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Micron (/headlines/486) peloton-(hit p.://www.lijnksdinkony/sharshatticls?uary 20, 2020 | De the First to Comment na: 1 II s&via=SumZero) mi 1 = nue url=https://sumzero.com/headlines/consumers and retailing/pton/461-nton/headlines/search?tags=nton) NLS (/headlines/search?tags=NLS) 2. Investors Place Their Bets on Gambling Stocks: DraftKings

pelotonnautilus)



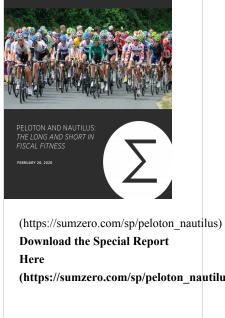
technology intended to quantify performance or physiological metrics. Speedometers, pedometers, heart rate monitors, and calorie calculators – once separate tools – can now be found on the least advanced stationary bicycles or treadmills at nearly any gym across the world as well as in wearable devices and phones. At a certain point, the number of useful metrics drops off for the average exerciser. Although hardcore enthusiasts may find value in knowing their VO2 max or their lactic acid threshold, most people who are trying to get in shape don't need more than what they can find at their local gym. What hasn't changed, however, are the physics of any fitness routine: the

fact that human couch potatoes, once inert, tend towards inertia. That's a fact that gym owners are well aware of: conservative estimates indicate that over 80% of gym memberships go unused after the surge in signups that occurs in December and January. What tends to get – and keep – people off the couch is the discipline that accompanies a sense of community and accountability: group classes, personal trainers, and workout partners. **Peloton: Hardware Peddlers or Tech Pedalers?** At least one company, Peloton (PTON: US),

and Short in Fiscal Fitness Σ SUMZERO

Peloton and Nautilus: The Long

Commentary



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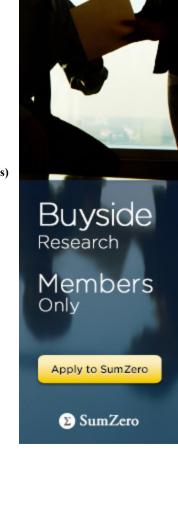
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10. Fight or Flight? Two Deep Value Investments While Air



(https://sumzero.com/apply)

There are a few pieces to Peloton's model: exercise equipment (a stationary bike and

build that experience into technology.

logistics company."

\$2245 price tag – remains pending.

month.

a treadmill, both equipped with touch screen computers loaded with metrics tools), an app, and a community built around professionally led pre-recorded and live streamed video classes accessible through the app. Their marketing is slick, targeting busy professionals for whom fitness classes and gyms aren't just lifestyle components, but

social capital that asserts status and financial posterity. As with other hyped recent

(https://sumzero.com/pro/entities#/28200/primary) seems to have found a way to

IPOs from companies that have self-branded as tech, the question raised isn't whether or not PTON is valuable to investors, but rather in quantifying how valuable it actually is. In his short position on Peloton (https://sumzero.com/pro/research/ideas/17995), SumZero contributor Sharif Farha (https://sumzero.com/pro/members/profiles/10095? user=true#/), a portfolio manager at Safehouse Capital Ltd., sharply dismisses the company as "an overvalued hardware company that is massively over-earning" while "portraying itself as a subscription-based software company." This is a far cry from Peloton's prospectus

(https://www.sec.gov/Archives/edgar/data/1639825/000119312519230923/d738839ds1.htm),

which declared itself "the largest interactive fitness platform in the world" and the

pioneer of "connected technology-enabled fitness, and the streaming of immersive,

technology, media, software, product, experience, fitness, design, retail, apparel,

While none of this really matters to Peloton aficionados, it's one of many things cited

instructor-led boutique classes," and simultaneously calling themselves "a

by investors who've been bearish on the company even before its Wall Street debut last September, where the company saw its stock close at 11% below (https://www.cnn.com/2019/09/26/tech/peloton-ipo/index.html) its IPO price. As Farha notes, the company was hit with a \$150M lawsuit last March (https://www.inc.com/guadalupe-gonzalez/peloton-ipo-challenges.html) from the National Music Publishers Association (NMPA) alleging copyright infringement: the company filed a countersuit which was thrown out last week, but not before the NMPA doubled the damages sought to \$300M (https://www.billboard.com/articles/business/8549528/peloton-head-of-musiclawsuit-interview) in September and customers began complaining about the music they were left with (https://www.businessinsider.com/peloton-users-complain-of-80smusic-after-300-million-lawsuit-2019-10). In addition, although Peloton settled its

intellectual property lawsuit against competitor Flywheel last week, its lawsuit against

sues-cycling-rival-echelon) – who offers a similar bike for \$999 compared to PTON's

competitor Echelon (https://www.latimes.com/business/story/2019-10-08/peloton-

Farha's "hardware company" argument is not without merit. As he points out,

makes almost 80% of its revenue from the sale of its equipment (bikes &

treadmills)." He continues, asserting that "Peloton should have followed a

money through their subscription business, which could be sold at a higher

"Despite claiming to be a subscription-based technology company, Peloton still

razorblade model by selling their hardware at breakeven to gain share and make

price." Farha's skepticism about the competitive cost of Peloton's cycles resonates across the market's short positions. NASDAQ contributor Richard Saintvilus points out in a preearnings article (https://www.nasdaq.com/articles/peloton-pton-2nd-quarterearnings%3A-what-to-expect-2020-02-05) on the company, that this hardware-based model (he cites the figure as "roughly 50%" of revenue) "has made it tough for investors to justify giving it a higher multiple."

