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PTON.OQ - Q3 2022 Peloton Interactive Inc Earnings Call

EVENT DATE/TIME: MAY 10, 2022 / 12:30PM GMT

OVERVIEW:

Co. reported 3Q22 results.

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PRESENTATION

Operator

Good day, and welcome to the Peloton Interactive Third Quarter 2022 Earnings Conference Call. (Operator Instructions) Please note this event is being recorded. (Operator Instructions)

I would now like to turn the conference over to Peter Stabler, Senior Vice President, Investor Relations. Please go ahead.

Peter Stabler

Good morning, and welcome to Peloton's Third Quarter Fiscal 2022 Conference Call. Joining today's call are CEO and President, Barry McCarthy; and CFO, Jill Woodworth.

Our comments and responses to your questions reflect management's views as of today only and will include statements related to our business that are forward-looking statements under federal securities law. Actual results may differ materially from those contained in or implied by these forward-looking statements due to risks and uncertainties associated with our business. For a discussion of the material risks and other important factors that could impact our actual results, please refer to our SEC filings and today's shareholder letter, both of which can be found on our Investor Relations website.

During this call, we will discuss both GAAP and non-GAAP financial measures. A reconciliation of GAAP to non-GAAP financial measures is provided in today's shareholder letter.

With that, I'll turn the call over to Barry.

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Good morning, everyone, and thank you for joining today's call. Earlier this morning, we released the letter to shareholders, which discusses our strategy for growing Peloton's business and the Q3 performance. I'm not going to repeat what was said in the letter, except to thank our employees for their hard work and our 7 million members for giving our work meaning and purpose.

Before we begin today's Q&A, I'd like to acknowledge the contributions of William Lynch to the growth of Peloton. As part of the leadership transition at Peloton, William's decided to resign from our Board to pursue other interests, and we wish him continued success in his next endeavor.

Operator, let's turn to our first question.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question comes from Doug Anmuth with JPMorgan.

Douglas Till Anmuth - *JPMorgan Chase & Co, Research Division - MD*

Barry, trying to understand the recent hardware price reductions just in the context of your bigger plans. Are they just an effort to move inventory and perhaps drive a little bit more revenue near term and to really envision FaaS becoming the primary or only business model over time besides the digital app? And what are you seeing in those early tests? And what could that service look like?

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

So the price increase was geared towards moving hardware and alleviating some of the stress we're seeing in inventory. We've also learned quite a bit about price elasticity and have seen a significant increase in total revenue as a result of the price decrease.

So I'm feeling pretty good about that, and I'm looking to sustain it. The framework for thinking about the unit economics begins and ends with LTV and then the CAC expense associated with the LTV. And today, we're operating -- we operate in the range of, I would say, broadly 2:1 to 3:1 depending on seasonality, which I feel really good about. What was the third part of the question?

Douglas Till Anmuth - *JPMorgan Chase & Co, Research Division - MD*

Just what the SaaS -- yes.

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

FaaS will be a complement to our business. So there are absolutely members who want to own the bike outright, and we're delighted to sell it to them. And then there's others for whom that the cost of entry poses a barrier. And roughly 53% of our customers year-to-date, by the way, have household incomes of less than $100,000.

So FaaS is an opportunity for us to continue to introduce consumers, mass market to our value proposition. I'm not sure what the mix will be over time. We need to test our way into an understanding of that as well as an economic model that enables us to earn an attractive return on investment.

What we can say with a certainty at the moment is that we're seeing faster growth than I had hoped we would see. So I'm enormously encouraged by early test results. But it's early.

The total number of units that we placed is still relatively small on the order of 1,000. We're looking to aggressively expand the test on our e-commerce platform. I think we'll be fully live with the A/B test in -- by the end of June. We've got some engineering work to do to enable that.

Maybe it will be a couple of weeks sooner, we'll have to see. So FaaS, complementary to the core business, not yet sure what the mix over time will be or what the ultimate pricing will be. But we need to test our way into figuring that out.

Operator

The next question comes from Justin Post with Bank of America.

