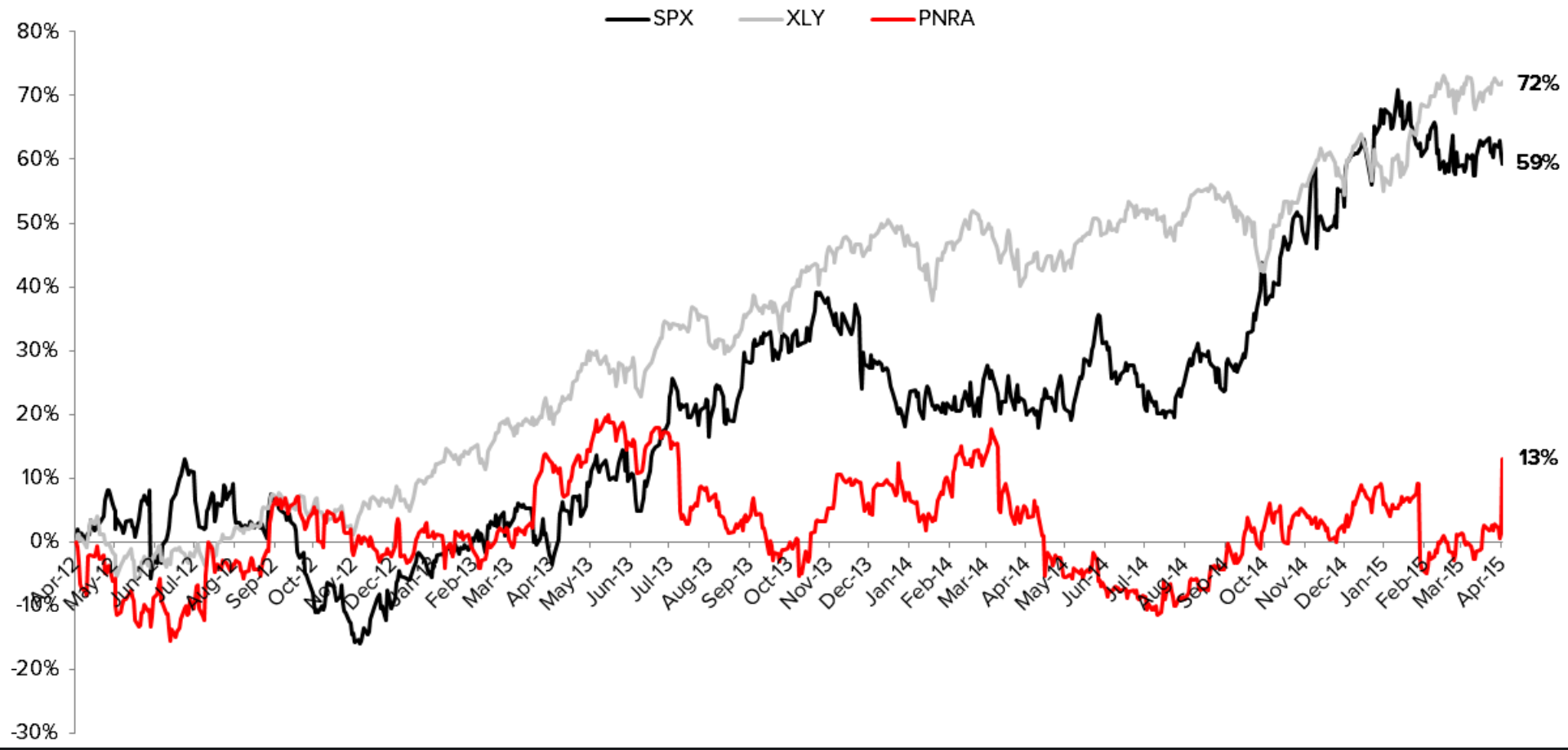
BACKGROUND

ONE YEAR PRICE PERFORMANCE



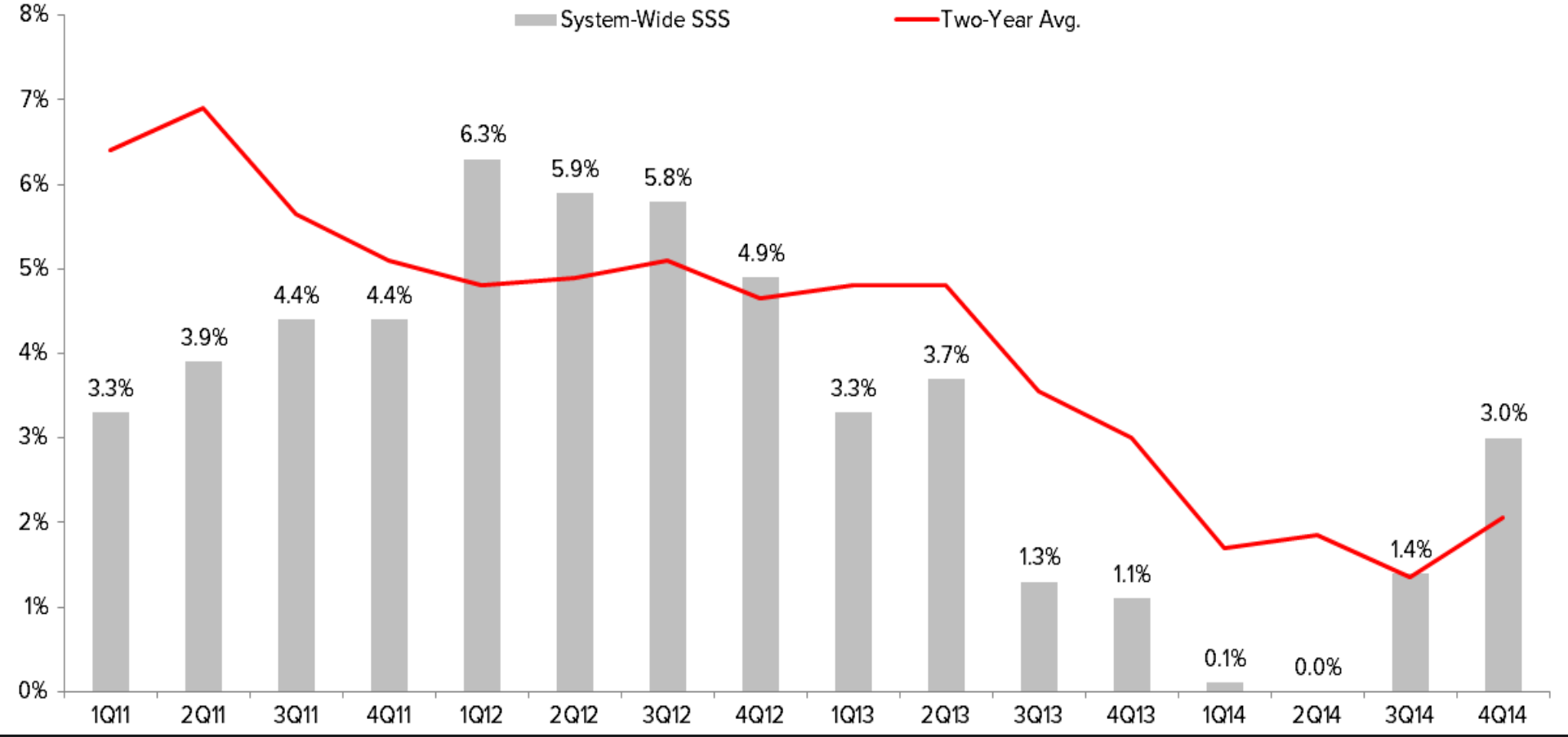
Sources: Hedgeye Research; FactSet

THREE YEAR PRICE PERFORMANCE



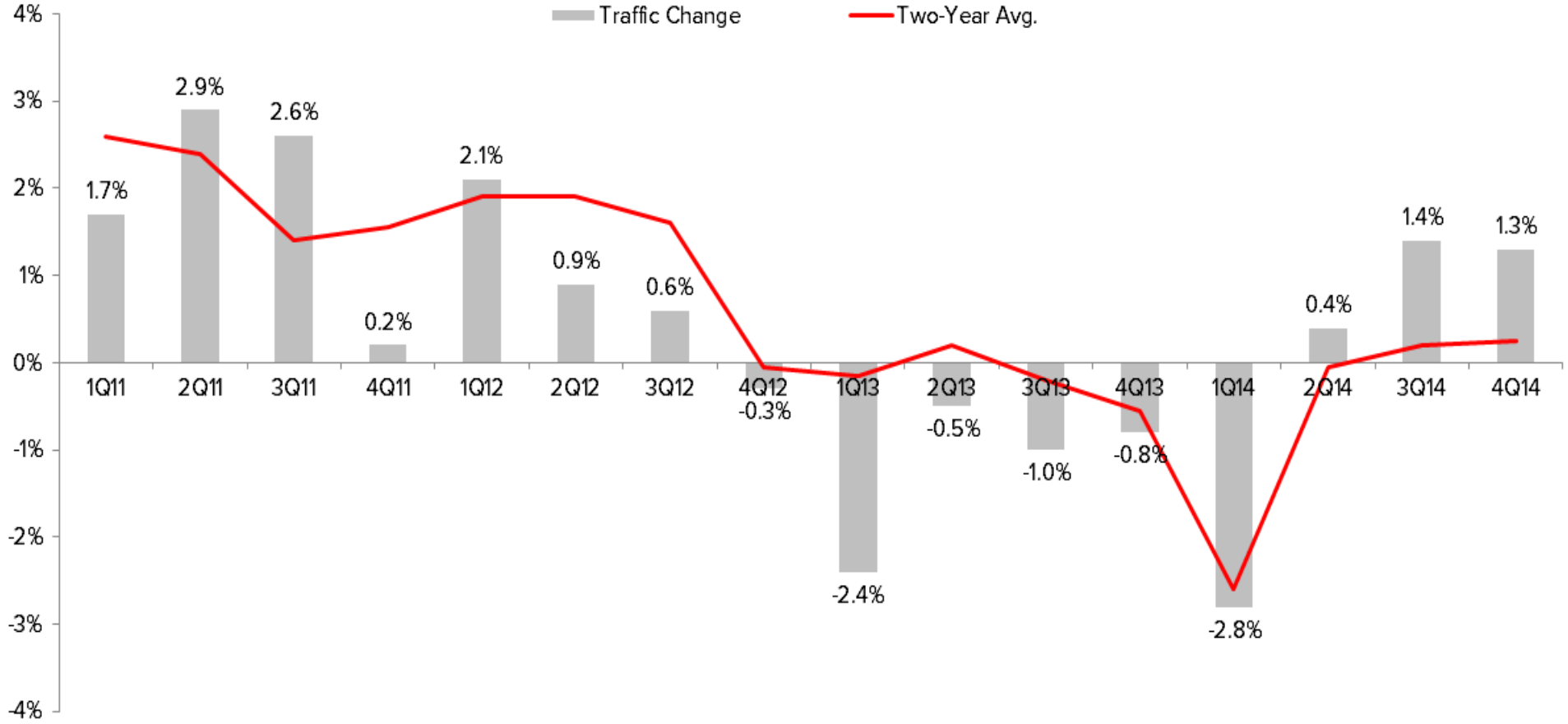
Sources: Hedgeye Research; FactSet

