iRobot Fourth-Quarter and Full Year 2009 Conference Call Script

February 17, 2010

Operator:

Good day everyone and welcome to the iRobot fourth-quarter and full year 2009 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 tax rate for fiscal 2010, the first quarter ending April 3, 2010 and the second quarter ending July 2, 2010, our financial position at the end of fiscal 2010, demand for the company's products and services, the timing of funding and contract awards under the FCS Program (now referred to as the Brigade Combat Team Modernization program), our plans for expansion and new product development, backlog and demand for our Government and Industrial robots, mix of product revenue 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 various 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 and non-cash stock compensation expense. A reconciliation between net income– the GAAP measure most directly comparable to Adjusted EBITDA - and Adjusted EBITDA is provided in the financial tables at the end of the Q4 2009 earnings press release issued last evening, which is available on our website www.irobot.com.
A live audio broadcast of this conference call is available on the Investor Relations page of our website and an archived version of the broadcast will be available on the same Web page shortly. In addition, a replay of this conference call will be available through February 25, 2010 and can be accessed by dialing 617-801-6888, access code 31678547.

On today's call, iRobot Chairman & CEO Colin Angle will provide a review of the company's operations and achievements for the fourth quarter and full year 2009 as well as our financial expectations and outlook for the business for 2010; and John Leahy, Chief Financial Officer, will review our financial results for the fourth quarter and full year of 2009 and provide additional detail on our 2010 financial expectations. 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.

I'm pleased to report that we delivered record quarterly revenue of more than **$100** million and full year revenue of nearly **$300** million. Earnings per share and Adjusted EBITDA significantly exceeded expectations for the fourth quarter and full year.

Lifetime sales of our home robots surpassed five million units. And as we recently announced, deliveries of PackBot robots have exceeded 3,000. Both are significant milestones for the company and validation that demand continues to be strong for our products.

Our continued focus on strengthening the balance sheet resulted in a year-end cash and investments position of **$77** million, up significantly from **$41** million a year ago. A critical component of improving our financial position over the past year has been driving Adjusted EBITDA and operating cash flow. Adjusted EBITDA was **$21 million,** up **61%** from 2008 and we generated **$41** million of operating cash flow in 2009, compared with **$19** million in 2008.

2009 marked an important step to achieving our three year strategic goals, maintaining our industry-leading position of delivering robotic technology-based solutions that leverage common platforms and software, and the financial goals that underpin our strategic plan, which are:

- Mid to high teen revenue CAGR;
- Mid-teen Adjusted EBITDA margins and;
- High single-digit operating cash flow margins

We recently added Paul Sagan, chief executive officer of Akamai Technologies, Inc., to our board of directors. Paul brings extensive technology, consumer and global business expertise to iRobot at a critical time in our development, given our projected global growth, and we are very pleased to have him join our team.

We began 2010 with **$42** million in backlog in our G&I business, the highest level in our company's history. This positions us well to deliver another year of solid financial performance, with increased top and bottom line growth, while continuing to invest in the future of our business, as we keep making progress on delivering against our strategic plan.

In Home Robots, strong demand for our Roomba 500 robots in international markets continued to fuel Home Robot growth overseas. International Home Robot revenue was up **35%** from the prior year and represented more than half of 2009 Home Robot revenue. We expect to see significant overseas growth in 2010 within existing markets. In addition we are exploring opportunities for market expansion into Latin and South America as well as Eastern European countries, but we assumed minimal contribution from these new markets in our 2010 financial expectations. In the United States, our strong Q4 sell through results coupled with closely managed production have driven replenishment orders ahead of expectations. As a result, we anticipate first quarter 2010 U.S. revenues will be higher than 2009 Q1 U.S. revenues. Executing against our plan of tightly controlling inventory while fulfilling customer commitments was critical given the uncertainties we faced in this past holiday season.

2009 was a year of revitalization for our home robots business. We hired a new division president with a strong general management background in operations and he has successfully built a team of experienced product development, finance and operations professionals, refined the home robot strategy and implemented disciplined processes to support continued profitable growth. With all signs pointing to some level of economic recovery in the U.S. in 2010, we are well-positioned with our core products to capitalize on improving conditions.