Justin Post - *BofA Securities, Research Division - MD*

Great. A couple of questions. Can you help us understand the churn contemplated in your sub growth outlook for Q4? It looks like you have subs up 1% quarter-over-quarter. Just the dynamics of the quarter with the testing you're doing and then the churn.

And then OpEx was up 19% year-over-year. Any update on your cost-cutting efforts and whether you're trending ahead or below your plan?

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

I'll take the churn part, and Jill will take the cost-cutting part. So we're hedging our bets a little bit in guidance related to churn. We saw a very small increase in cancellations when we announced the price increase, one of all-access service from $39 to $44.

But the price change doesn't actually hit until June 1. And so we're still a little bit uncertain about what -- when the dust settles, the churn impact will be to date. I would say it's been quite small.

Jill Woodworth - *Peloton Interactive, Inc. - CFO*

And on the restructuring side, if you look at the OpEx and COGS savings in the second half of fiscal '22, so what's already achieved, we expect about $165 million of OpEx savings in the second half. And we're certainly on track for $450 million in OpEx savings for fiscal '23.

In terms of COGS, we expect about $30 million to $35 million in savings in the second half already baked in, and we're on track for about $100 million of COGS savings in fiscal '23. So as we outlined last quarter, this is something we're incredibly committed to, and we've already made a lot of progress. And I think, culturally, the organization understands what we have to do.

Operator

The next question comes from Youssef Squali with Truist Securities.

Youssef Houssaini Squali - *Truist Securities, Inc., Research Division - MD & Senior Analyst*

Barry, just in terms of supply chain issues, can you maybe just clarify a bit how Andy and Angel are improving the process? I think you had a nice mention of them in the letter.

And just broadly speaking, your predecessor had followed the strategy of maybe owning a bunch of productive assets, including Precor. Is that still strategic to the direction of the company and how that fits in your overall solution?

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Well, about the supply chain, let me say that I don't think we had the visibility that maybe we would have wanted. And we had a number of systems issues related to supply chain that we needed to address, and we've taken steps to do both.

I think we also haven't made quite as much progress in rightsizing the production as we needed to. We've been working as closely with our partners in the supply chain as we needed to related to the ordering of long lead time parts.

And so Andy and his team have taken important steps in addressing all of those issues. And in the process, we have a much greater visibility into how the supply chain issues affect the business overall.

So I'm -- it was an area where we had work to do. We're making a lot of progress. We'll make more, but I'm feeling pretty good about that piece of the business. I would characterize it as an urgent need when I stepped in, and I'm proud of the progress we're making.

With respect to Precor, there were a couple of things we were trying to accomplish with that acquisition. It bolsters our go-to-market strategy in commercial, which, along with corporate wellness, is an important area of growth for us in our core business.

Beyond that, I haven't spent a lot of time yet thinking about -- we're looking at the Precor business. So for the moment, I just want to put a pin in it. I'm not signaling that it's not core, but I'm not signaling that it is core either. I just -- there've been so many other issues to address. I just haven't gotten there yet.

But the overarching strategy is, look, it's all about Connected Fitness. It's about the magic that happens in the tablet, right? We need to be good at hardware.

But being good at hardware is not nearly sufficient. The thing that makes us special that accounts for the low churn rate that drives the outrageously high Net Promoter Scores is all the magic that Jen Cotter and her team and our instructors, who's into the service, and we need to be absolutely great at that.

And that calls for, I think, a shift in the investment priorities of the business, at least as compared with where we spent money historically, in order to double down on the things that have made us great.

Operator

The next question comes from Ron Josey with Citi.

Ronald Victor Josey - *Citigroup Inc. Exchange Research - Research Analyst*

Maybe I want to talk a little bit more or help to understand, better understand gross margin assumptions and third-party delivery. I think in the note in the letter, we talked about lower gross margins for product in the range of $300 million.

So maybe, Jill, help us understand where these savings are coming from. Is it greater efficiencies in manufacturing, delivery? And Barry, you mentioned some issues in last mile. Maybe help us understand how those have been fixed, or what's going on there?

And then lastly, just Jill. I think, in the letter, we talked about free cash flow timing changes and how that impacted free cash flow this quarter versus going forward. Any insights there would be helpful.