SYSTEM-WIDE SAME-STORE SALES



Sources: Hedgeye Research; Company Filings

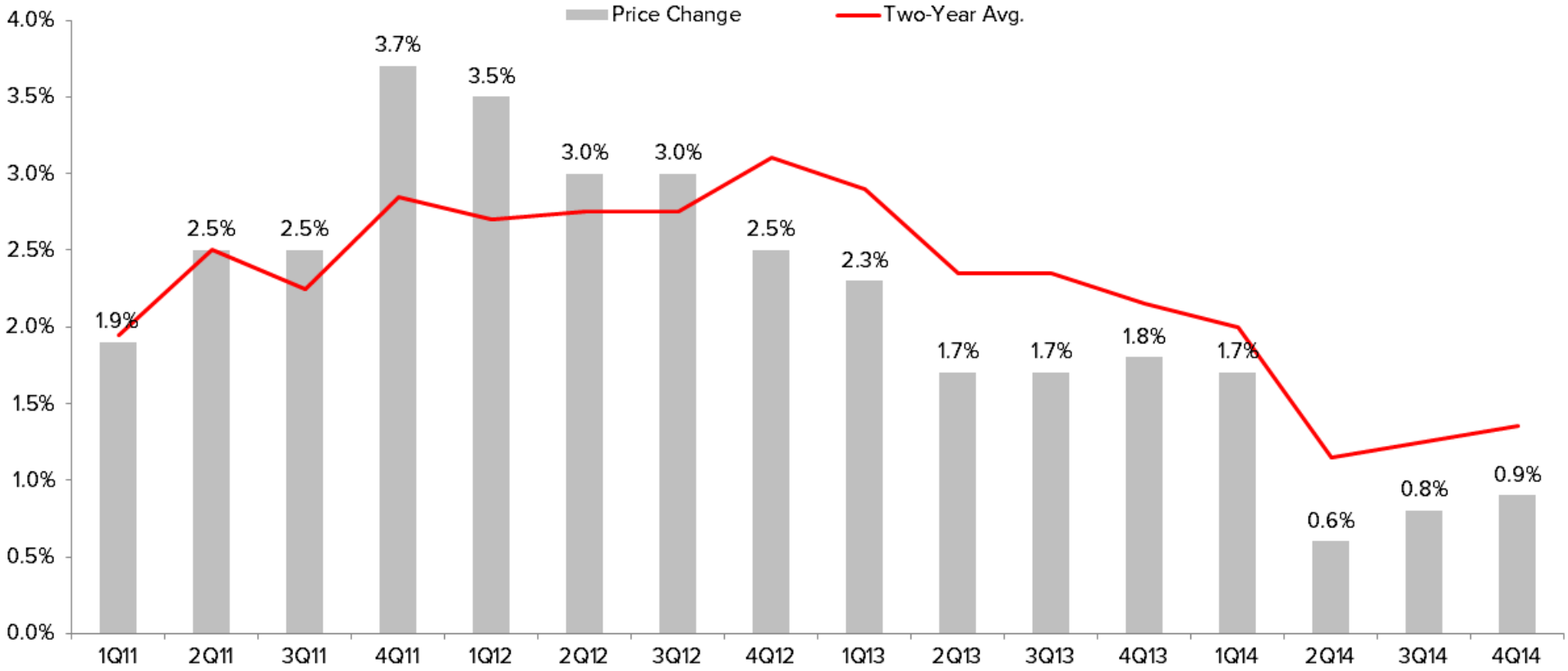
TRAFFIC HAS BEEN SOFT



Sources: Hedgeye Research; Company Filings

PRICE CHANGE

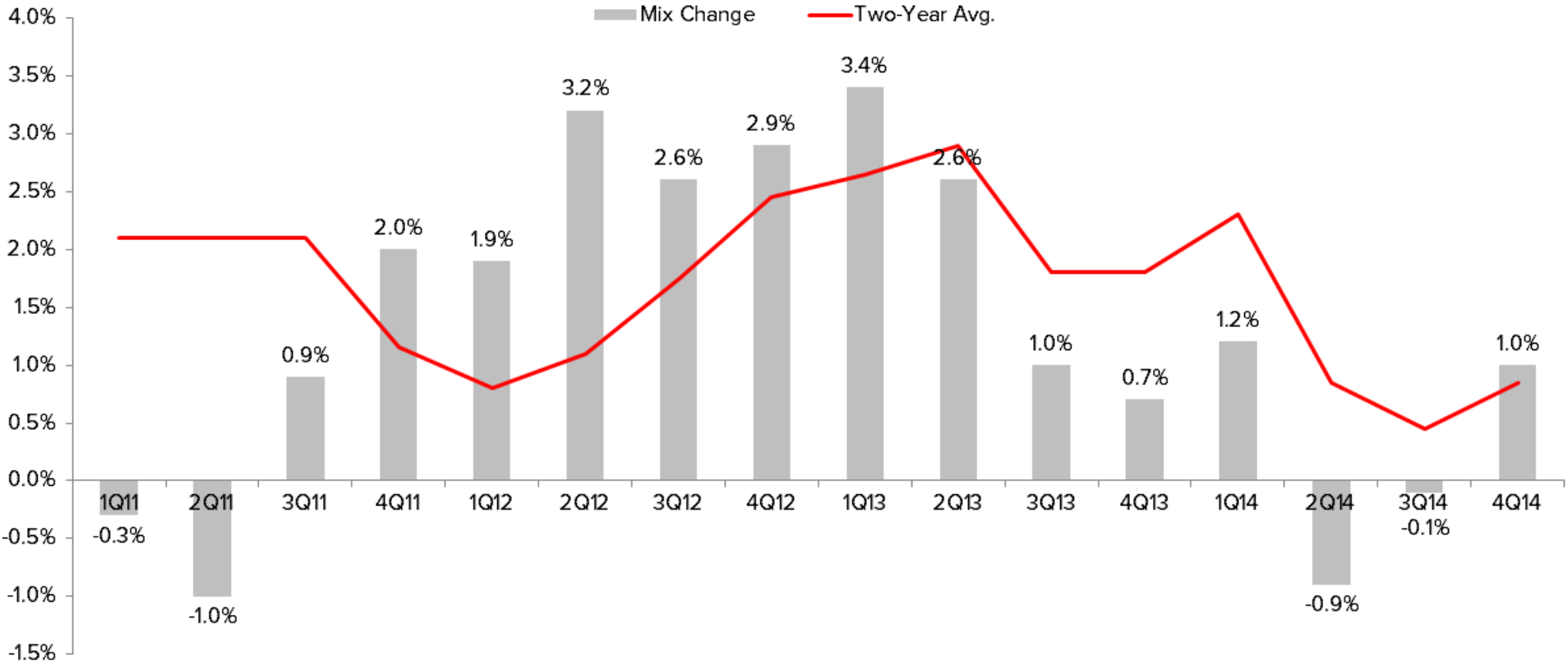
PNRA HAS USED PRICE AGGRESSIVELY IN THE PAST



