



Circle of Influence

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By Jim Hopkins, USA TODAY

LOS GATOS, Calif. — Netflix (NFLX) CEO Reed Hastings sounded frustrated.

The scene: The weekly meeting where top employees pitched ideas to bolster the online DVD-rental company's website.

He zeroed in on the button that customers click to say they are not interested in films Netflix recommends to them. In earlier meetings, everyone agreed to ditch the button to make the site less cluttered.

Yet there it was.

"Less is more," Hastings reminded the eight employees assembled in a conference room last month.

Hastings' focus on such details is a major reason the company he founded in 1997 is reshaping how millions of Americans watch movies. He's also helping upend the film industry. Netflix makes it easy to watch DVDs at home, delivered by the millions in Netflix's ubiquitous red envelopes.

The Friday meeting was one of many at which Hastings, 45, cajoled, quizzed and pushed workers in his drive to keep Netflix No. 1. He led 150 staffers in a pep rally at the Silicon Valley headquarters. He asked about store closings at rival Blockbuster. And he fretted over post office delivery schedules.

No surprise, says Bob Pisano, president of the Motion Picture Association of America, and a former Netflix director. Hastings, an engineer, is analytical and "very charismatic," he says. "That's a rare combination."

Hastings has fended off Wal-Mart and Blockbuster, sending Netflix shares soaring. Wall Street is expecting more good news today when Netflix reports quarterly results after markets close.

 But Hastings isn't out of the woods. He's trying to protect a customer base of more than 4 million as digital entertainment shifts rapidly. Broadband distribution of movies and TV shows is fast becoming reality. ABC will start testing free online delivery of *Desperate Housewives* and other top shows next Monday.

Online retailer Amazon has talked to Hollywood studios about adding movie and TV show downloads to its website. Apple Computer hit the gas pedal last fall when it launched \$1.99 downloads of ABC shows and other videos at its iTunes online store.

"All these competing products via digital delivery and not mail order," says analyst Frank Gristina at investment banker Avondale Partners. The pace, he says, has "clearly accelerated."

Hastings, a Boston native, isn't sweating yet. He's aiming to build an even bigger customer base — 20 million as early as 2010 — to ready Netflix for an eventual shift to downloads. That switch depends on several factors, he says. Critical hardware and software haven't been perfected. There aren't enough movies available in downloadable form. Plus, studios must still work out licensing agreements with existing distributors.

Eureka moment: \$40 late fee

 Hastings looks a bit like a younger version of another movie industry pioneer: producer George Lucas, best known for his *Star Wars* blockbusters. Yet, it was another space-themed film that inspired Hastings — indirectly, anyway — to start Netflix.

First, the back story: After getting a math degree at Bowdoin College in 1983, Hastings sought adventure for more than two years as a Peace Corps math teacher in Queensland


 Enlarge By Martin E. Klimek for USA TODAY

Reed Hastings' focus on details, such as de-cluttering Netflix's website, has helped the company compete with Blockbuster.

ABOUT REED HASTINGS

Age: 45.

Born: Boston.

Education: Bowdoin College, bachelor's in math, 1983; Stanford University, master's in computer science, 1988.

Compensation last year: \$300,000 in salary; \$585,000 in gains from exercising options, plus option grant potentially worth more than \$7.6 million. He holds about 9.5% of the company's stock.

Earlier career: Founder, Pure Software, built into one of world's 50 biggest public software makers. Sold to Rational Software in 1997.

Interests: Education philanthropy. President of California Board of Education, 2000-04. Led campaigns for more charter public schools.

Top of his personal Netflix film wish list: *Something the Lord Made*, *Door in the Floor*, *House of Cards*, *My Voyage to Italy* and *Match Point*.

Sources: Company, USA TODAY research

BEHIND THE SCENES

SUNNYVALE, Calif. — Netflix distribution centers look deceptively low-tech.

Workers at long tables under fluorescent lights stuff DVDs into paper sleeves with barcodes identifying the movies. Then they put the sleeve in a mailing envelope.

But it's more high-tech than that. Proprietary software matches the envelope to a customer request in Netflix's vast database. As DVDs are returned, Netflix ships out more from lists customers build in online accounts.

Other proprietary software powers the website, generating recommendations based on ratings customers are encouraged to give films. The more films they rate, the more likely they'll be referred to other films they'll want the next time they visit.

More than 90% of subscribers get movies with one-day service, mailed through the U.S. Postal Service in postage-paid envelopes. Subscribers pay \$9.99 to \$47.99 monthly to have as many as eight movies at once.




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years as a Peace Corps math teacher in Swaziland. "Absolutely loved it," he recalled in an interview.

