



FOR IMMEDIATE RELEASE  
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**NETFLIX ANNOUNCES 73 PERCENT YEAR-OVER-YEAR SUBSCRIBER  
GROWTH FOR THE THIRD QUARTER;  
RAISES GUIDANCE FOR GAAP NET INCOME**

LOS GATOS, CA — October 4, 2004 — Netflix, Inc. (Nasdaq: NFLX) ended the third quarter of 2004 with approximately 2,229,000 total subscribers, within the Company's guidance range of 2,150,000 to 2,350,000 total subscribers. Subscribers grew 73 percent year-over-year from 1,291,000 total subscribers at the end of the third quarter of 2003 and 6 percent sequentially from 2,093,000 total subscribers at the end of the second quarter of 2004.

**Paid Subscribers**

Of the 2,229,000 total subscribers at quarter end, 96 percent or 2,135,000 were paying subscribers. The other 4 percent, or 94,000 subscribers, were new trial subscribers. Paying subscribers represented 96 percent of total subscribers at the end of the third quarter of 2003 and 97 percent of total subscribers at the end of the second quarter of 2004.

**Household Penetration**

Household penetration in the San Francisco Bay Area rose to 8.1 percent of households at the end of the third quarter of 2004, up from 5.4 percent at the end of the third quarter of 2003 and up from 7.6 percent at the end of the second quarter of 2004. Household penetration in the rest of the country reached 1.9 percent at the end of the third quarter of 2004, up from 1.2 percent at the end of the third quarter of 2003 and up from 1.8 percent at the end of the second quarter of 2004.

## Updated Third Quarter Business Outlook

The Company's revised guidance for the third quarter is:

Consolidated -

- GAAP net income substantially above the high end of the range of \$6.7 million to \$10.2 million and could reach \$17.5 million.
- Non-GAAP net income substantially above the high end of the range of \$10.2 million to \$13.7 million and could reach \$21 million.

US Domestic -

- SAC at or near the mid-point of the range of \$37 to \$39.
- Gross margin substantially above the high end of the range of 43 percent to 45 percent and could reach 51 percent.
- Churn<sup>1</sup> at the high end of the range of 4.8 percent to 5.6 percent.

Earnings will be substantially above the high end of the range of the Company's earlier guidance because of strong gross margin. Gross margin will exceed the high end of the Company's gross margin guidance, in part because movie rentals in the quarter were lower than expected. Lower rentals may have resulted from consumer interest in the Olympic broadcast.

### Catalogue More Productive

For the last several years, the rich content on the Netflix web site, including personalized recommendations, has driven high utilization rates as subscribers have been discovering great movies from the Company's huge library of DVD titles, including the inventory of older titles.

Following an analysis of new release and back-catalogue utilization, the Company has learned that back-catalogue titles have a significantly longer life than previously estimated. As a result, the Company has revised its amortization policy for its back-catalogue DVD library from a "sum of the months" accelerated method using a one-year life to the same accelerated method of amortization using a three-year life to more accurately reflect the productive life of these assets. In accordance with APB 20, the change in life will be accounted for as a change in accounting estimate on a prospective basis from July 1, 2004. New releases will continue to be amortized over 12 months.

Netflix CFO Barry McCarthy commented, "Three years ago we shortened the estimated useful life for our DVD rental library from three years to one year. For a young company with limited operating experience, that accounting estimate was management's best judgment of the useful life of catalogue content at that time. However, with several years of operating history behind us and based on analysis of this historical data, management's current best judgment of the useful life of

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<sup>1</sup> Churn is defined as customer cancellations in the quarter divided by the sum of beginning subscribers and gross subscriber additions, divided by three months.

catalogue content is three years. Because these assets have a longer productive life than we previously estimated, the Company is earning a higher return on invested capital than we previously reported. Once we analyzed the historical data, we were required by GAAP to change the estimates.”

The accounting change this quarter will contribute approximately 4 percentage points of gross margin improvement.

### **2005 Impact**

This change in accounting estimate is expected to raise long-term profit margins by approximately 2 percentage points. However, investors should note that the Company expects average movie rentals per subscriber to increase significantly in the first quarter of 2005 as it has in the first quarter in each of the last two years. An increase in movie rentals would decrease 2005 gross margin. Investors may wish to consider the two year trend in movie rentals when they consider 2005 usage and its impact on gross margin expectations.

### **Third Quarter Earnings Release**

Netflix will release its third-quarter 2004 financial results on Thursday, October 14, 2004 after the market close. A web cast of the quarterly conference call will begin at 2 PM PDT and can be accessed via the web at <http://ir.netflix.com>.

### **Fourth Quarter Subscriber Release**

In a break with past practice, the fourth quarter subscriber release, and all future subscriber releases, will be incorporated into the earnings release and not issued separately. Consolidating quarterly results into a single release will enable investors to see all the key metrics and financial results for the business in context.

### **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. However, Non-GAAP measures should be considered in addition to, not as a substitute for, or superior to net income or other financial measures prepared in accordance with GAAP. Management believes that gross margin and subscriber acquisition cost guidance for the U.S. business in the third quarter are useful measures because they give insight to investors with respect to the ongoing operations of the Company's primary business and allow for an equivalent comparison to prior results. Furthermore, there is no reconciliation to consolidated GAAP measures for gross margin or subscriber acquisition costs as impacts from UK operations are immaterial.

## **About Netflix**

Netflix (Nasdaq: NFLX) is the world's largest online movie rental service, providing more than two million subscribers access to over 25,000 DVD titles. For \$21.99 a month, Netflix subscribers rent as many DVDs as they want, and keep them as long as they want, with three movies out at a time. There are no due dates, no late fees and no shipping fees. DVDs are delivered for free by first-class mail from regional shipping centers located throughout the United States. Netflix can reach more than 85 percent of its subscribers with generally one business-day delivery. The company provides subscribers extensive information about DVD movies, including critic reviews, member reviews, online trailers, ratings, and personalized movie recommendations. For more information, visit [www.netflix.com](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 acquisition cost, gross margin, Churn, GAAP net income, Non-GAAP net income for the third quarter of 2004, the impact from the change in our accounting estimate upon gross margin in 2005 and anticipated subscriber usage in 2005. 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 manage our growth, in particular managing our subscriber acquisition cost as well as the mix between revenue sharing titles and titles not subject to revenue sharing that are delivered to our subscribers; fluctuations in consumer usage of our service; competition; changes in the costs of acquiring DVDs; 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 SEC on February 27, 2004. We undertake no obligation to update forward-looking statements to reflect events or circumstances occurring after the date of this press release.

**Netflix, Inc.**

**Non-GAAP Guidance Reconciliation Schedule**

(unaudited)

(in thousands, except subscriber acquisition cost)

	<b>Third Quarter 2004</b>
<b>Non-GAAP net income reconciliation:</b>	
Net income	\$ 17,500
Add back:	
Stock-based compensation	3,500
Non-GAAP net income	<u>\$ 21,000</u>