Jill Woodworth - *Peloton Interactive, Inc. - CFO*

Sure. So on -- I think what I'll talk about first is Connected Fitness gross margin, right? So what you have happening currently and what we saw in Q3 were a few sort of onetime items, right? You have an increase to Tread+ returns reserve.

We also took additional inventory reserves around accessories, primarily driven by a strategy shift in the way we went to market with the Peloton Guide. And we also had higher scrap reserves for Bike, which essentially is not resalable inventory that has been returned to us and cannot be refurbished.

And what we've also seen, which we will experience in Q3 and Q4, is higher detention and demurrage and storage costs, given the fact that our inventory position is higher than we expected given the decline in our demand forecast. So a lot of these issues are onetime in nature or short term in Q3 and Q4.

In terms of just the overall restructuring efforts in COGS, though, there's a lot behind that, right? Some of that was related to the shift to 3PL, right, which we did realize some savings, certainly going from a much larger than we needed fleet of our in-house delivery. And so moving to 3PL helped us variabilize that expense and reduce some of that fixed cost overhead that was a challenge to leverage with lower demand volume.

But there's a lot more optimization we can do here. There's more we can do in better warehouse management, better optimization of our labor structure. So that's part of what I think we can see on the horizon for fiscal '23.

And what I would add to that is, next year, we've negotiated better freight rates, which we've talked about. I do think there is future opportunity in the longer term to look at better procurement, better sourcing and better product margins as a result of reworking the way that we're designing and building our products and taking some costs out.

And then lastly, I think on warranty management, if we deliver products better, if we service products better, I think there's a way for us to, with improved quality, to also bring down our cost of warranty. So I think there's a lot for us to do within that segment over the next year or 2.

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

As it relates to last mile, let me say we have parts of the world, like Australia, where our partnerships with 3PL work seamlessly for us. And users have a good experience when we transitioned to 3PL after the restructuring, had put in place any systems integration that enables us to work and assume this way with those partners. And as a consequence, our members, who are being serviced by some of those partners, had extremely frustrating experiences.

So to begin with, when we transitioned to 3PL, there are about 10,000 orders in our system that got transferred to 3PL. That means, right out of the box, 10,000 people got rescheduled. And we did nothing to communicate to those people initially about that transition.

And then many of them had deliveries that were rescheduled and rescheduled and rescheduled. And we had no ability in our customer service organization to see into the delivery schedules of our 3PL partners to help deal with the delivery issues that our members were experiencing. So these are just some of the examples of some of the implementation-related issues that we've experienced that have created some membership-related issues that had been a tax on our Net Promoter Score that we're looking to address on a go-forward basis.

Jill Woodworth - *Peloton Interactive, Inc. - CFO*

And sorry, I just realized I missed part of your 3-part question on free cash flow. Certainly, as outlined in the letter, we're focused on getting to free cash flow positive in fiscal '23.

And there's really 4 drivers. And one of those is obviously growing the business, which we outlined in the shareholder letter, the various strategies that we're going to employ over the next several months to grow our subscriber base.

We have multiple levers in Connected Fitness margin improvement. Again, we've outlined a lot of these so I won't rehash them. But again, a lot to optimize to get back to a positive Connected Fitness gross margin structure.

Restructuring savings, we touched on, are on track. Next year, we expect significantly lower CapEx spend. We expect to sell the land and the facility that we purchased for our Ohio manufacturing. And then, of course, most importantly, inventory, we expect to turn from a source of cash or a use of cash to a source of cash in fiscal '23.

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Yes. Let me just jump in here and say, with respect to free cash flow, the objective here is to get the business to positive free cash flow in FY '23, just full stop. And with the money that we raised in the term loan, I'm very confident.

We've got plenty of capital to do that, regardless of what happens in the economy, full stop. So to the extent that there are any concerns amongst investors about our ability to do that, I don't share them, and I want to be clear about that.

Operator

The next question comes from Shweta Khajuria with Evercore.

