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PRESENTATION

Operator

Good day, and thank you for standing by. Welcome to the Peloton Interactive's Second Quarter 2023 Earnings Conference Call. (Operator Instructions) Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your speaker today, Peter Stabler, Head of Investor Relations. Please go ahead.

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

Good morning, and welcome to Peloton's fiscal second quarter conference call. Joining today's call are CEO, Barry McCarthy; and CFO, Liz Coddington.

Our comments and responses to your question 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 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.

I'll now turn the call over to Barry.

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

I want to do something a little bit out of the ordinary just to kick off today's call, if you all indulge me. A good friend of mine named Gail Tifford once best summarized what's special about Peloton, I think, when she described the brand as golden and the member community as platinum. And what makes that possible is the incredible work done by our content team and by the instructors who give it life.

And because of that, and in particular, I want to welcome back to the platform today one of our instructors in London by the name of Leanne Hainsby, who after disclosing her recent battle with cancer and her announcement that she's cancer-free, is today once again back on the platform. And the start of her class just coincidentally happens to coincide with the start of this earnings call. So welcome, Leanne, and thank you for all you do for us.

And with that, we'll turn the call back to the operator and take our first question.

QUESTIONS AND ANSWERS

Operator

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

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

Barry, you wrote about how the new initiatives across rentals and retail partnerships and just changes in the overall go-to-market drove 19% of the CFU volume in the quarter. I was hoping you could talk more about how you think that will progress over the next 12 months. And which of these initiatives do you expect to be most impactful to drive growth going forward?

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

Well, based on last quarter's performance and quarter-to-date, I think FaaS and the pre-owned business will be the most significant on a quarter-over-quarter basis, last quarter to the quarter before. FaaS has doubled by way of example, and it's continuing to grow rapidly this quarter. And a very large percentage, 63%, I think, with a 95% confidence is incremental to the business. They are -- tend to be slightly higher household income who -- but for the fact they don't have to make contractual commitment would not have come on to the platform. Now -- one.

Two, what about third-party retail? It has less incrementality, but we don't have enough data to be confident that we know how much of the revenue is incremental, meaning whether we would have sold that on our own platform but for the fact that we partnered with third parties. It did outperform our expectations in the quarter. But of course, we had no history going into the quarter. So it's difficult for us to know as with FaaS and CPO how exactly to forecast it.

So we continue to be optimistic. We're quite pleased with the performance during the quarter, uncertain about the incrementality, although we are invested in continuing to grow it. And we'll know more as the year progresses.

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

If I could just follow up. I know Leslie is joining as the new CMO. Do you feel like there's strong awareness of the new initiatives and the go-to-market strategy among potential consumers? Or is that going to be a big focus in your advertising and marketing efforts?

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

Well, it's -- awareness is low still, but it's new. Are we going to make it a focus? No, not particularly. I think the focus is going to be anyone, anytime, anywhere. It would be less about bike. It will be about all of the occasions for use and inclusiveness.

Operator

Our next question comes from the line of Justin Post with Bank of America.

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

Can you talk about hardware gross margins in the quarter? What were some of the puts and takes there? What is going to take to get those to breakeven? And when you think about the model, like how much are you willing to lose or take upfront cost to get a subscriber? And do you think the model is working now as you think about your hardware sales-producing subscribers?

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

Liz and I will tag team this. Let me do the high-level stuff and shift back to her on the specifics. So let me say we managed through LTV to CAC. And in making those calculations, we take a holistic view of the revenue stream and the expenses associated with both the hardware and the subscription associated with it. So for my part, I don't particularly care about the hardware margin or particularly about the subscription margin. I care about it on an aggregate basis, and I care about the relationship between the lifetime value of the customer relative to the cost of acquisition. And that's the framework we're using in deciding whether or not the model is working. And in the recent model, I think we were operating at 1.4:1 LTV to CAC, which means that each time we add a new subscriber to the business, we increase the enterprise value because that customer will be net profitable over their life.

