MGT 6568 01-02 Pricing Strategies (2026), Peloton Interactive Inc. Case Writeup
By: Sparsh Singhal

There are several consequences of Peloton's price changes. I believe that customers who initially bought a Peloton for a higher price will be upset due to the constant drops in prices as they are loss averse. Missing out on the potential $300+ in savings will anger customers, leading to reputational damage as these consumers will bombard Peloton with negative reviews to display their frustration. These customers will also become prone to being captured by competitors. Although, it must also be noted that many consumers purchase a product regardless of price. Such consumers are known as innovators. These people will purchase the product purely out of interest knowing the risks associated with doing so, due to which, they will likely not be upset. Conversely, customers who might have bought a Peloton at a lower price will not be as satisfied in contrast to those who incurred a loss by purchasing a Peloton at a higher price due the principles of Prospect theory.

Over the course of 4 years, Peloton has changed its prices 6 times. Consequently, it prompts the consumers to start gaming the system. Consumers start holding on purchases intentionally to see when the price will drop, leading to reduced sales. Additionally, during the time they wait for such a price drop, they may be swayed by a competitor, leading to large losses to market share. Forcing existing customers to pay more has large consequences as well. As seen in the case, due to the rise in subscription prices, churn rates doubled (0.75% to 1.41%).

Constantly changing prices may also convey an image that the product's quality is inferior and struggles to sell. Additionally, a major caveat of constant price reductions on high value products is that it diminishes the perception of a brand as 'premium'. This can lead to long term damage to the brand and potentially permanently cripple the company's ability to charge a premium for their product.

Constant price changes also cause large financial damage. Peloton was forced to raise runway funds twice due to decline of profits, sell off their production facility in Ohio and had to also lay off employees twice to sustain themselves. This resulted in a reduction of their stock price, because of which, Peloton lost 95% of its market cap. Moreover, a company that regularly lays off its employees can be perceived to have incompetent leadership which can lead to reputational damage. It can also lower the confidence of investors. Laid off employees may display their anger on social media platforms which if gone viral can amplify reputational damage.

Holistically speaking, the one major advantage of constantly dropping prices was the fact that Peloton was able to capture a large share of the market. This led to them raising the barriers of entry due to which many competitors were unable to sustain themselves in the industry. Moreover, increasing prices allows Peloton to increase their gross margins without having to optimise their operations. Changing prices so many times has also provided Peloton with a large library of data they can now use to analyse elements associated with price such as demand elasticity, etc. and make more informed decisions later.

Overall consequences of Peloton's price changes include damage to reputation, stock price, and bottom line. Larger market share, and obtainment of a large library of data are the core benefits of the price changes.

Moving forward, I believe Peloton should charge a monthly subscription inclusive of all costs, like McCarthy suggested, starting at $49 (**Exhibit 1** for all prices + thought process behind them).

Price is the biggest barrier to purchasing a Peloton, therefore, I believe they will greatly benefit from breaking down their large upfront cost into smaller ones, allowing them to reduce sticker shock and induce a higher trial rate, leading to more customers and therefore, ultimately to a larger market share. This pricing model will also allow Peloton to discourage competitors due to its low subscription pricing. Competitors can try to price below Peloton, but I believe a consumer will not pay much attention to $50 if they can get the Peloton experience for that amount. However, Peloton may face competition in the case of Tread & Tread+ ($199 and $249 respectively) due to their high prices.

Peloton will also see cost savings through this pricing strategy. Since consumers will have to return the product after their subscription ends, Peloton can retain ownership and dismantle and refurbish the product to be sent to a new customer, greatly reducing manufacturing costs. Moreover, the low perceived prices are likely to lead to a huge demand for their products, leading to low inventory holding costs. Additionally, Peloton will also make a higher ROI through this model as seen before. (**Exhibit 2,** 2022 (Q1 & Q2)). Consequently, it will help restore Peloton's diminished market cap and lead to a higher stock price.

Customers are also likely to use the product more under a monthly subscription model over upfront cost because of the principle of Sunk cost fallacy. The customer will know their subscription will end by the end of the month due to which they will try utilising it as much as possible, leading to higher usage rates. Due to higher usage rates, a customer will get the whole Peloton Experience, leading to an increase in customers as customers will likely promote the product they've used many times to their friends and family through Word-Of-Mouth (WOM). The subscription model will also benefit from the Endowment effect as once customers purchase the membership, they will feel like they own the product due to which they will likely avoid cancelling their membership, allowing Peloton to earn more revenue while retaining ownership of the product.

However, this pricing model has disadvantages as well. Customers will be able to return the product without incurring a large cost, leading to higher churn rates, whereas as opposed to a high upfront fee model where they would likely use the product due to its high associated costs. Moreover, an all-inclusive subscription may harm Peloton's brand perception as a premium brand. Lastly, the Break-even duration will also be longer due to the low cost of a subscription.

