

iRobot First-Quarter 2013 Conference Call Script

April 23, 2013

Operator:

Good day everyone and welcome to the iRobot first-quarter 2013 financial results conference call. This call is being recorded. At this time for opening remarks and introductions, I would like to turn the call over to Elise Caffrey of iRobot Investor Relations. Please go ahead.

Elise:

This conference call may contain express or implied forward-looking statements relating to the company's financial results and operations for full year 2013 and the second quarter ending June 29, 2013, our expected quarterly and full year 2013 financial performance, the growth and revenue impact of our businesses, our expectations regarding revenue, Adjusted EBITDA, operating cash flow, operating expenses, gross margins, restructuring charges, stock compensation expenses, depreciation and amortization expenses, tax rates, profitability and earnings per share, demand for our home robots, our expectations regarding domestic and international Home Robot revenue, the impact of our Mint[®] robot, the impact of our marketing campaigns and the timing and impact of related investments, the timing and fulfillment of government contracts and orders, demand for our Defense and Security robots and related parts and services, orders for and sales and deliveries of our PackBot, SUGV and FirstLook[®] robots, our Defense and Security contract, product lifecycle and recurring revenue, the mix of product revenue and impact on operating margins, our integration of Evolution Robotics, the impact of our acquisition of Evolution Robotics on our financial results, our plans for expansion, our introduction and delivery of new products and new product capabilities and functionality, the impact of our RP-VITA robot and our Remote Presence business on our financial results, the availability, capabilities and functionality of new technology, our competitive position, our market share, and business conditions. These statements are neither promises nor guarantees, but are subject to a

variety of risks and uncertainties, many of which are beyond our control, which could cause actual results to differ materially from those contemplated in the forward-looking statements. In particular, the risks and uncertainties include those contained in our public filings with the Securities and Exchange Commission. Investors are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. iRobot undertakes no obligation to update or revise these forward-looking statements, whether as a result of new information, future events or circumstances or otherwise.

During this conference call, we will also disclose non-GAAP financial measures as defined by SEC Regulation G, including Adjusted EBITDA, which we define as earnings before interest, taxes, depreciation, amortization, merger and acquisition expenses, restructuring expenses, net intellectual property litigation expenses and non-cash stock compensation.. A reconciliation between Adjusted EBITDA and net income – the GAAP measure most directly comparable to Adjusted EBITDA -- are provided in the financial tables at the end of the first quarter 2013 earnings press release issued last evening, which is available on our website <http://investor.irobot.com/phoenix.zhtml?c=193096&p=irol-news&nyo=0>. A live audio broadcast of this conference call is also available on the Investor Relations page of our website and an archived version of the broadcast will be available on the same Web page following the call. In addition, a replay of this conference call will be available through May 1, 2013 and can be accessed by dialing 630-652-3042, access code 34160563#.

On today's call, iRobot Chairman & CEO Colin Angle will provide a review of the company's operations and achievements for the first quarter of 2013 as well as our business outlook for the rest of 2013; and Alison Dean, iRobot Chief Financial Officer, will review our financial results for the second quarter and provide our financial expectations for the full year 2013 and the second quarter ending June 29, 2013. Then we'll open the call for questions.

At this point I'll turn the call over to Colin Angle.

Colin:

Good morning and thank you for joining us.

We kicked off 2013 with an outstanding quarter. The results and outlook for our Home Robot business are excellent. We are very excited to have begun shipping our RP-VITA telemedicine robot in Q1 and our Defense & Security business delivered solid results.

Based on our view of the rest of the year, we are increasing our full-year financial performance. We now expect to deliver fiscal 2013 revenue of **\$485 to \$495** million, EPS between **\$0.80 and \$1.00** and Adjusted EBITDA of **\$55-\$61** million. The revenue increase is being driven by better than anticipated Home Robot demand in the United States. The full-year expectations for our D&S business remain unchanged. Improvements in gross margin, rapid integration of Evolution Robotics' (ER) manufacturing processes and product rollout, improved operating efficiency in D&S and tighter expense control will each contribute to increased profitability and enable us to deliver on our commitment to profitable growth.

Now, I'll take you through some of the details of the first quarter and our expectations for the rest of 2013.

Total Q1 revenue of **\$106** million, Adjusted EBITDA of **\$15** million and EPS of **\$0.29** all exceeded our increased expectations.