Liz Coddington - *Peloton Interactive, Inc. - CFO*

Yes. To just add a little bit more detail to what Barry mentioned, because we did enrich our holiday promotion, that, of course, has an impact on our hardware gross margin. And we did manage to our LTV-to-CAC ratio. So we may have spent more in promotion, but it balanced out and resulted in that 1.4 ratio of LTV to CAC.

I also want to comment that our overall gross margin when we outperform on Connected Fitness, what that means is the lower margin of our hardware becomes a -- it sort of has a higher penetration relative to subscription. And so that will depress the overall margin a bit, but we're happy with that because we get the subscribers and the subscription revenue over time that comes with them.

The other thing, I think, that is worth pointing out here on our gross margin is that this quarter, we did take a number of reserves. We had higher cost -- the cost of revenue were impacted by some excess and obsolescence reserves. So after we got through the holiday period, for example, we looked at our Guide inventory and realized that we had more than we needed and took a reserve against that. We also had some very specific returned inventory that we had on hand that we no longer plan to refurbish and sell. So we took a reserve for that. And then we continue to have some reserves associated with inventory from our Tonic manufacturing facility. So all of those had roughly about a $32 million impact on our Connected Fitness gross margin in the quarter.

I think there was a question about when is our hardware Connected Fitness margin going to turn gross margin positive, and we're not giving any guidance on that timing. But as Barry said, we are continuing to focus on optimizing our LTV to CAC. And if you think about the factor -- some of the levers that go into that, as we mentioned, promotions are part of that. Financing is part of that. Third-party channel strategy is part of that equation. All of those things have created a drag on our gross margin, and those get offset by lower sales and marketing expenses in the form of lower media spending. So you have to look, as Barry said, at the whole thing and not just micro focus on gross margin.

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

One additional comment, and that is to remind everyone that there are clear trade-offs between the rate of growth of the business fueled by the pace of marketing -- sales and marketing spending on the one hand and the impact that spending has on free cash flow. So if we spent more on marketing, we could have grown faster. But it would have come at the expense of free cash flow and our overarching objective, which is to move the business to free cash flow on a sustained basis so we can control our own destiny. So our first priority is to manage the business for free cash flow and then within that framework to manage for growth.

Operator

Our next question comes from the line of Eric Sheridan with Goldman Sachs.

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

Maybe if I could ask a 2-parter. Obviously, there was a lot of demand pull forward through the pandemic, and you went through this sort of normalization dynamic post the pandemic. Are we back on firm ground where you think you understand with the sort of normalized end demand trends are in the category? And therefore, you're now in a mode of sort of executing on leaning in or leaning out with respect to promotion and marketing, and we could be back to some sort of normal seasonal cadence in the business? That's number one.

And number two, maybe following up on Doug's question from earlier. Just can you help us better understand how the mobile app strategy fits broadly into the Connected Fitness goals? Are you still viewing it as a potential feeder product for conversion and the subscriber funnel? Or is there an increasing view that maybe this can operate as sort of a stand-alone strategy for folks who might never come around to the hardware?

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

I'll jump in first and then hand it over to Liz. We outperformed in the quarter. The good news and the bad news is -- the good news is we outperformed. The bad news is our -- the accuracy of our forecasting, our ability to forecast the business and particularly given the many changes we made in the business model is not as highly evolved yet as it will be. Is that because of the changes we made in the model or because there's -- the consumer behavior is different than we have understood it to be historically? I think maybe it's some of both. And the reason I think that is because we've continued to outperform even our updated forecasts in the quarter. And so we don't quite have our handle -- our arms around consumer behavior. So I think the answer to your question is, no, we're not back to normal yet. If there's some new normal that's happening, and I don't feel like we quite grasp what it is, one.

Minor point with respect to seasonality. I should have mentioned in answering Doug's question about FaaS that among the things we're seeing that we didn't expect is that FaaS does not -- has not been exhibiting the seasonal characteristics of the rest of the business. Wasn't -- it didn't spike at all, for instance, during the holidays. It's just continued its march as if holidays didn't happen.

