Magellan – In The Know: Episode 49

Chipotle's winning growth recipe

Announcement (00:00):

The information contained in this podcast is for general information purposes and does not constitute investment advice. You should seek investment advice tailored to your circumstances before making an investment decision. This podcast was recorded on the 13th of August 2024, Australian Eastern Standard Time, prior to the news of Chipotle's CEO transition.

Host (00:23):

This is In The Know, a monthly Investment podcast brought to you by Magellan Asset Management.

Jack Hartung (00:29):

We knew that we were going to invest in things like food and people for the long term, and so there wouldn't necessarily be a short-term payoff, which is sometimes challenging for franchisees to be able to buy in that kind of a longer term horizon. And we also felt like we could run our own restaurants. And so the typical things that restaurant companies would want to resort to franchising for where they either need capital or they are unable to run the restaurants or they don't have enough people to run the restaurants, or in some cases the economics just may not be attractive, we didn't have any of those things. We had capital, we had great economics, and we could run our own restaurants.

Host (01:05):

That's Jack Hartung, the chief financial officer of Chipotle Mexican Grill, explaining how the company has been able to grow to 3,500 restaurants without relying on franchising or compromising on its long-term investments in food quality and people.

(01:20):

Welcome to Magellan - In The Know.

(01:27):

Chipotle is one of the best known brands in the North American fast casual restaurant sector. In this episode, Emma Henderson, acting sector head of franchises and healthcare at Magellan, speaks with Jack Hartung about Chipotle's amazing growth story and unique business model. They explore the brand's competitive advantages and huge future potential. It's a fascinating dive into the company's unique approach and strategic decisions that have allowed Chipotle to scale successfully, maintain high quality, and produce industry-leading margins. But first, here's a warm welcome from Emma Henderson.

Emma Henderson (02:07):

Welcome to Magellan's podcast, In The Know. I'm Emma Henderson, acting sector head of consumer franchises and healthcare. And today I'm joined by Jack Hartung, the chief financial officer of Chipotle Mexican Grill. Welcome, Jack.

Jack Hartung (02:21):

Emma, thanks for having me.

Emma Henderson (02:22):

For any of our listeners who may not be familiar with the company, Chipotle is a fast casual Mexican restaurant chain that was founded in 1993 in Denver, Colorado. Today, Chipotle has grown to over 3,500 restaurants, mainly across the United States, but also with a small footprint of stores in Canada, the United Kingdom, France, Germany, and most recently, Kuwait. Today, the company's continuing to deliver growth at a strong pace, targeting new store openings at a rate of 8% to 10% per annum, and is unique for a business of its size in that it owns and operates almost all restaurants directly rather running a franchising model.

(03:01):

Our guest today, Jack Hartung, has played an instrumental role in Chipotle's growth story over the last two decades, having served as the company's chief financial officer since 2002, making him one of the longest tenured CFOs in the US. We have particularly fortunate to be able to speak with him on this month's podcast to reflect on Chipotle's growth story, the brand's competitive advantages and purpose, and the large opportunity that continues to live ahead. But before we dive deeper into the Chipotle story, Jack, I would love our listeners to hear a bit more about your professional background and how your path originally crossed with Chipotle so many years ago.

Jack Hartung (03:38):

Yeah. So Emma, again, thanks for having me. It's a great pleasure to be here with you. I started with a typical finance role. I went into public accounting, which was a typical role that you go into after getting a finance. And I actually got a finance and accounting degree out of college.

(03:53):

After four years, a couple of friends of mine actually joined McDonald's Corporation and they called me and said, "This is a great company. They have lots of opportunity, they're still growing." This was in the early 1980s. I know it's hard to think about McDonald's. They're not the same growth company today, but back then they were still very much a growth company both in the US and globally of course. And so I joined the company and got some great experience about the restaurant industry. I was able to move from area to area in the company-owned restaurants and international, in the franchise business, the real estate business. So I got to see a broad spectrum of the largest restaurant company in the world at that time.

