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Netflix Announces Q4 2009 Financial Results

Subscribers – 12.3 million Revenue – \$444.5 million GAAP Net Income – \$30.9 million GAAP EPS – \$0.56 per diluted share

LOS GATOS, Calif., January 27, 2010 – Netflix, Inc. (Nasdaq: NFLX) today reported results for the fourth quarter and year ended December 31, 2009.

"Adding more than one million net new subscribers in the fourth quarter and nearly three million over the full year highlights the growing appeal of the Netflix service as we further expand access to and adoption of streaming movies and TV episodes over the Internet," said Reed Hastings, Netflix co-founder and chief executive officer. "In 2010, we expect to extend our operating momentum as we grow the business both rapidly and profitably."

Earnings Call Format

Netflix is changing the format of the company's fourth quarter earnings conference call. The call will consist solely of Q&A. In conjunction with the press release, the company has posted a written version of management's commentary to its Web site at http://ir.netflix.com. The conference call will be webcast today at 6:00 p.m. Eastern Time / 3:00 p.m. Pacific Time. If the format change is well received, future earnings calls will follow the same format. Please see conference call details below.

Fourth-Quarter and Fiscal-Year 2009 Financial Highlights

<u>Subscribers.</u> Netflix ended the fourth quarter of 2009 with approximately 12,268,000 total subscribers, representing 31 percent year-over-year growth from 9,390,000 total subscribers at the end of the fourth quarter of 2008 and 10 percent sequential growth from 11,109,000 subscribers at the end of the third quarter of 2009.

Net subscriber change in the quarter was an increase of 1,159,000 compared to an increase of 718,000 for the same period of 2008 and an increase of 510,000 for the third quarter of 2009.

Gross subscriber additions for the quarter totaled 2,803,000, representing 34 percent year-over-year growth from 2,085,000 gross subscriber additions in the fourth quarter of 2008 and 29 percent quarter-over-quarter growth from 2,180,000 gross subscriber additions in the third quarter of 2009.

Of the 12,268,000 total subscribers at quarter end, 97 percent, or 11,892,000, were paid subscribers. The other 3 percent, or 376,000, were free subscribers. Paid subscribers represented 98 percent of total subscribers at the end of the fourth quarter of 2008 and at the end of the third quarter of 2009.

Revenue for the fourth quarter of 2009 was \$444.5 million, representing 24 percent year-over-year growth from \$359.6 million for the fourth quarter of 2008, and a 5 percent sequential increase from \$423.1 million for the third quarter of 2009. Revenue for fiscal 2009 was \$1.67 billion, up 22 percent from \$1.365 billion for fiscal 2008.

<u>Gross margin</u>¹ for the fourth quarter of 2009 was 38.0 percent compared to 35.2 percent for the fourth quarter of 2008 and 34.9 percent for the third quarter of 2009. Gross margin for fiscal 2009 was 35.4 percent compared to 33.3 percent for fiscal 2008.

GAAP net income for the fourth quarter of 2009 was \$30.9 million, or \$0.56 per diluted share compared to GAAP net income of \$22.7 million, or \$0.38 per diluted share, for the fourth quarter of 2008 and GAAP net income of \$30.1 million, or \$0.52 per diluted share, for the third quarter of 2009. GAAP net income grew 36 percent on a year-over-year basis and GAAP EPS grew 47 percent on a year-over-year basis.

GAAP net income for fiscal 2009 was \$115.9 million, or \$1.98 per diluted share compared to GAAP net income of \$83.0 million, or \$1.32 per diluted share, for fiscal 2008. GAAP net income grew 40 percent on a year-over-year basis and GAAP EPS grew 50 percent on a year-over-year basis.

Non-GAAP net income was \$32.7 million, or \$0.59 per diluted share, for the fourth quarter of 2009 compared to non-GAAP net income of \$24.6 million, or \$0.41 per diluted share, for the fourth quarter of 2008 and non-GAAP net income of \$32.1 million, or \$0.55 per diluted share, for the third quarter of 2009. Non-GAAP net income grew 33 percent on a year-over-year basis and non-GAAP EPS grew 44 percent on a year-over-year basis.