There is significant opportunity for additional penetration of Roomba in existing markets. In North America alone, the market for vacuum cleaners costing more than **$200** was **$1** billion in 2009 and we generated revenues from the sales of Roomba of approximately

10% of that amount. Functional differentiation, effected through continuous platform upgrades and increased software content, will enable us to position Roomba products as good, better, best which will also help drive higher margins.

Likewise, overseas, the markets are relatively untapped. Both Europe and Asia provide significant opportunity for expansion. In Europe, we estimate our position as **11%** of the **$600** million annual addressable market and in Japan and Korea, **12%** of the **$125** million annual market.

I am very excited about the opportunity for home robots. We have the team in place to take us forward, a tremendous opportunity for expansion with existing products in our current markets and a well defined plan to add new distribution channels internationally. As we look to the development and introduction of new products for the home, we will focus on those that not only meet the needs of our customers but also leverage our investments in order to continually improve margins.

Given our position and the recovering economy, I am cautiously optimistic about our year over year expectations for growth in all segments of our home robot business.

In our Government & Industrial division, we also delivered a record quarter driven by the shipment of PackBot FasTac robots, ordered under contracts from the Robotics Joint Program Office. Quarterly contract revenue, up **36%** year over year, was fueled by the government's acceleration of funding under the FCS development contract for SUGV, the Small Unmanned Ground Vehicle. We expect funding under this program to continue to grow in 2010 to support transition to a production program.

In 2009 we began to deliver SUGV 310s, a variant of the robot that will be a key growth driver over the next couple of years as it is rolled out to the infantry. In February we received a **$17** million order for the iRobot/Boeing developed robots, bringing the total units ordered to date to **229**. At the customer's request we did not issue a press release nor can we discuss the details of the contract.

I'd like to take a minute to review the status of this program and our expectations for the different SUGV variants in 2010.

As we discussed last quarter, the FCS program is now referred to by the Army as Brigade Combat Team Modernization (BCTM) program. In December, the Increment 1 Infantry Brigade Combat Team capabilities completed a Defense Department Milestone C review, under which the maturity, requirements, testing and evaluation and production plans for Increment 1 capabilities, including SUGV, were reviewed and approved. We submitted an LRIP (Low Rate Initial Production) proposal to support the first increment, of an additional **124** SUGVs, and expect to be on contract for this effort in the second quarter of 2010.

We are currently developing and delivering **3** SUGV variants to the marketplace:

- The SUGV 310 - of which we delivered approximately **50** units in 2009;
- The SUGV 320 - for which we are expecting the LRIP contract just described, and;
- A Commercial Off-The-Shelf version of the SUGV 320 for which we are pursuing contracts to supply to infantry current forces.

While built on the same **20** pound chassis, each variant has distinct functionality addressing the needs of different customers from EOD, special ops and engineer teams to the infantry current forces. From the time we began developing the SUGV several years ago, we expected ALL of the current forces to want them once the SUGVs were fielded to the FCS brigade soldiers.

When Defense Secretary Gates terminated the program formerly known as FCS and restructured its successor referred to as BCTM, he accelerated the development of the SUGV 320 and expanded its deployment to all of the Army Combat Brigades. His action was a strong vote of confidence in the SUGV, and provided increased support for our SUGV market estimates. The Army has estimated that its SUGV requirement exceeds **8,000** robots and has documented this need in a draft Capability Production

Document. When this requirement is added to the projected demand from the Marines and other services, the international market, and the domestic civil market we estimate an overall market demand of between **10,000 – 20,000** SUGV robots.

Beyond supplying robots to the U.S. Government, we continue to make inroads in international markets. International revenue increased **69%** to **11%** of G&I product revenue compared with **6%** last year. In 2009 we closed our first major Foreign Military Sale to Iraq, and sold robots in **5** new countries bringing our international presence to **19** countries We are well positioned with a team and product offerings to build upon and accelerate international growth in 2010.

In summary, both of our businesses performed well in a difficult environment while we continued to invest in and build upon our competitive advantages. As a leader in delivering robotic technology-based solutions, we passed **2** significant milestones; **5** million home robots sold and **3,000** government robots delivered, but we must continue to make investments in critical technologies that widen our competitive moat.

