iRobot Fourth-Quarter and Full Year 2011 Conference Call Script

February 8, 2012

Operator:

Good day everyone and welcome to the iRobot fourth-quarter and full year 2011 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 2012 and the first quarter ending March 31, 2012, our expectations regarding longer-term profitability, our expected quarterly financial performance, seasonality, our expectations regarding revenue, Adjusted EBITDA, operating cash flow, operating expenses, gross margins, restructuring charges, stock compensation expenses, depreciation and amortization expenses, tax rates and earnings per share, demand for our home robots, the timing and fulfillment of government contracts and orders, demand for and adoption and backlog of our Government and Industrial robots and related parts and services, orders for and sales and deliveries of our PackBot and SUGV robots, our Government and Industrial contract, product lifecycle and recurring revenue, international home robot revenue, mix of product revenue and impact on operating margins, our plans for expansion, our introduction and delivery of new products and new product capabilities and functionality, 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 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 Q4 and full year 2011 earnings press release issued last evening, which is available on our website http://investor.irobot.com/phoenix.zhtml?c=193096&p=irol-irhome. 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 February 16, 2012 and can be accessed by dialing **630 652-3042**, access code **31615791#.**

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 2011 as well as our outlook on the business for 2012; and John Leahy, Chief Financial Officer, will review our financial results for the fourth quarter and full year 2011 and, Colin and John will also provide our outlook for financial expectations for the first quarter ending March 31, 2012 and fiscal 2012. 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.

2011 was another outstanding year for iRobot. We:

- **Delivered** record setting results;
- Launched **two** new consumer robots, the Roomba® 700 series and the Scooba 230 **and** a new military robot, FirstLook™;
- **Introduced** our first human interface robot, Ava™, and signed a joint development and licensing agreement with InTouch Health, to explore potential opportunities for healthcare applications on iRobot platforms. We further expanded that relationship through a financial investment in early 2012;
- **And** we met our 3-year financial targets a year ahead of expectations. Based on our confidence in continuing to expand margins through increased product software content and operating expense leverage, I am excited to increase the profit target in our new 3-year goals.

In 2011 our Home Robot division had another great year. We began to see the positive impact of our increased marketing investments in Home Robots, as domestic revenues increased **6%** year over year. Throughout 2010 and 2011 we strategically exited certain lower margin products, channels and retailers making this growth even more significant. Our international Home Robot revenues grew nearly **30%,** driven by the Far East market which was up more than **50%** in 2011 year over year. EMEA (Europe Middle East Africa) also showed strong growth, up more than **20%** for the year**.** In 2012, we expect continued growth in both the U.S. and overseas markets from expanded distribution of new products, improvement in the domestic economy and further expansion into Latin America and China.

Our government business grew nearly **10%** in 2011 in a difficult and ever-changing environment that included a continuing resolution, program cancellations, a new secretary of defense, significant troop withdrawals and ongoing budget reductions. We responded quickly to meet the soldiers' need for a lighter weight reconnaissance robot with FirstLook, demonstrating the adaptability of our technology, the relevance of our products and our close working relationship with the soldiers in the field.

In 2011, we made our first foray into the healthcare market with considerable ir&d investment and work done under a joint development and licensing agreement with InTouch Health. As many of you know, I have been passionate about finding a way to help solve the challenges of our aging population. I believe the opportunities to serve this population, initially through telemedicine applications in hospitals and healthcare facilities and ultimately in the home, are enormous.

Since 2002, iRobot's revenue has been generated primarily by the sale of Roomba, PackBot and SUGV robots. In 2011, we introduced our prototype Ava robot and demonstrated how our Aware® 2 software supports autonomy, navigation, and motor control, and provides interfaces with third party developed technology. Our Ava robot will change the way the world thinks about robots.

Turning now to our financial results, we delivered EPS and Adjusted EBITDA far exceeding our fourth quarter and full year expectations, on revenue in line with our expectations. Full year 2011 revenue of **$465** million grew **16%** year over year while earnings per share of **$1.44** and Adjusted EBITDA of **$73** million increased by approximately **50%** over last year. Our exceptional results were driven by strong performance in our home robot business. We demonstrated our ability to improve profitability while continuing to invest in research & development and marketing, critical to maintaining our industry-leading position.

Our continued focus on strengthening the balance sheet resulted in year-end cash and investments of **$184** million, up more than **50%** from **$122** million a year ago. In 2011, we generated **$56** million in operating cash flow as a result of significantly improved Adjusted EBITDA.

With these strong results, we achieved our 3-year financial goals in 2011 - a full year ahead of expectations and are very proud of this accomplishment.

Now, I'd like to take you through additional highlights of 2011 and discuss our outlook for 2012 and beyond.

On the home robots front, revenues increased more than **20%** for the full year, driven by strong growth overseas, particularly in Japan. At the end of the third quarter of 2011, we began shipping the Roomba 700 series to several international customers for limited distribution in overseas markets including Japan. The response has been overwhelmingly positive and we expect expanded worldwide distribution of the 700 series to be a growth driver in 2012.

