REFINITIV STREETEVENTS

# EDITED TRANSCRIPT

PTON.OQ - Q1 2021 Peloton Interactive Inc Earnings Call

EVENT DATE/TIME: NOVEMBER 05, 2020 / 10:00PM GMT

**OVERVIEW:**

Co. reported 1Q21 total revenue of $758m and net income of $69.3m or $0.20 per diluted share. Expects FY21 total revenue to be $3.9b or better and 2Q21 revenue to be approx. $1b.

## CORPORATE PARTICIPANTS

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

**John Paul Foley** *Peloton Interactive, Inc. - Co-Founder, Chairman & CEO*

**Peter Coleman Stabler** *Peloton Interactive, Inc. - SVP of IR*

**William J. Lynch** *Peloton Interactive, Inc. - President & Director*

## CONFERENCE CALL PARTICIPANTS

**Bernard Jerome McTernan** *Rosenblatt Securities Inc., Research Division - VP & Senior Research Analyst*

**Deepak Mathivanan** *Barclays Bank PLC, Research Division - Research Analyst*

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

**Edward James Yruma** *KeyBanc Capital Markets Inc., Research Division - MD & Senior Research Analyst*

**Heath Patrick Terry** *Goldman Sachs Group, Inc., Research Division - MD*

**James Lloyd Hardiman** *Wedbush Securities Inc., Research Division - MD of Equity Research*

**John Ryan Blackledge** *Cowen and Company, LLC, Research Division - Head of Internet Research, MD and Senior Research Analyst*

**Justin Post** *BofA Merrill Lynch, Research Division - MD*

**Lee Horowitz** *Evercore ISI Institutional Equities, Research Division - Co-Head of Internet Research*

**Ronald Victor Josey** *JMP Securities LLC, Research Division - MD & Equity Research Analyst*

## PRESENTATION

**Operator**

Ladies and gentlemen, thank you for standing by, and welcome to the Peloton Interactive First Quarter Fiscal Year 2021 Earnings Conference Call. (Operator Instructions) As a reminder, this conference call is being recorded.

I will now turn the call over to your host, Mr. Peter Stabler, Head of Investor Relations. Sir, you may begin.

---

**Peter Coleman Stabler** - *Peloton Interactive, Inc. - SVP of IR*

Good afternoon, and welcome to Peloton's fiscal first quarter conference call. Joining today's call are John Foley, our Co-Founder and CEO; President, William Lynch; 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 John.

**John Paul Foley** - *Peloton Interactive, Inc. - Co-Founder, Chairman & CEO*

Thanks, Peter.

2020 has been an incredibly stressful year, and we continue to be grateful for the small, positive role we play in our members' lives. COVID-19 has changed nearly every aspect of how we live, including how many of us are staying active and healthy. Of course, this has benefited our business results, but it has also brought with it unprecedented operational challenges. So before I jump into our results, I'd like to offer some thoughts on the operating landscape.

Since our founding, we've prided ourselves on being a "Members First" organization. And an important part of having a "Members First" focus is providing superior customer service, service that starts with the purchase process and extends all the way through delivery, setup and ongoing member support. We obviously don't just sell bikes and treads. We have an ongoing service relationship that we hope will extend for many, many years.

Therefore, it pains us that we've been underperforming recently versus the high standard we strive for. Wait times for our products have been unacceptably long. But none of us could have predicted that we'd see all-time spikes in COVID-19 cases in October and the threat of new lockdowns in our global markets. High organic sales growth has been steady since March and the lowering of our original Bike price and the launch of Bike+ has steepened that demand curve.

We did our best to estimate the demand for Bike+. But while we are incredibly excited about the positive reaction to Bike+, sales outpaced our internal estimates, quickly causing wait times for Bike+ to balloon. As such, we are working swiftly to pivot manufacturing capacity to Bike+.

Product wait times have also been impacted by port congestion, periodic warehouse closures associated with COVID-19, West Coast forest fires and hurricanes, forcing us to reschedule many deliveries. These external factors, unfortunately, extended already long delivery times.

Launching the Bike+ was an exciting milestone in our history. However, it also drove high call volumes and very long wait times to reach our sales support teams, which impacted our customer experience.

In response to long product wait times and elevated customer support volumes, we are specifically taking the following measures. One, we are, of course, continuing to add manufacturing capacity.

Two, we are investing in expedited shipping from our Taiwanese factories into the U.S. by adding air shipments of Bike+ and also utilizing expedited ocean shipping and ground truck logistics. All with the goal of improving our delivery times. While these actions result in higher-than-typical logistics costs, we feel that incurring these incremental expenses in the short term is the right trade-off to improve our member experience.

Number three, we are working hard to scale our member support team as quickly as possible to handle call volumes and limit wait times getting through to our teams.

Four, lastly, to give our future members complete transparency, we are communicating clearly on our website the expected order-to-delivery dates by product. Please know we're fully up to the challenge and are 100% committed to again delivering the level of excellent customer service our members deserve and expect, but it will take us a bit more time to get there.

Now on to some highlights from the quarter. Net Connected Fitness subscription additions in the quarter totaled approximately 243,000, bringing our end-of-quarter total to over 1.33 million, up 137% year-on-year. As of September 30, we had over 3.6 million global members, inclusive of our over 510,000 Digital Subscribers.

As I mentioned previously, we're extremely pleased with the successful launch of Bike+, a product truly developed in collaboration with our member community. Our plan to introduce our new Peloton Tread is progressing, and we expect to provide additional details about its availability soon. In the meantime, we continue to capture e-mail addresses of interested consumers and plan to allow prospective members to see the new Tread in our showrooms prior to Thanksgiving. I know I speak for the entire Peloton team when I say we can't wait to bring this game-changing product to market.

