THE DEVIL'S ADVOCATE REPORT

September 2, 2020

Peloton Interactive, Inc.

(SELL)

Price:	$91.50	**Ticker:**	PTON
52-Week Range:	$17.70-$92.50	**Dividend:**	Zero
Shares Outstanding:	283.2 million	**Yield:**	Zero
Market Capitalization:	$25.9 billion		

Data As of September 2, 2020

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Investment Thesis

Peloton Interactive, Inc. (PTON), with a $26 billion market capitalization, is a relatively young company (founded 2012) that has been one of the main beneficiaries of the COVID-19-related lockdown. The company offers a very popular product (mainly its spin bike) and also generates substantial recurring revenue from its subscription-based model. Even so, since revenues for the yet-to-be-announced fourth quarter of fiscal 2020 are expected to increase 160% over last year, based on Wall Street's consensus forecasts, it appears a substantial amount of demand has been pulled forward by the pandemic. Gyms across the nation have been forced to close and many members are too afraid to use the few gyms that have reopened or never closed. Therefore, many gym members and individuals seeking to stay active have purchased a Peloton bike and added the required $39 per month subscription service, which gives them access to a vast library of live and on-demand classes.

Fueled by the strong revenue growth, Peloton's shares have advanced approximately 330% since the March lows and now trade at 17x book value and 12x run-rate revenues. On a GAAP earnings and free cash-basis, the company loses well over $100 million per year. Of course, this is to be expected from a company that was founded just 8 years ago and which is expanding rapidly. That said, because its main product is expensive, starting at $2,245 plus the monthly subscription fee, there is only a small percentage of consumers who would be interested in, and who have the means to, purchase a Peloton spin bike. And a lot of those individuals have done just that in the past six months, as a result of the COVID-19 related lockdowns, gym closures and forced working-from-home situation. Consequently, should the pandemic end today, to the degree than no one is afraid to go to a gym or ride a bike outdoors, it is likely that Peloton growth would stagnate, if not turn negative.

While some have compared Peloton to Netflix, and assumed that the market is large and that there is substantial international potential, it is important to keep in mind that Netflix charges much lower rates in certain countries than it does in the US. For example, it charges $5.38 per month in Mexico and just $2.78 in Turkey[1]. Given the price of a Peloton bike, it is a product for a small segment of the global market – mainly in the US. This is tacitly acknowledged in the company's own projections, according to which management estimates that Peloton's serviceable addressable market (SAM) is 16 million households, 14 million of which are estimated to be in the US. Currently, it has just around 1.0 million households.

Even assuming that Peloton is successful in penetrating 100% of its SAM, then the company would generate approximately $36 billion from bike sales. The problem remains that the profit margin that has thus far been negative on the bikes. Instead, it is the subscription revenues that have the potential to scale better. Once every prospective customer has purchased their bikes, Peloton would only collect the $39 per month, which equates to $7.5 billion per year for the 16 million subscribers. Salesforce.com is trading at 11.9x its

[1] https://netflixjunkie.com/netflix-cheap-expensive-price-comparison-country-2020/

consensus 2021 revenues (even though it usually reports GAAP losses), so assuming Peloton would trade at such a multiple, the company would be worth $89 billion Assuming no dilution, that represents a 243% return from current levels, and if it happens within five years, Peloton's shares would return approximately 28% per year, on average. In reality, the stock market would realize that Peloton has largely saturated the market towards the end of that period and the multiple would narrow dramatically. For example, if the $7.5 billion of subscription revenues are valued at just 4x by 2025, the company's market value would be $30 billion, which represents just a 15% return over the period, or 2.9% annualized. Again, that assumes the company will penetrate 100% of its SAM. There are approximately 60 million gym members in the US and assuming there are two gym members per household, there are 30 million households with gym memberships, so if Peloton penetrates 100% of its SAM, approximately half the gym members in the country would have a Peloton bike at home. More likely, it will only get to a 20-25% market share as prospective customers will chose competing alternatives and some will be content with gyms and spin studios.

Competition is also intensifying. Some competitors, such as Echelon's connected spin bike (priced at $850 with a $20 per month subscription fee) on the low end and SoulCycle's $2,500 ($40 monthly subscription fee) spin bike on the high end, are probably selling well also. SoulCycle's customer base is used to paying $30-$50 per workout in the company's studios, so that brand's awareness is high among the most desirable demographics (well-off spin enthusiasts). Even more serious competition comes from the new and rapidly improving indoor bike riding software such as Zwift, Sufferfest, Rouvy and Fulgaz, which turn indoor bike riding into a video game-like experience. The new indoor trainers that work with this software support realistic road-feel, climbing at an angle, steering and rocking the bike side to side, much like one can do with a road bike outdoors. Consequently, existing and prospective Peloton members might join that hardware-software ecosystem instead.

The stay-at-home-trade theme in which Peloton is included has received a considerable boost in the past few months as investors appear to take for granted that the behavioral changes experienced by consumers since the COVID-19 outbreak are more permanent than temporary. That potential fallacy is also what has boosted Peloton's share price to the point at which it trades at approximately 60x the amount of recurring revenues it is expected to have generated in FY2020 (ended June 30, 2020). That could be considered a relevant metric, since the company does not earn an operating profit on the hardware (bikes and treadmills). If the sales generated in 2020 are largely sales that would otherwise (in a pandemic-free world) have occurred in 2021 or 2022, there will be considerably lower growth in those years, and from a considerably higher base. Consequently, if the pandemic is largely over a year from now, whether because of a successful vaccine or because herd immunity has largely stopped the spread, Peloton's revenue growth would stall, as has been the case with companies such as GoPro, Fitbit and Nautilus. If so, the shares could trade at approximately 1.0x sales, as those companies do, rather than the current 12x sales. Since the downside appears to be substantial, as the company seem to be priced for perfection, shares of Peloton Interactive are recommended for sale or short-sale.

Company Overview

Background

Peloton was founded by John Foley in 2012. He noted that spin classes in New York City often tended to sell out, had to be scheduled far in advance, and were expensive, and therefore, he set out to develop a service that would improve on these shortcomings. It was believed that the experience would be best if Peloton became as vertically integrated as possible, and so the company built teams that span software development, product design, fitness instruction, content production, marketing, music, logistics, retail, and apparel. At scale Mr. Foley believed he could pay for the best instructors, music, and continually improve the quality of experience. He also gave the instructors stock in the company as added incentive. The company's spin bike was introduced in 2014 and its treadmill in 2018. Peloton came public on September 26, 2019 and closed at a price of $25.76 on its first day.

Operations

Peloton Interactive is the largest interactive fitness platform in the world, with a community of over two million members using its bikes, treadmills or just the stand-alone app. The company has grown rapidly, from having 108,000 connected subscribers at the end of FY2017 to an expected 1.05 million connected subscribers at the end of fiscal 2020 (ended June 30, 2020)[2]. Revenues have increased similarly, from $219 million in FY2017 to an expected $1.8 billion in FY2020, based on the average Wall Street estimate. In addition to its interactive services, Peloton also had 74 showrooms, at the time of its IPO, with sales specialists, a high-touch delivery service, and member support teams.