Non-GAAP net income was \$123.5 million, or \$2.11 per diluted share, for fiscal 2009 compared to non-GAAP net income of \$90.7 million, or \$1.44 per diluted share, for fiscal 2008. Non-GAAP net income grew 36 percent on a year-over-year basis and non-GAAP EPS grew 47 percent on a year-over-year basis.

Non-GAAP net income equals net income on a GAAP basis before stock-based compensation expense, net of taxes.

Stock-based compensation was \$3.0 million for the fourth quarter of 2009, compared to \$3.2 million for the fourth quarter of 2008 and for the third quarter of 2009. Stock-based compensation for fiscal 2009 was \$12.6 million compared to \$12.3 million for fiscal 2008. Stock-based compensation is presented in the same lines of the Consolidated Statements of Operations as cash compensation paid to the same individuals.

<u>Subscriber acquisition cost</u>² for the fourth quarter of 2009 was \$25.23 per gross subscriber addition compared to \$26.67 for the same period of 2008 and \$26.86 for the third quarter of 2009. Subscriber acquisition cost for fiscal 2009 was \$25.48 per gross subscriber addition compared to \$29.12 for fiscal 2008.

² Subscriber acquisition cost is defined as the total marketing expense, which includes stock-based compensation for marketing personnel, on the Company's Consolidated Statements of Operations divided by total gross subscriber additions during the quarter.

¹ Gross margin is defined as revenues less cost of subscription and fulfillment expenses divided by revenues.

<u>Churn</u>³ for the fourth quarter of 2009 was 3.9 percent compared to 4.2 percent for the fourth quarter of 2008 and 4.4 percent for the third quarter of 2009. Churn includes free subscribers as well as paying subscribers who elect not to renew their monthly subscription service during the quarter.

<u>Percentage of subscribers who watched instantly</u> more than 15 minutes of a TV episode or movie in the fourth quarter of 2009 was 48 percent compared to 28 percent for the same period of 2008 and 41 percent for the third quarter of 2009.

<u>Free cash flow</u>⁴ for the fourth quarter of 2009 was \$30.2 million compared to \$51.0 million in the fourth quarter of 2008 and \$25.5 million for the third quarter of 2009. Free cash flow for fiscal 2009 was \$97.1 million compared to \$94.7 million in fiscal 2008.

Cash provided by operating activities for the fourth quarter of 2009 was \$105.8 million compared to \$92.1 million for the fourth quarter of 2008 and \$78.3 million for the third quarter of 2009. Cash provided by operating activities for fiscal 2009 was \$325.1 million compared to \$284.0 million for fiscal 2008.

Business Outlook

The Company's performance expectations for the first quarter of 2010 and full-year 2010 are as follows:

First-Quarter 2010

- Ending subscribers of 13.5 million to 13.8 million
- Revenue of \$490 million to \$496 million
- GAAP net income of \$26 million to \$32 million
- GAAP EPS of \$0.47 to \$0.58 per diluted share

Full-Year 2010

- Ending subscribers of 15.5 million to 16.3 million
- Revenue of \$2.05 billion to \$2.11 billion
- GAAP net income of \$125 million to \$137 million
- GAAP EPS of \$2.28 to \$2.50 per diluted share

Earnings Call

The Company has posted a written version of management's commentary to its Web site at http://ir.netflix.com. Therefore, the conference call, which will be webcast today at 6:00 p.m. Eastern Time / 3:00 p.m. Pacific Time, will consist solely of Q&A, with questions submitted via email. Please email your questions to dcrawford@netflix.com. The company will read the questions aloud on the call and respond to as many questions as possible. All media inquiries should be directed to Steve Swasey at (408) 540-3947or sswasey@netflix.com.

Following completion of the call, a replay of the webcast will be available at http://ir.netflix.com. The telephone replay of the call will be available from approximately 6:00 p.m. Pacific Time on January 27, 2010 through midnight on February 2, 2010. To listen to a replay, call (719) 457-0820, access code 5243602.

³ Churn is a monthly measure defined as customer cancellations in the quarter divided by the sum of beginning subscribers and gross subscriber additions, then divided by three months.