On the content side, we're thrilled to introduce Bike Bootcamp and Barre to our class library in September. Our Barre class collection, led by Hannah Corbin and Ally Love, was highly requested by our members and represents an important pillar in building out our strength platform. Within the first weeks of launch, our members consumed over 0.5 million Barre workouts.

Bike Bootcamp brings the amazing full-body bootcamp workout to our Bike members taught by our world-class instructors, Robin Arzon, Cody Rigsby and Jess Sims. Since launch, our Bike Bootcamp classes have amassed over 350,000 workouts.

And as you've heard us say before, our #1 goal is to add more and more value to the Peloton membership over time. I'm excited to say that there's a lot more new, world-class content in the pipeline, so stay tuned.

Member engagement remained strong this quarter, with 20.7 workouts per Connected Fitness subscription versus 11.7 in the year ago quarter, an increase of over 75%. The sequential quarterly decline in workouts for Connected Fitness subscription reflects the typical seasonality tied to warmer weather in Q1. As we've said previously, I encourage you to focus on year-on-year growth and workouts per subscription.

Before I turn it over to Jill to cover our financial performance, I'd like to highlight our new partnership with Chase announced last week. This is a first-of-its-kind arrangement for Peloton. Chase will offer up to $60 in statement credits towards Peloton subscriptions for Chase Sapphire Preferred Card holders and $120 in statement credits for Chase Sapphire Reserve Card members through December 2021. We are very excited to leverage the Chase platform to further build Peloton brand awareness while offering substantial benefits to our mutual member base. We hope that this partnership continues to drive awareness of the Peloton App, incremental Digital Subscribers, and ultimately, more Connected Fitness Product sales over time.

Lastly, to our Peloton team members, thank you. Rapidly scaling a business during a global pandemic is difficult. You have met this challenge and made us so proud of your incredible energy and commitment to our member community. Again, thank you for what you do.

Now over to you, Jill.

---

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

Thanks, John.

I will start with a review of our first quarter results. In Q1, we generated total revenue of $758 million, representing 232% year-over-year growth, exceeding expectations across all geographies. Our revenue performance benefited from continued strong organic demand for our Bike, an incredible reception to Bike+ from both our new and existing members and a significant number of undelivered bikes that were carried over from the fourth quarter.

Gross margin for the quarter was 43.4%. Connected Fitness Product gross margin was 39.4%, better than expected due to sales flow through and lower-than-expected costs for expedited shipments. This partially offset the year-over-year decline due to the price reduction of our original category-defining Bike. We were incredibly pleased to pass our substantial manufacturing efficiencies we've garnered over the past few years on to our customers. In addition, lowering the price of our Bike will allow us to continue to rapidly expand our global market opportunity.

Subscription gross margin was 58.5%, and subscription contribution margin was 64.1%, slightly ahead of expectations due to some streaming cost efficiencies. Total operating expense as a percentage of revenue was 34.3% compared to 68.4% in Q1 of last year.

Sales outperformance drove significant leveraging of operating expenses in the quarter. Sales and marketing expense represented 15.1% of total revenue versus the prior year period of 34%. For the launch of Bike+, we incurred modest advertising spend. We also proudly launched our first brand campaign featuring Peloton members entitled, We All Have Our Reasons, which has been running on multiple advertising platforms.

General and administrative expense was 14.3% of total revenue versus 26.7% in the prior year despite significant continued investment in our team and systems to scale our business. Research and development expense was 4.8% of total revenue versus 7.7% in the year ago period, even with increased investments in new software and hardware.

With better-than-expected sales, gross margin and operating expense leverage, our fiscal '21 Q1 adjusted EBITDA was $118.9 million, representing an adjusted EBITDA margin of 15.7%. Net income for the first quarter was $69.3 million or $0.20 per diluted share. And we ended the quarter with over $2 billion of liquidity and have additional liquidity in the form of an untapped $250 million credit facility.

Now on to our outlook. While the operating environment continues to throw several challenges our way, we endeavor to give guidance that reflects our best estimate as of today of our expected operating performance. I'd like to remind everyone that quarterly flow can vary significantly given the operating environment due to COVID-19 and other factors John mentioned.

Before walking through the guidance, I'd like to point out that we have decided to move to single-point estimates for our financial guidance. Take it as our best estimate of the upcoming quarter's performance. While full year guidance brings a higher level of uncertainty, especially during this time, we have elected to continue to share an estimate of our performance, which we view as achievable given our current view of the business.

In Q2, we expect revenue of approximately $1 billion, representing 114% year-over-year growth. Continued high global demand for our products resulted in an increased backlog of deliveries at the end of the first quarter. In addition to the strong sales we've seen since the early spring due to COVID-19, recent sales performance has been driven by our Bike price reduction and stronger-than-expected reception to Bike+. Also, the recent spikes in COVID cases and newly imposed lockdowns in some of our markets have had a significant positive impact on sales.

We have expanded our manufacturing capacity severalfold and expect to continue to grow our supply of Bike and Bike+ in the coming months with the help of our third-party manufacturing partners and the opening of our new Shin Ji factory at Tonic at the end of this calendar year. We expect the growth in our supply chain to allow us to get back to normal order-to-delivery time frames for our Bike by the end of this calendar year. However, we will likely be operating under Bike+ supply constraints for the foreseeable future, causing longer order-to-delivery time frames for Bike+ for a couple more quarters. We are already shifting manufacturing capacity in favor of Bike+ but continue to expect our original Bike to be our top-selling product in fiscal 2021.

In Q2, we forecast end-of-period Connected Fitness subscriptions of 1.63 million, representing 129% year-over-year growth. For Q2, we expect average net monthly Connected Fitness subscriber churn under 0.85%. As you can appreciate, churn is challenging to predict with accuracy given the evolving COVID-19 landscape as well as the uncertainty surrounding the overall macroeconomic environment.

