Limited-Service, Unlimited Possibilities

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Quiznos & Sbarro: What Went Wrong?

Experts weigh in on two latest quick serves to file for bankruptcy.

Quiznos and Sbarro this month became the latest two quick-service chains to file for bankruptcy, the result, experts say, of not being able to keep up with the growing competition in their respective categories.

Sbarro, once a staple in the pizza category and among the top five pizza brands, has seen sales slide in the last decade. The brand fell off the QSR 50 list of top 50 quick-serve chains in 2013, coming in at No. 55 with 2012 sales of $400 million, seventh most among pizza chains. Sbarro filed for Chapter 11 reorganization early in March, but executives promised a quick exit from bankruptcy after planning to close around 230 under-performing stores.

Quiznos, meanwhile, was once among the top performers in the quick-service industry. But it, too, has seen sales and unit counts drop, and ranked fifth among sandwich chains and No. 32 overall in the 2013 QSR Top 50 rankings with 2012 sales of $838 million. Quiznos filed for Chapter 11 in mid-March and unveiled a restructuring plan designed to reduce the company's debt by more than $400 million.

"Sbarro and Quiznos have similar financial problems: exceedingly high debt, which they are shedding via bankruptcy, in Sbarro's case shedding bad leases," says Michael Whiteman, president of Baum & Whiteman restaurant consultancy in Brooklyn, New York.

"These types of companies are over-leveraged. The initial borrowing was too high, plus there are cost pressures," adds Aaron Hammer, an attorney with Sugar Felsenthal Grais & Hammer, which handles bankruptcy protection cases for restaurants and other companies. "The capital structure that was set years ago might not work today." An extremely harsh winter across the U.S. that dampened overall restaurant sales may have been the final factor that pushed Quiznos and Sbarro to file for bankruptcy protection, Hammer says.

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In addition to the two quick-serve operators' high debt, foodservice industry consultants say, both Quiznos' and Sbarro's bankruptcies were a product of being crowded out by their competitors.

Quiznos' profits have suffered at the hands of Subway, the top performing sandwich chain, but

Firehouse Subs, Jimmy John's, and other sandwich operators that have grown quickly and differentiated their offerings in recent years have also eroded its market share.

Subway has dominated the sandwich space, says Aaron D. Allen, owner of global restaurant consulting firm Aaron Allen & Associates, because it was among the first national chains to capitalize on the most bankable word in foodservice today: *fresh*.

"Subway cornered the 'healthful' positioning opportunity with the quick-serve segment and has been reaping the benefits for more than a decade now," he says, adding that while Quiznos differentiated itself several years ago as the first brand to capitalize on the toasted sub, many other chains, including Subway, have invested in toaster ovens.

Sbarro's primary problem, experts say, is the location of its stores. A majority of its units are located in mall food courts, which have suffered from steadily declining traffic over the past few years.

"Sbarro was saddled with debt, and their real estate strategy was also questionable and relied perhaps too much on mail traffic, which has been declining since the dawn of the Internet," Allen says.

In addition, like Quiznos, Sbarro's food offerings haven't kept up with innovation from its primary competitors, including Pizza Hut, Domino's Pizza, Papa John's, as well as a growing crop of fast-casual players.

"[Consumers] want fresh and light and made to order," Whiteman says, "which precisely is why everyone's rushing into the fast-casual area."

The consultants say there is plenty of opportunity for both Sbarro and Quiznos to turn their business models around. Both have pursued aggressive international growth. Sbarro, meanwhile, is exploring the fast-casual category with its Pizza Cucinova spin-off concept, and Quiznos plans to boost franchisees' profitability with advertising, technology implementation, a franchise-owner rebate program, and other initiatives.

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