Sources: Hedgeye Research; Company Filings

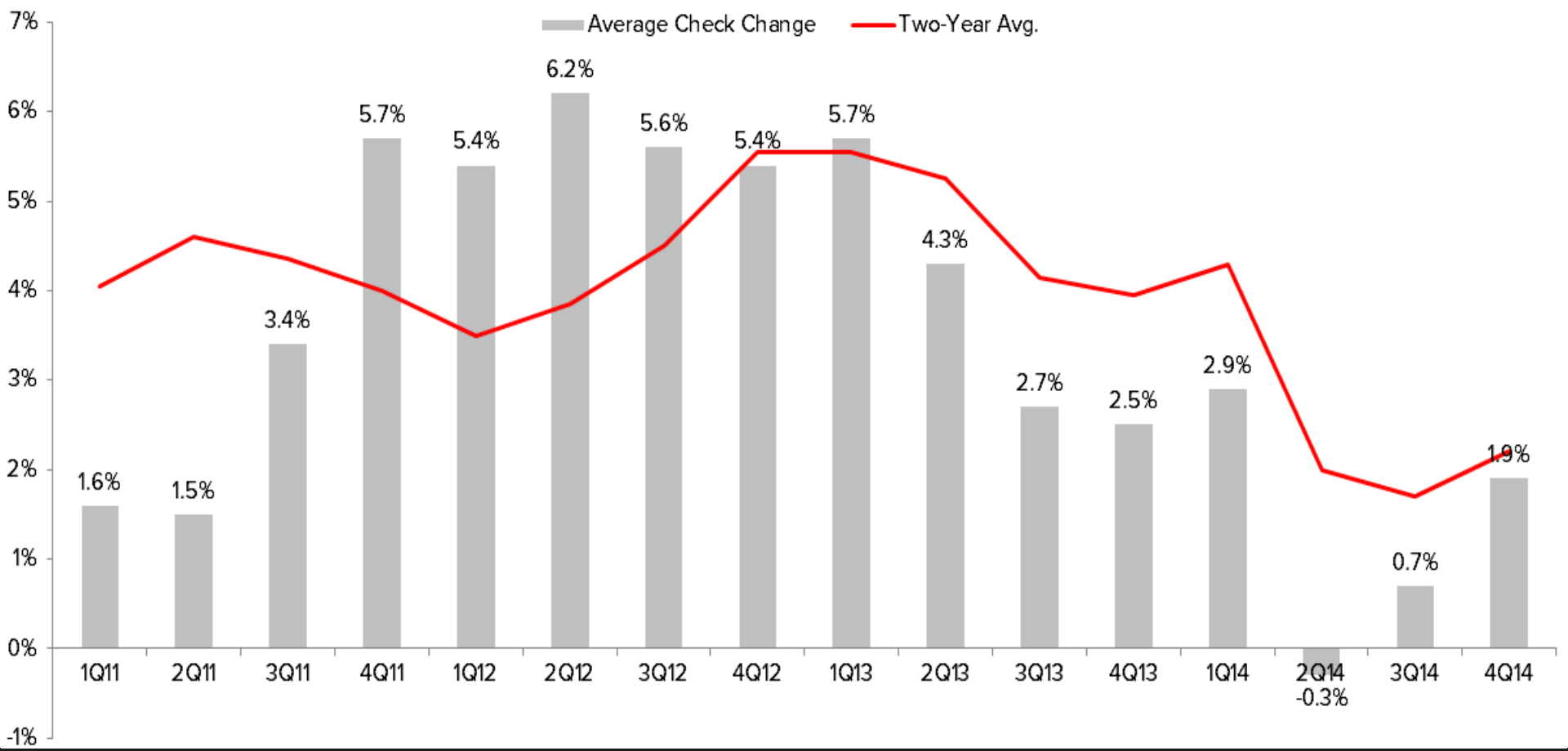
MIX CHANGE

TO IMPROVE TRAFFIC, THEY'VE INTRODUCED LOWER PRICED ITEMS



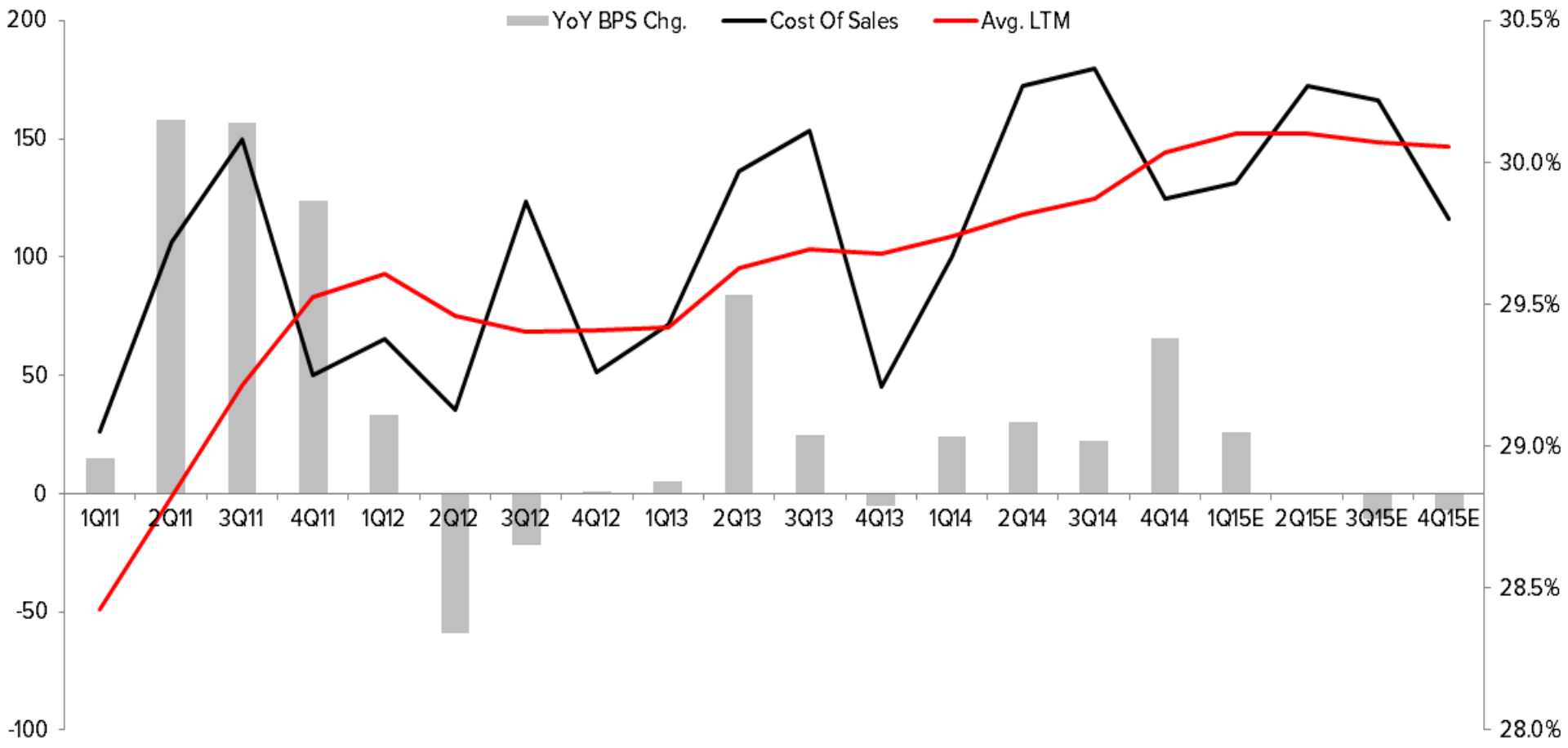
Sources: Hedgeye Research; Company Filings