Moving on to margins. The strong reception of Bike+, combined with challenges associated with port congestion and COVID-19-related warehouse closures, impacted Bike+ delivery dates for many of our customers and caused significant member experience challenges. Therefore, as John mentioned earlier, we are incurring outsized additional shipping-related expenses in Q2 in order to alleviate some of the delays ahead of the holiday period. As a result, we expect Q2 gross margin to temporarily decline to approximately 39%, comprising of a Connected Fitness Product's gross margin of 35% and subscription contribution margin of approximately 63%.

These shipping expenses also impact adjusted EBITDA profitability for the quarter, but we believe these are important investments we need to make in order to get bikes as quickly as possible to our new members.

These additional shipping costs in Q2 will be partially offset by significant year-on-year leverage in sales and marketing expense as well as G&A expense despite continued robust people and technology investments across our company in order to manage our growth. As a result, we expect Q2 adjusted EBITDA of $70 million, representing an adjusted EBITDA margin of 7%.

For fiscal year 2021, we are raising our estimates of full year total revenue to $3.9 billion or better, representing 114% year-over-year growth. In fiscal '21, we expect modest quarterly sequential revenue growth as we add manufacturing capacity throughout the fiscal year. For fiscal year '21, we now forecast 2.17 million ending Connected Fitness subscriptions or more and an average net monthly Connected Fitness churn to stay under 0.9%.

For fiscal year 2021, gross margin is unchanged from our previous full year guidance of roughly 41%. Despite some current Q2 investments for air shipments of Bike+, we still expect full year Connected Fitness Product gross margin [to decline to 36%], driven primarily by our recent Bike price reduction and continued mix shift to Tread.

We leave our expectations for subscription contribution margin for full year fiscal '21 unchanged at approximately 64% as we continue to expect leverage and fixed cost of content production to be offset by elevated engagement levels, higher Digital Subscriber growth and continued investments in global fitness and wellness programming.

As we move through the balance of the year, we expect to ramp marketing spend, which will be more than offset by revenue flow-through, leading us to revise our adjusted EBITDA to at least $300 million.

I will now turn it over to the operator to take your questions.

---

## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) Our first question comes from Doug Anmuth of JPMorgan.

---

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

First, I was just hoping you could provide a little bit more detail on the supply bottlenecks and just try to maybe break out or prioritize for us a little bit across port congestion versus manufacturing versus kind of shipping and more last mile type of delivery? And then just second, just given those supply constraints and the elevated wait times, can you just talk about your marketing plans and how that impacts them around the holidays?

---

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

Doug, it's William Lynch. Thanks for the question. I mean, first, we'd like to thank the team across the company who have worked, as John noted, tirelessly to support the incredible growth. As Jill mentioned, Q1, we did $758 million in revenue. And you look at Q1 '20, that was $228 million. In Q1 '19, that's $112 million. So in 24 months, we've grown our business almost 7x. And so we appreciate the extraordinary effort that the teams across the company have undertaken to make that happen.

In terms of breaking it out, what I would say is, one, we'd mentioned in the previous call that we felt like we were digging out from Bike. And then as Jill noted, that's still our #1 selling SKU, and we have seen progress there. So -- and just, in fact, yesterday, we dropped OTD in all our sales channels on that product, 4 to 6 weeks, which if you look back since the pandemic started, that is the shortest lead time since April.

And then as both Jill and John mentioned, Bike+ is elevated, and that's really -- and will stay elevated as we get through Q2 and into Q3. And the reason for that is 2 things. One, as John mentioned, that product is exceeding our expectation. It's a new product with a new supply chain. And so ramping that supply chain up and reacting to that demand is a little trickier than a more stable, more mature product like Bike, which we've been able to react to.

And so Bike+ -- the port closure, L.A., the port delays really hurt Bike+. We had a lot of Bike+ coming in against that demand, and that delay has hurt specifically that product. We think that is largely due to the environment and just a lot of product coming in, e-commerce product coming in. And then as we get through that, as John noted in his opening remarks, we've switched product lines to focus on Bike+, and this team can react very quickly.

And so we -- and breaking it out specifically, we think the port delays will persist for a period of time, and that's baked into everything Jill talked about. But as we get through those, we feel good about continuing to draw down our core Bike OTDs back to where we want them to be, which is inside of 2 weeks as we get through Q2. And then Bike+, we're quickly reacting with all the actions we mentioned to get that product line into that same 2-week window, but that's going to take a while into Q3.

---

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

Great. On the marketing front -- and obviously, William, feel free to chime in. We do expect throughout the year, as we said on the last earnings call, that we will be ramping marketing spend through the next few quarters. So expect to see some sequential deleveraging of sales and marketing as a percentage of sales through the end of Q3.

Obviously, Q4, we're obviously lapping a quarter where we were completely dark. So we plan on, again, continuing to ramp marketing spend pretty reasonably on a year-over-year basis in Q4.

So I think if you take a step back, what's going to be really important is obviously getting to our goal, which is getting our original Bike delivery days down by the end of this year. As you can imagine, so far this year, we've focused on our brand campaign that featured our members. We focused on telling the market about Bike+, but we haven't really gone out broadly yet on original Bike and the price reduction, which is now $49 a month on financing.

And so as we get through that crucial period of getting those order-to-delivery dates down, we're really excited to tell the world about the value proposition of the Bike. So you can expect through the year that we will continue to spend and make sure that we're top of mind with the consumer.

---

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

Yes. And just to add to Jill's point, we also see continued opportunity in the international markets from a marketing standpoint as we've gotten a lot of traction in U.K., Germany, Canada and continue to grow awareness and establish our Connected Fitness leadership there. So between really telling the world about this amazing price point on Bike and then continued development of those international markets, that's what you're seeing with the more aggressive marketing plan in the back half.