Peloton's spin bike and connected subscription service is no doubt an innovative way to offer consumers quality workouts and it and has, to a degree, disrupted gyms and spin-studios, since it offers a service that is considerably more convenient and time-saving. During the Covid-19 pandemic, the last place many fitness enthusiasts want to be is in a crowded, sweaty spin room, so Peloton offer consumers a chance to recreate this experience at home, which has proven to be a strong value proposition, given the prevailing circumstances at least.

Peloton's spin bike comes with a 22" LCD screen on which live, or on-demand workouts are shown, in addition to statistics about the workout, such as a user's heart rate, resistance level, power output and cadence. Such metrics are sometimes targeted during the workouts; that is, the instructor tells the class to stay within a certain heart rate range or cadence range. Peloton also offers a treadmill known as Peloton Tread, which has a 32" LCD screen:

[2] A Connected subscriber (bike or treadmill owner) is different from the members discussed in the prior paragraph since a member is defined as anyone with a Peloton account, such as users of the stand-alone app.

Peloton's spin bike

Peloton Tread

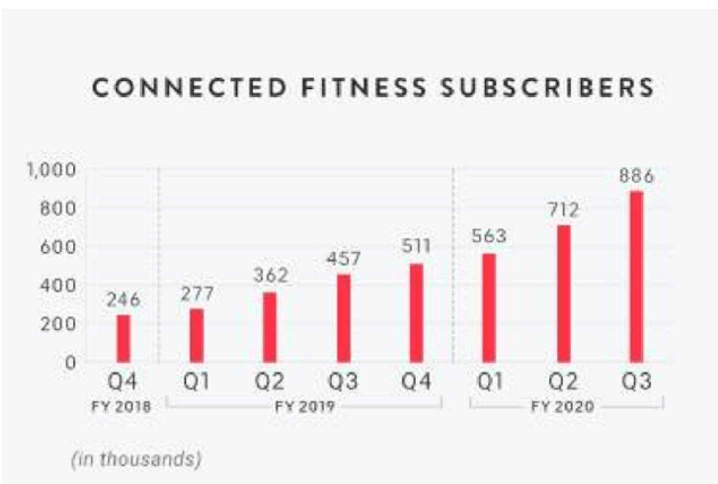
These products retail for $2,245 and $4,295 for the spin bike and treadmill, respectively. Peloton offers to finance these products interest free, in which case users would pay $58 or $111 per month for 39 months, respectively. However, that only provides the hardware. To get the full use of it, customers must use the $39 per month subscription service. Without that, the large LCD screens are practically useless. Subscriptions are, in fact, required, with the purchase of a bike. Cycling, yoga, stretching, boot-camp cardio and strength workouts are all available on the app, as both live or previously recorded classes in their library. There is an extensive library of over 12,000 pre-recorded workouts to choose from and these can be accessed on any iOS or Android device, Apple TV, Fire TV, Roku TVs, and Chromecast and Android TV, in addition to the Peloton spin bike and treadmill LEDs.

In addition to these products and services, Peloton also offers a stand-alone app for $13 per month, for users who do not have a Peloton spin bike or treadmill. Users of that app can still stream classes, although they have to do the workouts on their own (or on their gym's) equipment. Such a user, particularly in the case of the spin bike, will not get access to the data provided by the Peloton bike, such as cadence or resistance (although they might get heart rate and power output depending on which spin bike they use), nor will their workout statistics show up on the Peloton leaderboard. When performed on a Peloton bike, the right-hand panel is devoted to a leaderboard in which users who are taking the class (or have taken it, if the workout is from the archive, i.e. not live) are ranked. Not only can a user compare their data to other Peloton members taking the same class, but users are also compared to their own personal records during each workout, for extra motivation. Users of the stand-alone app do not get that functionality, since Peloton cannot receive the required data from non-Peloton bikes and treadmills.

Because of the pandemic, Peloton announced in March that it will temporarily suspend the delivery of its treadmills, as delivering them to customers' homes poses a risk of spreading infection of the coronavirus, according to the company. These concerns do not apply to the spin bike, which requires less assembly and is lighter and smaller. Since then, treadmill sales have been resumed, at a limited capacity.

Because of the spike in demand due to the lockdown, Peloton has more than doubled its production and plans to open a new factory in Taiwan by December 2020 to keep up with demand. Traditionally, the holiday season is the strongest quarter, although that might change this year if COVID-19-related fears of going to the gym fade. Naturally, the rapid increase in demand since March was a surprise to Peloton's management and posed a challenge for the company to keep up. One of the measures Peloton took was to stop its media marketing, since it simply could not fulfil the demand.

One year ago Peloton had 511,000 connected fitness subscribers and now the company is expected to announce that it had 1.05 million subscribers at June 30th, which would represent 105% year-over-year growth:



Source: Peloton Q3 2020 8-K filing

Each of those subscribers generates on average of around $1,176 in revenues for Peloton per year ($98 per month), assuming they finance the bike over 39 months, which the company offers, and pay the monthly subscription fees. Peloton members completed over 58 million workouts on the company's platform in fiscal 2019 which, given approximately one million active Peloton members on average, indicates approximately 58 workouts per year, per member, which shows that unlike some gym equipment that consumers buy after watching infomercials, Peloton's equipment is actually being used. In fact, in its third quarter earnings release, Peloton announced that the average number of workouts per member has now increased to 17.7 per month, which was an increase from 13.9 workouts per month in the same period last year.

Peloton's hardware, which is to say the bikes and treadmills, accounted for 80.1% of the total revenues in the most recent quarter, which was a slight decline compared to 82.6% in the same period last year. Subscription revenues increased from 16.1% to 18.7% of total revenues in the same period. It should be noted that almost all of the subscription revenues are derived from subscription fees paid by owners of the Peloton bike and treadmill, since the digital-only subscription revenue (i.e., the stand-alone app) accounted for just 1% of total revenue.

Peloton does not break out how many spin bikes and treadmills it sells; it just provides a total number of Connected Fitness Subscribers who either have bought a bike or a treadmill. Realistically, the vast majority of those are probably spin bike users, rather than treadmill users, since the spin bike was introduced in 2014, while the treadmill was only introduced in 2018, plus the fact that no treadmills have been sold in the past six month, as previously discussed. The company has stated that as of March 31st, approximately 3% of its Connected Fitness Subscribers owned both the Peloton treadmill and the Peloton spin bike. Such customers only have to pay one $39 subscription fee even though they own two products. Assuming that only owners of the Peloton bike have bought the Peloton treadmill, and that there were 886,000 Connected Fitness subscribers as of March 31st, perhaps there were around 26,000 treadmills sold and 860,000 spin bikes sold, as of that date. Since then, the company probably sold close to 200,000 additional spin bikes in the soon-to-be-announced fourth quarter of fiscal 2020, and few, if any, treadmills.

As of March 31st, Peloton had more than 2.6 million members, out of which 886,000 were Connected Fitness subscribers (owners of a Peloton spin bike and/or treadmill). The difference between these two figures is that a member is defined as anyone with a Peloton account and each Peloton bike/treadmill owner can have multiple accounts. The number of Connected Fitness subscribers increased 94% compared to March 31, 2019 and the retention rate of such subscribers was 93% over the 12-month period. In the third quarter of FY2020 (ended March 31st) the company had a monthly churn rate of only 0.46%, which perhaps was kept unusually low because of the ongoing pandemic and ensuing gym closures, which essentially forced consumers to find ways to work out from home. A low churn rate is to be expected, since the spin bike costs $2,245 and its large LED screen is useless without a subscription, in which case a Peloton bike is essentially the same as one would get from a $900 Schwinn or Bowflex spin bike. Thus, consumers who purchase a Peloton bike probably remain subscription customers for several years. At least, that has been the case until now, but it is possible that the pandemic attracted customers with a slightly different mindset, perhaps with a shorter time horizon, but that is yet to be determined. It is noteworthy that 95% of Connected Fitness Subscribers are on month-to-month payment plan. Therefore, there is a risk of customers cancelling their membership (perhaps for the summer months, or permanently, and switching to cheaper options, particularly as gyms begin to reopen).