We have a robust, expanding and defensible intellectual property portfolio. Our proprietary Aware® 2 robot intelligence software, which has dynamically evolved from continuing investment over the past 10 years, is an essential element of our business growth strategy. Increasing software and IP content on our robot platforms will enable us to provide increased functionality to customers in both divisions, while generating sustainable higher margins.

- In G&I, our customers are demanding increased mission autonomy that allow robots to perform the more dangerous tasks which will be enabled by more advanced software.
- In home robots, we see software playing a bigger role in products, AND
- We believe there is a great opportunity for more software enabled products in the healthcare sector. During the fourth quarter of 2009 we announced the formation of our Healthcare Business Unit. We hired a seasoned technology executive to

explore ways in which our platforms and software can be leveraged to develop solutions that meet the needs of our aging population.

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We will continue to invest in areas where we see opportunities to create high value products with high software and IP content that leverage our platforms in order to improve competitive positioning and drive increased product margins over time.

In 2010 we anticipate delivering strong revenue and profitability growth in an economy that's still recovering while we continue making robust and long term investments in building for our future and maintaining our market-leading position.

Now I'd like to provide you with our 2010 financial expectations.

For the full year we expect revenue to be between **$345** and **$360** million, roughly **20%** growth over 2009. We expect to see growth in both of our divisions with Home Robot revenue being driven by growth in both international and U.S. markets and G&I revenue primarily from the sale of SUGVs and PackBots.

For full year 2010 we expect EPS to be between **$0.20** and **$0.25**, and Adjusted EBITDA to be between **$24** and **$28** million.

In the first quarter of 2010 we anticipate revenue of **$82** to **$87** million, EPS of **$0.01** to **$0.04** and Adjusted EBITDA of **$4** to **$6** million.

I will now turn the call over to John to review our fourth quarter and full year financial results in more detail.

John

Thanks Colin. And good morning everyone.

Our performance in the fourth quarter was very strong with revenue reaching the highest quarterly level in our history. Earnings per share, Adjusted EBITDA and cash flow all exceeded expectations. Revenue of **$102** million was up **12%** for the quarter year over year**.** Growth in our international Home Robot business continued to be robust, up **29%** for the quarter . Likewise, our government business was up **11%** for the quarter and had a **$42** million backlog coming into 2010.

Earnings per share for the quarter and full year was **$0.20** and **$0.13** compared with **$0.21** and **$0.03** per share in Q4 and full year 2008 respectively. EBITDA for Q4 was **$13** million, and for the full year EBITDA grew to **$21** million, up **61%** over 2008. Operating cash flow of nearly **$41** million has driven our cash position to **$77** million, up **$36** million from the end of last year. The cash balance includes **$5** million in liquid investments.

Our focus on driving EBITDA and cash flow has clearly produced strong results.

In the Home Robot division, shipments of **324** thousand units generated **$55** million in revenue during Q4, compared to **293** thousand units and **$48** million in revenue a year ago. International revenue increased **29%** in the quarter year over year and comprised approximately **55%** of Home Robot revenue. For the full year, international was **54%** of Home Robot revenue, compared with **38%** in 2008. Improvements in Home Robot gross margins were largely due to this increase in international as a percent of total revenue.

In the G&I Division, total revenue was **$47** million in the quarter compared with **$43** million a year ago. This increase was due to higher product shipments, primarily PackBot FasTacs, and higher contract revenue generated under the FCS development program. Contract revenue comprised **23%** of G&I revenue for the quarter and **27%** for the year compared with **19%** and **20%** respectively last year. Contract work is a critical component of our R&D effort, but gross margins tend to be lower than on product revenue. As a result, increased contract revenue adversely impacted G&I margins for the quarter and year.

G&I product revenue was **$36** million in the fourth quarter, compared with **$35** million last year. A key component and growth driver of our government business is product lifecycle revenue or PLR. Our rapidly growing installed base of robots requires spare parts, support, maintenance and training. In the fourth quarter, PLR was **$9** million or **26%** of G&I product revenue, and for the year it totaled **$24** million or **25%,** compared with **19%** of product revenue in 2008. In addition, providing software enabled solutions through upgrades to robots in the field is an emerging opportunity. We expect PLR to average **25 – 30%** of G&I product revenue annually, although it can vary significantly quarter to quarter.