Shweta R. Khajuria - *Evercore ISI Institutional Equities, Research Division - Analyst*

Let me try 2, please. You mentioned several growth drivers. One of them was third-party retailer partnerships. Possible to please provide a little bit more color on how the economics of those partnerships would work? Understood it may be very early, but how you're thinking about it, perhaps?

And then the second question is, another growth driver you called was value prop -- adding value prop of digital app subscriptions. So as that subscription base grows, where do you think churn rates could shake out over the next, call it, a couple of years with growing digital app subscribers as well as Connected Fitness subscribers?

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Well, I don't know the answer to the second question, honestly. And until we know what the monthly revenue is, the gross margin and the acquisition cost, we won't really have context for thinking about the churn.

I know from experience -- why is that? Because I know from experience that the way you build a successful subscription business model is by managing the interplay of its CAC, churn and gross margin, and no one of them independently of the other 2. So I realize that may not yet be satisfying, but it is what it is.

We need to figure out how to widen the marketing funnel and to use the digital app as a vehicle to do that. It could be some premium kind of model. It could be a straight subscription model. Not yet sure.

The consumer mix is about 80% female, 20% male. I think we need to drive it more towards an Internet norm of kind of 50-50. The Net Promoter -- sorry, the unaided brand awareness is like 4%. So it's the greatest app nobody has ever heard of, and we absolutely need to fix that. And of course, because it's relatively lightweight, it has the potential to grow rapidly across geographies. And expanding the business internationally is one of the priorities.

So the first part of the question related to third-party retail. We're not -- I'm not actually going to talk about that today, other than I wanted -- I thought it was important given the strategy of -- that preceded me to signal a shift, a potential shift.

We're in discussions with several potential retail partners now. I would say it's still early, early enough for us to have a sense for what some of the cost benefit trade-offs might be, but too early for us to talk publicly about it. No reason particularly to think that any deal that we were able to negotiate would be different than anybody else who distributes hardware through third-party retailers.

Operator

The next question comes from Arpine Kocharyan with UBS.

Arpine Kocharyan - *UBS Investment Bank, Research Division - Director and Analyst*

I was wondering if you could walk through the hardware versus software margin outlook for Q4? And what makes up the 31% guidance? Because it implies a meaningful improvement versus Q3, so I'm just trying to understand sort of how you get there.

Jill Woodworth - *Peloton Interactive, Inc. - CFO*

Yes. So I think what you can see on the subscription margin is probably versus Q3, a slight continued leveraging of fixed costs. And we'll have a small benefit from the pricing increase from 1 month of that. But remember, most of our costs within subscription are variable.

On the Connected Fitness side, we expect a negative margin. There's a few factors at play. We just reduced our prices pretty meaningfully across the portfolio back in April to drive scale and drive growth.

But we also have some items that are consistent with Q3 around managing our excess inventory. We're still going to see elevated detention and demurrage and storage costs. But we think those will largely abate as we move through fiscal '23. So those are not permanent.

But we -- and I guess, the third factor in Connected Fitness margin is going to be around logistics. Again, with the lower demand forecast we're not getting the fixed cost leverage that we would have expected within logistics.

But our new supply chain leadership team has only been here for about 6 weeks, and this is certainly an area of focus to get that better optimized. And as I said previously, with labor force optimization and better utilization of our warehouse space, I think there's a lot we can do in the short term to make some good improvements.

Arpine Kocharyan - *UBS Investment Bank, Research Division - Director and Analyst*

That's helpful. And then just a quick follow-up. Is there anything you could share on price elasticity of demand that you saw as a result of price cuts? Anything you could sort of quantify?

I understand commentary could be limited given some of the competitive nature of pricing in general. But anything else you could share in terms of demand change that you saw as a result of your pricing initiatives?

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Well, we talked about the unit increase in the letter, right? So that was in the range of 70%. And the revenue increase was less, of course, but it was also pretty dramatic. Like, from memory, I think it's in the order of 50% as compared with sort of the baseline growth we were seeing before we made the price change.

So it's abundantly clear that the business was better served as a result of the reduction. Now it still remains to be seen what the net impact is once the price increase kicks in, in June. But early indicators are that the churn related to that will be slow, but we won't know till we know.