Peloton's quarterly revenues for the past two years are depicted below:

Source: Peloton Q3 2020 8-K filing

As the chart indicates, revenue growth in the third quarter of fiscal 2020 was 12.5% compared to the immediately preceding quarter, which is actually lower than the 20% growth in the same period in fiscal 2019. Also, in 2019 revenue actually declined 30% sequentially in the fourth quarter while this year Peloton is expected to deliver 5% sequential growth, even though the company will not generate any revenues from its treadmill product (since that factory was shut down throughout the quarter). That said, Wall Street's consensus revenue estimates for the June quarter is $575 million, which would be a sequential increase of $50 million. There is a wide range of estimates, with the highest being $723 million, which, if it materializes, would represent growth of 224% compared to the same period last year.

Given the consumer behavior in time of this pandemic, it is not impossible that Peloton will reach $700 million of revenues in the soon-to-be-reported fourth quarter of fiscal 2020. Anecdotally, a company known as Echelon sells a similar-looking spin bike in a price range of $800 - $1,200 and the president of that company recently stated:

"At Walmart alone, the company went from selling 80 units ***a week*** to 160 ***a day*** during COVID-19". That equates to unit sales around 14x as high during COVID vs. pre-COVID. While certain trading algorithms might price shares of companies with these kind of growth rates as if they are sustainable, they really are not, and when the growth rates inevitably moderates, so too will the valuation multiples.

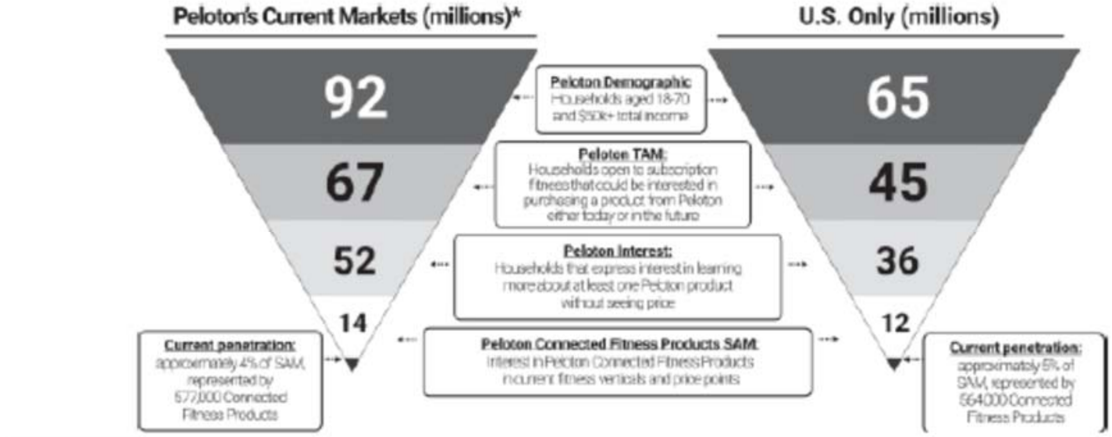
On the cost side, half of Peloton's current revenues is spent on marketing and SG&A expense. Peloton has stopped its marketing activities in mid-March because demand was outpacing supply, which should result in a meaningful decrease in marketing expense for the fourth quarter of fiscal 2020. However, as experienced in the fiscal third quarter, SG&A expenses surged, driven by supply chain challenges. In fact, despite a 66% increase in revenues, Peloton generates a higher net loss in the third quarter 2020 ($55.6 million) compared to the same period in the prior year ($38.6 million). Wall Street's consensus indicates an expectation of $575 million in revenues, which would represent a year-over-year growth rate of 157% and $0.09 per share in earnings, which would be the first quarter of profitability. Whether that will materialize might depend on whether savings on marketing expenses will be greater than increases in G&A. For the full year fiscal 2021, which started on July 1st, Wall Street expects a loss of $0.26 per share, so the profitability expectation is temporary.

Over time, Peloton might introduce a more affordable treadmill as well as a rowing machine, based on comments from management. The market for treadmills is highly competitive, with brands such as Life Fitness, Precor, NordicTrack (owned by Icon Health) and Nautilus dominating, and those companies are already introducing more interactive treadmills with large screens to compete with Peloton. Also, the market for rowing machines is most likely considerably smaller than that for spin bikes, given how infrequently the rowing machines in gyms tend to be used and the almost complete absence of group row workouts in most gyms. Consequently, the spin bike will most likely contribute the vast majority of Peloton's subscriber base for the foreseeable future.

It is possible, though, that Peloton might enter the interactive home gym market at some point, since it would be synergistic to some of the workouts it offers on its app, such as strength training, yoga and stretching. Lululemon recently acquired a home gym company known as Mirror, which is essentially a large LCD screen, on the wall, in the shape of a mirror (or a TV hanging sideways), on which instructors provide live and on-demand instructions, such as cardio, boxing and strength training. There is a similar company known as Tonal, which could be an acquisition target of Peloton's now when it has been provided a cheap currency (its stock) with which to transact, or it might develop a similar product internally. Still, the economics of such products are unproven and Lululemon paid just $500 million for Mirror, which is a market leader in this emerging area.

Addressable Market

One of the most important questions is how large the addressable market is for Peloton. In its S-1 filing, the company showed the following picture:



* Represents our total addressable market within our current and announced markets—the United States, the United Kingdom, Canada, and Germany.

At the time of the IPO, the company estimated that it had reached a penetration rate of just 4% of its Serviceable Addressable Market (SAM) of around 14 million. That SAM has most likely been expanded due to the pandemic. During March and April, 1.1 million consumers took Peloton up on its one-time, pandemic-related, "90-days for free" offer for its stand-alone app. This increased Peloton's brand recognition through word-of-mouth, and it probably converted some of those users into Connected Fitness subscribers, that is, buyers of the $2,245 spin bike and related $39 per month subscription service. In either case, it was opportunistic marketing by the company and it probably contributed to an expansion of its SAM.

It could be argued that the longer the lockdown continues, the greater chance Peloton has to attract and retain customers, permanently altering their behavior. On the other hand, some new customers probably view their Peloton purchase as a temporary investment in their health, perhaps over a year or two, until it is safe to go back to the gym or spin-studio, as there are compensating factors that attract people to those venues even though it takes longer and is less convenient. Ultimately, the SAM and TAM have probably not changed dramatically. COVID-19 accelerated secular trends, but it is doubtful that the market will be dramatically larger in 10 years than it would have been without the pandemic.

Also, unlike products such as the Apple iPhone, Peloton cannot count on repeat purchases of its hardware every couple of years. Therefore, once the market is saturated with Peloton's treadmill and spin bike – which really has not changed to the degree that anyone would notice since it was introduced six years ago – the streaming service will become the company's main product, but it remains to be seen if that will be enough to fend off competitors and justify its valuation.