⁴ Free cash flow is defined as cash provided by operating activities and investing activities excluding the non-operational cash flows from purchases and sales of short-term investments and cash flows from investment in business.

Use of Non-GAAP Measures

Management believes that non-GAAP net income is a useful measure of operating performance because it excludes the non-cash impact of stock option accounting. In addition, management believes that free cash flow is a useful measure of liquidity because it excludes the non-operational cash flows from purchases and sales of short-term investments, cash flows from investment in business and cash flows from financing activities. However, these non-GAAP measures should be considered in addition to, not as a substitute for or superior to, net income and net cash provided by operating activities, or other financial measures prepared in accordance with GAAP. A reconciliation to the GAAP equivalents of these non-GAAP measures is contained in tabular form on the attached unaudited financial statements.

About Netflix

With more than 12 million members, Netflix, Inc. (Nasdaq: NFLX) is the world's largest subscription service streaming movies and TV episodes over the Internet and sending DVDs by mail. For \$8.99 a month, Netflix members can instantly watch unlimited TV episodes and movies streamed to their TVs and computers and can receive unlimited DVDs delivered quickly to their homes. With Netflix, there are never any due dates or late fees. Members can select from a growing library of titles that can be watched instantly and a vast array of titles on DVD. Among the large and expanding base of devices that can stream movies and TV episodes from Netflix right to members' TVs are Microsoft's Xbox 360 and Sony's PS3 game consoles and, this spring, Nintendo's Wii console; Blu-ray disc players from Samsung, LG and Insignia; Internet TVs from LG, Sony and VIZIO; the Roku digital video player and TiVo digital video recorders. For more information, visit http://www.netflix.com.

Forward-Looking Statements

This press release contains certain forward-looking statements within the meaning of the federal securities laws, including statements regarding our subscriber growth, revenue, GAAP net income and earnings per share for the first quarter of 2010 and the full-year 2010. The forward-looking statements in this release are subject to risks and uncertainties that could cause actual results and events to differ, including, without limitation: our ability to attract new subscribers and retain existing subscribers; our ability to manage our subscriber acquisition cost as well as the cost of content delivered to our subscribers; fluctuations in consumer usage of our service; the continued availability of content on terms and conditions acceptable to us; maintenance and expansion of device platforms for instant streaming; continued weakness in the U.S. economy and its affect on online commerce or the filmed entertainment industry; conditions that effect our delivery through the U.S. Postal Service, including regulatory changes and postal rate increases; changes in the costs of acquiring DVDs or electronic content; consumer spending on DVDs and related products; disruption in service on our website or with our computer systems; competition and widespread consumer adoption of different modes of viewing in-home filmed entertainment. A detailed discussion of these and other risks and uncertainties that could cause actual results and events to differ materially from such forward-looking statements is included in our filings with the Securities and Exchange Commission, including our Annual Report on Form 10-K filed with the Securities and Exchange Commission on February 25, 2009. We undertake no obligation to update forward-looking statements to reflect events or circumstances occurring after the date of this press release.

Netflix, Inc. Consolidated Statements of Operations

(unaudited)

(in thousands, except per share data)