AVERAGE CHECK CHANGE



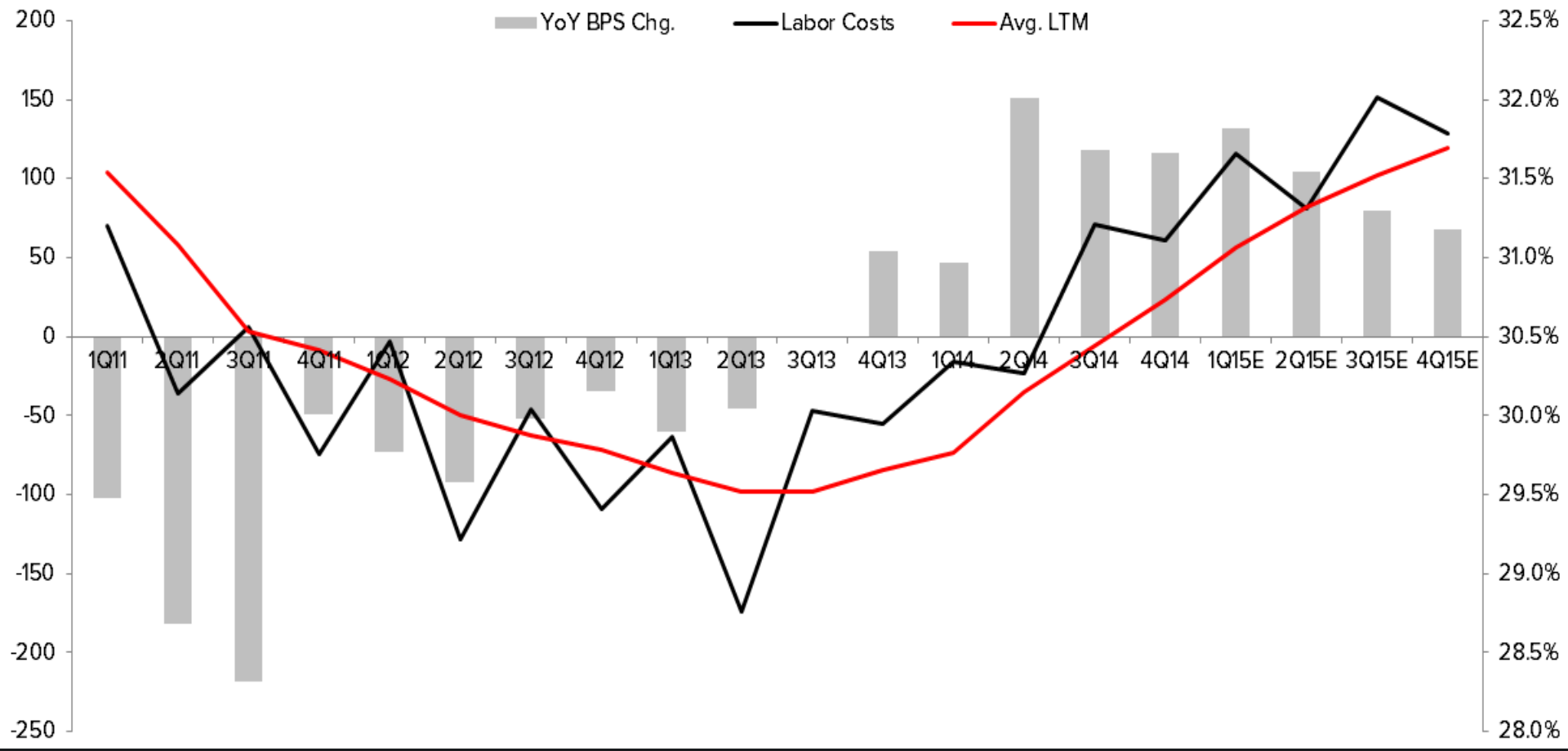
Sources: Hedgeye Research; Company Filings

COST OF SALES



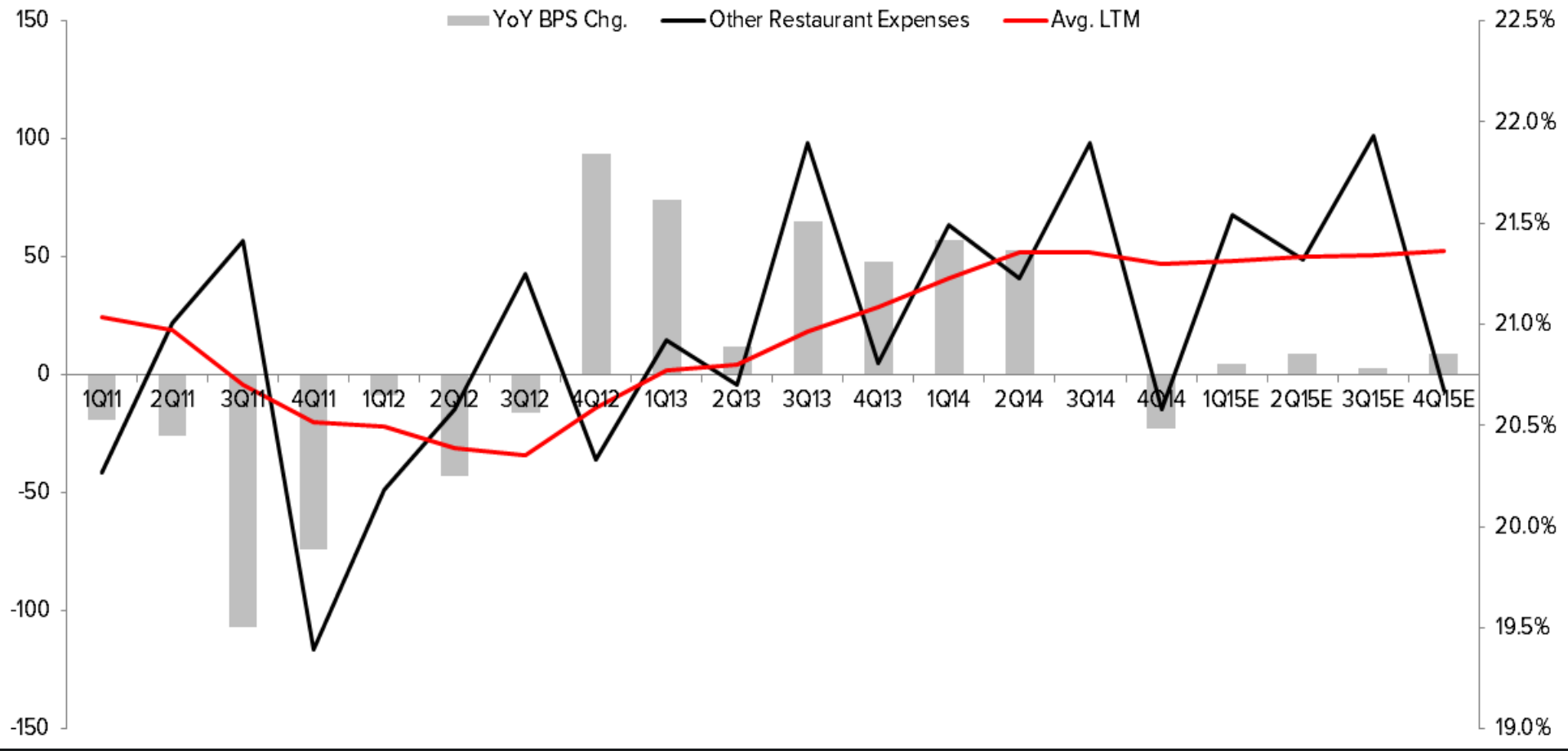
Sources: Hedgeye Research; Company Filings; Consensus Metrix

LABOR COSTS



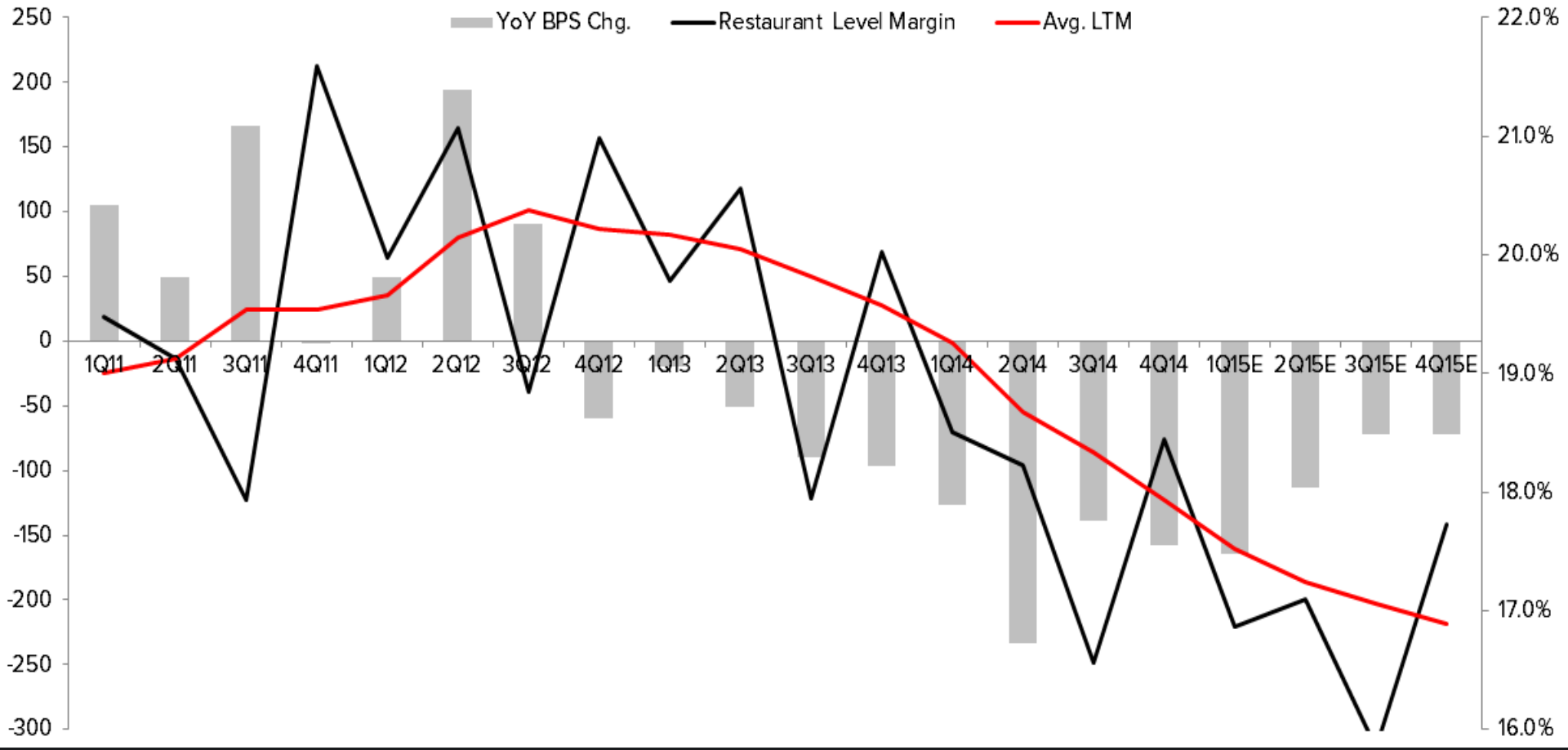
Sources: Hedgeye Research; Company Filings; Consensus Metrix