Holistically speaking, I do recognise the benefits of the upfront fee model as well. The upfront fee model will convey a premium brand image for Peloton and allow them to earn higher margins due to the high sale value. Having a high sale value also will allow Peloton to have a much higher cash flow and liquidity due to which their break-even duration will be much shorter. Since the product will have a large cost (**Exhibit 2** for cost breakdown), it will become highly unlikely for a customer to refrain from using it due to being waste averse, leading to a lower churn rate. Although the customer's usage of the product will be lower than the subscription model as they will not have the same urgency of using the product every day, the upfront fee model will still allow Peloton to make more revenue in the short run as it will be equivalent to selling a membership for 2 years.

However, the upfront fee model has some major caveats. The largest barrier to purchasing a Peloton is price. Seeing such a high price may induce sticker shock, leading to lower sales. Moreover, setting a high upfront cost will encourage competition, leading to a lower market share. Additionally, it will also lead to larger inventory holding costs as the product will be kept in the warehouse for a long period of time as selling such a high value item will be much more difficult than a subscription due to the vast cost differences unless Peloton manages to formulate a strong position as a premium brand.

At a glance, choosing the subscription pricing model allows us to obtain a higher trial rate, market share, product usage, word of mouth, ROI and lower costs. As for cons, it leads to a longer break-even duration, higher churn rate and a cheaper brand image.

In contrast, choosing the upfront fee model allows Peloton to obtain a premium brand image, reduced churn rate, higher cash flow/liquidity. As for cons, it leads to a lower trial rate, lower market share, higher competition risk and higher costs.

Therefore, considering the following pros and cons, I strongly recommend Peloton to adopt the subscription fee pricing model.

As for the marketing of the product, it will be marketed to have a free of charge return policy. This will allow Peloton to benefit from the principle of waste aversion as customers will have flexibility to return their product any time, inducing the feeling that they are not wasting money. Moreover, allowing a free return policy instils confidence in customers that the product is superior and therefore, Peloton does not mind selling it to someone else. We will also communicate the intangible benefits associated with the product such as the experience & time savings as well as the amount of cost savings a customer will get through purchasing a Peloton by comparing costs associated with opting personal/group training by a world class trainer, as well as commuting costs.

Exhibits

1. **Exhibit 1: Pricing Strategy for Both Models**

a. Pricing Strategy for Subscription Model
Each product will be priced as follows: $44 flat subscription fee + each product's original cost as of 2023 divided over the course of 2 years.

This cost will then be rounded up.

(i) **Peloton Guide:** $44 + (300/24)= $56.5= rounded to **$49**
(ii) **Bike:** $44 + (1445/24)=$104=rounded to **$99**
(iii) **Bike+:** $44 + (2495/24)=$148=rounded to **$149**
(iv) **Tread:** $44 + (3495/24)=$190=rounded to **$199**
(v) **Tread+:** $44 + (4295/24)=$223=rounded to **$249**
(vi) **Peloton Row:** $44 + (3195/24)=$177=rounded to **$149**

Since the whole purpose of the subscription model is to break down large prices into small prices in order to reduce sticker stock for price sensitive buyers, we should have a **.9 price** to benefit from left digit bias so people will infer the price to be more affordable.

b. **Pricing Strategy for Upfront Costs Model**

Each product will be priced as follows: $44 flat subscription fee over the course of 2 years + each product's original cost as of 2023.

This cost will then be rounded up.

(i) **Peloton Guide:** (44x24) + 300= $1356= rounded to **$1500**
(ii) **Bike:** (44x24) + 1445=$2501=rounded to **$2500**
(iii) **Bike+:** (44x24) + 2495=$3551=rounded to **$3500**
(iv) **Tread:** (44x24) + 3495=$4551=rounded to **$4500**
(v) **Tread+:** (44x24) + 4295=$5351=rounded to **$5500**
(vi) **Peloton Row:** (44x24) + 3195=$4251=rounded to **$4500**

We won't try to utilise the .9 digit here as that effect works best for products that are meant to be portrayed as cheap. In this scenario, our goal is to portray Peloton as a premium product.

Note: We will also avoid using any **commas** (,) as they may make the price of the product harder to enunciate and will likely lead to the consumer to state more syllables to state the price of the product. Research shows that the easier it is to state the price of the product, the less expensive/painful it will feel to purchase.

2. **Exhibit 2: ROI Calculation**
Node: The reason we are taking year 2022 Q1 and Q2 as an example is due to COVID leading to unusual results in the previous results as well as the product gross profit being in the negatives post 2022 Q2. Doing so allows us to draw a fair comparison.

Formula: Gross Profit/COGS

a. Subscription ROI
for every $1 spent, we earn
2022 Q1: $2
2022 Q2: $2.11

b. Product ROI
for every $1 spent we earn
2022 Q1: $0.136
2022 Q2: $0.06

(See data obtained from the Case Study below:)

	2022 Q1	2022 Q2
REVENUE (millions)		
Product Revenue	501	796.4
Subscription Revenue	304.1	337.5
Total Revenue	**805**	**1134**
COGS (millions)		
Product COGS	441	745.5
Subscription COGS	101.4	108.3
Total COGS	**542**	**854**
GROSS PROFIT (millions)		
Product Profit	60	50.9
Subscription Profit	202.7	229.2
Total Gross Profit	**263**	**280**