(04:28):

Well, in the late '90s, McDonald's was looking to diversify. Their growth was starting to slow. They started to invest in some non hamburger businesses. Chipotle is one of those businesses. That's how I came across Chipotle in about the year 2000. I started to work with Chipotle more as a way to oversee our investment in Chipotle. And so I started to work with the management team. I joined their private company board. They were a small company at the time, the original investment, they were 12 restaurants by the time I first met the founder and visited them out in Denver. They had about 30 or 40 restaurants or so, a far cry from the 3,500 we have today. But I was enamoured when I first went into Chipotle.

(05:06):

I love the food, I love the attention to detail. I spent time with the founder who was a chef. He didn't know anything about creating a chain of restaurants, but he knew about fine dining and he knew about cooking and he knew about securing real whole ingredients and cooking food that would be delicious and craveable. So I was enamoured. After a couple years in 2002, I joined. My dreams at that time was just to help Chipotle, this small private company, reach its growth potential. I had no idea that we would become a public company a few years later and then be on the trajectory we're today where not only are we at 3,500 restaurants, mostly in North America as you mentioned, but we have the potential to get to over 7,000 in North America, let alone our opportunity outside the US. So it's been quite a journey for me. I've loved every minute of it.

Emma Henderson (05:52):

And looking back to that time where you made the decision to join Chipotle, what was it about the category about fast casual? What was it that most excited you about the growth opportunity?

Jack Hartung (06:03):

Yeah, I mean I remember like it happened yesterday. So here, I'm coming from the largest, most successful global restaurant company in the world, at least from a market cap standpoint and sales standpoint. I spent time with the founder going through the line and tasting every ingredient. And he told me as we tasted the rice... I had had the burrito, but I had the burrito with all the ingredients altogether wrapped in a tortilla. When we walked the line, we would taste the rice and he would tell me exactly the flavour, the texture. "There should be a little bit of a citrus flavour. It should be fluffy, not starchy in your mouth." We would then taste the beans, the fajitas, the salsas all individually. Every single ingredient had a purpose. There was a taste profile. And if it wasn't perfect, he would be very unhappy. We would take that pan out and replace it.

(06:49):

And so I was blown away by the fact that this wasn't just this burrito where you throw a bunch of things into a tortilla and hope for the best. This was making sure every single detail of the restaurant was perfect so that when you did take the ingredients, roll them together into a burrito or into a bowl, which is what most people do today, it is a delicious dining experience.

(07:09):

The beauty of it, I felt at the time, was here's somebody that would spend hours cooking in the kitchen so that you could be served in just a matter of a few minutes and have a really delicious wholesome meal. And that really connected with me. And at that point I felt like I know the restaurant business, I can't cook, I can't work in the kitchen the way that the founder Steve Ells could, but I thought that I could bring my business acumen and help this very young, really a pioneer in the fast casual be successful from a business standpoint.

Emma Henderson (07:38):

So if we fast-forward to today, Chipotle has obviously grown into a very strong brand in a competitive US market. In fact, the Chipotle Rewards loyalty membership base is now larger than the entire population of Australia. What do you think it is that differentiates that Chipotle product offering, the customer experience at scale, that has supported this really strong loyalty over so many years?

Jack Hartung (08:01):

Yeah, I think what's really different about Chipotle than other companies who have grown to the scale that we are is that we've stayed true to our purpose and stay true to the things that make Chipotle special. And that means we still source just a few ingredients. We have 52 ingredients or 53 ingredients I think with queso now. All the ingredients are known ingredients like chicken and rice and peppers and onions, and so there's not any chemicals. There's not any preservatives. There's not any of the things that you will commonly see if you walk the grocery aisles today, and if you take food off the shelf and you read what's in the food, there's all kinds of things that you can't pronounce. And in Chipotle, even today, it starts with 52 whole ingredients that every customer would understand. And we're still doing real cooking. And so we still have open kitchens. We're still grilling the meats right before the customer. And those meats are cut right in front of the customer, brought to the front line.

(08:52):

And so it's really like a fine dining except the kitchen is open. In a fine dining restaurant, you won't necessarily see what they're cooking, but in Chipotle, it's the same cooking that would happen in a higher-end restaurant, but it's all right in front of you. Those are the things that Chipotle stood for back over 20 years ago when I first walked into Chipotle, and we're still doing the same things today.