OTHER RESTAURANT EXPENSES



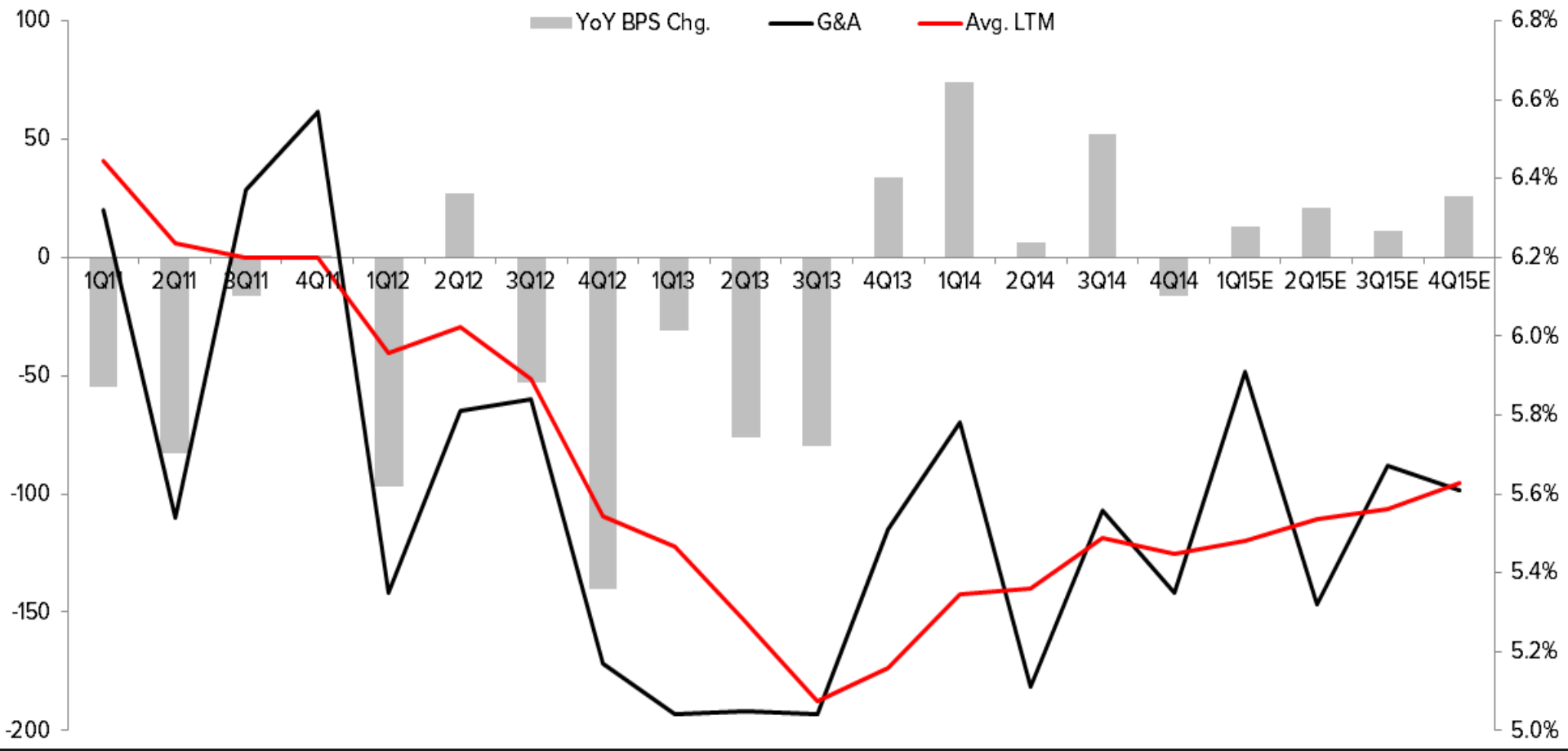
Sources: Hedgeye Research; Company Filings; Consensus Metrix

RESTAURANT LEVEL MARGIN



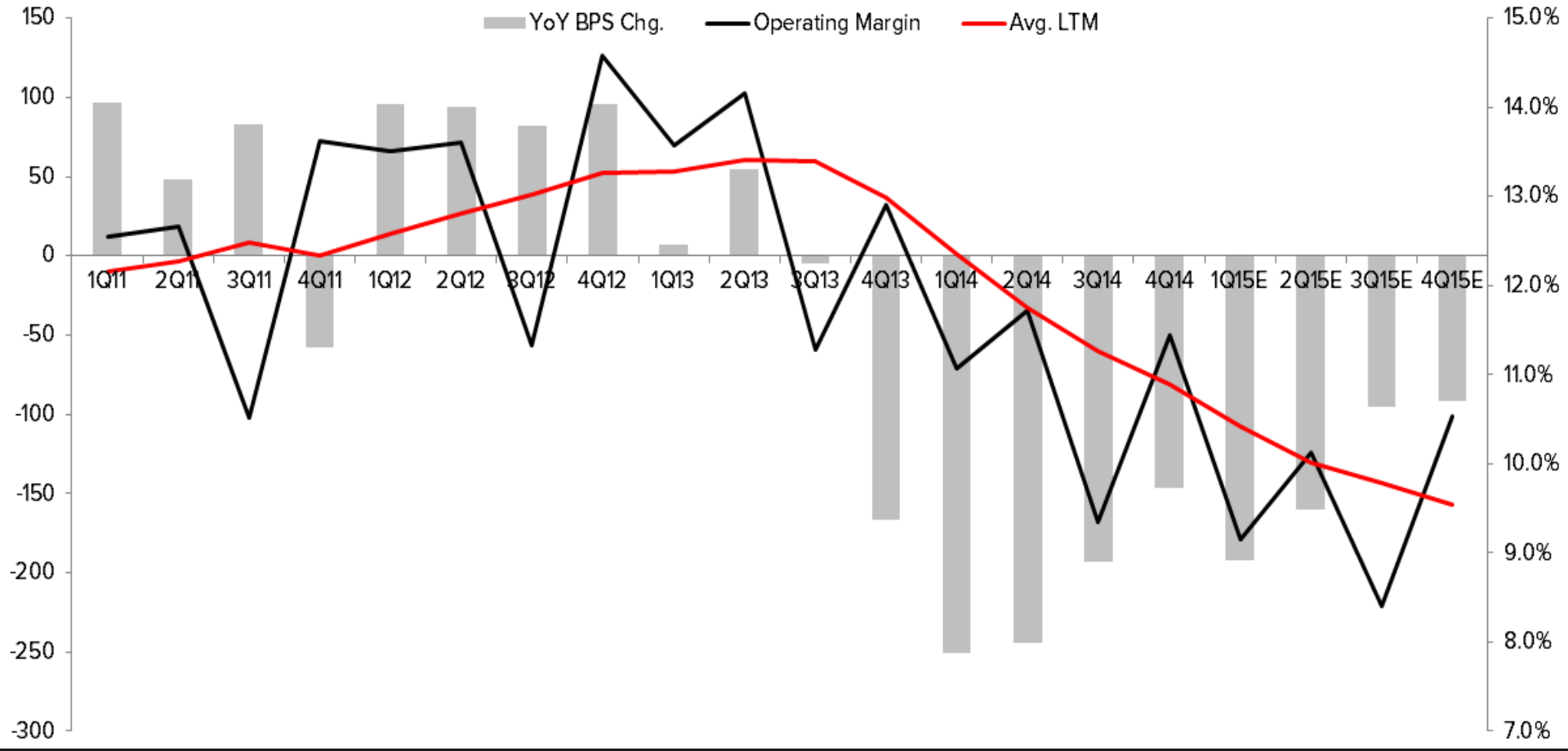
Sources: Hedgeye Research; Company Filings; Consensus Metrix

G&A EXPENSES



Sources: Hedgeye Research; Company Filings; Consensus Metrix

OPERATING MARGIN



Sources: Hedgeye Research; Company Filings; Consensus Metrix

RECENT DEVELOPMENTS

SUMMARY OF WEDNESDAY'S PRESS RELASE

- Panera plans to assume $500mm of debt to repurchase shares over the next twelve months.
- Management also disclosed updated details on its plan to refranchise 50 to 150 stores.
- 73 company stores will be sold to existing franchisees with proceeds going toward additional share repurchases of about $125-150mm.
- This represents an increase from the previous assumption of $100mm of share repurchases.
- The Panera model now assume 2015 share repurchases of $650mm, which will add approximately $0.15 to 2015 EPS.