(in thousands, except per share data)	Three Months Ended					Twelve Months Ended					
	December 31,			tember 30,		ember 31,	De		December 31,		
		<u>2009</u>	•	<u>2009</u>		<u>2008</u>		2009		2008	
Revenues	\$	444,542	\$	423,120	\$	359,595	\$	1,670,269	\$	1,364,661	
Cost of revenues:											
Subscription		231,598		233,091		193,635		909,461		761,133	
Fulfillment expenses *		43,888		42,183		39,211		169,810		149,101	
Total cost of revenues		275,486		275,274		232,846		1,079,271		910,234	
Gross profit		169,056		147,846		126,749		590,998		454,427	
Operating expenses:											
Technology and development *		33,209		30,014		24,052		114,542		89,873	
Marketing *		70,715		58,556		55,617		237,744		199,713	
General and administrative *		13,524		11,543		10,762		51,333		49,662	
Gain on disposal of DVDs		(1,741)		(1,604)		(1,603)		(4,560)		(6,327)	
Total operating expenses		115,707		98,509		88,828		399,059		332,921	
Operating income		53,349		49,337		37,921		191,939		121,506	
Other income (expense):											
Interest expense		(4,457)		(674)		(677)		(6,475)		(2,458)	
Interest and other income (expense)		2,444		1,808		852		6,728		12,452	
Income before income taxes		51,336		50,471		38,096		192,192		131,500	
Provision for income taxes		20,423		20,330		15,364		76,332		48,474	
Net income	\$	30,913	\$	30,141	\$	22,732	\$	115,860	\$	83,026	
Net income per share:											
Basic	\$	0.58	\$	0.54	\$	0.39	\$	2.05	\$	1.36	
Diluted	\$	0.56	\$	0.52	\$	0.38	\$	1.98	\$	1.32	
Weighted average common shares outstanding:											
Basic		53,609		56,146		58,906		56,560		60,961	
Diluted		55,479		57,938		60,311		58,416		62,836	
*Stock-based compensation included in											
expense line items:											
Fulfillment expenses	\$	59	\$	99	\$	126	\$	380	\$	466	
Technology and development		1,023		1,169		1,095		4,453		3,890	
Marketing		433		452		462		1,786		1,886	
General and administrative		1,461		1,512		1,511		5,999		6,022	
Reconciliation of Non-GAAP Financial Measures (unaudited)											
Non-GAAP net income reconciliation:											
GAAP net income	\$	30,913	\$	30,141	\$	22,732	\$	115,860	\$	83,026	
Stock-based compensation		2,976		3,232		3,194		12,618		12,264	
Income tax effect of stock-based compensation		(1,184)		(1,302)		(1,287)		(5,017)		(4,585)	
Non-GAAP net income	\$	32,705	\$	32,071	\$	24,639	\$	123,461	\$	90,705	
Non-GAAP net income per share:	_		_				_				
Basic	\$	0.61	\$	0.57	\$	0.42	\$	2.18	\$	1.49	
Diluted	\$	0.59	\$	0.55	\$	0.41	\$	2.11	\$	1.44	
Weighted average common shares outstanding:	Ψ	0.07	Ψ	0.55	Ψ	0.11	Ψ	2.11	Ψ	2	
Basic		53,609		56,146		58,906		56,560		60,961	
Diluted		55,479		57,938		60,311		58,416		62,836	
		-,		. ,				-7 -		,	

Netflix, Inc. Consolidated Balance Sheets

(unaudited)

(in thousands, except share and par value data)

	As of				
	Dec	ember 31,	December 31,		
		<u>2009</u>	<u>2008</u>		
Assets					
Current assets:					
Cash and cash equivalents	\$	134,224	\$	139,881	
Short-term investments		186,018		157,390	
Prepaid expenses		12,491		8,122	
Prepaid revenue sharing expenses		17,133		18,417	
Current content library, net		37,329		18,691	
Other assets		23,818		16,424	
Total current assets		411,013		358,925	
Content library, net		108,810		98,547	
Property and equipment, net		131,653		124,948	
Deferred tax as sets		15,958		22,409	
Other non-current assets		12,300		10,595	
Total assets	\$	679,734	\$	615,424	
Liabilities and Stockholders' Equity					
Current liabilities:					
Accounts payable	\$	91,475	\$	100,344	
Accrued expenses		33,387		31,394	
Current portion of lease financing obligations		1,410		1,152	
Deferred revenue		100,097		83,127	
Total current liabilities		226,369		216,017	
Long-term debt		200,000		-	
Lease financing obligations, excluding current portion		36,572		37,988	
Other non-current liabilities		17,650		14,264	
Total liabilities		480,591		268,269	
Stockholders' equity:					
Common stock, \$0.001 par value; 160,000,000 shares authorized					
at December 31, 2009 and 2008; 53,440,073 and 58,862,478 issued					
and outstanding at December 31, 2009 and 2008, respectively		53		62	
Additional paid-in capital		-		338,577	
Treasury stock at cost (3,491,084 shares at December 31, 2008)		-		(100,020)	
Accumulated other comprehensive income, net		273		84	
Retained earnings		198,817		108,452	
Total stockholders' equity		199,143		347,155	
Total liabilities and stockholders' equity	\$	679,734	\$	615,424	