(09:14):

A lot of other companies, what they've had to do when they try to get to scale, they've had to take shortcuts and have the food prepared off-site and then bring in and then just reheat it. And it's been something we've worked since we are a very small company. And we made sure that before we grew and before we got to scale, that we could really execute this. It's why we've maintained ownership of all our restaurants so we can really keep this specialness of securing these 53 wholesome ingredients and do real cooking in the restaurants. And when you do it, the flavour of the food, it's just a whole cut above if you have food that's cooked somewhere else and then brought into the restaurant and reheated.

Emma Henderson (09:49):

Yeah. I think it's always been remarkable to us, this food with integrity standards. And how true you've stayed to it really stands out relative to other names in the space. But then on the other side, you've also got pretty remarkable unit economics. So for our listeners, last year, Chipotle's restaurant margins reached over 26% on an average restaurant sales volume of $3 million per store.

(10:11):

What is it about the food assembly process, the labour model that lets you deliver this level of profitability without having to compromise on those food sourcing standards that you still hold so true?

Jack Hartung (10:21):

Yeah, it's a great question, and really the source of that happened almost 20 years ago. Food with integrity started in the early 2000s, and it started with pork. And it started with this idea that Steve read about Niman Ranch pork. It was a company that was raising the hogs outside free-ranging as opposed to in confinement, which in the US, most of the pork is raised in confinement. Steve was intrigued by this idea of free-ranging pork, so he ordered some pork, he cooked with it. It was absolutely delicious, way better than any pork he'd ever worked with. He then spent time, and when I joined, I spent time on farms and we spent time on the Niman Ranch Farms. And then we spent time in the confinement farms. And we all made a decision. Steve put a stake in the ground, and we all kind of rallied around this idea that we are not going to let Chipotle success be based on the exploitation of animals or the environment or the health of our consumers.

(11:13):

So at that point though, it was much more expensive. We had to find a way from an economic standpoint to be able to afford to source this better pork. And by the way, eventually it led to better chicken and then better steak and then better produce and then local produce. So there was iteration after iteration, and all of it was more expensive, but we had to along the way find efficiencies. So our restaurants are a little smaller, which means the rent is a little bit less, real estate taxes a little bit less. We kept it a very, very focused menu. The menu is 90 something percent the same today as it was when the restaurant opened in the early '90s, even so over 30 years ago.

(11:49):

We do LTOs. For anyone who doesn't know what an LTO is, that's a limited time offer. But even those, we often get asked by investors, "Why don't you just keep the LTO? It was so successful, why don't you keep it?" Well, that complicates things to a point where we would not be able to serve our customers at the speed that we're capable of serving. We would have inefficiencies where we'd have to over hire and labour. We'd probably have extra waste as well. So all these little things that can lead to a weaker economic model, we were very protective.

(12:18):

And so in those early days, because what we didn't want to do is we didn't want to have to charge premium prices. We wanted to be affordable, and yet we still wanted everyone to eat this way. So we had to find efficiencies in every single line item on the P&L. Marketing, by the way, is something we spend less on marketing than most other chains of our scale. The idea being that we wanted as much of the P&L to be on the food line, and then we want to find efficiencies everywhere else. That allowed us now to continue to invest in this higher quality food, to be very affordable and to have industry leading margins.

(12:49):

Now, when I went to finance class a long, long time ago, our finance professor said, "You couldn't have those three things. You can't have premium ingredients, affordable prices, and high margins. You can pick one or maybe two of them, but you can't have all three." We by necessity, because we believe so much in this idea of food with integrity, and we believe so much that we wanted it to be affordable, that we find efficiencies when we were smaller and that we just kept those efficiencies as we grew.

Emma Henderson (13:14):

And so we've spoken about that scale can create challenges and staying true to the vision of a company when you are a smaller company. But we also know from across the consumer sector that scale advantages relative to peers can be very beneficial to companies. As you've seen Chipotle grow, what have been the positive scale advantages that the company's been able to leverage and drive further differentiation?