---

**Operator**

Our next question comes from Ron Josey of JMP Securities.

---

**Ronald Victor Josey** - *JMP Securities LLC, Research Division - MD & Equity Research Analyst*

I wanted to ask a little bit about member engagement and understood seasonality maybe coming back in here, John and Jill. We mentioned that in the past. But can you talk about engagement from the newer subs that you've seen that joined from April to present? Just trying to get a better sense of how newer subs are interacting with the platform.

And then, John, you talked about Bike Bootcamps and Barre A classes -- Barre classes launching. Can you just talk about content availability and then also how you're balancing that with the instructor base? I'm assuming with more subscribers, you need more content and more instructors. I'm just wondering about that investment.

---

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

I can start it out. And then John and William, feel free to chime in. And I think we have shown in the past some really exciting data that does show that our newer cohorts tend to work out even more than our older cohorts, which I know has been counterintuitive over the years as people think that the people that jumped on board with Peloton years ago were really the super users. But it's really the younger cohorts, I think, for a variety of reasons. One, as you know, we've made such great strides in broadening our demographic. And I think that value proposition for someone who is now using the Peloton Bike and the Peloton App to replace what they used to do, whether it be boutique fitness or the gym, I think, they're deriving a ton of value from it.

And then specifically to answer your question since April, as you can imagine, a lot of the new buyers around COVID, especially right at the spike of COVID in March, was -- were people that had regular gym routines and boutique routines and all of a sudden found themselves in a spot where they didn't have a routine anymore. And so I would say the engagement of the members that have joined since April has likely outstripped that. I don't have the specific data, but we've looked at it a few times over the last several months. I would say that their engagement levels are even higher than the cohort data that I believe we showed during our investor session back in September. So really encouraging trends.

---

**John Paul Foley** - *Peloton Interactive, Inc. - Co-Founder, Chairman & CEO*

And Ron, I'll take the first part of your content question. I don't know whether William will want to jump in. But if I understood your question correctly, you were saying that as we scale our member base, we need to grow our instructor base, which to the letter is kind of a false assumption, right? The beautiful thing about our model is the scale where we go from 2,000 people consuming a class to 20,000 people consuming that same class and that same instructor. That's kind of the beautiful thing that we see in our model.

But to your point, we are investing in content. It is something we do plan to innovate on and stay out in front of any would-be competition. You said Bike Bootcamp, yes, it's doing very well. Barre's exceeding our expectations. We have new content coming in the coming months and certainly quarters.

One thing I'm excited about is new languages. As you know, we're in German and we're in English. And as we push to be a global technology platform, foreign language is obviously one place you would expect us to invest, and I'm really excited about that. But I don't know whether I'm specifically answering your question.

But I don't know whether, William, you had other thoughts.

---

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

No, I would say all that's right. I mean if you look strategically at what we've said is important to us, it's, as John mentioned earlier, to continue to make that $39 a month membership more and more valuable. And if you look at our cardio offering, certainly with Bike, we have had and continue to add the best instructor roster on the planet and diversify the content offerings.

And then we said strength as a strategic pillar is vital for us, and it's one of our fastest growing categories. And so you have seen us add a lot of content programming, Jen Cotter, Kevin Chorlins and that team have been busy experimenting with new things. It's been incredibly successful, Barre, we actually count as part of that strength programming. And that has been one of the fastest-growing, in terms of adoption, fitness verticals out of the gate. John mentioned 500,000 classes taken. And so you'll see us continue to really lean in on strength in investments.

John mentioned instructor portfolio internationally. And we have nothing to announce today, but you'll -- we've definitely been busy in that front as well. And so yoga as well, another area that is taking off along with meditation. And it's a big focus for us, and we're really pleased so far with the adoption across not only bike, but nonbike, noncardio verticals.

---

**John Paul Foley** - *Peloton Interactive, Inc. - Co-Founder, Chairman & CEO*

One thing, Ron, [encourage you -- on] this question, I will add that it's not just the amount of content and the number of instructors and the number of languages, but it's also the quality of the content that we're producing, that we're investing in. I encourage everyone to take a recent class, Jess King Experience from a couple of weeks ago, her first one back that I sent a note to the team. I thought the innovation on some of the camera angles and lighting and just the production value of our content is going to be increasing and improving under Jen Cotter and Kevin Chorlins' leadership. So stay tuned on that front.

---

**Operator**

Our next question comes from Justin Post of Bank of America.

---

**Justin Post** - *BofA Merrill Lynch, Research Division - MD*

Great. I guess I'll ask about supply just because it's such an important factor. Just maybe give us an update on the factory. Is it on track to be ready to start shipping? And is that mostly treads? Or are they going to be doing everything out of there? And then maybe you could give us an update on kind of used inventory that you've been collecting and how you're thinking about the CPO rollout at some point.

---

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

Justin, maybe I'll take the first one. This is William Lynch.

And then, John, maybe you comment on CPO.

So in terms of -- I think you were referencing Shin Ji, which is one of the pillars of our expansion on capacity. It's a foundational element for us, that factory we've been building. We're excited to announce that construction is largely complete. And Jill in her opening comments talked about us ramping production very early in the New Year as we end this year, and that's on track. And so we're excited.

You'd asked about capacity there. We said 1.5 million units. Think of that as a blended Tread and Bike. And so -- but it's just one part of our expansion. Obviously, with this kind of growth there is no one silver bullet. So our existing factories, we've been expanding with Tonic in that acquisition, and Tainan and then Rexon has done a great job scaling Bike and Tread+ in their factory. And also, we've been deeply investigating and investing in a domestic U.S. manufacturing capability, and we expect to have some announcements on that shortly.