A HOLISTIC APPROACH TO RESHAPING PNRA

SIGNIFICANT OPPORTUNITY TO CREATE VALUE

- Change is inevitable.
- Since the early days of the company back in 1981, consumer tastes, behavior, and technology have all changed drastically – rendering parts of the Panera model outdated.
- The best way forward today is vastly different from the ways of the past.
- Our thoughts are in line with Mr. Shaich's belief that Panera's success is dependent on its ability to create "long-term concept differentiation."
- Consumer behavior and tastes are evolving, and the changes Panera is making to its food policy are just the beginning.
- Ultimately, significant change will make Panera and even stronger company while creating significant shareholder value.

PANERA 2.0 ROLLOUT & BEGIN MOLDING A CONCEPT OF THE FUTURE

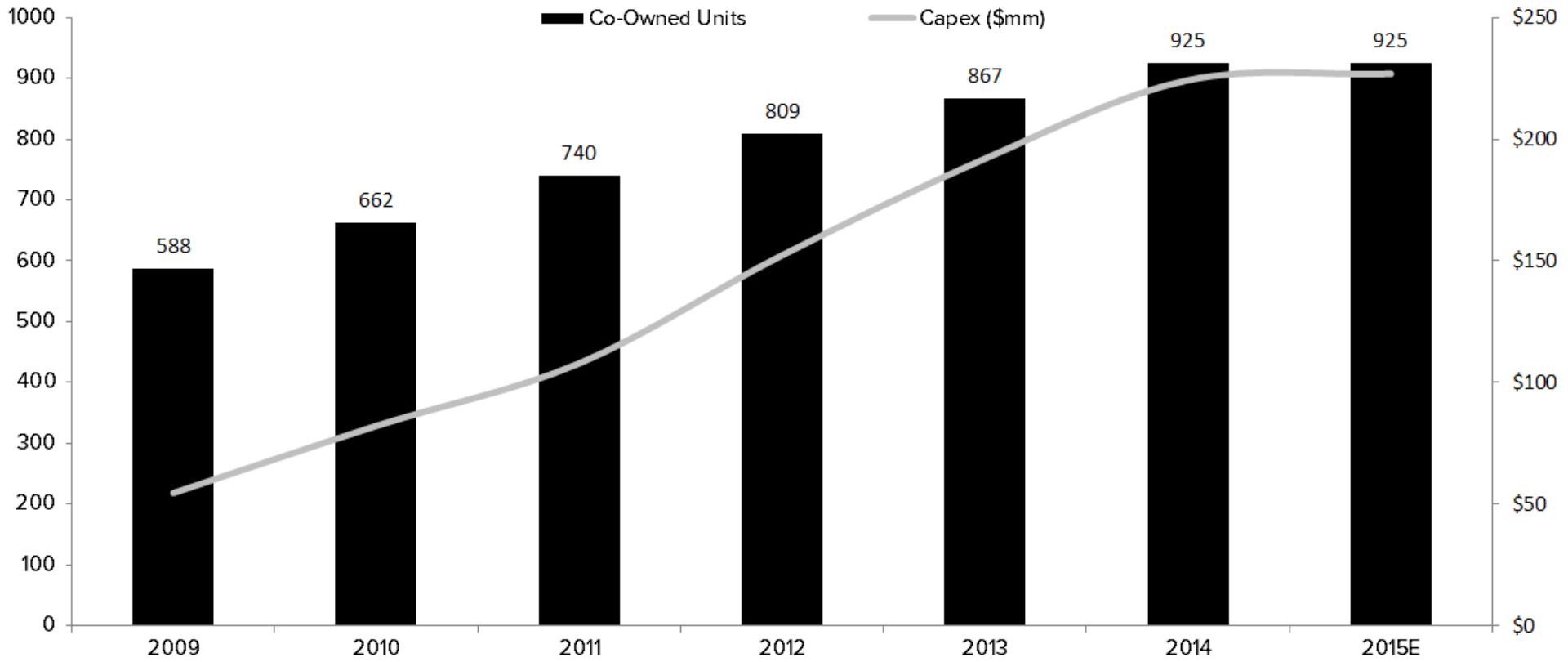
PANERA 2.0 & A LOOK AT PANERA 3.0

- Has Panera 2.0 accomplished what Mr. Shaich intended it to?
- Did Panera 2.0 go far enough?
- There can be much more done to improve the efficiency of the box.
- Panera 3.0 needs to be a holistic approach to the Panera of the future.
- None of the initiatives management has previously laid out address improving pain points that exist in the back of the house.
- Panera needs to eliminate menu items that are difficult to prepare and don't have the customer sell through.
- Management must rethink the part of the box that is dedicated to selling bread, which is less than 7% of sales.
- Per capita consumption of bread has been declining since 2000.