Jack Hartung (13:36):

Yeah, it's a great question because while we do things like we have local produce as much as we can when the climate allows, we also have this idea of we have so many restaurants now that avocado... I'll give you an example, avocados. When we were a small company, all of our avocados came from either Mexico or California, and most came from Mexico. As we've grown, we have buying power sets that we have now special relationship with growers in Peru, we're building relationships with growers in Colombia, and we're looking at other areas of South America as well.

(14:09):

So when we're a small company, if we tried to build a relationship with countries in South America, they would not have paid attention. It wouldn't be worth to build that kind of relationship. So we've now been able to diversify so that when there are challenges in one area of the world with some of our ingredients, we now can diversify that because we do have buyers in other countries and other parts of the US that want to support and they want to grow with our business. So that scale is coming in handy for us to not only build the supply chain so it can grow with us, but to diversify it so that we can really avoid or at least hedge some of the disruptions that you can get when you have a wholesome fresh supply chain like ours. This diversification really comes in handy.

Emma Henderson (14:50):

Another way we see scale benefits play out has increasingly been on the digital and technology side. One thing we've always appreciated about Chipotle and its success has been that the company has a very forward-thinking and innovative culture. Looking back, what technology and innovation developments at Chipotle have you been most proud of? And then I guess second question, looking forward, what excites you about the digital and automation opportunity that lies ahead for the restaurant sector?

Jack Hartung (15:18):

Yeah, I think the thing that I like the most, and we've done a great job and Kurt and the team have done a great job in investing in a lot of innovative technologies, but the thing I think that I'm most proud of and is the most impactful is our digital make line and all the tech that goes along with that. That now represents about 35% of our business. If you look just even 10 years ago, it was less than 10% of the business. And what I love about it is we didn't dumb down the experience. When you open up the Chipotle app, it feels like you're walking down the line. So you start at tortilla, you decide what protein you want, you decide what kind of rice you want. It's the same order that you go through the front line. And so it's very familiar to our customers. And the customization, it's instead of interacting with our crew, it's a click along the way. So you get the exact same customization in the exact same order. And it's frictionless as well.

(16:09):

We kept the app. And again, when I say we, Kurt and his team, have kept the app very simple. So just like in our restaurants, we pride ourselves in fast throughput. We want the customers to come into our app and have a seamless experience, a frictionless experience so that they can get in and out, get exactly what they want. And then at the end of it, we have an agreed upon time. So if you order at say it's 5 to 1 o'clock and you're ordering lunch, we'll agree that your order will be ready at 10 after 1:00. And so you show up, your order is ready to go either through our pickup window if it's Chipotle or you come into the restaurant and it's on the shelf. So I think that end-to-end experience from first getting into the app to coming to the restaurant and picking up your meal, I think is seamless, frictionless, and it feels very, very familiar to our Chipotle customers.

(16:55):

Now, beyond that, we've got lots of technology that's going to help the back of the house, which we've got a Hyphen, which it's our digitised make line, automated make line. One of the challenges is when we have a busy lunch and we have a lot of digital orders come in, it's hard for our teams to keep up. So automation can help our teams significantly in that way. We also have avocado, which we're hoping to get into a restaurant very soon here, which will cut core and peel the avocados. That's a very labour-intensive process.

(17:26):

The beauty of that, Emma, is that it'd be easier to order from our suppliers avocado paste and then just add our ingredients and off you go. We won't do that. We're going to start with whole avocados. But if we can take one of the time-consuming manual tasks away, we still have fresh avocados and then our teams will still add our ingredients and mash the avocados by hand. So it's still the same delicious guacamole, but it just takes one of the more unpleasant tasks away from our crew. And so there's other automations that we're looking at as well. But the one common theme is the food is still central. The food is still original whole ingredients, and we're still using the original recipes.

Emma Henderson (18:06):

And I mentioned in the introduction that Chipotle is quite unique in the restaurants industry being the scale that it is at 3,500 restaurants and owning and operating most of those directly. One benefit of that we've seen over the years is that owner operators can tend to move quicker on the digital side. But I'd love to hear your views on the other strategic and financial benefits of retaining control as an owner operator. And then on the other side, how have the discussions around franchising Chipotle evolved over your time at the company?