And so if you look at just supply chain and operations as a percent of sales, the growth in OpEx as we plan this year, is -- it's our fastest growing area. And so we see what everyone sees, which is incredible growth that we obviously want to support and bring OTDs down. So we're -- we've got a lot of different vectors here and are excited about it. But yes, Shin Ji is tracking, and we can't wait to start producing units out of that factory.

---

**John Paul Foley** - *Peloton Interactive, Inc. - Co-Founder, Chairman & CEO*

Yes. What's up, Justin? This is John. Yes, the CPO, certified preowned rollout, is something we remain excited about. We continue to think it's a massive opportunity in the years to come. Unfortunately, in the short term, we don't have the inventory. There's no big opportunity for us with CPO in the short term. We are testing it to the extent we get some bikes back, but without the inventory, there's no certified preowned business. So we're quarters, if not years, away from that being a big driver for us.

We -- again, we love it. I will tell you an interesting dynamic that kind of surprised us. As a lot of our existing Bike members that upgraded to Bike+, now we were expecting to get those bikes back and just kind of prime the pump for our certified preowned opportunity, we found that a disproportionate number of those folks that are existing members decided to keep their existing Bike, their original Bike and buy a Bike+.

And whether they used it, the original Bike in their second home or gave it to their college age daughter or son or kept it in the family, so to speak, because they were -- they understand that these are hot commodities and people want those on bikes. So we got fewer of them back than we had expected when we launched Bike+. So it's just an interesting dynamic that we're tracking, obviously.

**Operator**

Our next question comes from Heath Terry of Goldman Sachs.

**Heath Patrick Terry** - *Goldman Sachs Group, Inc., Research Division - MD*

Great. I was wondering if you could give us a bit of an update on sort of where your in-store business stands at the moment. And particularly as you get into the launch of Tread coming up, how you think about the role that stores will play in the Tread business. It seems like Tread will be -- it will be an important part of your Tread launch, particularly here in the U.S. So anything that you could sort of share with us on planned Tread launch as we get closer to that and then sort of where your store footprint stands at the moment?

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

Sure.

I'll take that, John. Feel free to chime in.

So currently, we're at 105 retail stores. We are going to continue to expand intelligently, but we see opportunity for expansion, the 4-wall profitability on the stores. And as you note, and it's an astute observation, especially as we launch new products, it's an incredible platform for us, and we think a strategic advantage for us to have that kind of reach.

As we look at retail, we look at how do we access population centers in the U.S. And increasingly, we're covering the large, large majority of the population. And so in terms of how we're operating now, it's been by appointment only for the most part. And that's, obviously, against our strategy of keeping our employees and members and prospects as safe as possible. We have seen that those stores over-indexed on new product, and it's just vis-à-vis the average if you look at our channel.

And so we love retail. We're actually being super innovative. If you look internationally, Kevin Cornils and that team, our great international team, did a partnership with John Lewis. And so we're testing store-in-a-store concepts over there. And so far, it looks successful. We're in 4 of those, and we're going to measure it through the holiday.

And so we're -- this company is about innovation, and we're going to find ways to reach the customers. We continue to expand our SAM and TAM. And so as you know, you're 100% right on. As we think about the Tread launch, and we'll have more to announce there shortly, retail is going to play a very, very big role, so stay tuned.

**Operator**

Our next question comes from Edward Yruma of KeyBanc Capital.

**Edward James Yruma** - *KeyBanc Capital Markets Inc., Research Division - MD & Senior Research Analyst*

I guess, first, you spoke a lot about manufacturing. I was wondering if you could just readdress maybe last mile, the kind of investments you need given the strong ramp you're seeing. And then as a follow-up, congrats on the Chase deal. Does that change the economics for you? Or is that simply just Chase subsidizing for their cardholders, the membership? And to your point, John, that was a great Jess King ride.

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

John, maybe I'll take the last mile, and then -- so it's a great question on logistics. It's not just about manufacturing. And so we've been investing in new warehouses and distribution capabilities. We're up to 47 last mile hubs and warehouses, which like, as with retail, give us strategic coverage in close proximity. We measure it within 60 miles in most metros. Can we get to most of the population? And increasingly -- and we have a large majority of coverage. And that's just with our own warehouses. We also, as you know, employed 3PLs for heavy spill and volume, so we have that flexibility.

If you look at -- and so that's big growth from '19 just on the last mile hubs on the total delivery team. Last year, at this time, we were about at 900. We're at 2,200 this year. Bands we've more than doubled. We have well over 700 bands across the U.S.

And so it's not just about infrastructure either, we're investing in people. We were really excited about 2 new leaders we've got in the ops team, Jennifer McKeehan, who was a Senior Executive over at Home Depot we brought in; and Dan O'Brien, VP of Manufacturing. So it's infrastructure, it's people, it's investments across the board. And so that has us excited.

---

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

And I'll just chime in quickly on the Chase partnership. Obviously, we're very excited to partner with Chase, the nation's largest card issuer, and bring this benefit to our mutual member basis to both our Connected Fitness subs or All-Access subscribers as well as our Digital Subscribers. So we can't really get into the details of the agreement between us and Chase, but we do expect that this partnership will help us with developing further our brand awareness with the Chase customer.

We're excited about incremental Digital Subs that may sign up as well given the credit that they will get through these various credit card offers. And eventually, as you know, we look at our digital as an incredible top funnel for Connected Fitness sales. So we do believe, since Digital has been such a strong lead gen for us, that over time, this will convert into Connected Fitness sales. But I can't really get into the details, unfortunately, but we're really excited about it.

---

**Operator**

Our next question comes from John Blackledge of Cowen.

---

**John Ryan Blackledge** - *Cowen and Company, LLC, Research Division - Head of Internet Research, MD and Senior Research Analyst*

A couple of questions. You talked about marketing ramping through this year for the original Bike being a value prop. How should we think about what Peloton is planning to drive awareness of the lower-priced Tread? Will there be a big marketing push ahead of the launch of the lower-priced Tread right after the holidays?