Next came Stanford in Silicon Valley's sunny Palo Alto, a dream compared to chilly New England. "You'll never see me again,"

he told his parents. "I've found nirvana."

He got a computer science degree in 1988, then jumped into the region's entrepreneurial hothouse. He launched a software maker, Pure Software. It was a trying time. His engineering background made him too much of a perfectionist. As CEO, he was too hard on himself. He told his board of directors to replace him with a "real" CEO.

"I tried to fire myself — twice," he says. "I was losing confidence."

No dice, the board said. Pure Software eventually was sold to Rational Software for more than \$500 million. Hastings got a pile of loot. He moved to his other passion, public education reform, as head of the California Board of Education.

Then nine years ago, Netflix. The eureka moment arrived when he handed over \$40 in late fees after returning a copy of *Apollo 13* to a rental store. He wasn't especially a film buff; his tastes lean toward foreign and independent films. Still, he figured there had to be a better way, built on the fast-growing Internet. He dangled an irresistible carrot to customers: No late fees, which he knew consumers loathed.

Netflix is now the world's biggest online DVD rental service. It went public in 2002. It has 4.2 million subscribers across the USA. They tap a library of 55,000 titles and 42 million DVD copies shipped from 37 distribution centers.

Netflix's current stock sizzle is a switch from when Hastings was battling new entrants Wal-Mart and Blockbuster. Wal-Mart retreated last year. "Blockbuster was a much bigger threat," Hastings says. "It was a strategic area for them."

A price war drove Netflix shares below \$10 before they rebounded. They closed Friday at \$30.80, down 31 cents for the day but up from \$12.15 a year ago.

Blockbuster is still struggling with its rent-by-mail service. Its shares closed Friday at \$4.81, down 7 cents — and well off its year-ago \$10.28. It's fighting back by aiming for 2 million online subscribers by year's end, up from 1.2 million in December, spokeswoman Karen Raskopf says.

An Oscar boost

At the meeting last month, Hastings wore jeans, a brown leather sport coat and a wall-to-wall smile.

He was in high spirits at the Netflix complex, where bathroom doors bear pictures of Fred Astaire and other stars. Hastings and other top executives briefed staffers in an auditorium. Blockbuster had just reported dismal quarterly results.

The meeting highlight was a traffic report from the previous Sunday's Oscars telecast. Customers swarmed the site throughout the show, adding a combined 33,449 movies to the wish lists they build in their online accounts.

Finally, Hastings asked employees for surveillance reports on nearby Blockbuster closings. An employee shouted the location of one with the enthusiasm of a hunter bringing home a trophy.

The meeting ended, and workers filed past a huge bottle of sparkling wine, festooned with the tag: "To be opened when we surpass five million subscribers."

Hastings hustled to an underground garage for a drive in an unusual hailstorm to a huge distribution center in nearby Sunnyvale, pausing just long enough to check his ever-present BlackBerry.

He's intensely private about his personal life. Asked for names of friends or contacts who know him outside work, he supplied a list of industry veterans. They included Pisano, the motion picture association president.

Pisano, who left the Netflix board when he joined the trade group, says it's "astonishing" that Hastings has scored two start-up home runs. It's all about engineering — Hastings' background. "Business is essentially assembling a whole bunch of moving parts," Pisano says.

To be sure, Netflix's much-praised customer service has had hiccups. Subscribers have complained about its so-called throttling policy, where it sometimes delays shipments to frequent renters to give priority to customers who hold DVDs longer. The company settled a class-action lawsuit over the practice.

To win more business, Hastings pushes to fine-tune Netflix's software and the website's appearance. That was the agenda for the meeting later that afternoon where Hastings groused about the "not interested" button.

Employees demonstrated software that would let customers access the site from cellphones, searching for DVD titles and adding them to wish lists. Hastings warmed to the idea, but asked how it would work on different cellphone screen sizes. The meeting ended on a high note. Hastings called the ideas presented "unbelievably cool."

More changes are afoot. Last week, Netflix announced a further expansion into buying and distributing independent films and TV shows with the hiring of two entertainment industry executives for Netflix's Beverly Hills office.

In Hastings' march to 20 million subscribers, he's aiming for customers such as Jon Murray in Lansing, Mich. Murray, 50, his wife and two teenage daughters rent about two movies a month from Blockbuster. They were Netflix customers two years ago. They quit because they don't like choosing and scheduling movies in advance.

Hastings doesn't give up on the Murrays of the world without a fight. He beats the customer-service drum. The never-ending goal, he says: "connect people to movies they'll love — easily."

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