

iRobot First-Quarter 2015 Conference Call Script

Operator:

Good day everyone and welcome to the iRobot first-quarter 2015 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, operations and performance for fiscal 2015 and the second quarter ending June 27, 2015, the growth, performance, revenue impact and prospects of our businesses including the international growth and revenue of our businesses, our expectations regarding seasonality and predictability 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, inventory, shares outstanding and earnings per share, the impact of our continued marketing investments, the impact of our continued investments in technology, demand for our home robots, demand for our wet floor care robotics, the mix of product revenue, and the impact on operating margins, the timing and fulfillment of government contracts and orders, demand for and adoption of our Defense & Security robots and related parts and services, our plans for expansion, 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 2015 earnings press release issued last evening, which is available on our website <http://investor.irobot.com/phoenix.zhtml?c=193096&p=irol-eventDetails&EventId=5168625>. 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 29, 2015 and can be accessed by dialing **630-652-3042**, access code **38036249#**.

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 2015 as well as our outlook on the business for 2015; Alison Dean, Chief Financial Officer, will review our

financial results for the first quarter of 2015; and, Colin and Alison will also provide our financial expectations for the second quarter ending June 27, 2015 and fiscal 2015. 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.

Our first quarter results exceeded our expectations. Home Robot revenue was up slightly over last year while D&S revenue grew **17%**. Earnings per share were **\$0.16**. Adjusted EBITDA was **\$13** million or **11%** of revenue.

Based on our Q1 results and our outlook for the rest of 2015, we continue to expect 2015 revenue of **\$625** to **\$635** million, driven by Home Robot growth. We are reducing the high end of our EPS and Adjusted EBITDA ranges for 2015 and now expect EPS of between **\$1.25** and **\$1.35** and adjusted EBITDA of **\$85** to **\$90** million or roughly **14%** of revenue.

These expectations reflect our confidence that Home Robot revenue will grow **11-13%** for the full year as we discussed in February, with U.S. growth in the mid-teens and overseas in single digits. The market in China is very strong while, EMEA and Japanese markets continue to be negatively impacted by macros.

Also included in our revised expectations are incremental marketing investments. It is important for us to continue to strengthen brand and awareness in the United States and China, growth regions not impacted by macros, as well as support our international partners through difficult economic times. We need to ensure traditional levels of demand generation spending continue, so they are well positioned for growth when markets improve. For 2015, that means a larger financial investment than we contemplated in the expectations we provided in February.

Now I'll take you through some of the details of the first quarter and our expectations for the rest of 2015. In the first quarter:

- Our Home Robot business was up **3%** year over year as expected, and;
- Our Defense & Security and Remote Presence businesses also delivered results consistent with our expectations.

International Home Robot revenues were up **5%** year over year driven by strong growth in EMEA and China from higher Roomba 800 sales. Last year we began shipping limited product to select international distributors late in Q1 compared with a full quarter of availability this year. EMEA grew roughly **20%** while APAC was down approximately **10%**. Growth in China was strong but not enough to offset the expected year-on-year decline in Japan. While macros continued to negatively impact consumer spending as we expected, we believe the worst is behind us. Our Japanese distributor reported an improvement in sell through at the end of Q1 but it will take a while for this trend to positively impact our revenue.

In the United States, Q1 sell through at our top five U.S. retailers increased roughly **20%** over last year. Strength in this market is masked by the **30+%** growth in Q1 2014 last year from distribution of the then new Roomba 800 into retail channels. As we've consistently discussed, year-over-year quarterly comparisons can be difficult due to the timing of new product introductions and where we are in the distribution cycle of those products.

While Roomba is driving overall revenue growth this year, we are seeing Braava doing well in China where it's been sold for less than a year. We continue to see the wet floor care market as a growth opportunity as we improve its positioning and better articulate its value proposition.

In Q2, we expect U.S. revenue to grow in the mid-teens, and total Home Robot revenue to be flat year-over-year. International revenue is expected to decline when compared to the **20%** growth in Q2 last year from the initial distribution of Roomba 800.

Turning now to our Defense & Security business, first quarter results were in line with our overall expectations with more than **70%** of revenue from spares and support or PLR.

We have good visibility through the second quarter when D&S revenue is expected to be more than double Q2 2014. Delivery of robots and services under the Canadian contract we won last year will comprise most of the Q2 revenue.