If Peloton ultimately reaches a 20% penetration rate of its SAM, and assuming the SAM itself increases by around 4% per year, Peloton would get to around 3.4 million Connected

Subscribers within five years, which is around 167% higher than the recent figure. Thus, if it takes five year to reach the 3.4 million Connected Fitness Subscriber mark, that represents 26% per year for the next five years. However, subsequent to that period, growth would decline to reflect the annual increases in SAM, of just around 4% per year. At that point, the market would be saturated, with only a small percentage of existing customers buying a new bike each year, so most of them will simply pay the $468 annual subscription fee. If so, there will come a point in the near future at which revenues will peak as the number of new bikes sold will peak. Subsequent to that, revenues will decline, but profit margins should begin to widen, since the subscription revenues should be higher-margin than the spin bike margins.

Post-Pandemic Consumer Behavior Uncertain

The current environment is a tailwind to Peloton as people are choosing to avoid gyms amid the pandemic. Because of that, monthly net churn is expected to be under 1% even as subscriber growth accelerates. Peloton's CEO stated in the most recent earnings call:

> "We believe that a component of the COVID effect on our business is undeniably temporary, as gyms open and their capacity increases over the next 12 to 18 months, demand for our products will likely decline from the current elevated levels."

While some individuals purchase a Peloton bike as a replacement for a gym (or spin club) membership, a Peloton bike does not have to replace the gym. For more affluent households that can afford a Peloton bike and related subscription fees, it can also be used as a complement to the gym. The Peloton bike offers a workout that is time-optimized, since it requires no drive to the gym, check-ins and busy locker rooms, and it is available any time of the day.

On the other hand, going to the gym is part of many people's routines and some individuals prefer working out in a different place from where they live, as they desire a change of pace, much like going to the office to work, or running outside. The vast majority of gym-goers probably prefer to lift weights, use a treadmill, elliptical machine, take classes, etc., and do not specifically go to the gym for the purposes of spinning, so a Peloton spin bike does not replace the gym membership for most people. Furthermore, humans are naturally social creatures and may have friendships, training partners or value physically meeting other people at the gym. In fact, most surveys suggest that while some people remain hesitant to return to the gym today, that hesitancy will fade within the next few months or once a vaccine has become available and/or the spread of the virus continues to moderate. A survey by Morning Consult found that 70% of fitness enthusiasts miss going to the gym, while a TruePublic survey found that once a vaccine is ready, most gym goers will feel comfortable going back to the gym. When they do, the Peloton value proposition could return to what it was before Covid-19. Still, consumers who have spent the $2,245 on a Peloton bike will likely keep their subscription to the live and on-demand classes for a while in order to feel that they got value out of the bike, or they might attempt to sell the bike. Obviously, if enough consumers try to sell their Peloton bike, that would negatively impact the sale of new bikes.

Another factor to consider is that people might seek to reduce their screen time once they feel comfortable doing so. Because of the pandemic, fitness enthusiasts in Peloton's targeted socio-economic market segment most likely work from home, using a computer, having meetings on a service such as Zoom and talking to friends and family using apps such as FaceTime or Skype. While they might be receptive to use another screen (Peloton) to do a workout, at some stage actual human interactions might be desired once again, as too much screen time can have negative consequences. As far as children with developing brains are concerned, too much screen time is a well-known problem, but much of that applies to adults as well. Some research indicates that adults might experience gray matter atrophy, diminished white matter, impaired dopamine function, damaged relationships, obesity, and sleep disruption, when spending too much time in front of a screen[3].

Competition

Peloton is a leader in its field, but there are many alternatives for consumers who are looking for a good workout. To the extent that they are allowed to open, spin enthusiasts can take live in-studio spin classes at Orangetheory (8 classes for $99), SoulCycle (around $30-$50 *per class*) as well as gyms such as Equinox ($125+/month). These companies have spin studios all over the US, but, because of the pandemic, Orangetheory is exploring live, online workouts at home, or a business model more akin to Peloton's, even though that might cannibalize their in-person services.

SoulCycle has taken it a step further and is offering a spin bike known as the Variis for $2,500 that is virtually indistinguishable from a Peloton bike. This is accompanied by a $40 monthly subscription fee[4], which allows users to access live and on-demand classes in a manner very similar to Peloton. Thus, SoulCycle has essentially marked itself as a Peloton alternative that is directly competing in price and features, and it has the brand recognition among the cycling enthusiasts that are used to spend $30-$50 for a single workout. Hence, this is the coveted demographic that Peloton is trying to target and, as such, SoulCycle represents a serious competitor if it can meet demand. Right now, the bike can be delivered in 3-5 weeks, which is similar to Peloton's delivery time. Online reviews appear to give a slight edge to the SoulCycle bike when compared to the Peloton.

The most affordable Peloton alternative is the Echelon Connect bike (depicted on page 8), which starts at $840 with a $20 per month subscription fee. As discussed previously, sales of that bike have surged 14-fold, based on Walmart sales, since pre-COVID-19.

[3] https://www.medicalalert.com/too-much-screen-time-is-bad-for-kids-and-adults/

[4] Equinox members do not have to pay the monthly fee

NordicTrack's Studio Cycle line has a starting price point of $1,599, which includes access to a live, on-screen training experience and a variety of workout options. The price compares favorably to Peloton's $2,245. Similarly, The Bowflex C6 bike can connect owners with a handful of interactive workout apps at a lower price point ($999), as can ProForm's equipment, ranging from ellipticals, rowing machines and treadmills. In fact, much of ProForm's equipment is free to purchase for consumers willing to make a 3-year subscription commitment to its fitness app for $39 per month in what can be described as an innovative spin on packaging, pricing, and positioning of the company's hardware. Consequently, while Peloton was the first company to market with a connected spin bike for the home, there are now many alternatives.

For consumers who do not want to buy the bike, Peloton offers a Digital Only memberships for $13 per month. This product is separate from Peloton's connected devices and offers access to its live classes as well as its vast library of on-demand spin workouts, run workouts, yoga, stretch and strength classes. However, this market segment is getting crowded as well. The present competition includes the following:

	Cost per month	Free Trial	Availability
Daily Burn	$19	30 days	iOS, Android, Apple TV, Roku, Amazon Fire TV, web browser
Peloton App	$13	30 days	iOS, Android, Chromecast, Amazon Fire TV, Apple TV, web browser
CorePower On Demand	$19	7 days	iOS, Android, Apple TV, Roku, Amazon Fire TV, Chromecast, web browser
Glo	$18	15 days	iOS, Apple TV, web browser, Chromecast (coming soon)
Aaptiv	$15	7 days with an annual $99 membership	iOS and Android
Barre3	$29	15 days	iOS, Android, Apple TV, Chromecast, web browser
Crunch Live	$10	10 days	iOS, Android, Apple TV, Roku, Amazon Fire TV, web browser
TA Online Studio	$90	Two weeks	Web browser

These services offer similar workout choices, with the exception of Aaptiv, which offers audio-only workouts. In addition to these, Apple is expected to offer a similar app with live and on-demand classes, available through a monthly subscription[5]. The classes would stream on Apple products including iPhones, iPads, and Apple TVs. Consequently, this could prove problematic for Peloton, or at least its stand-alone app, simply because there are over one billion active iOS users and most treadmills and exercise bikes found in gyms include a means of attaching a phone or tablet, which enable gym-goers to take interactive trainer-led workouts.