And then second, obviously, experiencing -- continue to experience incredible demand. But with the pandemic surging again in the U.S., U.K. and Germany, have you seen an uptick in demand over the past month or so?

---

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

William, do you want to take the first question on Tread marketing plan? And then maybe I can talk a little bit about sales over the last several weeks.

---

**John Paul Foley** - *Peloton Interactive, Inc. - Co-Founder, Chairman & CEO*

And I can weigh in real quick on the lower-priced Tread because I'm so excited about it.

So sorry, William, I'm going to jump in because I got -- I've got to talk about it.

Our lower-priced Tread is such an incredible product, John, that I believe that against our millions of members, adding millions more with each year that ticks by, we're not going to have a problem selling this lower-priced Tread. I think as some of the other analysts have asked that the problem is going to be on the supply side or the opportunity. And I think William and Jon Adee and the whole team are -- have an incredible plan of kind of belt and suspenders approach to making sure that we can make enough of these.

But I hope we're in a situation where we get to market the lower-priced Tread. I mean we have such an incredible marketing organization at this point. And we talked about the footprint of our retail stores. It's just such a beautiful flywheel that allows us to create demand. Layer on top of that, the word-of-mouth that our high Net Promoter Score and our super engaged members have. And so with the millions of people that will have a Peloton Bike, we believe that once they have a friend that tells them about how good the Tread is, they're going to go to a store, check it out, realize that they need it and they want it, realize that it scales their $39 membership.

So John, you probably know that if you get a Peloton Bike, then you pay $39. If you get a Peloton Tread, you don't pay an incremental monthly fee. So it's a real great opportunity if you were a Peloton member to get the best treadmill in the world and engage in these bootcamp classes.

So I just kind of wanted to reframe your question a little bit is I hope to God we're able to run TV for the lower-priced Tread because we want to get the word out, but I think the word is going to get out in front of our marketing organization is the sad reality.

---

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

Yes. And just to build on what John alluded to, there's going to be substantial marketing around the Tread launch, and it won't be necessarily as big in terms of big TV awareness campaigns. But the enthusiasm is already there. I think John mentioned in the leads, we're capturing leads on Tread, and we're really pleased and energized by the lead and the interest around Tread.

So you will see us marketing into -- in next year. It's the biggest -- it's been, historically, the biggest category in fitness. We think that's a foundational product for us. We're going to continue to ramp supply to allow us to market into it so that we're not marketing into huge OTD. So we'll balance that.

---

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

And then just quickly on the demand question. As you can imagine, since the middle of March, we have seen very steady organic demand for our product. Clearly, when we saw the second spike happen in the U.S., and of course, with some of the announcements around the lockdown in the U.K., you do see some spikes, of course, around these types of things. But as you can imagine, in the U.S., obviously, we're continuing to see record cases. And then to slightly add to that perfect storm, we obviously also saw for Bike+ and the price reduction of our Bike, this was all sort of coinciding in time as well.

So I would say demand has never been stronger, and we're very excited. But our -- clearly, our Q2 outlook and our revised outlook for the full fiscal year takes into consideration the trends that we're seeing.

---

**Operator**

Our next question comes from Bernie McTernan of Rosenblatt.

**Bernard Jerome McTernan** - *Rosenblatt Securities Inc., Research Division - VP & Senior Research Analyst*

I was wondering if you could just frame the higher logistic costs. So how much does it normally cost to ship a unit? And how much will it now? And how long do you anticipate the higher logistic costs will last? And then secondly, just on Digital Subscribers, there's a massive growth. And it could be too early to know, but has that historical conversion rate of 10% converting to Connected Fitness held up? And generally, how long does it take for that conversion to happen what it does?

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

Great. I can handle the first one.

I don't know, William, if you want to talk a little bit about the Digital to Connected Fitness conversion and some of the things we're doing there.

But obviously, as you know, Bernie, in our Connected Fitness gross profit margin, we don't break out, obviously, what is shipping cost, what is last mile delivery and what is product cost. Q2 is going to be an anomaly. It is pretty unusual for us to use air shipments for our products. And so this is an anomaly, not something that we necessarily expect to move forward. And so it obviously is multiply-- it's obviously a multiplier of what we would typically cost to ship our bikes in from Taiwan into the U.S.

So it is an anomaly. We don't expect it necessarily moving forward, but we thought it was 100% the right thing to do, to do whatever we could to push these delivery dates in as soon as possible. So given the fact that it's kind of onetime and shipping costs are typically a fairly small percentage of the overall cost to us, so this obviously is moving the needle for us here. But again, it was a cost we thought that was very warranted for what we're dealing with right now.

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

And then on the second point about conversion rates to Connected Fitness from Digital, that's exactly our playbook, which is expand the Peloton entry point with Digital. And that was the premise with the price drop last year and the increased marketing, and it's been working.

As you know, Digital memberships have grown and exceeded our expectation. And so the playbook then is to convert those over time to Connected Fitness users. And the team there, Karina Kogan and our team have been really focused on tactics and strategies against that. And they've been successful.

We measure Connected Fitness upsells. We measure it daily. We measure it weekly, monthly, and those rates have improved steadily through tactics like in-app, finding out what Connected Fitness Product that members -- that digital member is interested in, suggesting a test ride or test run at retail. Just to the point on how we leverage our retail assets and also segmenting based on interest of various Connected Fitness Products, adjusting our contact strategy around activities that we're doing based on the product they're interested in. So a lot of these things, adjusting the app overall and cross-selling certain workout types like Bike Bootcamp.

So we're focused on it. It's one of our top marketing objectives. And yes, they are improving, and we have goals to continue to improve them.

**Operator**

Our next question comes from Lee Horowitz of Evercore ISI.