Netflix, Inc. Consolidated Statements of Cash Flows

(unaudited) (in thousands)

		Three Months Ended					Twelve Months Ended			
	December 31, September 2009 2009			7 30, December 31, 2008						
Cash flows from operating activities:				·						· <u></u>
Net income	\$	30,913	\$	30,141	\$	22,732	\$	115,860	\$	83,026
Adjustments to reconcile net income to net cash										
provided by operating activities:										
Depreciation and amortization of property, equipment and intangibles		10,238		9,618		9,141		38,044		32,454
Amortization of content library		60,261		56,690		47,579		219,490		209,757
Amortization of discounts and premiums on investments		168		126		184		607		625
Amortization of debt issuance costs		1,124		-		-		1,124		-
Stock-based compensation expense		2,976		3,232		3,194		12,618		12,264
Excess tax benefits from stock-based compensation		(3,584)		(1,600)		(753)		(12,683)		(5,220)
Loss on disposal of property and equipment		-		-		-		254		101
(Gain) loss on sale of short-term investments		(54)		(984)		618		(1,509)		(3,130)
Gain on disposal of DVDs		(2,607)		(2,491)		(3,494)		(7,637)		(13,350)
Gain on sale of investment in business		(1,783)				-		(1,783)		-
Deferred taxes		1,789		(15)		1,350		6,328		(5,905)
Changes in operating assets and liabilities:										
Prepaid expenses and other current assets		(9,390)		7,625		11,038		(11,001)		(4,181)
Content library		(22,785)		(9,998)		(11,123)		(64,217)		(48,290)
Accounts payable		8,894		(13,173)		(7,917)		(2,256)		7,111
Accrued expenses		7,506		2,752		171		13,169		(1,824)
Deferred revenue		20,974		(1,372)		17,232		16,970		11,462
Other assets and liabilities		1,177		(2,240)		2,148		1,685		9,137
Net cash provided by operating activities		105,817	_	78,311	_	92,100	_	325,063	_	284,037
Cash flows from investing activities:		,	_	,		,				,
Purchases of short-term investments		(125,841)		(21,006)		(76,118)		(228,000)		(256,959)
Proceeds from sale of short-term investments		36,037		85,904		58,723		166,706		304,163
Proceeds from maturities of short-term investments		4,688		3,480		1,000		35,673		3,170
Purchases of property and equipment		(22,433)		(9,994)		(7,471)		(45,932)		(43,790)
Acquisitions of intangible asset		(22, .55)		-		-		(200)		(1,062)
Acquisitions of content library		(57,048)		(46,273)		(38,295)		(193,044)		(162,849)
Proceeds from sale of DVDs		3,934		3,345		4,695		11,164		18,368
Proceeds from sale of investment in business		7,483		-		-		7,483		10,500
Investment in business		-,403				_		7,403		(6,000)
Other assets		(72)		134		(32)		71		(0,000)
Net cash provided by (used in) investing activities		(153,252)	_	15,590		(57,498)	_	(246,079)		(144,960)
Cash flows from financing activities:		(133,232)	-	13,390	_	(37,496)	_	(240,079)	_	(144,900)
Principal payments of lease financing obligations		(300)		(294)		(237)		(1,158)		(823)
Proceeds from issuance of common stock		9,182		2,725		3,231		35,274		18,872
Excess tax benefits from stock-based compensation		3,584		1,600		753		12,683		5,220
Borrowings on line of credit, net of issuance costs		18,978		-		-		18,978		5,220
				-		-				-
Payments on line of credit		(20,000)		-		-		(20,000)		-
Proceeds from issuance of debt, net of issuance costs		193,917		(120, 60,6)		(0.000)		193,917		(100.004)
Repurchases of common stock		(79,419)		(125,686)		(9,992)		(324,335)	_	(199,904)
Net cash provided by (used in) financing activities		125,942		(125,655)		(6,245)		(84,641)	_	(176,635)
Net increase (decrease) in cash and cash equivalents		78,507		(31,754)		28,357		(5,657)		(37,558)
Cash and cash equivalents, beginning of period	_	55,717	_	87,471	_	111,524	_	139,881	_	177,439
Cash and cash equivalents, end of period	\$	134,224	\$	55,717	\$	139,881	\$	134,224	\$	139,881
Non-GAAP free cash flow reconciliation:										
Net cash provided by operating activities	\$	105,817	\$	78,311	\$	92,100	\$	325,063	\$	284,037
Purchases of property and equipment		(22,433)		(9,994)		(7,471)		(45,932)		(43,790)
Acquisitions of intangible asset		-		-		-		(200)		(1,062)
Acquisitions of content library		(57,048)		(46,273)		(38,295)		(193,044)		(162,849)
Proceeds from sale of DVDs		3,934		3,345		4,695		11,164		18,368
Other assets		(72)	_	134		(32)		71		(1)
Non-GAAP free cash flow	\$	30,198	\$	25,523	\$	50,997	\$	97,122	\$	94,703