While Peloton is the market leader now in its niche, long-term, the industry could evolve in different directions. There could be augmented reality (AR) and virtual reality (VR) workout options, and it cannot be certain that Peloton will maintain its leadership position in such a case. New technologies, such as special workout headsets or goggles, could be required, or completely different screens. Consequently, Peloton could be disrupted and, given how fast technologies are developing, it is almost a certainty that in-home cycling will look completely different five years from now.

The Next Generation – Smart Trainers and Zwift?

While Peloton has recreated the spin class in a home environment, it has only attracted a fraction of the larger recreational cyclist community. Some cyclists note that the Peloton bike records and shows readings for cadence, resistance and power on its large screen, but the power data is a calculation based on cadence and resistance, so not as true a reading as one would get from a dedicated power meter such as a hub or crank on a road bike. Also, gears do not exist on a spin bike; instead, a knob between the handlebars can be twisted to gradually adjust the resistance. The cycling workouts themselves resemble traditional spin classes, which means a considerable amount of the workout is spent out of the saddle. While this is certainly taxing and will develop core strength, some of the demands of outdoor riding are neglected. These are shortcomings that have made cyclists likely to choose alternatives to spin bikes for their indoor riding.

In the last few years, there has been a lot of development in the area of indoor bike trainers, dedicated indoor bikes, as well as indoor bike riding software, such as Zwift, Fulgaz, Rouvy and Sufferfest. A company known as Wahoo is offering the smart bike trainer pictured below:

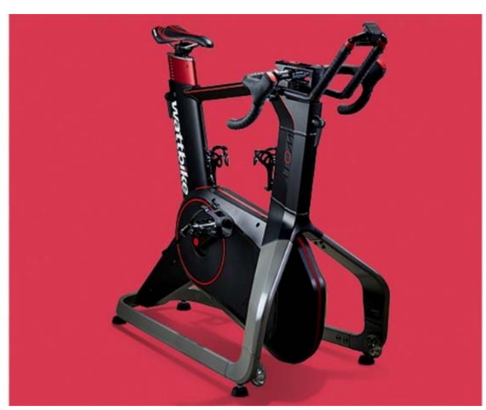
[5] According to Bloomberg

The trainer allows users to bike on their own bikes (after removing the wheels) and the unit in the rear simulates resistance while the unit in front simulates uphill/downhill elevation, while the software (in this case, Zwift) is sending instructions to Wahoo to control the resistance and vertical slope to fit the virtual course one is riding, in a video game-like manner.

Wahoo also offers a complete bike, known as the KICKR Bike, which works in the same fashion but is preferred by some users, since it does not require a preexisting bike. The KICKR Bike is priced at $3,499 whereas the KICKR smart trainer is $1,199. The climb functionality (grade simulator) is another $599.

Garmin, through its recent purchase of a company known as TACX, is offering similar smart trainers and a similar stationary bike (below, left) that retails for $3,199:

Yet another competitor is the Wattbike Atom, which is priced at $2,599:



While Peloton's appeal could be said to be mainly for people who just like spin classes and want to stay active, Wahoo, TACX and Wattbike tend to attract more serious cyclists, who are perhaps part of a cycling or triathlon club, or who like to also ride outdoors. These three bikes have real gears and accurate power meters, which makes indoor riding more realistic, like outdoor riding, and development continues in this area with steering capabilities (above) being the most recent offering.

In addition, the $1,100-$1,400 TACX Neo and Neo 2 smart trainer can simulate the road-feel of riding a bike on gravel, dirt-road or a boardwalk, so that if a virtual ride on Zwift incorporates such riding on a course, the cyclist will have a more realistic experience. Similarly, Wahoo has developed a technology known as "AXIS feet", which lets cyclists experience a more realistic training setup by providing up to 5 degrees of side-to-side movement, which simulates the rocking of the bike when standing up while climbing a hill.

Consequently, many indoor bike riders probably start out riding on a Peloton bike but if they become more serious, and perhaps start riding outside as well, they might 'graduate' to one of these, more serious bikes, or smart trainers, and start using software such as Zwift, which has revolutionized indoor bike riding in the past five years.

Developed by video gamers, Zwift is an online platform where cyclists train in nine different virtual worlds. Some are familiar, such as New York's Central Park as well as a number of courses throughout London and the French countryside, but there are also completely fictitious worlds such as Watopia. While Zwift is a private company and information is not readily available, it surpassed one million users two years ago. The number of daily uses has doubled during the pandemic, and it recently set a record of approximately 35,000 concurrent users (i.e., users who are riding in their virtual worlds at the same time).

To use Zwift, cyclists need a bike (road bike, mountain bike, triathlon bike, so pretty much any bike), a screen (TV, tablet, phone), the Zwift app and a smart trainer (which will transmit data to the platform). Smart trainers start at around $500 and go up to around $1,500. The app costs $15 per month, relative to Peloton's $13 per month for its app and $39 monthly subscription fee for customers with the bike or treadmill.

Zwift is already global in its reach, since users just need the app and no customized programming is required. This software is very addictive, much like a video game, as users advance through 50 levels and unlock new worlds and courses and new virtual bikes, gear and clothes for use inside the game. In addition, it is easy to arrange group rides on Zwift, where users can log on from anywhere in the world and join a workout, or one can just meet up with other individuals and ride together on the same course. There are also structured training programs with various intensities that are based on each user's own fitness level.

Thus, for more serious cyclists who want to train in a certain heart rate zone or at a certain power output, while being entertained at the same time by essentially riding in a video game, Zwift is a very strong competitor to Peloton. In contrast, when riding a Peloton bike, users try to follow the enthusiastic guidance of the instructor, but each instructor has their own format for the workout, so it is more difficult for Peloton users to get the kind of workout they want, whereas that is much easier on Zwift. Zwift also has a companion app that lets users communicate with each other and the leaders on group rides, whereas on Peloton, users can chat with each other, but only on live classes (naturally, not on the thousands of stored classes, which perhaps is what most users access).

(Picture of a Zwift workout, with a substantial amount of data provided to the rider)

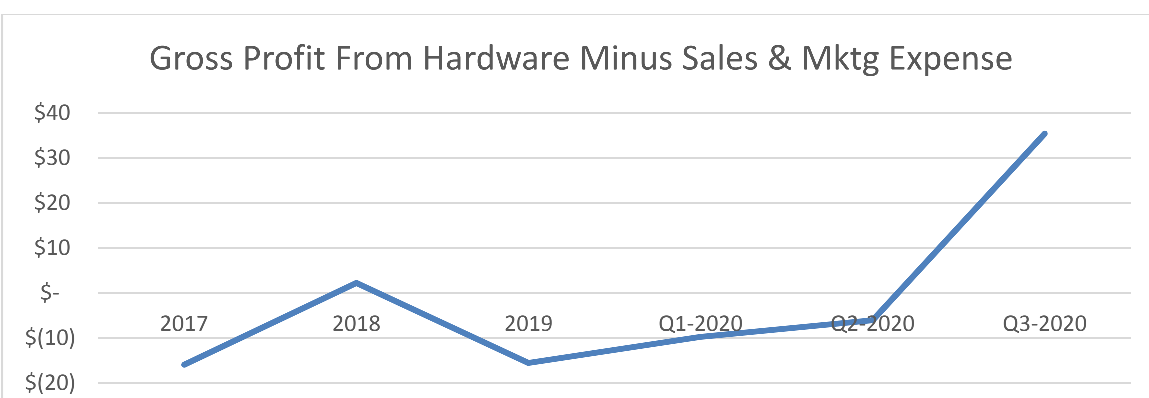
Beside Zwift, other fitness platforms include Fulgaz, Rouvy, TrainerRoad and The Sufferfest. While Peloton's user interface has not changed meaningfully in the past five years, these alternative services have improved considerably and are providing better experiences and better motivation for its users. Therefore, it is not farfetched to expect that Peloton will either have to develop its own virtual world software, to give users the option to have such an experience on a Peloton bike (which would be costly to develop), or it might just have to partner with, or acquire, one of these services.