Jack Hartung (18:36):

When Chipotle was a young company in the early days and food with integrity was in its infancy, it would've been difficult to get franchisees on board to want to invest in higher quality food. At that point, the idea of investing in higher quality food with the belief that over time people will come to love Chipotle more and visit more often would be a hard proposition for a franchisee who they're typically leveraged, typically they're watching their monthly cash flow, they don't necessarily have the balance sheet that Chipotle has would be a hard proposition. So in the early days, we felt like we had to maintain control.

(19:08):

As we grew, we continued to grow without debt. We still have a very, very healthy balance sheet, so we didn't need outside capital. We knew that we were going to invest in things like food and people for the long-term, and so there wouldn't necessarily be a payoff again, which is sometimes challenging for franchisees to be able to buy in that kind of a longer term horizon.

(19:29):

And we also felt like we could run our own restaurants. And so the typical things that restaurant companies would want to resort the franchising for where they either need capital or they are unable to run the restaurants or they don't have enough people to run the restaurants, or in some cases the economics just may not be attractive. And so you may want to get some partners in that could bring more leverage and then accept the lower economics, we didn't have any of those things. We had capital, we had great economics and we could run our own restaurants.

(19:57):

Now we have recently, we did franchise to Alshaya in the Middle East. That is an area where we don't have those capabilities, we don't have the contacts, we don't have the ability to secure the real estate, we don't have the supply chain there. And so we felt like that was an area of the world where franchising does or licencing does make the most sense. The partnership is off to a great start. We opened up our restaurant back in the March, April timeframe. The feedback from our culinary team is the food tastes as delicious in Kuwait as it does here in the US, which we're delighted to hear. Everything's got to start there, but the reaction so far has been absolutely fabulous, beyond our expectations. So that's off to great start.

(20:34):

So as we look to other areas of the world, we will consider things like our ability to put capital in, safely put capital in, our ability to build a supply chain to support our restaurants, and then our ability through partnerships to either secure real estate or have the partnerships, supplied partnerships. You need to have to run a successful business. We'll consider all those things when we consider what kind of business model to bring to each market. And we'll be flexible. We know we can run restaurants, we know we can licence restaurants. And there might be even some hybrids where we might do some kind of joint venture partnership as well.

Emma Henderson (21:08):

You mentioned as an owner operator being able to take a very long-term view on things like food investments, investment in people. I think it stands out that as an owner operator, that Chipotle does directly employ a large number of people in its restaurants that can create both risks and opportunities. I think it was obvious to everyone during the pandemic years the negative impact that disruption to labour force and staff turnover had on the customer experience and profitability in restaurants. What have been some key lessons you've learnt about the people side of the restaurant business and how is Chipotle ensuring that it is investing to attract and retain sufficient talent for the future?

Jack Hartung (21:45):

Yeah, I mean obviously when you run your own restaurants, you need great people. We have over 120,000 people in our restaurants today. And what we've learned is if we invest in our people, they'll invest in themselves and they'll commit to our purpose. And so we've done things like, of course it starts with having fair pay, and a fair pay means not minimum wage, not what typical fast food is paying. You've got to pay something more than that.

(22:10):

But it also means in terms of having benefits like not just health benefits, which of course we have, but also mental health benefits and finance consulting, things like that, one of the most important things that we offer is debt-free degrees. And that's something that if somebody wants to go to college and they can't afford to do it, we have an online programme where our folks can get up to a hundred different degrees and it's all debt-free. They don't have to pay for anything. Now they do choose to go to a college. That's not one of the online choices, but we have a tuition reimbursement programme as well.

(22:42):

What we found is the folks that are involved in those education programmes, either online or through a university, they tend to stay a lot longer with the company and they tend to move up into other levels, into higher levels within the company, which tells us that if we invest in our folks, they'll invest in their own development and then they'll contribute to our purpose by seeking higher level positions in the company. So that's something we've done since the beginning. We'll continue to do it. And this idea of our goal is to have as close to 100% of our promotions be internal.

