Google's rapidly rising expenses crimp 1Q earnings (Update)

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In this July 8, 2010 file photo, Google co-founder Larry Page arrives to a morning session at the annual Allen & Co. media summit in Sun Valley, Idaho. Larry Page is expected to make his first public remarks since returning to his original job as Google Inc.'s CEO when the Internet search leader releases its first-quarter earnings Thursday, April 14, 2011, after the market close.(AP Photo/Nati Harnik, File)

Google is helping the economy and hurting its stock. The company is hiring so many employees for projects outside its thriving search advertising business that its expenses are growing much faster than its revenue.

The strategy came into sharper focus in Google Inc.'s first-quarter earnings report released Thursday. Higher costs spooked investors who are already nervous about a new CEO who detests Wall Street's fixation on short-term results.

Google has committed to hiring at least 6,200 workers this year, the most in its 13-year history. It added more than 1,900 people in the first quarter, a pace that would translate to more than 7,600 for the year. Google ended March with more than 26,300 workers, 28 percent higher than a year ago.

The push coincides with Google co-founder Larry Page's return to his original job as CEO. Page, who ended Eric Schmidt's decade-long tenure as CEO after the first quarter ended, has indicated he plans to keep investing in opportunities that may take years to pay off, even if that drags down results in the near term.

Page, known for his aloofness, made a few tame remarks on Google's earnings conference call Thursday. He then turned things over to Chief Financial Officer Patrick Pichette, who has been steering the presentations for the past year.

"I'm very excited about Google and our momentum, and I'm very, very optimistic about our future," Page said.

He also assured listeners that the management transition announced three months ago is unfolding as the company envisioned. Page is overseeing day-to-day operations while Schmidt handles government relations and stalks possible acquisition targets in his new role as executive chairman.

Before taking his new role, Schmidt, 55, regularly shared his thoughts with analysts. He participated in every Google's earnings conference call until a year ago.

Page, 38, evidently intends to avoid the quarterly calls. In a Thursday interview, Pichette said Page only swung by for two minutes Tuesday as a courtesy to reassure investors. "He was just being gracious and dropped in to say hi," Pichette said.

It didn't seem to reduce the anxiety about Google's spending and the competitive threat it faces from Facebook, whose popular website has been drawing Internet traffic and advertising away from Google.

Google shares shed $31.50, or 5.5 percent, to $547.01 in extended trading Thursday after the release of the results. At that price, the stock has now fallen by about 13 percent since the announcement that Schmidt would replace Page.

Although Schmidt always emphasized that he wasn't managing Google to hit analysts' earnings targets, the company exceeded those expectations in all but six of his 27 quarters as CEO - a success rate of 78 percent. His final quarter as CEO turned out to be among the rare misses.

The company earned $2.3 billion, or $7.04 per share, in the period ending in March. That was an 18 percent increase from nearly $2 billion, or $6.06 per share, last year.

If not for the cost of stock-based employee rewards, Google said it would have earned $8.08 per share. That was below the average estimate of $8.11 per share among analysts surveyed by FactSet.

Revenue reached nearly $8.6 billion, a 27 percent increase from last year.

After subtracting the commissions paid to ad partners, Google's revenue stood at $6.54 billion. That figure topped the average analyst estimate of $6.33 billion, according to FactSet.

But those numbers were overshadowed by significantly higher expenses. Excluding the ad commissions and employee stock compensation, first-quarter expenses rose 44 percent from last year to $3.7 billion.

Labor costs appeared to be the biggest factor. The company gave all its workers a 10 percent raise at the beginning of the year and then went on a hiring splurge.

More than half of the new staff is working on products and services to supplement the search advertising network, which makes most of Google's money. The new growth opportunities include video ads on Google's YouTube site, ads on smartphones, and more banner advertising to lessen the company's dependence on text ads that appear alongside search results and other Web content. The company also is spending more to promote its Web browser, Chrome.

"We are doing what we believe is in the interest for the long term for shareholders by building great businesses and great products," Pichette said in an interview.