Written questions

1. Why did Peloton gravitate to such a highly vertically integrated strategy?
2. Do you believe this was the correct decision to become so vertically integrated? Why or why not?

Written response

*Peloton’s Success with Vertical Integration*

Many companies before Peloton had achieved success with vertically integrated strategy, relying on internal divisions to handle things instead of third parties. Vertically integrated strategies are focused more on efficiency and control over the entire creation and distribution of the product, with some notable examples being Apple and Tesla. Because of the success of those two companies and many more, Foley was able to “study what other people are doing”[[1]](#footnote-0) and obtain a “second-mover advantage”[[2]](#footnote-1), avoiding some pitfalls that the other companies before him had experienced.

When Peloton did rely on third-party companies to deliver on something, they often produced underwhelming and sometimes reputation-damaging results. When they relied on a third party to deliver and install their products, Foley himself said that “often, third-party fulfilment partners didn’t have the human resources to meet the level of Peleton-caliber people”.[[3]](#footnote-2) The people that they were tasking to carry out the deliveries and installation of the machines were, in Foley’s eyes, inadequately trained and were not up to the task of everything that the final installation steps of the bike - “adjust[ing] the seat and the handlebar to comfortably fit the customer, connect[ing] the bike to the owner’s home Wi-Fi, and walk[ing the customer] through basic operating instructions”[[4]](#footnote-3). Later on, when Peleton had more capital and looked inwards to fix long-standing issues, they established an internal logistics division in 2018, which would contain a fleet of trucks and properly trained delivery personnel.

Another instance of Peloton being let down by a third party was when they partnered with a Taiwan-based manufacturer to build the first prototype bike. The prototypes that they received from the manufacturer were too big - the first prototype was 40% larger than the intended size - or had serious design flaws - upon pedaling faster, the bike would wobble so badly that focusing on the tablet screen was next to impossible. Eventually, Peloton would acquire the manufacturer, because “having greater control over our supply chain will enable us to strengthen and scale production, increase innovation, and allow us to continue to deliver the highest quality connected fitness products in the market”.[[5]](#footnote-4)

Why did the founders of Peloton want the company to become so vertically integrated? Was it really worth it to invest so much manpower and money into buying or creating aspects of the supply chain specifically for the company’s products, or was there a cheaper option that could deliver the same amount of quality? I believe that although the barrier to entry is definitely greater than no integration or horizontal integration, the potential reward is also greater - in this case, Peloton creating their own logistics division or acquiring their manufacturing partner meant higher profit margins. It also gave them more control over the supply chain, enabling them to be more efficient and adapt faster than others.

A big reason why they favored vertical integration so much was because they just couldn’t find any willing partners. Foley tried to strike a deal with either Soul Cycle or Flywheel, two major studio cycling chains, but they either expressed no interest from the beginning or quickly backed out, seeing little reason to partner with or invest in “a pre-revenue company pursuing an untested business model”[[6]](#footnote-5). Because no existing companies were willing to partner with Peloton, they had no choice but to do it by themselves, whether it be finding proper fitness instructors or having a suitable studio to film their videos in. There was also a case of Foley trusting in one of his co-founders to create the operating system for the tablets on the bikes rather than outsourcing it. All of these examples show Peloton’s dogged persistence in capitalizing on the then untested business model of in-home studio cycling.

Works Cited

Shreman, Len. "How Peloton Built the Foundation for Enduring Success." *Columbia Caseworks*, Sep. 24 2003. Case Study. *Harvard Business Publishing Education,* <https://hbsp.harvard.edu/download?url=%2Fcourses%2F798768%2Fitems%2FCU274-PDF-ENG%2Fcontent&metadata=e30%3D>

Sherman, Leonard. "The Secret To Peloton, Apple, Netflix, And Tesla's Growth: It's Vertical Integration". *Entrepreneur*, 2021, <https://www.entrepreneur.com/article/356181>.

"Peloton And The Existential Need For Vertical Integration". *Loose Threads*, 2021, <https://loosethreads.com/research/2019/11/14/peloton-and-the-existential-need-for-vertical-integration/>.

Hanbury, Mary. "Peloton Acquires Bike Manufacturer, Addresses One Of Its Biggest Risks". *Business Insider*, 2019, <https://www.businessinsider.com/peloton-acquires-bike-manufacturer-addresses-one-of-its-biggest-risks-2019-11>.

1. Sherman, Len. “How Peloton Built the Foundation for Enduring Success.” [↑](#footnote-ref-0)
2. ibid. [↑](#footnote-ref-1)
3. ibid. [↑](#footnote-ref-2)
4. ibid. [↑](#footnote-ref-3)
5. Hanbury, Mary. "Peloton Acquires Bike Manufacturer, Addresses One Of Its Biggest Risks". [↑](#footnote-ref-4)
6. Sherman, Len. “How Peloton Built the Foundation for Enduring Success.” [↑](#footnote-ref-5)