(23:16):

Typically, we're in the 90 to 95%, which means if you come to Chipotle as a crew person, because we're growing at the level that we're growing and because we promote more than 90% of our folks are internal, you can count on the fact that if you contribute to our purpose and if you work hard and you learn how to work in a kitchen, learn how to lead people, learn how to run a business, you can have a successful career at Chipotle and financially do very, very well off. That's an investment we'll always have to make, and you have to do it as an owner operator of 35 or 100 restaurants on the way to 7,000.

Emma Henderson (23:48):

So you did just mention the growth target I was going to talk about next, so this is a nice segue. We've spoken a lot about the incredible growth Chipotle is being able to deliver since you originally came across the company so many years ago, but I'd love to talk a little bit more about the growth opportunity that still lies ahead. You just mentioned that at 3,500 restaurants today, the management team still sees the opportunity to double that size of the footprint in North America. I'd love to hear more about what gives management the confidence that there is sufficient white space for basically another Chipotle in North America.

Jack Hartung (24:21):

Yeah, the math is actually really quite simple. We have 3,500 restaurants today. But if you look in our most dense markets, the five or six or seven, they tend to be our oldest markets and they have the most restaurants per capita. If all we do is match those densities across the country, I'm not talking about small towns, I'm talking about the medium and the larger towns, you get to 7,000. So it's not a stretch. It's not a wish that something can happen such that we can increase our density. So all we have to do is match the density in our new markets that we have in our most mature markets.

(24:57):

Now, the encouraging thing, Emma, is our sales volumes and our margins and returns are among the highest in these most dense markets. So it's not like the economics tend to erode, which sometimes happen with companies. The more restaurants you add, your economics tend to degrade over time. It's actually been the opposite, so that as we've grown in these most dense markets, our sales, our margins and our returns are among the highest in the company. It gives us a very high degree of confidence that the 7,000 in North America is not all achievable. I suspect as we get closer to that number, the number's only going to go up.

Emma Henderson (25:32):

And then moving to the international side, we spoke a little bit about the recent partnership in the Middle East with Alshaya, but you've also been directly investing in a handful of international markets. So Canada, which is included in North America, but also the UK, France, and Germany. One of the things we've really appreciated about Chipotle has been a very thoughtful and disciplined approach to capital allocation. The company follows a stage gate process across many parts of this business. I'd love to hear a little bit more about the stage gate process you think about when looking at those other international markets. What would you need to see to be able to accelerate investment in markets such as Europe?

Jack Hartung (26:11):

Yeah. So the economics in Europe are not what they are in the US. They may never get quite to what they are in the US. In the US, our cash on cash returns are in the 60 to 70% range. So that means on a per restaurant basis, we invest a little over a million dollars. Within a few years, we expect to get a 60% or 70% return. There are cost structures in Europe that may prevent us from getting all the way up to that level, but we do see a pathway to get somewhere in the 40, 45, 50% range. And really it's a function of, first, we need to make sure that the culinary matches what's in the US.

(26:48):

Over time what we've noticed, and frankly we've made a lot of progress over the last year or two in closing the gap, but what we've noticed in Europe is that some of the ingredients varied a little bit. Some of the cooking techniques varied a little bit, and all these little things add up. If I go back to the original comment when I first went to Chipotle and I talked about how the founder went through all the details of making sure every ingredient and every recipe was perfect, we weren't quite perfect in Europe, and so the food tasted a little different.

(27:15):

I'm pleased to say, in fact, I just met with one of our folks today that we've, for the most part, closed that gap. Th... Food now does, it comes from virtually the same ingredients that we use in the US. They're local, so it's from Europe, so we're not importing from the US, but the cooking techniques, the recipes, the taste profile has really pretty much closed that gap completely. So that's where it's got to start with Chipotle, it's got to start with the food.

(27:39):

We've also made some leadership changes where we've taken some of our successful leaders in the US and Canada, they're now overseeing the European business. And they're starting to bring some of the tools and some of the things that have been successful in the US over to Europe, and we're starting to see the margins improving, the returns improving as well. So really, really good early progress. We are young there. We have used a stage gate.