Netflix, Inc. Consolidated Other Data

(unaudited)

(in thousands, except percentages, average monthly revenue per paying subscriber, average monthly gross profit per paying subscriber and subscriber acquisition cost)

subscriber and subscriber acquisition cost)	As of / Three Months Ended						
	December 31,	September 30,					
	2009	2009	2008				
Subscriber information:	<u> 2009</u>	<u> 2009</u>	<u> 2008</u>				
Subscribers: beginning of period	11,109	10,599	8,672				
Gross subscriber additions: during period	2,803	2,180	2,085				
Gross subscriber additions year-to-year change	34.4%	42.7%	39.5%				
Gross subscriber additions quarter-to-quarter sequential change		12.6%	39.5% 36.5%				
	(1,644)	(1,670)					
Less subscriber cancellations: during period	* * * *	, , ,	(1,367)				
Subscribers: end of period	12,268	11,109	9,390				
Subscribers year-to-year change	30.6%	28.1%	25.6%				
Subscribers quarter-to-quarter sequential change	10.4%	4.8%	8.3%				
Free subscribers: end of period	376	274	226				
Free subscribers as percentage of ending subscribers	3.1%	2.5%	2.4%				
Paid subscribers: end of period	11,892	10,835	9,164				
Paid subscribers year-to-year change	29.8%	27.6%	25.1%				
Paid subscribers quarter-to-quarter sequential change	9.8%	4.4%	7.9%				
Average monthly revenue per paying subscriber	\$ 13.04	\$ 13.30	\$ 13.58				
Average monthly gross profit per paying subscriber	\$ 4.96	\$ 4.65	\$ 4.79				
Percentage of subscribers who watched instantly more than 15							
minutes of a TV episode or movie	48%	41%	28%				
Churn	3.9%	4.4%	4.2%				
Subscriber acquisition cost	\$ 25.23	\$ 26.86	\$ 26.67				
Margins:							
Gross margin	38.0%	34.9%	35.2%				
Operating margin	12.0%	11.6%	10.5%				
Net margin	7.0%	7.1%	6.3%				
Expenses as percentage of revenues:							
Technology and development	7.5%	7.1%	6.7%				
Marketing	15.9%	13.8%	15.5%				
General and administrative	3.0%	2.7%	3.0%				
Gain on disposal of DVDs	(0.4%)	(0.3%)	(0.5%)				
Total operating expenses	26.0%	23.3%	24.7%				
Year-to-year change:							
Total revenues	23.6%	24.0%	18.9%				
Subscription	19.6%	24.9%	14.8%				
Fulfillment expenses	11.9%	11.2%	25.0%				
Technology and development	38.1%	28.4%	30.3%				
Marketing	27.1%	19.0%	7.6%				
General and administrative	25.7%	(1.7%)	(20.7%)				
Gain on disposal of DVDs	8.6%	(1.5%)	(5.5%)				
Total operating expenses	30.3%	19.1%	8.3%				
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