In the first quarter, domestic revenue growth of **44%** fueled a **14%** year-over-year increase in Home Robot revenue. Lean inventory levels and strong Q4 sell through across all domestic retailers helped drive the Q1 growth. Mint and expanded distribution of the Roomba 600 and 700 robots to retailers have all contributed to the increase in Home Robot revenue. Our U.S. retailers reported strong sell through again in Q1, and we expect better full-year growth than we did in February when we first shared our

outlook for fiscal 2013. We expect the domestic market to continue to be strong as our U.S. advertising and media investment ramps in Q2.

In the second quarter last year we launched one of the largest domestic marketing campaigns in iRobot history. Last year's program contributed to domestic annual net growth of roughly **30%**. The objective of these programs is to increase awareness of iRobot and position our home robots as mainstream solutions to practical problems. Over the past year we have talked about the importance of investing in brand and marketing to support our strategic growth plans. We saw the positive impact of our investments on domestic results in 2012 and expect this program to drive even greater awareness in the U.S. market in 2013.

Our strategy for this year's campaign is similar to that of last year's. We will be continuing our successful "iRobot Do You?" advertising on channels that reach our modern professional target audience, such as HGTV, Travel and DIY, where they ran last year and expanding to Bravo, CNBC and BBC America this year. In addition, we will be running an infomercial for Mint on Travel, Style, Lifetime Movie Network, DIY and BBC America which were high performing sites for the product in 2012.

Overseas, demand in Japan was very strong and China's performance was consistent with our expectations. We did experience some softening in EMEA, due to macros, resulting in a relatively flat year-over-year international Q1. We are closely managing inventories in EMEA so we can ensure that there is not excess product in the channel.

In Q2, we expect the European launch of Braava, our iRobot-branded version of the Mint robot, coupled with continued Roomba sales into China, to drive overseas growth in Home Robots while domestic revenue will be driven by further penetration of our core products.

Turning now to our Defense & Security business, Q1 results exceeded our expectations due to the timing of government PLR orders for PackBot and SUGV robots. Greater DoD Q1 demand for spares, service and training, to support the iRobot fleet of roughly

5,000 unmanned ground vehicles, resulted in higher quarterly revenue than we anticipated.

Last quarter the government disclosed a **\$14.4** million order for more than **600** FirstLook robots. This order was anticipated and included in our 2013 expectations. In addition we received a **\$7** million international order at the beginning of the quarter which we discussed on the last call. We now have more than **80%** of the roughly **\$50** million in 2013 expectations in either booked orders or funded backlog and are highly confident in achieving the full year number which will be down from last year.

Also important to note is that we expect non-DoD revenue to comprise more than **40%** of 2013 D&S revenue compared with **16%** of 2012 revenue. This market diversification is important given the near term uncertainty created by competing budget priorities in Washington and changes in the Defense Department's mission requirements.

We began shipping the RP-VITA to InTouch in Q1 2013. To date we have shipped roughly 2 dozen robots on which ITH has integrated their proprietary technology for telemedicine to facilitate its use in remote diagnosis and treatment. Half of these robots have been shipped by ITH to both new and prior users of InTouch's products.

These are very early days but initial feedback has been positive. We expect to sell additional units this year but our Remote Presence business unit is not expected to generate meaningful revenue in 2013. We are very excited about our progress in this segment and do expect the product to be a growth driver over the next couple of years.

In summary, first quarter results exceeded expectations and some of the drivers are expected to result in favorability for the year, so we are increasing our full year expectations.

Before turning the call over to Alison to review our first quarter results and Q2 expectations in more detail, I wanted to comment on last week's marathon tragedy here

in Boston. Shortly after the two explosions near the Boston Marathon finish line, we contacted the Massachusetts State Police to offer assistance and robots in addition to the ones they owned. On Friday, during the intensive manhunt, our robots were once again front and center, keeping law enforcement officials out of harm's way. The Mass State Police expressed their gratitude for iRobot's timely responsiveness.

The company's response to the Boston Marathon bombings continues a long tradition of iRobot's responsiveness in a time of crisis and it speaks volumes to our values and commitment as an organization.

Alison

Thanks Colin.

Revenue in the first quarter was **\$106** million compared with **\$98** million last year. Revenue, earnings per share and Adjusted EBITDA all exceeded expectations.