**Lee Horowitz** - *Evercore ISI Institutional Equities, Research Division - Co-Head of Internet Research*

Two, if I could. One on the supply chain constraints, and you mentioned that Bike+ could last for several quarters now. How, if at all, could these constraints potentially impact the way you're thinking about a time line towards scaling a certified pre-owned program?

And then secondly, maybe a little bit on showrooms. I believe in prior quarters, you had mentioned that Tread would be in showrooms ahead of the holiday quarter, but perhaps not shipped just yet. I guess, one, is that still the case? And two, can you comment at all in terms of what you're seeing in terms of showroom traffic as we've seen COVID cases spike globally? And could that potentially impact in the way you're thinking about the timing around Tread?

---

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

John, do you want to take CPO and then I'll take the Tread?

---

**John Paul Foley** - *Peloton Interactive, Inc. - Co-Founder, Chairman & CEO*

Yes.

I mean the CPO is not a business that we can build without supply, right? It's not -- we can't manufacture certified pre-owned. We needed to get them back from our members. And at this point, the velocity that our members are interested in coughing up bikes is anemic at best.

So to your point, we are going to -- we are 100% focused on scaling the supply chain to create new products, new bikes, both the Bike+ and original Bike, and then both treads, Tread and Tread+, is 100% our focus. And again, I am anxious and excited about the CPO business, but it just isn't there until our members are willing to part with their products.

---

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

And adding to that, obviously, we have very low return rates for our products. And so you can imagine, we're very excited about the idea of further expanding our market opportunity, our demographic reach through a program like this. We just don't have the current supply, and -- but we hope to build it over time.

---

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

And then on the Tread launch and the role of retail, presale, we have announced that we plan to -- I mentioned the role of retail and that it's going to play a big role with Tread, marketing and trial, and that -- it remains the case. And we expect to have something to announce on that very soon. And then in terms of on sale date, we mentioned the U.K. of 12/26, so we're excited about that.

---

**John Paul Foley** - *Peloton Interactive, Inc. - Co-Founder, Chairman & CEO*

And Lee, I don't know [if you recall, we] -- the treads will be in stores by Thanksgiving.

---

**Operator**

Our next question comes from James Hardiman of Wedbush Securities.

---

**James Lloyd Hardiman** - *Wedbush Securities Inc., Research Division - MD of Equity Research*

A couple for me. If I'm doing this math right on the guidance, you're raising the Connected Fitness subscriber number about 9%. Revenue guidance is going up about 18%. What's the delta there? Obviously, there are a lot of moving parts. But I'm curious about mix, just given what you've said so far. Are your mix assumptions changing within the Bike or within the Tread or maybe between the 2?

And then my second question...

---

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

Yes. That -- oh, sorry. Go ahead. No, why don't I go ahead and answer that, and then you can ask your second question? The line's open, we're good.

So it's a very astute observation, but I think what you've heard us say is that Bike+ has certainly exceeded our expectations. And we are continuing to shift as we have done, obviously, since launch when we started witnessing the incredible reception of the product, we started shifting our manufacturing capacity towards Bike+. Our original Bike is $1,895, right? And our -- and Bike+ is $2,495. So there is a fairly big delta there. So that is part of the driver of the increase in revenue.

I would also say the delta is kind of something that's maybe not as obvious, which is as we progress through the year, we've said that our new Tread, right, as well as Tread+, which is already available, is going to come in towards the back end of the year. What we do expect is that a lot of that demand initially for that new Tread may go to our existing Bike owners, who are just chomping at the bit to get the product.

We did see that when we launched Tread+. We saw the overwhelming majority of those initial orders going to the Peloton diehard Bike owners. And so we could see, obviously, the sale of the product, but we might not necessarily create a new sub for that. We call that overlaps. And so that's a little bit of a phenomenon then that starts to create some of the delta between sub growth and revenue. And also keep in mind, churn, right, obviously does also impact subscription growth. So one other layer that sort of helps you bridge the gap between the different growth rates. So what I would call our Connected Fitness, revenue and our subscriber growth.

---

**James Lloyd Hardiman** - *Wedbush Securities Inc., Research Division - MD of Equity Research*

Those are all great points. I really appreciate that. And then as a follow-up here, I'm curious whether or not you think your competitors, if you have competitors, are having some of the same bottlenecks -- bottleneck issues as you. Some of that is, I guess, understanding their supply chain differences. But I guess, ultimately, what I'm going to at here is whether or not you think your potential customers are willing to wait given some of the extended wait times. Obviously, it's tough to track noncustomers, but I don't know if you have any metrics that look at inquiries versus sales or anything like that.

---

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

John, do you want to take the competitor point, and I'll take the trade-off with competitive products on OTD?

---

**John Paul Foley** - *Peloton Interactive, Inc. - Co-Founder, Chairman & CEO*

Yes. Sure.

So yes, James, you're right. It doesn't feel like we have a direct competitor right now. And as we invest aggressively in R&D and in stores and logistics and manufacturing and content and our whole vertically integrated product suite, we expect to continue to outpace and distance ourselves from a would-be competitor.

Our kind of true north, as we've talked about with you personally, James, is the -- if we can improve our products. And we have -- they're more integrated; they're better software, best-of-breed software, we're continuing to hire software engineers as fast as we can; more content choices; the best music in the world. A lot of would-be competitors or people you hear in a handful of people that come up in conversations don't have real music, I would say. They don't have the relationships on the music front that we do. So you're not listening to fantastic pop music or hip-hop or country or whatever you like.

And along with what we have is the biggest and most supportive community in fitness, as you know. And if we can have lower prices over time, we believe that the idea of us having a true competitor is going to be a waning idea, and we're going to be pretty hard to compete with.

But I do know, William, we track some of the different folks and how their order to deliveries are, if you want to give any color.

