

Netflix plan to conquer world stumbles, for now (Update)

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The plan by Netflix to conquer the world with its streaming video service is moving slower than expected.

Netflix shares skidded 13 percent to close at \$85.84 Tuesday, a day after reporting weaker-than-expected growth in its subscriber base.

The company said it ended the second quarter with 83 million subscribers, adding 1.7 million. That was well below Netflix's own forecast of 2.5 million additions and lower than many analyst forecasts.

Netflix said growth was hurt, especially in the United States, when it raised rates on many long-time subscribers who had been "grandfathered" in when it hiked most prices.

Netflix's market value has dropped by around one-third from its peak late last year to some \$37 billion, sparking speculation by some analysts that it could become a takeover target.

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The company effectively raised its price for many customers, which provided a boost to revenue but hurt new subscriptions and may have caused some customers to turn to rivals such as Hulu or Amazon.

Trouble in new markets

"These price hikes now place Netflix into a similar price category as its competitors," said Jonathan Broughton at IHS Technology in a note to clients.

Broughton said growth in new markets was disappointing, adding that Netflix may need to do more to connect with viewers around the world.

"Netflix has been slow to invest in international content, even in larger countries, and this has stalled growth," he said.

"Local content has been cited as key to expansion in international markets and pulling back from this may be detrimental to the company outlook outside the US and UK."

Daniel Salmon at BMO Capital Markets said Netflix faces "a period of challenging visibility" as it seeks to expand globally.

"While Netflix notes that local language content 'constitutes a small minority of viewing' we believe it has a higher likelihood than traditional, Western/Hollywood content to generate the positive word-of-mouth/local news coverage that could accelerate subscriber growth in a given country," Salmon said in a research note.

Michael Graham at Canaccord Genuity said Netflix may be seeing only a temporary pause in its growth spurt, and views the drop in Netflix as "a good long-term buying opportunity."

Graham said that he believes "that the full benefits from Netflix's international launch and content investments have yet to be realized."

Neil Saunders of the research firm Conlumino, said the troubling news from Netflix is in the United States, where it raised most subscribers to \$10 per month from \$8 after a period of "grandfathering."

"Inevitably, this change brought with it a great deal of churn, with some subscribers cancelling memberships," he said.

"As much as Netflix's growing international business affords it future potential, at present that division is loss-making. The US delivers the profits. And that means slower domestic growth will put a brake on

bottom line expansion."

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