Margins and Free Cash Flow

While Peloton's revenues increased 367% between the first quarter of fiscal 2019 and the third quarter of fiscal 2020, the gross profit margin did not widen meaningfully. It was virtually unchanged, from 45.9% in the former period to 46.8% in the latter. Breaking it down by revenue source shows that the Connected Fitness Products (the spin bikes and treadmills) widened their profit margin slightly from 54.2% to 54.7%, but the Subscription margin narrowed from 51.4% to 42.2%.

The operating margin has improved considerably, on the other hand, from a negative 50.4% in the first quarter of fiscal 2019 to a negative 11.3% in the most recent quarter (the third quarter of fiscal 2020). This is the result of the major components of operating expenses, Sales & Marketing, General & Admin., and R&D all having risen around 100%-200% over the period, but revenues having expanded 367%.

The largest operating expense is Sales & Marketing, although these activities were severely reduced in the fourth quarter of fiscal 2020 as a result of the supply/demand imbalance, so it is expected that Peloton will report a profit for that quarter because of the one-time reduction in operating expenses. To illustrate this point, the chart below takes the gross profit from the sale of spin bikes and treadmills for each period and subtracts total Sales and Marketing expenses. On this basis, the company just broke even in FY2018 but not in any other period until the third quarter of FY2020:



This is the trend that is possibly extrapolated in the fourth quarter of FY2020, as Sales and Marketing expenses should continue to decline, both as a percentage of revenue and in absolute terms. That said, Wall Street does not expect Peloton to generate positive free cash flow until 2022 at the earliest, a point at which the world will almost certainly have recovered from the COVID-19 pandemic.

Peloton's shares have doubled since the earnings announcement on May 6th, when the company posted 66% year-over-year growth in revenues and the first quarter in which it had a positive EBITDA (of $23.5 million). In its final quarter for fiscal 2020 (ended June 30th), Peloton is expected to report approximately $576 million in revenues and $25 million in profit (EPS of $0.09), which would be the first quarter in which Peloton has earned a profit. However, for FY2020 a net loss of $0.66 per share ($187 million in total) is still expected, which would represent a net profit margin of -10.4%. Consequently, it remains to be seen how much scale is required before Peloton can reach profitability on a sustainable basis (not counting the fourth quarter of fiscal 2020, during which Sales & Marketing expenses were abnormally low).

Valuation

At a recent $26 billion market capitalization, Peloton trades at 14.5x the consensus FY2020 revenues. While recurring revenues are usually valued at higher multiples, Peloton trades at approximately 60x the amount of recurring revenues it generated in FY2020 (ended June 30, 2020). That could be considered a relevant metric, since the company does not earn an operating profit on the hardware (bikes and treadmills). Indeed, if Peloton saturates the market within a few years, as it likely would, should the recent growth rates be extrapolated for another 2-3 years, all that will remain is essentially subscription revenue. Even fast-growing Software-as-a-Service (SaaS) such as Salesforce.com trade at just around 12x forward revenue. At such a valuation, Peloton's shares would considerably lower, since approximately 4.6 million subscribers (paying $39 per month) would be required to generate the $2.2 billion of annual subscription revenue that is needed to justify the current market capitalization, compared to the 1.05 subscribers it has now. In addition, while Salesforce.com can continue to grow, Peloton would cease to grow, once the market is saturated, so the valuation multiples awarded to these revenues could narrow considerably compared to fast-growing SaaS companies.

Valuation Based on Discounted Cash Flow Model

To reverse-engineer the assumptions required to justify a $26 billion valuation, one can estimate the terminal value of the company five years into the future and then discount it back to the present day. For example, assuming Peloton can generate $1.0 billion in free cash flow in 2025, the net present value of its terminal value would be approximately $16.4 billion, assuming a terminal valuation of 20x free cash flow:

Free Cash Flow (mill.)	$1,000
Wtd. Avg. Cost of Capital	8.00%
Terminal Growth Rate	4.00%
Years	5
Valuation Multiple	20
Terminal Value (mill.)	$16,439

In a discounted cash flow model, almost all of the value will be derived from the terminal value since Peloton will most likely experience negative free cash flow for the next few years, at least, and the relatively modest cash flow it will generate prior to the terminal year will be discounted back to a net present value that does not amount to much. The model above assumes a weighted average cost of capital (WACC) of 8.0% and a terminal growth rate of 4.0% from year 2025 on. While that might seem low, the assumption is that Peloton will saturate its market over the next five years and then grow at a rate similar to the overall fitness industry in the US.

Second, to estimate what is required to reach $1.0 billion in free cash flow by 2025, the assumptions below are presented:

	2019	*2020*	*2021*	*2022*	*2023*	*2024*	*Terminal Year*
Revenues	$915	$1,790	$2,660	$3,800	$4,800	$5,400	$5,750
-Growth Rate	110%	96%	49%	43%	26%	13%	6%
Connected Fitness Subs	511	1,050	1,700	2,600	3,160	3,600	3,800
-Growth Rate	108%	105%	62%	53%	22%	14%	6%
Serviceable Address. Mkt.	13.1	14.0	14.7	15.4	16.2	17.0	17.8
-Growth Rate		7%	5%	5%	5%	5%	5%
Peloton Market Share	4%	8%	12%	17%	20%	21%	21%
Operating Income	($220)	($148)	($75)	$100	$400	$800	$1,300
Operating Margin	-24.0%	-8.3%	-2.8%	2.6%	8.3%	14.8%	22.6%
Net Income	($220)	($148)	($75)	$75	$300	$600	$975
Deprec & Stock-Based Comp.	$111	$120	$144	$173	$207	$187	$168
Capital Expenditures	83	170	225	250	160	120	135
Free Cash Flow	($192)	($198)	($156)	($2)	$347	$667	$1,008

(in millions)

The assumptions include a rapid revenue growth phase, which will moderate in 2024-2025 when the market is largely saturated with spin bikes and treadmills. Connected Fitness subscribers will plateau at around 4 million, which then will represent approximately a 21% penetration of its then-SAM, which is projected to expand by 5% per annum. This model uses a simplified measure of free cash flow, derived as net income, plus depreciation and stock-based compensation, minus capital expenditures. The latter will probably expand over the next year or two in order to secure enough factory space to meet demand, but assuming post-COVID demand will moderate meaningfully, so should capital expenditures.