And then lastly, with respect to the app, I think of it as its own endgame. And maybe we'll see the All-Access subscription, hardware business or maybe not, I don't really care. The end goal for that strategy is to expand the TAM by reaching a user base that historically we've not been able to access to do it with our core strength, which is all of the content and the user experience that our instructors give life to and to enable consumers to use that content on competitive hardware and to use it in the home and to use it in the gym and to use it outside, whether it's strength or it's yoga or it's running outside or on a treadmill, whether it's rowing, what have you.

And today, it's a bike, it's a tread, it's a row, it's in your home. But tomorrow, it's all those other things. And the path to the promised land is the app, I think, at least that's how I conceptualized it. And that's the opportunity we're trying to pursue. Liz, do you want to add anything?

Liz Coddington - *Peloton Interactive, Inc. - CFO*

I think you actually explained it quite well, Barry. The only thing that I will add is there was a comment in there in Eric's question about seasonal cadence. And I just want to say that from a modeling perspective, we still expect that our revenue for the year is going to most closely resemble that of fiscal '22.

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

Let me just drive home the point, not to read too much hype into this call. But today, we have as many subs as we're forecasting we're going to have at the end of the quarter. We have seen plenty of churn historically, particularly at the end of the seasonal rush. And so we're forecasting that whatever incremental growth we have, we will get back in the form of churn. We're not forecasting a spike in the churn rate. It's just the math, to be clear. But it could be right, it could be wrong. We're going to find out.

Operator

Our next question comes from the line of Shweta Khajuria with Evercore ISI.

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

I guess I have a quick question on free cash flow. You got to positive free cash flow this quarter, excluding some of the supplier-related costs. How should we think about the magnitude of each of the key drivers of getting to positive free cash flow in fiscal year '24? So specifically, I'm talking about the cost cuts you've made have an impact, supplier contracts you've renegotiated have an impact, but also inventory drawdown has an offsetting impact. So could you help us in terms of what will be driving the trajectory of sustainable positive free cash flow?

Liz Coddington - *Peloton Interactive, Inc. - CFO*

Sure. So Shweta's question is really about like what is going to drive sustainable free cash flow into fiscal 2024. So you mentioned inventory. Inventory will continue to be a tailwind for us in fiscal '24. So that is a benefit. And then it's really all about being very conscious about our OpEx and making sure that we are as efficient as we possibly can be and then measure -- doing that LTV-to-CAC analysis to make sure that we are acquiring subscribers efficiently. And then it's about growth. We have to continue to figure out how to grow the business so that we have enough cash inflow to cover our operating expenses over time, net of the fact that we've already bought a lot of the inventory and have a lot of it on hand already.

So it's really just about operating the business in an efficient way to maintain that positive free cash flow or break-even free cash flow ideally. And yes, the key is really figuring out how to continue to grow the business. And by the way, as we grow the app part of the business, that is a higher gross margin business that is good for us over time as well.

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

Let me jump in and add that -- let's talk about maybe some of the changes in the year ahead compared with the past year in terms of savings. So we saw significant reduction in head count in the past year and savings commensurate with that. Will we see more of that on a go-forward basis? No, we won't. I made it clear in a previous call that as far as that is concerned, we're done with head count reductions, and let me reaffirm that to all of our employees who are listening on the call.

But we have significant opportunities for additional expense reduction in the business, and I expect that we will realize those in the next 1 or 2 years. They're in middle mile. They're in last mile. They're in all of the operating systems we use, ERP, warehouse, order management system, which has resulted in lots of manual processes. We still have a lot of inventory, and we pay a lot of money in storage costs. And as we work down our inventory positions, we have substantial additional savings to be realized by limiting those storage costs just as we have in the past year.

So the only offsets, important to bear in mind, is the trade-off between growth and cash flow and savings. So if we lean back into international growth by way of example, we're going to lose more money. We'll grow faster, and we'll only grow if the LTV to CAC shows net profit over time. But as you add new subscribers, you lose money. It's true with Netflix. It's true with Spotify. It's true with Peloton. And so we just need to figure out what -- artfully what the appropriate balance is.

Operator

Our next question comes from the line of Ron Josey with Citi.