Operator

The next question comes from John Blackledge with Cowen.

James McGee Kopelman - *Cowen and Company, LLC, Research Division - MD and Research Analyst*

This is James on for John. In the letter, you mentioned rolling out additional international markets. What geographies should we be thinking about next? Are you still focused on Latin America and European adjacent markets? Any color on timing would also be helpful.

And then as a follow-up, you mentioned the goal to reach 100 million members. Jill, could you provide any update on how you're thinking about it across the regions you're currently in? I think it's been a while since the last update, which I think was around 20 million global SAM back in 2020.

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Well, with respect to international, I'm not sure yet. And in part because we're still in the middle of developing our final FY '23 plan, one. Two, there are finite number of resources to spread across the business. The threshold question for us is how many of those resources to allocate to growth in international? It's something we need to be able to figure out how to do.

The reason I say that is, if we were to look, by way of example, that subscription revenue growth in the current quarter in North America, it was 53%, but in international, it was 92%. So international has potential to drive a lot of growth. But the more growth it drives early in its development, the more money we lose. And since the overarching goal is to get to positive -- sustained positive cash flow for the business in FY '23, positive cash flow trumps growth. So TBD.

Now there are things we are looking at internationally, which will make it more economical for us to launch new markets. I'm thinking particularly about last-mile delivery. An example would be just illustrative.

I don't mean to do any signaling, but we're -- today, our bike -- our Tread has to be installed. But a much simpler solution would be if we designed it and shifted in a way that it could be delivered by FedEx. You wouldn't have to be home to receive it and have it be installed, and it would cost significantly less. And it would be much easier logistically for us to launch new international markets.

Some of the ways we're thinking about flexing the model in order to make accessible to its markets that might not otherwise be. But the -- first, we have to make the asset allocation decision. And in order to do that, we need to weigh the trade-offs and the growth opportunities that we see in the business.

So new geos is one growth factor, and new products is another. I spoke earlier about consumer wellness, corporate, another growth opportunity, all of which we would like to lean into in the -- over the next 12 months.

James McGee Kopelman - *Cowen and Company, LLC, Research Division - MD and Research Analyst*

And then for Jill, just to follow up on -- if you could -- if you had any color on the SAM? I think it was 20 million when last provided.

Jill Woodworth - *Peloton Interactive, Inc. - CFO*

Sure. And obviously, that analysis hasn't been updated for the most recent price change, which, I suspect, will significantly expand TAM since that's the primary barrier. But the 100 million goal, I don't know, Barry, if you want to jump in, but obviously, it's a long way from where we sit today.

We have often looked at the number of people that have -- belong to a gym globally as an interesting data point to understand the number of folks who are interested in fitness, and that number is 180 million. We believe that tech-enabled fitness has a massive opportunity to expand the market. And we think that software will drive a transformative experience.

But we've got to evolve the strategy fairly significantly to get to that 100 million, and that could include FaaS. That could include further expansion and scaling of the app, much more international growth. And so there's a lot of different pillars to get to that, but that's a long way away.

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Yes. Look, we can't get there without making the digital app a big success, I mean, that's pretty clear. And we can't get there without having a broad-scale international business. It's clear that people outside the United States also care about fitness, and there's an opportunity for us to capitalize on that.

We'll know how big the TAM is when we get done at vetting it. I know of digital apps that already have more than 100 million people that are focused on fitness. And I can't, for the life of me, think why, given our success early in the category, that we couldn't be one of those digital apps. So stay tuned.

Operator

The next question comes from Eric Sheridan with Goldman Sachs.

Eric James Sheridan - *Goldman Sachs Group, Inc., Research Division - Research Analyst*

Maybe, Barry, I'd love to take a step back for a minute and just get your perspective. Having been inside the business now over the last couple of months, what did you find that surprised you to the upside from some of your outside perspective? Where are you finding that you need to spend more of your time?

Or do you think there's a bit of a more effort that has to be applied to sort of get the business to workovers over the medium term? So just sort of a broader question on your perceptions and how that's resulted in how you spend your time and realigning assets.

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Let me make sure that I got the question. What have I found internally that makes me optimistic about the success of the business?

