

iRobot First-Quarter 2014 Conference Call Script

Operator:

Good day everyone and welcome to the iRobot first-quarter 2014 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:

Thank you and good morning. Before I introduce the iRobot management team, I would like to note that statements made on today's call that are not based on historical information are forward-looking statements made pursuant to the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995.

This conference call may contain express or implied forward-looking statements relating to the company's financial results and operations for fiscal 2014 and the second quarter ending June 28, 2014; the growth, performance and revenue impact of our businesses; our expectations regarding profitability; our expectations regarding revenue, the rate of revenue growth, Adjusted EBITDA, Adjusted EBITDA margin, operating cash flow, gross margins, operating expenses, marketing expenses, research and development expenses, general and administrative expenses, operating margins, restructuring charges, stock compensation expenses, depreciation and amortization expenses, tax rates, shares outstanding and earnings per share; demand for our home robots; our expectations regarding international expansion and international home robot revenue; the impact of our continued investment in advertising, our brand and quality initiatives; the impact of our Roomba 880[®] and Scooba[®] 450 robots on our financial results; the impacts of our investment in navigations and mapping capabilities and our continued investment in new technology; the timing and fulfillment of contracts and orders for our Defense & Security robots; demand for and adoption of our Defense and Security robots and related parts and services; the mix of product revenue and impact on

operating margins; our introduction and delivery of new products and new product capabilities and functionality; 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 expense, restructuring expense, net intellectual property litigation expense and non-cash stock compensation expense. A reconciliation between Adjusted EBITDA and net income – the GAAP measure most directly comparable to Adjusted EBITDA - is provided in the financial tables at the end of the Q1 2014 earnings press release issued last evening, which is available on our website <http://investor.irobot.com/phoenix.zhtml?c=193096&p=irol-EventDetails&EventId=5041607>. 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 April 30, 2014 and can be accessed by dialing **630-652-3042**, access code **35939102#**.

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 2014 as well as our

outlook on the business for 2014; Alison Dean, Chief Financial Officer, will review our financial results for the first quarter of 2014; and, Colin and Alison will also provide our financial expectations for the second quarter ending June 28, 2014 and fiscal 2014. 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.

Last evening, we reported results exceeding our expectations. Home Robot revenue grew **17%**, driving first quarter company revenue up **8%** to **\$114** million despite the anticipated quarterly year-over-year decline in Defense & Security revenue. Earnings per share were **\$0.18**. Adjusted EBITDA was **\$14** million or **12%** of revenue. All three of our businesses met our expectations and made progress against their 2014 goals.

Based on our Q1 results and our outlook for the rest of 2014, our full-year financial expectations remain unchanged. We continue to expect revenue of **\$560** to **\$570** million, driven by Home Robot growth of **17-20%**; EPS of between **\$1.00** and **\$1.15** and adjusted EBITDA of **\$74** to **\$78** million or roughly **14%** of revenue. These expectations are a strong next step in progressing towards our three year targets.

Now I'll take you through some of the details of the first quarter and our expectations for the rest of 2014.

- Our Home Robot business continues to deliver excellent growth on an ever-increasing base. Revenue growth in all three geographic regions contributed to year-over-year growth of **17%** for the quarter;
- Our Defense & Security business delivered results consistent with our expectations, and;
- Our Remote Presence business announced the product launch our new Ava 500 Video Collaboration robot.

Quarterly Home Robot revenues were driven by **31%** year over year growth in the domestic market. Sell through at our top five retailers increased **28%** over last year. In the fourth quarter of last year, we launched the revolutionary Roomba 880 and sales of the product through the first quarter on our website have exceeded those of all of our other new products over the same timeframe. The product is now available in limited domestic retailers and in select European and Asian markets.

Likewise, the Scooba 450 robot, which we launched in early Q1 on our website, is enjoying success. Its improved cleaning performance and significantly improved easy-to-clean design is resonating with customers. We expect both products to contribute to Home Robot growth throughout 2014.

International Home Robot revenues grew **9%** year-over-year in the first quarter and we expect to see increased growth overseas as the year progresses and we expand distribution of Roomba 880 and Scooba 450 as well as record a full year of Braava revenue. The only anticipated growth attributable to geographic expansion in 2014 will be within China where we expect the number of doors to expand from roughly **420** doors in 2013 to **500** doors in **100** cities. As anticipated, EMEA returned to growth this quarter fueled by introduction of Roomba 880 into the region and strong sell through of Braava. EMEA grew approximately **9%** and revenue in APAC was driven by strong demand in China.

Our continued investment in advertising and our brand will help drive increased awareness of the category and growth of the global robotic vacuum cleaner market; and we are optimistic about our ability to capture an increasingly larger slice of the revenue pie. As always, we will balance continuing investments to support growth initiatives with generating increased profitability.

Turning now to our Defense & Security business, first quarter results were in line with our overall expectations.

Visibility into the DOD market remains poor. We have several international opportunities that we are expecting to close this year. Selling into that market is challenging given the longer sales cycles and it is difficult to predict the quarter in which we will close them. We are continuing to sell spares, service and support for the installed base of more than 5,000 iRobot unmanned ground vehicles and have begun using distributors to help us access the fragmented first responder market.

In Q1, we launched the Ava 500 video collaboration robot in the United States, Canada and limited European markets through select certified Cisco resellers. Our beta program, including Fortune 500 companies, has been successfully completed and we have received our first orders. With the benefit of telepresence, Ava 500 helps globally dispersed teams work more closely together without the need for costly and time-consuming travel. We are very excited to add a second remote presence robot to our product offerings.