Ronald Victor Josey - *Citigroup Inc., Research Division - MD*

Maybe, Barry, I wanted to follow up on your comments on churn just now and understood there's no real change, and you have maybe a little bit higher churn on seasonality just given the holiday. But do you think this 1.1% churn is, call it, the new normal for maybe full members now that we're in 3 quarters into the price hike and maybe any insights on the churn around FaaS subscribers? I think we added shoes and some benefits to the program this quarter that might have brought churn down for these FaaS subscribers. So any insights there would be helpful on churn.

And then, Liz, I think from a guidance perspective, because we're assuming greater FaaS and 3P distribution sales, and I think it's more FaaS than CPO, talk to us about how that rolls -- flows through the P&L.

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

Let's talk about the overall churn number. Let me talk about FaaS. So FaaS has a higher churn rate than the typical All-Access customer. It's running about 4.5%, 4.7%. That should not alarm you, and here's why. The sub base is still quite young. And over time, if you were to look at individual cohorts, the question that we need to answer for ourselves and for you is what does the shape of the retention curve, the churn curve look like. So -- and as the sub base ages, the average churn rate, which is what the 4.5%, 4.7% represents, will come -- of course, will come down. The question is what's -- where does it turn asymptotic? And at what rate does it turn asymptotic? Is it going to be 1% or is it going to be 3%?

Based on our understanding of consumer behavior to date, we think the payback for FaaS customers who receive a new bike is about 18 months and for customers who receive a used bike is 12 to 14 months, which is as good as we hoped. I thought, worst case, it'd be 2 years, then we need to go back and reengineer the numbers to get to a better outcome. And the best we could possibly hope for would be a 12-month payback. So looks to us, at least initially, like the program is working. And by the way, we're still not doing any kind of credit check verification on the front end to identify customers and shouldn't be doing business with, all of which would contribute to a better lifetime experience. So we're still learning how to operate the program. But at least initially, based on the churn behavior we're seeing so far, and we're only talking about roughly 24,000 FaaS customers in total, I think there's reason to be optimistic about it.

Now it is -- have some negative adverse consequences for cash flow because it's -- from a cash flow perspective, you're not selling hardware up front. So you're not recouping that investment in working capital as quickly, but we are seeing faster growth as a consequence. So I just want to remind everybody, if a program is really successful, growing really fast with attractive paybacks, then we're going to have to also figure out what the financing strategy is going to be for it because it will have different working capital attributes than the core business we currently have. But we should be so lucky to have that challenge. And if we have it, then I'm pretty confident in our ability to figure it out.

Liz, do you want to talk about churn?

Liz Coddington - *Peloton Interactive, Inc. - CFO*

Yes. Sure. I just wanted to add one thing that for the quarter, for Q2, we were actually closer to 28,000 FaaS subscribers at the end of Q2. And it was about double the number that we had in Q1. So really, really great growth, great for FaaS.

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

The CEO doesn't know the numbers. Sorry about that, folks.

Liz Coddington - *Peloton Interactive, Inc. - CFO*

Well -- but let's talk a little bit about churn. So our churn, flat quarter-over-quarter, and we're very pleased with our Connected Fitness potential levels overall. FaaS has a very minimal impact on overall churn at this point. And right now, we don't expect any significant changes to our current churn levels aside from the fact that we do have small seasonal variations from quarter-to-quarter. So that's a little bit about churn.

Ron, I think there was a part of your question that was asking about how like 3P, FaaS and our Peloton refurbish program flow through our P&L, and I can give a little bit of perspective on that. Barry already gave some. So the fact that FaaS is becoming a bigger growth driver for us means that we do get less revenue from a new FaaS member than we do from somebody who buys a Connected Fitness hardware product because they just pay for the $150 delivery fee and then the cost of their membership. That also impacts our gross margin in the month that they become a FaaS member, and we've talked about that before. So that is a near-term drag on margin. It's also a near-term drag on revenue, just as -- but over time, we recoup that.

For 3P, we've talked about that as well that because our third parties do extract a margin from us, there is a little bit of an impact to revenue from them. We also have terms in accruals. We also consider our marketing expense as a contra revenue adjustment for those relationships. So those are a drag on revenue as well and a bit of a drag on gross margin, too.