Jill Woodworth - *Peloton Interactive, Inc. - CFO*

Surprise.

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

What surprised me?

Jill Woodworth - *Peloton Interactive, Inc. - CFO*

Opportunity.

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Well, the nature of turnarounds is they're full of surprises. I would say the biggest surprise in the quarter was the cash flow. And related to that, the biggest surprise was our ability to quickly address it without diluting existing shareholders and adequately capitalizing the business.

So I'm just really, really pleased with the way the team executed to address that particular issue. I found more talent in the building, honestly, than I expected to find. And -- which is incredibly important if you're going to be able to execute.

We were weaker on everything supply chain than I expected. But we're fortunate to get Andy, and he's moved quickly to build out his team. And so I'm pretty optimistic about our ability to address that.

And then I would say, lastly, I was surprised to discover that when I first introduced the concept of Fitness-as-a-Service, the business had already been -- had thought about it 2 years ago and then sort of got sucked into the vortex of COVID. And so never really leaned into the opportunity but had already done thinking about it. And so we were able to move on it faster than we would have if they hadn't already thought about it.

And then, lastly, I would say, I'm really encouraged by the growth. And my -- I was hoping we'd get to 70% uplift, I thought that would be pretty spectacular, and we're pushing north of 90% at the moment. So it remains to be seen whether the value proposition that we're pushing will drive the kind of ROI that we would like to see to justify the investment.

But I think that's a really big idea, and it changed dramatically the P&L if we roll it. There is no hardware gross margin in that business. We own it. There's no transfer of -- we own the hardware, there's no transfer of title.

We amortize the hardware over the expected useful life of the bike. The frame has a different -- has a longer shelf life and the console. I expect the gross margins in that business to push high 70s, low 80s. And I think we would have a super attractive customer acquisition costs.

So I'm just in love with the whole thing. And nothing I've seen yet gives me pause related to it. I know it won't be a straight line from here to there, and we may have to do some engineering, but that's been the -- like the biggest surprise on the upside since I walked in the door, I would say.

Operator

The next question comes from Aneesha Sherman with Bernstein.

Aneesha Sherman - *Sanford C. Bernstein & Co., LLC., Research Division - Research Analyst*

So your point around digital being the tip of the spear and the leading force towards getting -- towards the 100 million, how does that fit with your point of international? Would you be considering digital-only or digital-first expansion internationally to get around some of those -- some of the drag on margins you talked about earlier in the call?

And then related to that, last quarter, you talked about going dark on marketing to understand the baseline. Has that plan changed now that you're thinking about top of the funnel and improving brand awareness?

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Well, yes, going dark on marketing was not my plan. And so mostly, I've been focused on what I think makes sense for driving business growth. And the frame of reference I have brought to that decision-making is LTV to CAC.

As it relates to international growth and the digital app, the answer to your question is yes, but remains to be seen what actually we're going to -- what the value proposition for consumers will be, what's going to be in the app and how do we position it relative to all-access. But historically, the approach has been all-access first, digital later, kind of maybe if we get to it. And I think we need to change the order.

Operator

The next question comes from Rohit Kulkarni with MKM Partners. This will be our last question.

Rohit Rangnath Kulkarni - *MKM Partners LLC, Research Division - MD*

Great. A couple of questions for you, Barry. Can you talk about the kind if obvious holes in talent that you're trying to fill here at Peloton? You talked about tech debt. Also, any examples as to if you're able to resolve the tech debt, what improvements in processes, execution time line that you could have?

And then maybe one [money] kind of question. On the $800 million annual run rate savings by fiscal year '24, why does it take so long to achieve these savings? And not just by next fiscal year itself. As you are trying to get to cash flow breakeven, is there a scenario that you could get these run rate savings a lot sooner?

Jill Woodworth - *Peloton Interactive, Inc. - CFO*

Do you want me to take that restructuring question first?

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Sure.

Jill Woodworth - *Peloton Interactive, Inc. - CFO*

So I can speak on the COGS side. I mean, really, when you think about having improved cost per unit, right, through better design procurement, you have to sell through your existing inventory. I think we will broadcast our inventory position at this juncture. But it will take us through fiscal '23 to sell down.