Our RP-VITA telemedicine robot continues to gain traction as doctors, hospitals and patients realize the value of remote diagnosis. Much has been written recently about its advantages. In fact, telemedicine has been spurred in part by the Affordable Care Act, which is funneling more patients into a system plagued by physician shortages. The feedback we are getting from doctors using our robot is that the user interface enabled by our navigation technology is proving to be highly valued in the more sophisticated areas of telemedicine.

With the launch of our remote presence robots, we have begun talking more about the importance of robot navigation and our leadership role in the space. After more than a decade of research, we are fielding robots with the capability of building maps and using them to precisely move about the environments in which they operate. This capability is creating opportunities for robots to perform more valuable work, more efficiently. Today, the enabling technology – Simultaneous Localization and Mapping (SLAM) is expensive as it requires lasers and significant computation, though it works extremely well and safely as evidenced by RP-VITA's FDA approval. Soon, a new generation of SLAM, visual SLAM, based on replacing lasers with low cost cameras will usher in a new generation of navigation robots. iRobot is a pioneer in vSLAM, holding exclusive access to critical technology, including many of the earlier filed patents in the technology, which positions us extremely well as the industry accelerates. It is our intent to continue to invest in this critical technology and the economic opportunities it unlocks.

In summary, we are off to a good start in 2014:

- Home Robot revenue grew **17%** and will continue to grow in both domestic and overseas markets driving full year 2014 total company growth of **15-17%**;
- We will continue to invest in marketing programs and ongoing quality initiatives that drive profitable Home Robot growth;
- We will expand our reach in the health care telepresence and video collaboration markets, and;
- We will continue to invest in key technologies that extend our market-leading position in practical robotics.

I will now turn the call over to Alison to review our first quarter results in more detail.

Alison

We delivered first quarter revenue and earnings per share slightly ahead of expectations and Adjusted EBITDA in-line with our expectations. Revenue of **\$114** million increased **8%** from Q1 last year driven by growth in Home Robot revenue. EPS was **\$0.18** for the quarter compared with **\$0.29** for the same period last year. Q1 Adjusted EBITDA was **\$14** million compared with **\$15** million last year. Q1 2013 earnings per share included an **\$0.08** benefit from investment tax credits.

Domestic Home Robot revenue growth was **31%** for Q1 reflecting strong online demand and expanded distribution of our new Roomba 880, as well as the introduction of Scooba 450. International revenue grew **9%** for the quarter driven by strong performance in China and EMEA. The introduction of Roomba 880 in select European markets and the first quarter of Q1 contribution of Braava sales overseas drove the improved performance in EMEA. We expect the international growth rate to increase throughout the year as the Roomba 880 and Scooba 450 are more widely distributed.

Defense & Security revenue of **\$6** million in Q1 was down year over year. Roughly **60%** of this quarterly revenue was from PLR and the balance was from robot sales.

For the total company, gross margin was **45%** for the first quarter 2014, slightly higher than the same quarter last year due to revenue mix of higher margin Roomba 880s.

Q1 operating expenses were **38%** of revenue, up from **35%** in Q1 last year. Increased R&D spending and higher marketing costs associated with the new product launches accounted for the increase. In Q2, you should expect to see higher marketing costs as the first phase of our 2014 advertising campaign kicks off. R&D will decline as a percent of revenue and we will continue to leverage our G&A costs. We still expect operating expenses of approximately **36%** of revenues for the full year as we discussed last quarter.

We ended the quarter with **\$185** million in cash and DII of **61**. Earlier this month, we announced a **\$50** million stock repurchase program to replace the **\$25** million program that expired at the end of March. We believe we can take opportunistic advantage of volatile market conditions to buy back our shares while maintaining the flexibility to make strategic investments in our future.

Now I'd like to provide you with additional detail for our Q2 financial expectations. The outlook for our Home Robot business remains very strong and will drive Q2 results.

We expect second quarter revenue of **\$138** to **\$145** million, an increase of **6-11%** over Q2 last year, EPS of **\$0.15** to **\$0.25**, and Adjusted EBITDA of between **\$13** and **\$17**. Keep in mind that EPS for Q2 2013 included a **\$0.07** tax benefit that we received in the quarter. We anticipate Home Robot revenue to grow **14-16%** in Q2 2014 over last year while D&S revenue is expected to decline versus Q2 last year.

There are a number of orders that will fall in either Q2 or Q3 but the precise quarterly timing is uncertain. As a result, our revenue range is wider than typical. Likewise, profitability will vary depending on the product mix of the orders so we have provided a range that addresses the potential variety of outcomes. We are confident that we will receive these orders this year which is why we have not changed full-year expectations. For the full year, we continue to expect revenue to grow sequentially throughout the year, based on our Home Robot new product distribution plans as we discussed last quarter, with Q4 growing substantially over the fourth quarter of 2013.

I'll now turn the call back to Colin.

Colin

We are off to a strong start in Home Robots and we expect that business to drive second quarter and full year 2014 top and bottom line growth; our defense business, though stable, will be down year over year in the second quarter before starting to grow in the second half; and we are optimistic that remote presence will continue to gain

traction in the video collaboration market while further expanding into healthcare's emerging telemedicine market.

With that we'll take your questions.

Following Q&A

Colin

That concludes our first quarter 2014 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.