And then for refurb, because it is a lower price point, obviously, we're getting less revenue from when we sell a refurbished bike. But on a cash margin perspective, it's great because we are getting cash for products that we would have otherwise just had as a return and not been able to do something with. So it's great overall economics. Although from a P&L standpoint, you will see the negative impact from that.

Operator

Our next question comes from the line of Brian Nagel with Oppenheimer.

Brian William Nagel - *Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst*

So maybe a couple of questions, maybe unrelated, I'll shove into one just make it simple. So first off, with regard to the now expanded distribution infrastructure with Amazon and DICK'S, any additional insights there as to how you may further develop that infrastructure?

And then my second question, I know we've talked about FaaS a bit here. But as you look at the initial growth there, are you basically just allowing that growth to be dictated by the market? Or are there governors in place right now that you could adjust over time to drive that growth one way or the other?

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

If you mean drive the growth up or down?

Brian William Nagel - *Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst*

Correct.

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

Well, the answer to that is yes. Let's say that we are concerned about the cash flow, the tax on cash flow would just slow it down. We could hit, let's say, 300 units a day and decide we're not selling any more in a particular day, and we just take it down from the web so that Zoomers can't order any more FaaS bikes in any particular day or week or month or quarter, by way of example.

Secondly, it's ripe for international expansion. The pace at which we decide to go is another lever. A third lever is, why don't we just change the value proposition and we make it more expensive? That has churn implications, of course, which has lifetime value implications and CAC implications. But it's absolutely one of the variables that we factor into the mix in deciding how to modulate growth or we can lower prices and almost certainly grow faster as a consequence.

Liz Coddington - *Peloton Interactive, Inc. - CFO*

Yes. The only thing to add, the first part of the question, I think, was around any insights on developing our infrastructure with Amazon and DICK'S as third parties. I think right now, if you look at these partnerships, it's still very new to us. We've only been roughly a quarter in terms of our relationship with DICK'S. We just went through our first holiday season with our third parties.

And so while our third-party sales, along with the rest of our sales, outperformed our expectations during holiday, we're still learning about those partnerships and figuring out how we want to continue to partner to make it a win for both our business as well as Amazon and DICK'S. Do you want to add anything to that?

Operator

Our next question comes from the line of Youssef Squali with Truist.

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

Two questions for me. First, can you maybe speak to the level of promotional intensity in the quarter and your plans and expectations for the second half? In other words, kind of what does the guide imply in terms of promotional activity?

And two, maybe just a clarification, Liz, on something you said earlier about the seasonality you're seeing this year similar to what you saw in 2022. In 2022, Q4, your fiscal Q4 was the lowest revenue quarter at about 19% of revenue. So I'm assuming that's kind of what you're telegraphing. But what else you'd like us to know about how maybe Q4 will turn out? I know you're not guiding yet, so maybe just directionally.

Liz Coddington - *Peloton Interactive, Inc. - CFO*

So with regard to revenue, that second part of your question, we are not providing guidance on Q4. So I think you can interpret my comment earlier about revenue seasonality how you want, but we're not providing specific guidance on the quarter.

On promotional intensity, and Barry, you can fill in for us anything I miss here, but I think the way that we think about promotional levers, we have to come back to the whole concept of LTV to CAC and that promo is part of one of the key levers in that equation, right? So as we look in the quarter, we are going to make trade-offs between our media spending, our financing offers and also promotion as an opportunity. And especially as we have a lot of inventory right now, it is a lever for us. And so we don't comment too much about promotional strategies. That's for competitive reasons, in part, but we are trying to balance across our inventory reductions, managing margin and cash flow. All of those are important parts about how we think about promotional activity.

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

I would just remind everybody that it's just a form of marketing spending. It just happens to land in a different part of the P&L, one; two, proven to be enormously effective for us; three, the more you do it, the more you erode the brand value proposition. And so you'd do well to use it sparingly. In the years that I've been here, we've had some form of promotional activity in almost every quarter, I think, to varying degrees. It's for Leslie to decide how aggressively or not. She wants to use it as part of the marketing mix on a go-forward basis, so TBD.

