Netflix's 1Q tops forecasts, stock still plummets (Update)

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In this Aug. 2, 2011, photo Netflix CEO Reed Hastings speaks at a meeting in Palo Alto, Calif. Netflix announced on Monday, April 23, 2012, it suffered its first quarterly loss in seven years as the video subscription service dealt with rising licensing fees and the bill for an international expansion. Netflix Inc. lost $4.6 million, or 8 cents per share, during the quarter. (AP Photo/Paul Sakuma)

(AP) -- Netflix's comeback from a customer backlash accelerated during the first quarter, but the recovery wasn't impressive enough to ease more pressing concerns about the Internet video subscription service's ability to cope with tougher competition.

Wall Street's worries about the challenges facing Netflix Inc. crystallized Monday with the release of the company's first-quarter results and forecast for the upcoming months.

The company, which is based in Los Gatos, Calif., posted its first quarterly loss in seven years during the three months ending in March. The setback, though, was far smaller than analysts anticipated.

Instead of celebrating several positives contained in the report, skittish investors keyed on a second-quarter forecast that calls for a slowdown in subscriber growth during the spring and early summer. The April-to-June period has historically been a sluggish period for Netflix because more daylight and warmer weather tends to discourage people from staying inside to watch movies and old TV shows.

That's the main reason Netflix cited for its prediction that its service for Internet video streaming might add as few as 200,000 U.S. subscribers in the second quarter after gaining 1.7 million customers in the first three months of the year.

At most, Netflix is hoping to add 800,000 video streaming subscribers in the U.S during the second quarter. That would still be less than the 1.8 million streaming customers that Netflix picked up in last year's second quarter. It's also less than the increase of 1 million subscribers registered in the second quarter of 2010.

Netflix says the comparisons to its subscriber numbers from past second quarters are no longer an accurate barometer because the company has become more susceptible to seasonal swings as its audience has swelled. Management says Netflix is more likely to experience more cancellations in the spring and more new customers to sign up during the final three months of the year.

But Investors instead seemed to interpret the projection for this year's second quarter as a sign that Netflix will have a more difficult time attracting new subscribers as more alternatives emerge for Internet video streaming, including services from bigger companies, said Raymond

James analyst Aaron Kessler.

Amazon.com Inc., Wal-Mart Stores Inc.'s Vudu and Comcast Corp all offer video streaming options. Verizon Communications Inc. is preparing to launch a service in a joint venture with Coinstar Inc., the owner of Redbox kiosks that rent DVDs in thousands of stores across the U.S.

"I don't think anyone is ready to give Netflix the benefit of the doubt at this point," Kessler said.

Netflix shares plunged $16.94, or nearly 17 percent, to $84.90 in Monday's extended trading.

In a conference call, Netflix CEO Reed Hastings urged investors to focus on the bigger picture. He predicted the company will add about 7 million streaming subscribers in the U.S. for all of 2012. That would be about the same number that Netflix attracted in 2010 - the company's biggest growth year so far.

"Everyone is realizing that consumers want `click and watch' on-demand" video, Hastings said. "We have been focused on this market for a very long time and have some substantial advantages because of that."

Monday's sour reaction on the stock market contrasted to the ebullience that prevailed when Netflix released its last quarterly report in late January. Investors were enthused then because the report showed Netflix had added about 600,000 U.S. subscribers during the final three months of last year.

Those subscriber gains were hailed as a sign that Netflix was well on its way to repairing the damage caused last summer when the company abruptly raised its prices by as much as 60 percent for customers who want to rent DVDs through the mail as well as stream video over the Internet.

The higher prices irked subscribers, causing Netflix to lose 800,000 U.S. customers from July through September.

Netflix fared better during the first three months of this year as it picked up 1.7 million subscribers to end March with 26.1 million U.S. subscribers. The growth hit the high end of Netflix's forecasts.

"Our brand recovery is well under way," Hastings said in an interview late Monday. "We still have a ways to go, but we are working hard."

The streaming service also won new fans in Netflix's market's outside the U.S. The company ended the first quarter with nearly 3.1 million subscribers in Canada, Latin America, the United Kingdom and Ireland, up from 1.9 million entering the year. Netflix now intends to expand into another international market near the end of this year.

Even the DVD-by-mail service that Netflix is gradually phasing out fared slightly better than many analysts had expected. Netflix lost about 1.2 million subscribers in the first quarter, down from 2.8 million during the final three months of last year. The company now has about 10 million DVD customers, including 7 million that also pay for streaming.

The first-quarter progress wasn't enough to avert Netflix's first loss for any three-month period since the first quarter of 2005. The red ink flowed mainly because of the company's costs for international expansion and rising fees to license content for its Internet video library.

Netflix lost $4.6 million, or 8 cents per share, during the quarter. That compared to net income of $60 million, or $1.11 per share, at the same time last year.

First-quarter revenue climbed 21 percent from last year to $870 million.

Analysts surveyed by FactSet had predicted Netflix would lose 27 cents per share on revenue of $866 million.