Earnings per share for the quarter were **\$0.29**, compared with **\$0.02** last year, and Adjusted EBITDA for Q1 was **\$15.2** million, compared with **\$6.1** million last year. Q1 EPS this year includes an **\$0.08** benefit from 2012 and 2013 investment tax credits,

In Q1, Home Robot units grew **7%** while revenue of **\$93** million increased **14%** from a year ago. The mix of higher ASP Roomba 600 and 700 robots this year accounted for the difference in unit growth versus increased revenue. We expect year-over-year double digit revenue growth to continue throughout 2013 driven by both product mix and unit volume. Based on current indications from our retailers and distributors, we anticipate revenue to be relatively level from Q2 through Q4. Total domestic revenues were up **44%** in Q1, following a **32%** increase in Q4, and compared with **21%** growth in Q1 last year, due to expanded distribution of Roomba 600 and 700 robots and the inclusion of Mint. Importantly, sell through, at our top **5** domestic retailers, was up **36%** year-over-year reflecting consumer demand and the impact of our marketing programs. International revenue was relatively flat for the quarter at **\$61** million and comprised approximately **66%** of Home Robot revenue.

Defense & Security revenue of **\$11** million was higher in Q1 than anticipated but down from a year ago due to both lower contract and product revenue, as expected. Defense & Security product revenue was **\$8** million in the first quarter, **\$6** million of which was product lifecycle revenue (PLR).

As a result of the 2012 corporate realignment, in which we centralized our engineering and operations units, we reclassified certain income statements costs. This change **does not** impact earnings per share or Adjusted EBITDA but is intended to provide additional financial statement transparency. The change decreases cost of sales and

increases operating expense by equal amounts. With our quarterly SEC 8k submission, we have furnished **4** years of historical financial information presenting income statement costs for those periods in a manner comparable to the reclassified 2013 presentation.

Based upon reclassified costs, Q1 gross margin was **43.8%** compared with **38.4%** last year, and opex was **35%** of revenue compared with **38%** last year. The year over year improvement in gross margin was driven primarily by favorability of Home Robot product mix, specifically expanded distribution of higher margin Roomba 600 and 700 robots this year compared with lower margin Roomba 500 robots in 2012. Tighter cost control and higher revenue in Q1 2013 resulted in improved operating expense as a percentage of revenue.

At the end of Q1, we had cash, including investments, totaling **\$138** million compared with **\$182** million last year and operating cash flow was roughly breakeven.

In Q2, we expect revenue of **\$128-\$133** million, driven by strong growth in Home Robots. We expect EPS in the range of **\$0.15** to **\$0.20** and Adjusted EBITDA of **\$13-\$16** million. Keep in mind that our seasonal investments in marketing, that Colin discussed, will be substantial in Q2 and Q4 as they were last year and that spend will impact EPS and Adjusted EBITDA in those quarters. Our full year revenue expectation of **\$485 - \$495** million assumes Home Robot revenue will grow approximately **22%** to **\$435 - \$440** million and comprise roughly **90%** of total company revenue. Our expectations for Defense & Security revenue remain unchanged at **\$45** to **\$55** million for the full year.

Last quarter we provided an estimated 2013 effective tax rate of **8-10%** based on the impact of the 2012 and 2013 investment tax credit for R&D. Driven by our revised full year profit expectations, we now estimate a full year rate of approximately **20%**. For Q2 through Q4 we are estimating roughly **25%**.

In summary, for the full year, strong domestic sales growth, the expanded distribution of Mint and Braava, and further penetration into long term international markets will drive

the Home Robot business. Orders for FirstLook, sales to foreign countries, and PLR will generate expected revenue in our Defense & Security business.

I'll now turn the call back to Colin.

Colin

Our results in the first quarter exceeded our increased expectations due to strong performance by our Home Robot business.

As we look at the rest of the year, we will diligently balance our investment in technology and the iRobot brand, with our commitment to deliver profitable growth. This year we are further deepening our presence in existing markets and expanding in new geographic markets enabled by our investments. Beyond this year, we see tremendous growth opportunities for our home robots and are very excited about the potential for our Remote Presence robots. While the current military climate is disappointing, the longer term drivers remain intact for our Defense & Security business, and we are well-positioned for those markets.

With that we'll take your questions.

Following Q&A

Colin

That concludes our first quarter earnings call. We appreciate your support and look forward to talking with you again in July to discuss our Q2 results.

Operator -That concludes the call. Participants may now disconnect.