Operator

Our next question comes from the line of Edward Yruma with Piper Sandler.

Edward James Yruma - *Piper Sandler & Co., Research Division - MD & Senior Research Analyst*

Barry, in one of your earlier answers, you talked about the puts and takes on the P&L from international growth and just that faster growth would cost more money. I know you cited that restoring international growth as a goal in year 2. Kind of what do you see other than the promotional level that could help do that? And do you expect to enter new countries?

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

Still figuring it out is the long and the short answer. I would like to enter new countries, probably Western Europe first. But I don't know when, and I don't know how much we would spend doing it. And I hope to have the answer to those questions in the next 3 months. But we just don't have it today, long story short.

Operator

Our next question comes from the line of Aneesha Sherman with Bernstein.

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

So 2 questions, please. So the first one is with higher FaaS demand and faster deliveries at the end of the quarter, does that suggest that there should have been some lag subs as in January? And is that already baked into your guide of 3.08 million to 3.09 million for Q3?

And then second, marketing is down even as a percent of sales. I'm curious if you could give us some color on how much of that is temporary as you're -- it sounds like you're holding back marketing on the digital app until you've relaunched it versus structural declines, including a leaner team, lower field expenses and maybe even structurally lower as you broaden your distribution footprint and maybe need less marketing. So any color on that would be helpful.

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

The sales and marketing line item on the P&L is a hodgepodge of a couple of different things, just by way of reminder. So some of it relates purely to marketing spend for the core business. Some of it relates to the commercial and wellness business. And what's the...

Liz Coddington - *Peloton Interactive, Inc. - CFO*

Retail.

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

Thank you. And the last piece is retail. And we've fairly -- we're in the process of dramatically shrinking the loss associated with that component of the business. Now all things being equal, as the subscription revenue grows, sales and marketing expense should shrink pretty dramatically as a percent of revenue. This is all part of a tutorial I gave investors at the Investor Day that Spotify hosted before. It's direct listing, by way of example. And at Netflix, as I recall, sales and marketing expense fell from something like 24% to 14%, even as CAC remained relatively constant just because of the attributes of a well-run subscription business. You only pay to acquire the marginal new sub. You don't pay for the recurring revenue. And the recurring revenue grows as a percentage of the total over time, which is why you see the reduction.

Now the offsets for us will be, let's say, international expansion. Well, our unaided brand awareness in new countries is quite low as you would expect. That means it's -- that CAC will be higher as you roll out your presence in those new markets. And so we're just going to have to balance it from an earnings and a cash flow perspective as we try to nail the growth. But we should be beneficiaries of increased word of mouth as the unaided brand awareness grows, particularly in North America and because of the growth in recurring subscription revenue, offset by growth in new markets and in new product categories that have relatively low growth like the digital app. Because last time I looked, I'm not sure what it is today, it was 4% unaided brand awareness. And the Net Promoter Score was the highest of all of the products we offer, something like in -- I can't remember if it's the low 80s or mid-70s, anyway, enormously high.

So question, how heavily from a marketing perspective where we're going to lean into to that opportunity, and the answer is, as we just walked in the door, give us some time to figure that out.

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

Got it. Really helpful. And on the lag subs from your later deliveries and FaaS demand, any comments on that?

Liz Coddington - *Peloton Interactive, Inc. - CFO*

So over the holidays, we -- this is not a particular impact that is unique to this particular holiday or this particular calendar year. Over the holidays, when we sell a lot of Connected Fitness units over the Black Friday, Cyber Monday, it does take us time to be able to deliver those. And so we generally do have situations where somebody may have ordered a Peloton bike or a tread or a rower, and we -- but they -- we don't actually deliver it to them, and they don't activate their subscription until January. So that's not a unique phenomenon to this year. So it's something that happens every holiday quarter into the -- from quarter 2 into quarter 3.

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

But there is kind of a peak backlog coming into this quarter...

Liz Coddington - *Peloton Interactive, Inc. - CFO*

Yes, relative to other quarters.

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

Relative to the other quarters, yes.