SLOW UNIT GROWTH AND CUT CAPITAL SPENDING

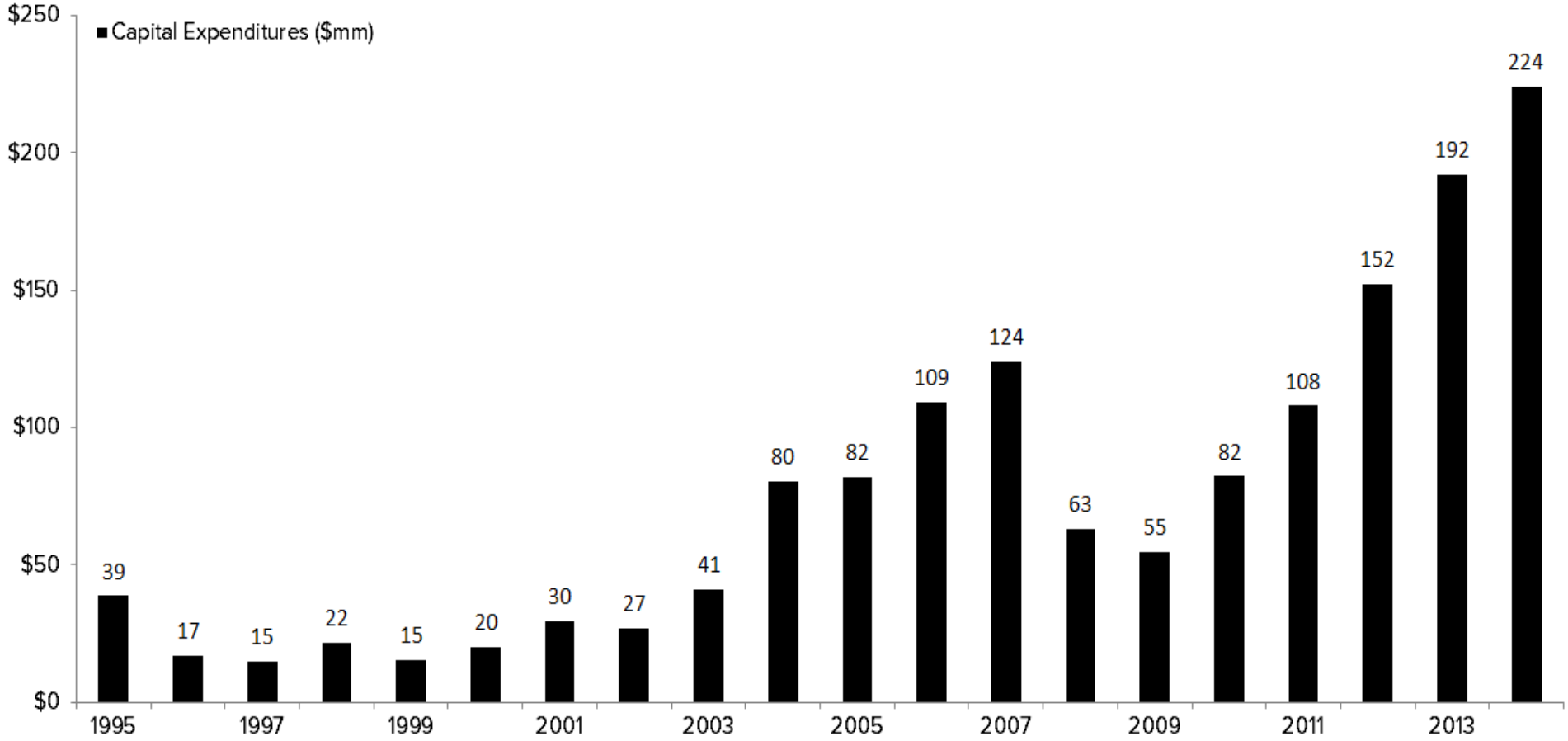
COMPANY UNITS VS CAPITAL EXPENDITURES

THIS IS AN EASY DECISION WITH SIGNIFICANT BENEFITS



Sources: Hedgeye Research; Company Filings; Consensus Metrix

RECENT ACCELERATION IN CAPEX



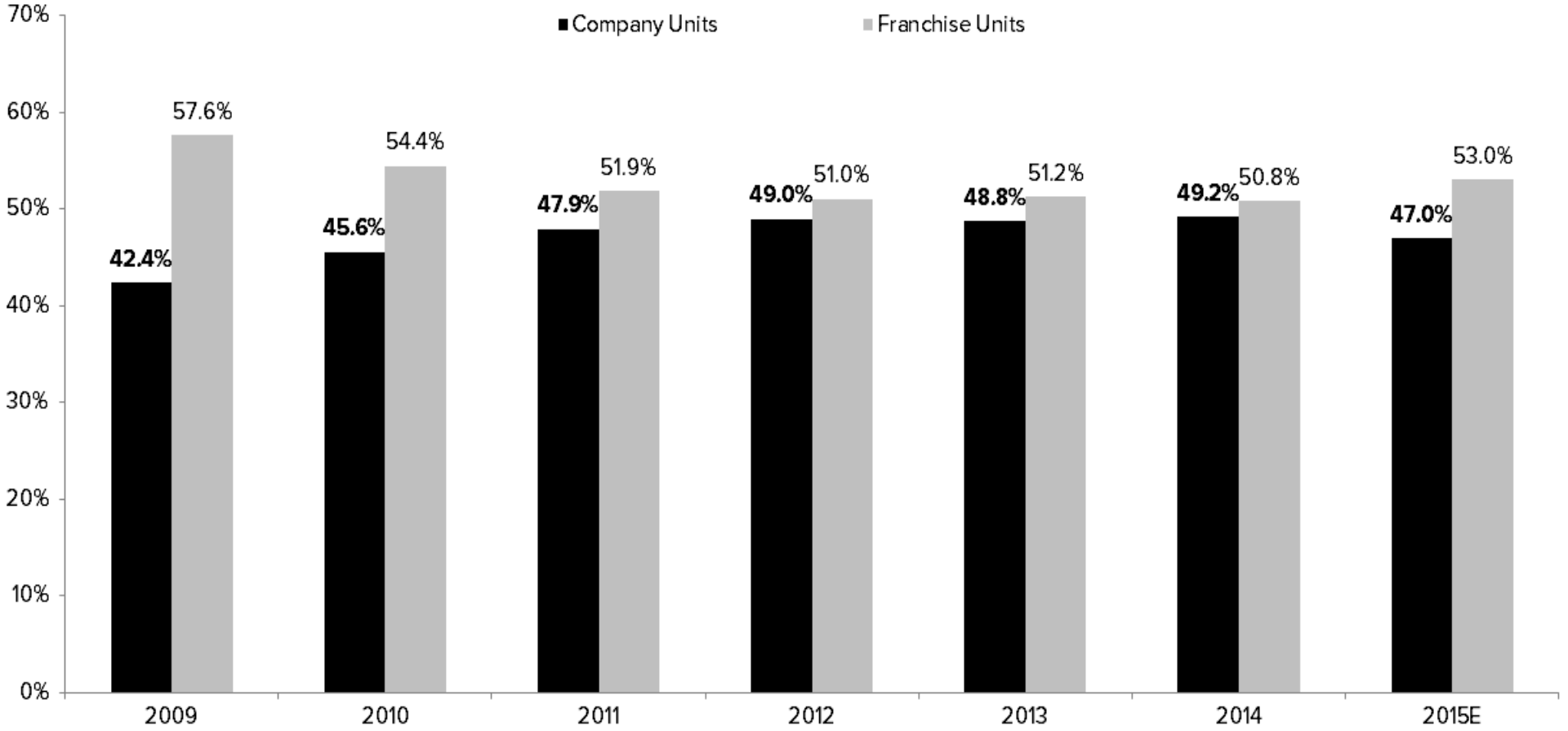
Sources: Hedgeye Research; Company Filings

SLOW UNIT GROWTH AND CUT CAPITAL SPENDING

- It’s not possible to focus the company and its resources on Panera 2.0, or Panera in general, when management is accelerated unit growth.
- There are a significant amount of unnecessary growth resources in place at Panera at a time when the box is in need of a major transformation.
- We worry that this is sending shareholders the wrong message.
- Given the size and scale of Panera 2.0, the company should be putting all of its resources into it.
- You can’t maximize profitability when you are increasing your “growth” G&A.

AGGRESSIVELY REFRANCHISE STORES

CAFÉ OWNERSHIP MIX



Sources: Hedgeye Research; Company Filings; Consensus Metrix

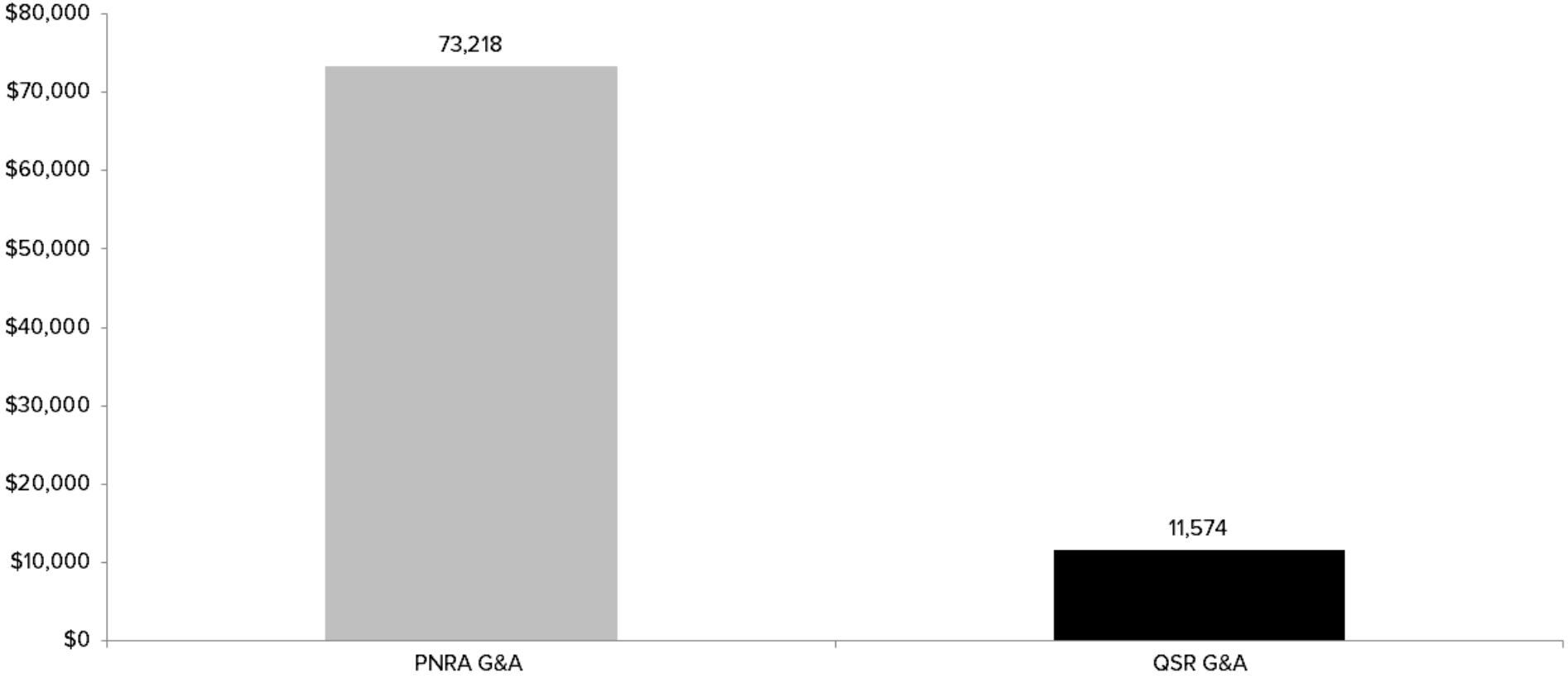
MOVE TO AN ASSET-LIGHT MODEL

- The company took a step in the right direction yesterday, but there is more to do.
- Refranchising will immediately help eliminate some unnecessary G&A.
- While the majority of players in the restaurant spaced have transitioned to more asset-light models, Panera has taken the opposite approach.
- Given that franchisees are well-capitalized – 35 franchise groups operated approximately 27 bakery-cafes each – selling stores shouldn't be a challenge.
- A 95% franchised PNRA could be worth above $300 per share

CUT G&A SPENDING

G&A SPEND PER STORES

PNRA COULD CUT $115MM (~77%) OF G&A IF IT HAD SIMILAR SPEND TO QSR



Sources: Hedgeye Research; Company Filings

STREAMLINE OPERATIONS

- Looking at comparable companies, Panera's G&A spend is much higher than needed.
- Panera is a vertically integrated restaurant company that is growing units at an inefficient pace.
- Both of these can be easily remediated by thinking differently about the business model.
- Every major restaurant company that has faced similar issues in the past has decided to streamline its structure and improve the operations of its existing asset base.
- Yesterday's press release addressed this issue, but the company must go further.