---

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

Sure. An interesting note is that when we -- ironically, when we extend order to delivery, often what we'll see is we'll see demand go up especially if there's rumors that, that's going to happen. Now we've been going fortunately the other way, as we mentioned, with Bike and shortening OTD. But it -- what we've seen is that people will just wait for a Peloton.

We track our share of Connected Fitness share vis-à-vis other competitors. And what we've seen is we don't think we've leaked demand for people who are impatient on getting a Peloton to some of those other competitors, if you think of them that way. We think people just wait for the Peloton.

And so -- and that's what all our data has shown is that -- and then the OTDs with those other fitness equipment manufacturers. I don't know who you're referencing in particular, but the -- in the ones we look at, you've had one who temporarily stocked out and just stopped selling their bike. And then another -- we think it's sort of 2, another one that we -- has not seen the kind of OTD delays that we have. But -- so that's -- as you might imagine, we track all this.

---

**Operator**

And our last question comes from Deepak Mathivanan of Barclays.

---

**Deepak Mathivanan** - *Barclays Bank PLC, Research Division - Research Analyst*

Great. And Jill, I'm not sure if you addressed this earlier. I was jumping between a couple of calls. But can you provide some color on the device mix that you're seeing in fourth quarter after the Tread relaunch and the new Bike+ that's out there? I know pre-COVID, Tread was about 10%, but now you have new device sales, new device upcoming. So what is the rough mix that you're seeing so far in 4Q?

And then the second question was, with Bike+ now being out there for a few months, are you seeing increased activity on any second sales marketplaces of the typical Bike? Is that something that's happened? I know -- just trying to understand if the $700 is the right Trade-In price point? And any comments there would be helpful.

---

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

Sure. I'll take the first one. And then William, I don't know if you want -- or John, want to take the second one on the secondhand market.

So we -- in terms of mix, here's what I'm going to say about mix because, as you know, we don't disclose the specific mix of our products, whether it be between Bike and Tread or now with the better best within the different portfolios and what assumptions we're making. In fiscal 2021, our original Bike will be our top-selling SKU. We've certainly seen over the last several weeks that Bike+ has been incredibly popular. We are likely to have long OTD for several quarters here.

So we -- obviously, I would say, the mix shift in some of the change in -- the uplift in guidance is the bullishness that we have around that great product. And obviously, at the higher price, it is driving higher revenue. But I think I've said this before, the margin profile between both of those products is pretty similar, so I wouldn't worry too much in terms of modeling than some of the changes to Connected Fitness margin.

We've said that the Tread, which I think we're all incredibly excited about the lower-priced Tread, is -- I mean, we're -- well, first off, just stepping back, of course, we've been selling Tread+ again now since about the middle of the summer in all of our markets and obviously, been incredibly pleased with the performance of Tread+. We know that the lower-priced Tread though will be a game changer for us. And -- but what we said is that we're going to need some time to build up manufacturing capacity.

We said on the last earnings call, we had to prioritize. And we were trying to prioritize our manufacturing capacity in favor of Bike. We obviously had the Bike+ launch coming as well. And so while we think it will be a game-changing product for us, it really will be a fiscal '22 story. So we will start to see towards the back end of the year. Obviously, with the launch of lower-priced Tread, we'll certainly see some volume in '21, but it's really a '22 story. So I wouldn't get too worried about thinking through mix there.

---

**John Paul Foley** - *Peloton Interactive, Inc. - Co-Founder, Chairman & CEO*

And Deepak, I'll take the question on the certified pre-owned or the -- is $700 the right price point. It's an astute observation that $700 might not be the right price point for a trade-in credit. And an intrepid or a hard-working Bike member might be able to sell their Bike on craigslist or eBay and get more than $700. There is absolutely an arbitrage opportunity for someone who wanted to do that. I haven't personally followed and seen if there's been an uptick. I would guess there might be.

The reason why we don't track it or care too much, to be honest, Deepak, is it doesn't matter to us. That person is, whether they give us the Bike and we refurbish it and put it back in the marketplace as a sort of a pre-owned or if they sell it on craigslist or eBay and get $1,500, $2,000 for the product, we are going to get a new subscriber. We're going to have a new relationship with the new owner. And we're just trying to create a turnkey easy path with the $700 trade-in credit. So that when we're delivering your new Bike+, we can take your other one out of your basement or your home gym so that it's easy and seamless. But certainly, if you wanted to work harder, you could do that.

---

**William J. Lynch** - *Peloton Interactive, Inc. - President & Director*

Yes. By the way, Deepak, just -- that's so much -- so true that we actually offer on our website FAQs on how to resell your Bike individually yourself. We think it's great. It's 2 members where there was 1. And so as John said, we're indifferent. And we actually want to help if -- direct the people to resell it if they choose that route.

---

**Operator**

I'm showing no further questions at this time. I'd like to turn the call back over to CEO John Foley for any closing remarks.

---

**John Paul Foley** - *Peloton Interactive, Inc. - Co-Founder, Chairman & CEO*

Thank you much.

Yes. So quickly, before we wrap, I did want to again thank our members for their patience as we work hard to scale our teams, our technologies and our operations to keep up with this massive global demand for our products and experiences. Like we said, we are investing aggressively in our supply chain capacity so that we can add more members on more platforms and without the frustrating long -- frustratingly long order-to-delivery times. So thank you for your patience. You -- please know that we are all over it.

And lastly, another thank you to our Peloton teams across Germany, the U.K., Canada, the U.S. and Taiwan. We are all so proud of your hard work and dedication to our members and our shared mission. We hope to see more of you in 2021. And hopefully, we see more of you in person with COVID-19 well in the rearview mirror by then.

So thanks, everybody. Good night. We look forward to talking with you next quarter.

---

**Operator**

Ladies and gentlemen, this does conclude today's conference. Thanks for participating, and you may all disconnect.

---