And so that is one of the main reasons for the longer time frame on getting to a better cost per unit and being able to realize a lot of the COGS savings, which I think we said $300 million by fiscal '25 -- '24 -- end of '24, sorry.

And then on OpEx, we are going as absolutely fast as we can. There are certain things that take a little bit more time as we move out of certain real estate that we occupy from a corporate perspective. But we are moving as quickly as possible.

And as I said, of the $500 million, we're expecting $450 million within fiscal '23. And our goal was to get to that $500 million run rate by the end of fiscal '23. But COGS will take more time.

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

And I'm going to say, some of that -- those savings are run rate-related. So taking $200 million out of marketing. Well, partly, that's a function of taking a different structural approach to how we market. The product and the savings get realized over time. Same thing with respect to some of the savings that we have projected that we will achieve in G&A.

The first part of the question was related to imbalance of what?

Rohit Rangnath Kulkarni - *MKM Partners LLC, Research Division - MD*

Talent.

Jill Woodworth - *Peloton Interactive, Inc. - CFO*

What any talent that you want [to hire] or the areas of talent hire?

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Well, none that I want to highlight on the call. People here at Peloton are getting tired of me saying talent density is job 1, talent density is job 1. So if there are additional -- additions that were going to happen as a team, you'll hear about it after the fact, not before the fact. But your going-in expectations, your understanding should be that there may be more talent in the building than you might have expected.

Rohit Rangnath Kulkarni - *MKM Partners LLC, Research Division - MD*

Tech debt.

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Well, so let me tell the story this way. The business was crowdsourced so there's a bunch of software that was hacked. The business started to have success, like all tech companies I've ever been associated with, all of the resources of the business were focused on engineering and product in order to accelerate growth.

And then COVID hit. And so the business explodes from 700,000 subs to 3 million subs. And all those systems-related issues are still present in the business today. So the order management system is still the original code that was hacked when the business was first organized. And pretty much all of that needs to be rewritten.

And then there are a bunch of downstream issues that happened because of the way that the order management system was architected and speaks to the -- to all the accounting-related systems, the ERP system. And if you work in customer service or I think I've heard there are 13 or 16 different screens you look at in order to be able to see the entire customer history. And Andy has just hired a new head of customer service, and we're going to be addressing some of those issues.

So when you actually call up, our customer service reps are actually able to be helpful because we've organized all that information on one screen. So those are kinds of -- those are examples of some of the kinds of issues we face.

Others relate to our ability to push code in our engineering team and the productivity of engineers. This is an issue, for instance, in the last couple of years that's [followed by the Barry effect] that we wrestled to the ground. But even after it was public, it was an issue that they had to address, and we have to address it here as well.

And so as a consequence, it slows down the speed at which we're able to A/B test and the speed at which we're able to update our e-commerce platform. You see that in our ability to quickly get to market to A/B test Fitness-as-a-Service, for instance. I mean, really, we have to wait until the end of June to be able to A/B test on the website. That's something that would take 1.5 days at Netflix, even early on.

But it is what it is, and we'll get through it. We understand what the issues are now, and we'll get the kind of expertise we need in-house to get it fixed. These are not unsolvable problems. They're not problems that companies like us haven't seen.

We just have to get our arms around it, and fix it. Then 12 months, we'll be in a much better place than we are today. So they don't threaten the business. It just slows us down, and we move a little slower than we would like to as a consequence.

Operator

This concludes our question-and-answer session, and I'll turn the conference back over to management for any closing remarks.

W. Barry McCarthy - *Peloton Interactive, Inc. - CEO, President & Director*

Okay. Well, I'm sorry that we sort of ended on that downward note because, actually, notwithstanding the stock price, feeling pretty optimistic about the path ahead and the number of levers that we have to turn to improve the operating performance of the business.

I don't mean to sound pollyannish, but I'm hopeful that, someday soon, we're going to look back on this call as one of the important turning points in the business. And look forward to checking in with you next quarter on our progress.

Operator

The conference has now concluded. Thank you for attending today's presentation, and you may now disconnect.