We have a solid pipeline of opportunities for both the DoD and international customers but the timing of orders and delivery is uncertain at this point. We have less visibility in the second half of the year.

We remain optimistic about the long term prospects for this business in both the DoD and international markets. We have a number of viable international opportunities, but selling into that market is challenging given the longer sales cycles and the complexities of working with foreign governments. We are continuing to sell spares, service and support for the installed base of more than 5,000 iRobot unmanned ground vehicles and we have increased our use of distributors in North America to assist us in capturing new opportunities with the DoD, Nuclear and to help us access the fragmented first responder market.

Turning now to our Remote Presence business, we've had some exciting developments over the past couple of months. We've previously talked about the importance of developing a list of referenceable accounts that we can leverage to help accelerate sales of our mobile telepresence robot, Ava 500. I am pleased to report that We recently installed multiple Ava 500s at Fidelity Investments FCAT center in Boston for various applications including collaboration and tours for internal and external customers as well as partners.

As we have said, our primary focus for Ava in 2015 will be scalability as we actively work with customers to shorten the sales cycle and simplify the implementation process. With marquee accounts like Fidelity we are progressing towards those goals.

In summary, we are off to a good start in 2015:

- In the first quarter, Home Robot revenue grew year over year despite the macro headwinds and is expected to grow in both domestic and overseas markets for the full year 2015;
- We will continue to invest in marketing programs to drive growth opportunities in non-FX impacted regions while helping our international partners weather the weak economies in their 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, earnings per share and Adjusted EBITDA slightly ahead of expectations. Revenue of **\$118** million increased **3%** from Q1 last year driven by growth in Home Robot and D&S revenue. EPS was **\$0.16** for the quarter compared with **\$0.18** for the same period last year. Q1 Adjusted EBITDA was **\$13** million.

Domestic Home Robot revenue was flat year-over-year in Q1. Keep in mind that in Q1 2014, domestic revenue was up **31%** from sales of our new Roomba 880, as well as the introduction of Scooba 450. International revenue grew **5%** for the quarter driven by strong performance in EMEA. The fully distributed Roomba 880 drove EMEA revenue up more than **20%** year over year. In APAC, China revenue doubled year over year but that was not enough to offset the expected decline in Japan. As a result, total APAC revenue was down roughly **10%** in Q1 compared with last year. We continue to expect growth in all three regions for the full year with the U.S. growing in the mid-teens and overseas growth in single digits.

Defense & Security revenue of **\$7** million in Q1 was up **17%** year over year. Roughly **70%** of this quarterly revenue was from PLR and the balance was from robot sales.

For the total company, gross margin was **45.5%** for the first quarter 2015, up slightly from the same quarter last year.

Q1 operating expenses were **39%** of revenue, up from **38%** in Q1 last year primarily due to increased R&D spending. In Q2, we expect opex in the low **40's** as a percent of revenue reflecting our normal higher Q2 marketing spending and some of the additional investments Colin discussed. For the full year we now expect operating expenses could be as high as **37%** of revenues up from our original 2015 target of **35-36%**.

We ended the quarter with **\$221** million in cash and DII of **71**. DII was higher than normal this quarter as we shipped additional product to the US to ensure that we had sufficient product to meet retailers' Q2 orders given the west coast longshoremen's

slowdown. We expect Q2 ending inventory to return to our normal level of roughly **60** days.

Last month, we announced a new **\$50** million stock repurchase program to replace the current stock repurchase program when it ends on April 30, 2015. 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 continues to be negatively impacted by overseas macros, and challenging comps regionally from Roomba 800 sell in last year. Therefore, we expect Q2 year-over-year revenue to be flat. We expect strong revenue growth in our D&S business driven by delivery of robots and services under the Canadian contract.

We expect second quarter revenue of **\$143** to **\$146** million, an increase of roughly **4%** over Q2 last year, EPS of **\$0.02** to **\$0.06**, and Adjusted EBITDA of between **\$8** and **\$10** million. Given this view, we now expect roughly **58%** of revenue to be generated in the second half of 2015.

I'll now turn the call back to Colin.

Colin

We are off to a good start in 2015 as we weather global macros and invest to drive Home Robot growth. Our D&S business will have a strong first half and we are closely monitoring opportunities in our pipeline for more visibility in the second half.

With that we'll take your questions.

Following Q&A

Colin

That concludes our first quarter 2015 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.