Palm Dives Headlong Into WebOS

By Scott Moritz 09/18/09 - 11:04 AM EDT

SUNNYVALE, Calif. (TheStreet) -- **Palm** (PALM Quote) is scrambling to get a piece of the holiday action.

The resurgent smartphone maker is taking a few dramatic steps like killing products, boosting advertising and rushing out its new, cheaper Pixi phone to avoid getting left behind in a fierce race with **Apple** (AAPL Quote), **Research In Motion** (RIMM Quote), **Nokia** (NOK Quote) and **Motorola** (MOT Quote).

Palm has been rebuilding itself around the development of WebOS, its mobile phone software. And Thursday, the company officially cast off its former business and all the efforts unrelated to WebOS.

Palm outlined its plans on a conference call with analysts Thursday, saying it would end new production of past generations of phones like the Treo and Centro. Palm also said it will now focus exclusively on its WebOS software and cut ties to **Microsoft's**(MSFT Quote) Windows operating systems. Palm also said, it expects to spend more on advertising push Pre and its new Pixi phone launch at **Sprint** (S Quote) in the fourth quarter.

"It seems a solid strategy but it will not be taken well by investors who are worried that Motorola's arrival at Sprint and the onslaught of smartphones in the second half of this year will overwhelm Palm's efforts to regain share," wrote Charter Equity Research analyst Ed Snyder in a note Thursday.

To make it all happen, Palm needs more cash.

During its fiscal first quarter, Palm burned through $45 million. At the end of August, Palm had $110 million in cash available, down from the $152.4 million available in the prior quarter.

And though Palm said in June that it had enough money to cover all its expenses, the news of yet another fundraiser wasn't a total surprise. Palm says it plans to sell 16 million new shares to the public, effectively diluting existing shareholders by 11%.

The rejuvenated smartphone pioneer did manage to trim more costs from its business. Palm posted an adjusted loss excluding one-time items of a dime, a smaller loss than the 40 cents in the May quarter and the 39-cent pro forma loss a year ago. The dime loss was much less than the 24 cents analysts expected, according to Yahoo! Finance.

Sales for Palm's fiscal first quarter ended last month were $360.7 million, up from the $113 million in the prior quarter but down from the $367 million level last year. Analysts were looking for sales of $298 million.

But looking ahead, Palm warned that the "timing and scale" of new product launches and low demand for older phones will drag down its fiscal second-quarter adjusted sales to a range between $240 million to $270 million. That midpoint of $255 million is well below analysts' estimates of $344.3.

But for the full fiscal year ending in May, Palm raised its target above the $1.6 billion analysts' estimate and called for total sales of $1.7 billion.

Helping to blur the performance of its WebOS effort by failing to disclose how many Pre phones it has sold, the company lumped all phones into one number, saying it sold a total of 823,000 smartphones in the fiscal first quarter. This added to suspicions that No. 3 telco, **Sprint** (S Quote), Palm's exclusive partner, is not the strongest ally in this battle.

Palm CEO Rubenstein is understandably eager to expand the roster of telco he works with.

"Sprint has been a great partner and we are pleased to team with them again for the introduction of the Palm Pixie," Rubenstein said, according to a transcript on SeekingAlpha. "At the same time, we are looking forward to announcing equally strong strategic relationships with additional carriers."

However, for now, and the rest of the year, Palm's one shot at a turnaround hangs perilously in the hands of the one telco that continues to lose customers faster than any other player.

-- *Written by Scott Moritz in New York.*