To bolster the hardware argument, Farha points out the availability of half a dozen

the Peloton "connected" experience of group classes and workouts for \$12.99 a

This is elaborated on by short-sellers Citron Research, who note

subscribers. Would anybody buy that strategy?"

cheaper alternatives – including offerings from well-known brands like NordicTrack,

Nautilus, and SoulCycle – that, combined with Peloton's app, give any stationary bike

(https://citronresearch.com/wp-content/uploads/2019/12/Citron-Research-Presents-Peloton-Investors-Pedaling-Themselves-into-Frenzy.pdf): "Peloton justifies this by saying the app is a lead gen source yet the company admits that less than 10% of digital subscribers end up purchasing a connected fitness product. To put it in terms of digital content... Imagine if Netflix decided

to increase its subscriber base by giving away its content to DirecTV subscribers

for \$3 a month rather than \$12.99 and justified it by claiming they hoped to

build enough brand loyalty that customers would eventually become Netflix

Those who are buying that strategy are those who benefit from it: consumers and competitors who advertise their cheaper products as being Peloton-compatible. Citron's price target for the company is \$5.00. These fundamentals, along with \$PTON's rocky start, concerns about slowing momentum, marketing costs, and the IPO lockup expiration on February 23rd* (making approximately 317.4 million shares eligible for sale), loomed large as **short** interest in the company reached 112% of float a day ahead of its Q2 2020 earnings report, representing about 45 million shares valued at approximately \$115B according

to IHS Markit Ltd. Despite beating on sales and earnings and showing increased

price of \$29.00, thanks in part to lowered guidance for Q3. The reaction on Wall

subscriber growth, the stock fell 10% the next day, dipping periodically below its IPO

Street (https://www.marketbeat.com/stocks/NASDAQ/PTON/price-target/) remained

divided with a consensus price of \$35.81 the day after earnings and a "buy" rating. Blagoveschensky and Farha's price target of \$15.00, are, like Citron's, far beneath the lowest price on that spectrum. Although Farha sees the potential for profitability if Peloton manages to keep competitors out of their space, he also identifies risk in one of their major differentiators: its instructors/influencers who could leverage their popularity for higher salaries or offers from competitors, the latter of which could result in member churn as their followers go with them. Blagoveschensky also identifies an inherent risk in home consumer: that inertia will get the best of them, despite Peloton's virtual community. He writes, "I cannot rule out that people who purchased Peloton will sooner or later find themselves not cycling and just cancel their subscription. People find it much harder to stick to the routine when

they train at home and that will ultimately lead to increasing churn rates."

*Although the lockup expiry is scheduled for March 23rd, it will take place on

February 23rd due to an agreement with the underwriters surrounding a quarterly

company on February 5th, 2020. (https://investor.onepeloton.com/sec-filings/sec-

filing/8-k/0001639825-20-000008)

Nautilus: Is What's Old New Again?

over the next few years."

blackout period also scheduled for March. This was indicated in an 8-K filed by the

Although Peloton is a relatively new name to the fitness equipment industry, Nautilus (NLS: US) (https://sumzero.com/pro/entities#/6335/primary) is not. With 30 years in the fitness industry and a portfolio of well-known brands including Bowflex and Schwinn, NLS is one of the most recognizable names in exercise equipment for both health club and home use. Although the company has faced fierce competition from Peloton and other companies over the last few years, some investors see plenty of upside in its brand robustness as a market leader. Among those espousing a long

thesis on NLS is Joe Knecht (https://sumzero.com/pro/cap-intro/funds/azarias-capital-

management#/), a partner at Azarias Capital Management and SumZero author. In his

recently trending SumZero idea on Nautilus (https://sumzero.com/pro/research/ideas/18099), which casts a price target of \$13.00 on a 2 - 5 year horizon, Knecht describes how NLS is adapting to the challenges presented by Peloton, despite losing market share to Peloton's "disruptive and effective marketing message." "A key competitive advantage is NLSs open architecture allowing consumers to utilize the Nautilus App or download their favorite content (including Peloton's)

while using a variety of Nautilus equipment. While subscription revenue may

someday be a meaningful part of its revenue stream, Nautilus is not dependent

on selling proprietary content in order to generate significantly higher earnings

including stationary bikes, to brand-conscious consumers at a fraction of the price. "Nautilus has a very competitive and diverse product offering, well-regarded brand names, and digital content that offers a similar experience to Peloton. In

In addition to the consumer-centric flexibility engendered by this open architecture,

NLS directly competes with Peloton by offering app-connected exercise equipment,

fact, Nautilus recently launched a Bowflex branded bike for \$900 vs \$2,500 for PTON and consumers can utilize any exercise App they choose, including Peloton's. The new Bowflex bike appears to offer very similar attributes to Peloton's. The initial consumer reaction to the new bike appears to be favorable."

Despite trading below \$5.00 over the last few months, NLS saw a sudden boost in

stock price after announcing a new five-year \$70M credit facility

(http://www.nautilusinc.com/investors/press-releases/) on February 4th 2020. This is expected to create greater financial flexibility, facilitate innovation, and, according to Knecht, "enable NLS to execute its turnaround and return to profitable growth." As the quest to find the most fiscally fit among those competing in the exercise industry arena continues, companies are exploring avenues of differentiation.

Companies like Peloton and Nautilus find themselves racing to develop technologies that will lure consumers off the couch, knowing that behind every plugged-in bike or screen or app are the human needs for validation, community, and connection. « Previous Article (/headlines/460) Next Article » (/headlines/462)

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