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Palm shares fall on worries about device sales

Wireless device maker reports strong shipments, but sell-through drops

By [Dan Gallagher](#), MarketWatch

SAN FRANCISCO (MarketWatch) -- Palm Inc. shares dropped Friday following the company's latest quarterly results, which showed a sharp decline in sell-through of its wireless devices.

By late afternoon, Palm shares slid nearly 14% to \$10.11. The stock is still up more than 200% for the year.

The stock was upgraded in the afternoon by Needham & Co. In a note to clients, analyst Charlie Wolf said the results were a disappointment, and that Palm will have to spend heavily to rebuild its brand. But he lifted his rating to hold, saying the shares are now in line with his free-cash-flow valuation model.

"Rebuilding the brand will be a challenge, requiring a large commitment of marketing dollars," Wolf wrote in a note to clients.

Late Thursday, the smartphone maker [/quotes/comstock/15*!palm/quotes/nls/palm \(PALM 10.17, -1.55, -13.23%\)](#) reported a reduction in its net loss along with a strong gain in revenue for its second fiscal quarter. The revenue results topped Wall Street's expectations for the period, and Palm said smartphone unit shipments hit 783,000 for the quarter -- solidly beating the 600,000 units expected by analysts. [Read full story on Palm's results.](#)

However, sell-through of the company's smartphones was only 573,000 units -- down 29% from the previous quarter. Tim Long of BMO Capital Markets said the sell-through figure indicates that more than 200,000 units are building in inventories, "which in our view points to weak demand."

"Twenty percent of the sell-through was legacy products, implying that webOS channel inventory increased by 300K devices in the quarter," Long wrote in a note to clients.

Palm is banking heavily on its webOS devices such as the Pre and Pixi. The company launched the new platform earlier this year with the Pre, but both devices are still available only at Sprint [/quotes/comstock/13*!s/quotes/nls/s \(S 3.72, -0.05, -1.33%\)](#) in the U.S.

EBay tours America

EBay is taking a "mobile boutique" of its top-selling products around the U.S. over the holidays, as part of an effort to win shoppers back to the online marketplace. WSJ's Geoffrey Fowler reports.

While the new operating system has won rave reviews, Palm faces heavy competition in the smartphone space. The BlackBerry from Research In Motion [/quotes/comstock/15*!rimm/quotes/nls/rimm \(RIMM 70.00, +6.54, +10.31%\)](#) and the iPhone from Apple Inc. [/quotes/comstock/15*!aapl/quotes/nls/aapl \(AAPL 195.43, +3.57, +1.86%\)](#) lead the market.

What's more, new devices that use the Android operating system developed by Google Inc. [/quotes/comstock/15*!goog/quotes/nls/goog \(GOOG 596.42, +2.48, +0.42%\)](#) have come on the market from companies such as Motorola, HTC and Samsung.

The company said it expects to sign up new carriers for the devices in the coming year, which it will need to hit its stated growth targets.

"The promise of new carriers in the next few months (read: Verizon) is driving optimistic guidance -- [second half of fiscal 2010] needs to be up 56% over [the first half] to hit the midpoint of the revenue target," wrote Matthew Sheerin of Thomas Weisel in a note to clients.

Betting on future growth

Several analysts remained optimistic on Palm, however, noting that adding more carriers is likely to improve the company's position in the competitive smartphone market.

"A much wider channel and more aggressive promotion than we saw at Sprint suggest it's too early to dismiss Palm or webOS," wrote Ed Snyder of Charter Equity, who believes that Palm will add Verizon and AT&T to its carrier base in early 2010.

Vivek Arya of Bank of America said Palm's results with its current webOS phones have been constrained by "multiple ineffective marketing campaigns; weak and limited Sprint channel; limited apps catalog; heavy competition from iPhone/Androids/RIM; and overhang from customers waiting for Palm to launch products at Verizon and AT&T."

"While Palm currently sells to only ~10 carriers, we note in past it has sold through 100+ channels," he wrote.

Jim Suva of Citigroup maintained a sell rating on Palm shares, however, noting that the company's future profits will likely be crimped by heavy marketing expenditures to promote new devices in a competitive market.

"We believe promotion commotion and stronger competition from Android, iPhone, and Blackberry will make it difficult for Palm to achieve Hero carrier support status and result in Palm spending more of its own money on marketing and promotions," Suva wrote.

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