Product backlog at the end of the quarter was **$42** million, compared with **$8** million at the end of 2008. This gives us the opportunity to deliver a strong Q1 and skew our earnings less heavily towards the back half of the year.

For the total company, gross margin for the year was **31% -**- about even with last year. Operating expenses increased **$3.3** million year-over-year in Q4 and totaled **25%** of revenue, unchanged from last year. The increase in operating expenses resulted from incentive compensation expense accrued in 2009 that was not accrued in 2008.

For the full year, operating expenses improved **$7.5** million or **29**% of revenue, compared with **30%** of revenue in 2008. The decrease in opex was driven by tight spending controls across the company.

2009 operating cash flow was nearly **$41** million compared with **$19** million in 2008. This significant improvement resulted from continued focus on managing working capital and in particular, improvements in inventory levels. Inventory was **$32** million at year end, down from **$35** million a year ago. Accounts receivable were also well managed, as evidenced by our DSO of **33** days at year end. Operating cash flow in 2010 and beyond will be much more dependent on improved EBITDA than working capital gains.

At the end of the year, we had cash, including investments, totaling **$77** million compared with **$41** million a year ago.

Now I'd like to provide you with some of the underlying assumptions for the financial expectations Colin discussed, as well as color on how we see the year unfolding.

For the full year we expect Home Robot revenue of **$180** to **$190** million and G&I revenue of **$165** to **$175** million. We expect roughly equal revenue contributions from SUGV and PackBot, with almost three-quarters of the SUGV revenue to come from the sale of the 310 robot.

Within G&I, contract revenue is expected to be between **$30** and **$35** million and product lifecycle revenue is expected to total **20-25%** of product revenue.

We expect revenue growth for both divisions in each quarter, with an especially strong Q1, which creates less dependency on second half Home Robot holiday sales. In Q1, continued shipments of PackBot FasTacs, along with fulfillment of several international orders, will drive G&I revenue. Second quarter revenue will decline sequentially to a range of **$75** to **$78** million due to the expected timing of government orders.

We anticipate positive EBITDA in each of the quarters this year. In Q2, EBITDA will decrease sequentially to between **$0.5** million to **$2** million due to lower revenue.

Full year gross margin will be relatively unchanged and will fluctuate quarterly consistent with revenue, and dependent on product and channel mix. We will continue to manage operating expenses carefully while investing in the company's future. As a percentage of revenue, opex will be consistent with 2009 levels.

Just a few additional data points. We are assuming:

- Stock comp expense of **$9-10** million
- Depreciation and amortization expense of approximately **$8** million
- Tax rate of **40%**
- Diluted share count of **26.5** million shares and;
- Operating cash flow of roughly **$20** million

I'll now turn the call back to Colin.

Colin

In 2009 we faced a challenging year due to the state of the economy and uncertainties around the timing of actions from the new administration in Washington. We said it wasn't going to be a revenue growth year for us, and it wasn't, but one in which we would focus on operating efficiency and building for our future and we did. We delivered substantial growth in EBITDA and operating cash flow with the net effect of dramatically increasing the strength of our business.

In particular during the year we:

- Delivered against our financial commitments; increasing EBITDA by **61**% and quadrupling EPS while significantly improving our balance sheet;
- Strengthened our senior leadership team and enhanced our board with an experienced and highly respected technology industry executive;
- Invested in and implemented critical operating process improvements resulting in lower and better managed inventory levels;
- Expanded the international reach of our Home Robot division which grew **35%,** and;
- Began delivering the SUGV robot for which we believe there is a **10,000-20,000** unit addressable market over the next 4-7 years.

We demonstrated that there is global demand for our products in both divisions and exited the year a stronger company. We are at a very exciting point in our longer term technology development and you will hear us talking more about our IP assets. As our customers demand more functionality on our platforms, we can meet their needs through higher software content on our products. Doing so also enables us to deliver sustainable increased profit margins.

With that we'll take your questions.

Following Q&A

Colin

That concludes our fourth quarter and full year 2009 earnings call. We appreciate your support and look forward to talking with you again in April to discuss Q1 results.

Operator

That concludes the call. Participants may now disconnect.