SELL OFF NON-CORE ASSETS

NO REASON TO BE VERTICALLY INTEGRATED

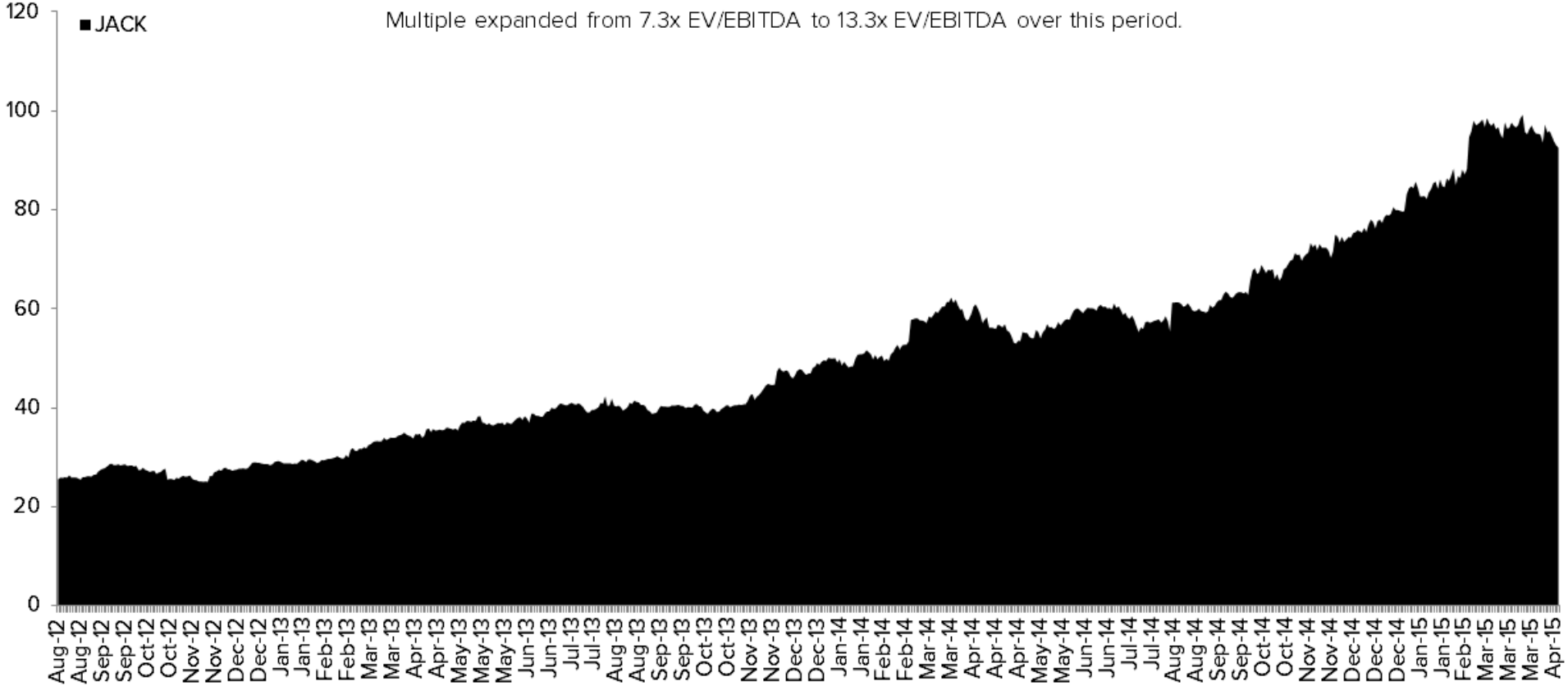
- Panera is the last remaining vertically integrated public restaurant company that we know of.
- Panera currently produces and distributes fresh dough through a leased fleet of 224 temperature controlled trucks owned and operated by the company.
- In addition, Panera owns 22 fresh dough facilities (24 total), including one located in Ontario, Canada.
- We suspect this asset may be particularly inefficient considering it only supports 15 bakery-cafes located within that market.
- In our view, distributing tuna, cream cheese, and certain produce to substantially all of its company-owned and franchise-operated stores doesn't give Panera any competitive advantage.

LOW MARGIN ASSETS MUST GO

- Ownership of your supply chain actually limits the company's future growth opportunities and creates inefficiencies on the P&L.
- The company currently uses other independent distributors to distribute some of its "proprietary sweet goods" and other materials to bakery-cafes.
- We believe the company should sell off its non-core assets and use independent distributors to distribute all of its products.
- Selling off low margin assets will improve profitability and increase the enterprises ROI.
- This will result in an increased valuation for the company.

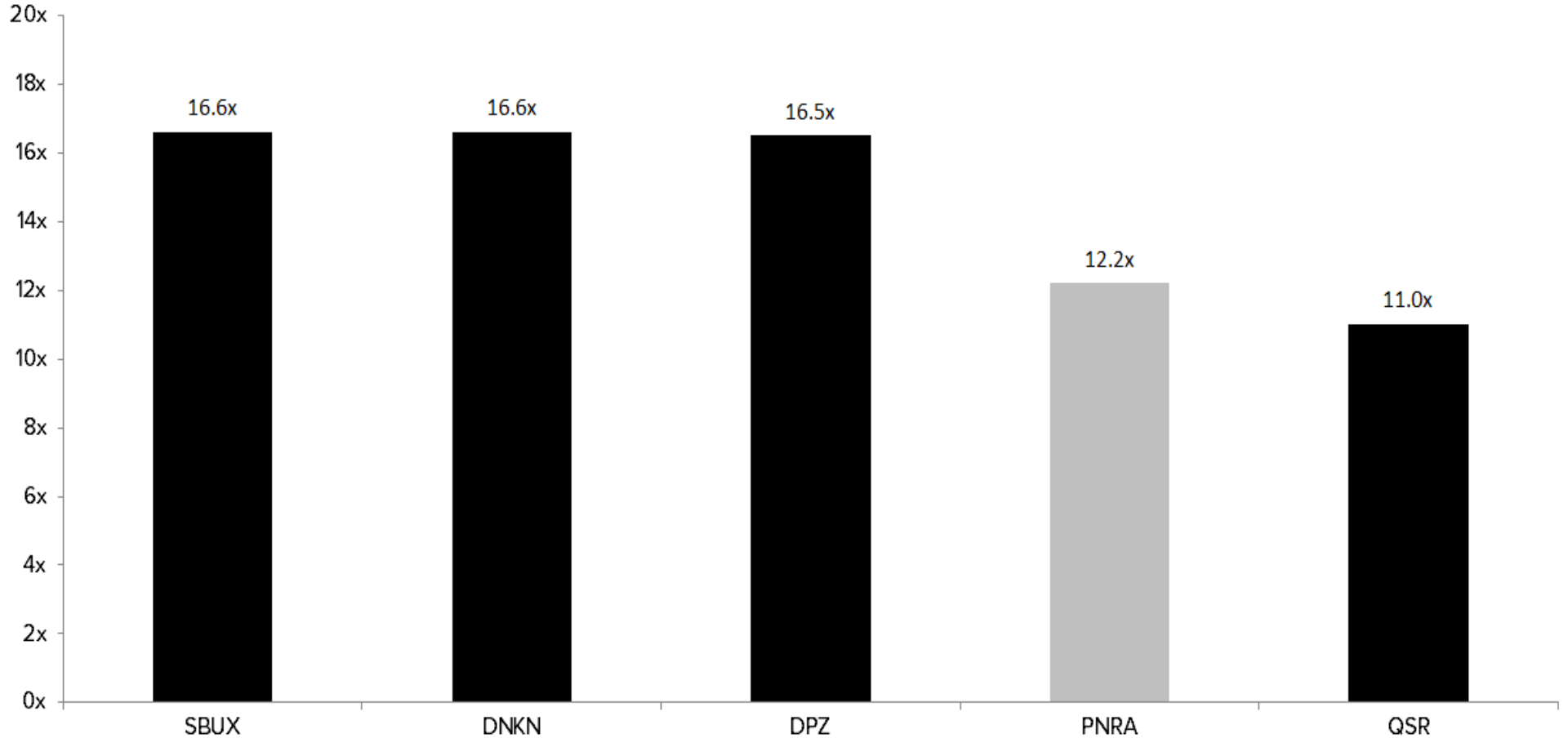
JACK IN THE BOX

JACK IS UP OVER 262% SINCE SELLING ITS DISTRIBUTION BUSINESS ON 08/08/12



Sources: Hedgeye Research; FactSet

EV/EBITDA (2015)



Sources: Hedgeye Research; Company Filings; Consensus Metrix

VALUATION

EV/EBITDA (2016) MULTIPLE

EBITDA	2016 EV/EBITDA Multiple											
	10.5x	11.0x	11.5x	12.0x	12.5x	13.0x	13.5x	14.0x	14.5x	15.0x	15.5x	16.0x
$413	$171	$179	$187	$195	$203	$211	$219	$227	$236	$244	$252	$260
$417	$172	$181	$189	$197	$205	$213	$222	$230	$238	$246	$254	$263
$422	$174	$182	$191	$199	$207	$215	$224	$232	$240	$249	$257	$265
$426	$176	$184	$192	$201	$209	$218	$226	$234	$243	$251	$259	$268
$430	$178	$186	$194	$203	$211	$220	$228	$237	$245	$254	$262	$271
$434	$179	$188	$196	$205	$213	$222	$231	$239	$248	$256	$265	$273
$439	$181	$190	$198	$207	$216	$224	$233	$241	$250	$259	$267	$276
$443	$183	$192	$200	$209	$218	$226	$235	$244	$253	$261	$270	$279
$447	$185	$194	$202	$211	$220	$229	$238	$246	$255	$264	$273	$281

BEAR	BASE	BULL
-7%	20%	54%

FOR MORE INFORMATION, CONTACT US AT:

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