Liz Coddington - *Peloton Interactive, Inc. - CFO*

Yes. But it's not a -- it's contemplated in our guidance, and it is not unique to this year versus other years.

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

By the way, shout out to the -- to all of the folks at Peloton involved in the delivery of Connected Fitness units to consumers' homes because they substantially outperformed our expectations for the quarter. And we're quite grateful to them for the efforts that they exerted on behalf of the business.

Operator

Our next question comes from the line of Kaumil Gajrawala with Credit Suisse.

Kaumil S. Gajrawala - *Crédit Suisse AG, Research Division - MD & Research Analyst*

Can you maybe just talk about -- you've laid out your various initiatives in some detail. Can you maybe just talk about the decisions on Precor and the Ohio facility and if there's any sort of shift in strategy or any impact keeping those assets for a bit longer may have on some of the initiatives you've outlined?

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

Liz will take POP, and I'll take Precor. Let me begin with Precor. When I -- I think it was in my first earnings call with investors, I said, look, strategy is about choice, and our choice is to commit ourselves to Connected Fitness. So if it's not Connected Fitness, we're not doing it. And that begs the question, well, okay, where does Precor fit and why are you doing it? And we had the worst-kept secret in the planet is that we've been exploring the sale of Precor. And we got pretty far down the path. And then the price that the buyer was willing to pay dramatically dropped. And we walked away from the table. I mean, at some point, it crossed the stupid line to the point where you're just not willing to dance anymore, and that happened for us.

Now for all of the time that we have owned it, we've done nothing to invest in the performance of the business to its own detriment. And we've done a reasonable job of kind of running it for our benefit, including sucking some talent out of it into our own hardware business. It was good for us, bad for them.

So we're going to reverse course. I think we understand how to add some incremental value without great expense and have a disproportionate increase in the value of the business. And the overarching strategy would be to run Precor for the benefit of Precor and to not dilute those efforts for the benefit of our own operating business, let that run as a freestanding subsidiary. And so that's the path we're on. And when we see success, we will see a dramatic increase in its market value. And then unless we have a shift in strategy or they have a shift in their product strategy, at some point, we would look to divest.

Liz Coddington - *Peloton Interactive, Inc. - CFO*

So I'll take the question about POP. So we had expected to sell our -- the Peloton Output Park facility in Ohio by the end of calendar year '22. Unfortunately, that process got delayed, but we are hopeful that we will be able to sell it by the end of the fiscal year. And we are confident that we will be able to sell it. It's just -- it's literally just taking us longer. Now end of the fiscal year is not guaranteed, but that is our goal.

Operator

Our last question comes from the line of Lauren Schenk with Morgan Stanley.

Nathaniel Jay Feather - *Morgan Stanley, Research Division - Research Associate*

This is Nathan Feather on for Lauren Schenk. Can you just talk through how the initial demand for the rower spend and where you and Rexon got production and then distribution? And then what portion of demand is coming from new versus existing subscribers?

And then just a follow-up last question, what exactly is causing the delay in selling POP? And how are you getting that fixed?

Liz Coddington - *Peloton Interactive, Inc. - CFO*

Okay. So as far as the demand for the rower, just like our other products, over the holiday season, the rower outperformed our expectations. It is a newer product for us, and awareness outside our Peloton member base, we're still building that quite a bit. So to your point, a larger share of the rower sales did go to existing members. It was roughly as high as 65% over the holiday period.

Now since the holidays, it has moved to be more in line with the percent of existing members that are purchasing our tread product, and that's in Q3. The trend is more in the 40-ish percent range in terms of overlap with existing subs. So that's a little bit about the rower and new versus existing.

On POP, the POP facility is a large facility. It's in Ohio. It's a great facility for the right use case for it, but we just have to find the right buyer for that facility. And so we're taking the time to be able to do that.

Operator

And I'm currently showing no further questions at this time, I'm sorry. I would like to turn the call back over to Peter Stabler for closing remarks.

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

Thank you, everyone, for joining us today. We'll talk to you next quarter. Have a good day.

Operator

This concludes today's conference call. Thank you for your participation. You may now disconnect.