Inherent in these assumptions is a widening of the operating margin from a negative 24% in 2019 to a positive 22.6% in 2025. This would result in earnings per share (EPS) of approximately $3.45 in 2025, assuming a 25% tax rate. This is higher than Wall Street's consensus of around $3.00 for 2025. Consequently, the assumptions required to justify just a $16 billion valuation (not the existing $26 billion valuation) for the company appear aggressive.

For example, assuming the above-referenced growth and penetration, the SAM would have to be around 18 million in five years, or approximately 14% of all US households, with a 21% penetration for Peloton, despite intensifying competition, and all subscriptions active (no churn, even though this measure has been approximately 8% per year historically). Even under those circumstances, the company's free cash flow would be just $1.0 billion by 2025 and by then its rapid growth phase is most likely over. Therefore, Peloton trades at approximately 26x the free cash flow it might generate in 2025 -- if it reaches all of its operating objectives. If it reaches all operating objectives but the free cash flow multiple the market is willing to pay for just moderately expanding revenues is just 15x by 2025, the shares would trade 43% below current levels. Moreover, these per-share calculations assume no dilution over the five-year period from stock-based compensation which is not insubstantial at close to $100 million per year for the past two years.

Based on "Normalized" Valuation Multiples and Growth Rates

While the COVID-19 crisis and subsequent lockdowns resulted in an increase in demand for Peloton's spin bike, as well as a meaningful increase in the downloading of its app (which was offered free of charge for the first two months), much of this benefit will reverse when the economy opens up again, and when gyms reopen and, eventually, mask requirements and social distancing rules will be dropped. While that might take an unknown number of months, it will probably end with a normalization in demand for Peloton bikes and its interactive services.

With its growth rates leveling off, or even declining relative to the peak-lockdown demand, Peloton's valuation multiples should also normalize, which would be to a level far below the present trading range. For its first six months as a public company (September 2019 to March 2020), Peloton's shares traded at $27 on average, which represented 8.3x the revenues generated in FY2019. Revenues in FY2020 probably doubled compared to FY2019, which would in theory justify a doubling in share price to $54.

That said, FY2020 is most likely the peak-growth year for Peloton and even Wall Street expects the company's revenue growth to moderate to 48% in FY2021, which should result in a reduction in the Price/Sales multiple. As revenue growth will probably continue to moderate for the next 3-4 years, the Price/Sales multiple should narrow over that time frame as well, since much of Peloton's FY2020 growth was simply an acceleration of sales it would otherwise have realized in 2021 or 2022. Also, once the pandemic subsides, churn rates will probably rise meaningfully as consumers re-embrace gyms, spin-studios and exercising outdoors to a greater extent, and perhaps attempt to sell their Peloton bike on sites such as eBay.

A company with similar hype surrounding its products was GoPro (GPRO), which came public in 2014 and reached a $14 billion market value shortly thereafter. This was based on its rapidly growing revenues, which had expanded over 40% y-o-y, to $1.4 billion. Hence, the Price/Sales multiple was approximately 10x on a trailing basis. Then, it turned out that the market was not as large as investors had thought, and GoPro's revenues have been relatively flat at around $1.0-$1.5 billion per annum since 2015. This has resulted in a 95% decline in its share price, and its current market capitalization is just $700 million, or less than 70% of the $1.06 billion in revenues Wall Street expects for next year. This is a reminder of how rapidly sentiment can shift for a company that used to expand rapidly but ceased to do so because the size of the addressable market was smaller than initially thought.

An almost identical scenario transpired with Fitbit, a company that sells fitness watches, and its shares also declined 95% in the past five years as its revenues began to decline after a few years of strong growth. Contributing reasons for GoPro's and Fitbit's disappointing results are the general deflation of technology hardware (prices go down, so unit sales need to increase just to keep revenues flat) as well as increasing competition – issues that apply to Peloton as well. Thus, even if Peloton were to double its revenues in FY2021 as well, to $3.6 billion, but if that is the level after which it can only grow moderately, if at all, and the market responds by giving it a GoPro multiple of 0.7x sales, its shares would decline almost 90%.

Yet another example is Nautilus, Inc., a company that produces workout equipment. While shares of Nautilus have advanced 10-fold from the March lows, it might still be considered more attractive than Peloton on a valuation basis, since it trades at approximately 9x the free cash flow it has generated over the past year. However, more than 70% of that free cash flow was generated in the second quarter, which was boosted by pandemic-related consumer behavioral pattern changes. Still, Nautilus is expected to grow revenues 44% in 2020, based on Wall Street's consensus, but then return to a no-growth pattern in 2021. Consequently, in the case of Nautilus, the revenue spike due to the pandemic is deemed temporary, and the company trades at 0.8x the revenues and 10-12x the earnings expected to be generated in 2020 and 2021. Needless to say, if such valuation multiples will be applied to Peloton in any of the next five years, the shares will decline sharply relative to current levels.

Valuation per Subscriber

With a $26 billion market capitalization and approximately 1.0 million Connected Fitness Subscribers, investors are paying close to $26,000 for each of these subscribers. By comparison, a company such as Altice (current owner of Cablevision), has an enterprise value of around $40 billion and 5.0 million unique subscribers, which indicates a value of $8,000 per subscriber. And those subscribers generate approximately $10 billion in annual revenues, or around $2,000 per subscriber, per year. This can be compared with Peloton, which generates $39 per subscriber, for its Connected Fitness subscribers, which equates to $468 per year, or just 23% of what Altice generates per subscriber. Yet, the market values a Peloton subscriber more than twice as high as an Altice subscriber. The only explanation for this is the fact that Altice only expands its revenues in line with the economy, at around 2% per year, whereas Peloton is in the middle of a growth spike. Still, the Altice comparison may prove useful for the time when Peloton has saturated its market and growth has been reduced to the low single-digits per year. Ultimately, the value of a Peloton subscriber paying $468 per year should be a lot less than an Altice subscriber paying $2,000 per year.

Compared to Netflix

Comparisons to Netflix are not valid, since the market of cycling enthusiasts, or even people who work out frequently, is just a tiny fraction of Netflix users. In addition to that, Peloton's price ($97 per month if the bike is financed, or $39 per month for the subscription that goes with the bike) is significantly higher than that for Netflix (which is available in some international markets for less than $5.00 per month), which shrinks Peloton's addressable market even further. Also, while Netflix has been successful in its international expansion, at least as far as revenues are concerned, for Peloton, most international markets would require classes in the native language, which would add significantly to operating costs. Peloton might also need a local presence with sales staff, stores and technical support for each country in order to reach adequate scale. For Netflix, just a small portion of its programming is in native languages but this would probably be different for Peloton. An original, English language Netflix show can be dubbed into German or be shown in Sweden with subtitles, but a Peloton workout with an American instructor would likely not be as well received if dubbed or shown with subtitles. Perhaps that is the reason that Peloton has indicated that 14 million of its potential 16 million worldwide addressable market is US-based.