(28:00):

One thing that we know is that you don't want to grow so fast when you're not really seeing either the brand performance that you'd like or the economic performance that you'd like. It's way better to get those things really dialled in and then you can grow. And so I expect it'll be similar to what we saw in Canada where we had similar challenges in Canada. We focused on making sure that the experience was great and then make sure the economics are attractive as well. And by the way, Canada economics are just about as attractive as they are in the US. And so that's now in full growth mode. I'm optimistic that within a few years we could see the same thing happen in Europe.

Emma Henderson (28:35):

And then I have to ask for our Australian listeners, but is there any chance we'll be seeing Chipotle in Australia anytime soon?

Jack Hartung (28:42):

You know what? It's definitely on the list. When we talk about what areas outside of the markets we're already in around the world, Australia is definitely one that's on our short list. And so I do think we'll be in Australia at some point, but nothing to report right now. Nothing eminent. So no grand openings planned yet.

Emma Henderson (28:59):

That's okay. We'll wait and see. To finish the conversation, I was hoping to ask I guess a broader final question on what you have learned over the years about taking calculated risks, particularly as a CFO, and balancing that prudent capital allocation with making sure you're investing sufficiently for the future.

Jack Hartung (29:17):

And I'll back up a little bit before I get into the financials. I think what's most important about investing in a company is to maker sure the company, or invest in a company that's got a purpose. When you have a purpose that people believe in, when you recruit into a company that has a purpose that people get excited about when they join the company and they say, "Oh my God, I was excited at the interview process and now I realise what you guys are doing around food is even better and more intense than I thought and it makes me prouder to work for this company," so I think it starts with making sure that there's a real purpose.

(29:50):

Making money is not a purpose. People won't get excited about coming to a company that's financially successful. That's nice to have, but if you have a company where they believe in what you're doing, they believe in the way we're raising ingredients, they believe in the way that we're investing in our people, and then you're financially successful, I think you've really got something that you can invest in overtime.

(30:10):

Now from a, "How do you do capital allocation and risk management?", I think the stage gate process is a great example of that. That's a term we've only been using since Brian joined us in 2018, I guess it was. But even before that, when we were entering new markets, our plan was to go in and open with maybe two or three restaurants and let's see how those go, let's see how our teams have performed, let's see what the customer reaction is, let's see how well we cook, prepare, and serve the food and let's see what the economics are before we invest a lot more money into that market. And we kind of use this term, Emma, that the market needs to earn the capital. And if the market performs well, it will earn the capital. And then we have plenty of capital to invest in that market. And so we use that approach as we went from city to city in the US. We've used that approach as we moved outside of the US and into Canada, and then also as we went to Europe as well.

(31:01):

And so this idea of, "Let's go ahead and plant..." And actually we used to call them bro seeds. "Let's plant the little seeds in a new market. Let's see how well they grow. And if they grow really healthy and tall and there's room for additional investment, we'll go ahead and make that investment. If not, let's take our time. Let's make sure we build the brand right. Let's make sure we run the restaurants right." And so we had categories of markets that were in various stages of earning the investment. We would invest really aggressively in markets that the brand is well known. Customers love the brand and the economics were great. And we'd be very cautious in those markets where the brand was still being discovered, relatively unknown, and the economics were relatively young. And I think no matter what you're investing in, I think that's a smart way to do it. I think investing haphazardly and hoping for the best is not a great capital allocation strategy.

Emma Henderson (31:51):

Thank you, Jack. Thank you so much for joining us today. And also as long-term shareholders in Chipotle, we want to thank you for your stewardship of the business over the last two decades.

Jack Hartung (32:00):

Emma, thank you so much. It was great to be with you today.

Host (32:03):

That was Magellan's acting sector head for Franchises and Healthcare, Emma Henderson, speaking with Jack Hartung, chief financial officer of Chipotle Mexican Grill. We trust you've enjoyed this episode. For more information on previous episodes, visit magellangroup.com.au/podcast, where you can also sign up to receive our regular investment insights programme. Thanks for listening.