Valuation Based on a Scenario

While the Peloton spin bike is highly regarded, it is also an expensive, bulky at-home fitness product designed for a niche fitness audience that can both afford the product and service, and sees the value in having a $2,300 fitness bike. Before the pandemic, the market segment that could afford this, and wanted it, was small. Once the pandemic has subsided, it will be slightly larger, but still small. The number of Connected Fitness subscribers has approximately doubled between FY2019 and FY2020 but such growth cannot continue much longer. Assuming sustained 50% growth rates for the FY2021-FY2025 period results in a cumulative 19.7 million Connected Subscribers:

Year	Connected Subscribers
2019	500,000
2020	1.0 million
2021	1.5 million
2022	2.25 million
2023	3.375 million
2024	5.063 million
2025	7.594 million
Total	19.78 million

There are only 60 million people in the US who have a gym memberships, so if there are two gym members in each household, that means that there are 30 million US households that are gym members. Thus, if Peloton sells 19.8 million bikes to 19.8 million households, it has essentially penetrated two-thirds of the gym-going population, or 15.4% of all US households, which is clearly preposterous. Also, with a new factory opening only in December, it is unrealistic to assume that Peloton will be able to take full advantage of the COVID-19 lockdowns and gym closures.

Consequently, a much more reasonable assumption is that Peloton's growth rate will start to moderate in 2021 and reach a single-digit rate within 3-4 years as the market becomes saturated and as new competition emerges. The highest earnings per share estimate on Wall Street for 2026 is approximately $3.00. Given the current share price, the market's five-year-average forward earnings multiple is 30x. Therefore, assuming the company is successful in reaching its objectives and Wall Street's financial targets are met as well, it is possible that the stock will be essentially unchanged, if it trades at 30x forward earnings five years from now. Except by then, its growth potential will be much diminished and the multiple lower.

Investment Summary

Peloton is a good company with outstanding products, but the shares are priced using unrealistic assumptions to justify its $90 share price. In a stock market that tends to extrapolate trends too frequently, Peloton's strong growth in the past six months appears not to be indicative of a much greater long-term potential but, rather, a temporary boost in demand, driven by the pandemic and resulting lockdowns and gym closures. Although it could take some time before the approximately 60 million gym members in the US are ready to return, research suggests that most of them will return in the not too-distant future. Therefore, five years from now, it is doubtful if the Peloton's addressable market will be larger than it otherwise would have been in the absence of the pandemic.

While Peloton is a market leader, with gyms and spin studios closed, competition has intensified in the workout-from-home market and there are many competitors emerging in various market segments. SoulCycle, for example, has a spin bike priced almost exactly the same as Peloton's, and it has brand recognition and a customer-base that is used to paying $30-$50 per class. Other technologies are also emerging, such as the smart indoor bike trainers that can be used with video game interfaces such as Zwift, which has been a global success and which has the potential to disrupt Peloton's spin class model. With the rapid development in this area, it is unlikely that indoor cycling will look the same as it does today five years into the future.

The pandemic is clearly providing an economic benefit for Peloton, but it might negatively impact the market valuation within the next year or two. For example, the market most likely assigns a higher valuation to the company with spiking revenue growth, but if such growth is temporary, and normalizes within a year or two, such valuation multiples will likely narrow substantially. If a lot of growth is pulled forward to this year that would otherwise have happened in 2021 or 2020, there will be considerably lower year-over-year growth in those years. If so, the multiples the market is willing to pay for Peloton's shares in 2021-2022 should be considerably lower. If Peloton's revenue growth stalls, such as has been the case with GoPro, Fitbit and Nautilus, it could trade at approximately 1.0x sales, as those companies do, rather than the current 12x sales. Clearly, the downside is substantial. Therefore, shares of Peloton Interactive are recommended for sale or short-sale.

PELOTON INTERACTIVE, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(in millions, except share and per share amounts)

	March 31, 2020 (unaudited)	June 30, 2019
ASSETS		
Current assets:		
Cash and cash equivalents	$ 509.0	$ 162.1
Marketable securities	923.7	216.0
Accounts receivable, net	51.2	18.5
Inventories, net	194.2	136.6
Prepaid expenses and other current assets	114.5	48.4
Total current assets	1,792.7	581.7
Property and equipment, net	207.3	249.7
Intangible assets, net	17.3	19.5
Goodwill	38.1	4.3
Restricted cash	1.5	0.8
Right-of-use asset	484.6	—
Other assets	28.0	8.5
Total assets	$ 2,569.4	$ 864.5
LIABILITIES, REDEEMABLE CONVERTIBLE PREFERRED STOCK, AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 141.5	$ 92.2
Accrued expenses	151.7	104.5
Customer deposits and deferred revenue	215.2	90.8
Other current liabilities	31.4	3.3
Total current liabilities	539.9	290.8
Deferred rent	—	23.7
Build-to-suit liability	—	147.1
Long term lease liability	497.7	—
Other non-current liabilities	14.5	0.4
Total liabilities	1,052.1	462.0
Redeemable convertible preferred stock	—	941.1
Stockholders' equity (deficit)		
Common stock	—	—
Additional paid-in capital	2,300.0	90.7
Accumulated other comprehensive income	0.3	0.2
Accumulated deficit	(783.0)	(629.5)
Total stockholders' equity (deficit)	1,517.3	(538.6)
Total liabilities, redeemable convertible preferred stock, and stockholders' equity (deficit)	$ 2,569.4	$ 864.5

PELOTON INTERACTIVE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in millions, except share and per share amounts)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2020	**2019**	**2020**	**2019**
Revenue:				
Connected Fitness Products	$ 420.2	$ 261.6	$ 958.9	$ 560.8
Subscription	98.2	51.1	242.5	120.1
Other	6.1	4.0	17.4	10.7
Total revenue	524.6	316.7	1,218.8	691.7
Cost of revenue:				
Connected Fitness Products	230.0	152.3	546.5	321.1
Subscription	41.4	38.0	103.3	74.6
Other	7.5	5.8	21.1	12.5
Total cost of revenue	278.8	196.1	670.9	408.2
Gross profit	245.8	120.6	548.0	283.5
Operating expenses:				
Sales and marketing	154.8	101.1	392.8	246.1
General and administrative	126.9	47.0	265.4	152.4
Research and development	22.5	13.8	60.6	37.8
Total operating expenses	304.2	162.0	718.8	436.4
Loss from operations	(58.4)	(41.4)	(170.8)	(152.9)
Other income, net:				
Interest income, net	5.6	3.0	12.7	5.2
Other expense, net	(2.9)	—	(3.1)	(0.3)
Total other income, net	2.7	3.0	9.6	4.9
Loss before provision for income taxes	(55.7)	(38.4)	(161.2)	(148.0)
Income tax (benefit) expense	(0.1)	0.2	(0.5)	0.2
Net loss	$ (55.6)	$ (38.6)	$ (160.7)	$ (148.2)
Net loss attributable to Class A and Class B common stockholders	$ (55.6)	$ (38.6)	$ (160.7)	$ (198.3)
Net loss per share attributable to Class A and Class B common stockholders, basic and diluted	$ (0.20)	$ (1.76)	$ (0.80)	$ (8.37)
Weighted-average Class A and Class B common shares outst., basic and diluted	280,879,011	21,959,822	199,769,233	23,673,350
Other comprehensive income:				
Change in unrealized loss on marketable securities	$ (3.1)	$ —	$ (3.3)	$ —
Change in foreign currency	0.1	0.3	3.4	1.0
Total other comprehensive (loss) income	(3.0)	0.4	0.1	1.0
Comprehensive loss	$ (58.6)	$ (38.2)	$ (160.6)	$ (147.2)