We continued our initiative to improve profit margins domestically through strategic management of channel, customer, and product mix. In successfully executing that plan, we discontinued several low-margin products, and stopped selling through certain lower-margin channels and customers. Despite these actions, we generated domestic revenue growth of **6%** for the year. Higher gross margins in the domestic market contributed significantly to an improvement in annual gross margin for the division of **500** basis points. The Roomba 700 was only available on iRobot's website and through select specialty online retailers in 2011. We will expand its distribution in the U.S. throughout 2012 and expect domestic growth in this year to exceed 2011's rate.

As we closed 2011, domestic retailer and international distributor inventories were low, setting us up for a strong 2012. Other initiatives driving home robot growth in 2012 are expanded distribution of the Scooba 230 floor washing robot beyond our website and a material contribution from Latin America where we began to establish a presence last year. In 2013, we expect further expansion in China to be a growth driver.

Our outlook for home robots is very positive and I am confident that we'll continue to see strong growth driven by our international customers, improvement in domestic consumer spending, and expansion of new product distribution.

Our Government & Industrial Robots division's revenue grew nearly **10%** in 2011, in the face of headwinds felt throughout the year. During the third quarter we announced the partial termination of the BCTM contract by the U.S. Army through Boeing. We are currently performing development work under a bridge contract and expect a new development contract in 2012 directly with the Army. Contract revenue for the year decreased in 2011 and we expect it will decline **25-35%** in 2012. Product revenue is also anticipated to be down slightly this year.

There continues to be very strong demand for SUGV from the soldiers in theater and support from the military leadership. We shipped more than **400** units in 2011 and expect to ship a similar number in 2012, despite the drawdown of troops in the Middle East. This speaks to the ongoing demand by the Department of Defense for cost-effective products that enable improved mission capabilities while keeping warfighters out of harm's way. Our robots are part of the future.

Although we began this year with the 2012 defense budget in place, and one that meets our funding expectations for the SUGV program, we have limited visibility on the rest of the G&I business for 2012. In a year dominated by election politics, when all DoD spending will be scrutinized, we expect G&I business performance to decline due to government contracting delays and budget uncertainty. We continue to believe that we are well positioned with a broad product base, and increased functionality enabled through technology to meet the evolving needs of global military and security forces, but at this point we are unsure as to how the year will play out. This uncertainty is reflected in our 2012 financial expectations.

In 2012, we expect to deliver SUGVs to multiple BCTM brigades. We further expect the commencement of Increment 2 of this program in calendar 2012. This Increment will outline the Army's SUGV requirement for the BCTM program.

We have shipped roughly **800** SUGVs since we began selling them in late 2009. Approximately **20%** of the units have been delivered under the BCTM program and the balance has been sold to numerous DoD customers outside of the program. In 2012, we expect about **60%** of the orders to come from non-BCTM customers further demonstrating demand for these robots throughout the military.

We anticipate receiving a contract in the first quarter to provide **105** FirstLook robots for operational assessment. The assessment will take place between March and June during which the robot specifications will be defined and after which a competitively bid contract will be awarded. We anticipate that two vendors will be awarded contracts totaling an estimated **4,000** robots and we are well-positioned to meet the customer's top requirements including weight, ruggedness, run-time and price.

In addition to robots, we expect a 2012 PLR opportunity for a user assist package upgrade for PackBot robots that will enable automatic self-righting, retro-traversing, and course correction. This is the software upgrade we expected last year.

The inherent lumpiness in our G&I business was exacerbated in 2011 by competing budget priorities in Washington resulting from the state of the U.S. economy. We expect a similar challenge in 2012 further complicated by the presidential election.

In total, as we look at 2012, we feel very good about the strength of our home robot business. However, we expect a decline in the top and bottom line in our government business this year due to limited visibility.

In the first quarter of 2012 we anticipate revenue of **$90** to **$100** million, EPS of (**$0.08)** to **$0.00** and Adjusted EBITDA of **$2** to **$5** million.

For the full year 2012, we expect revenue to be **$465** to **$485** million. We expect EPS to be **$0.75** to **$0.95,** and Adjusted EBITDA of **$56** to **$63** million.

In 2012 we will further widen our competitive moat by delivering robots that make a difference, built on common platforms using highly integrated iRobot-developed technology. We create robot-enabled solutions to real world problems, not just demonstrations, and that's a real differentiator for us in the robot industry. Additionally, our intellectual property is very strong and a key barrier to others considering entry into our markets. With more than **100** U.S. patents and more than **150** additional pending U.S. patent applications, we have a formidable market-leading position.

By leveraging our technology with that developed by third parties in areas such as VOIP, user interface, voice control, and facial recognition, we will develop high quality robots for multi-billion dollar automated home maintenance and remote presence markets.

Based on the opportunities we see for our portfolio of products and markets, we have re-assessed our goals for the next three years and I am confident in our ability to achieve an increased Adjusted EBITDA margin target. Our specific three-year goals are to deliver:

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

In order to achieve these goals, we will continue to make technology investments that ensure iRobot's market leadership position in providing remote presence and automated home maintenance solutions.

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

John

Thanks Colin.

Our performance in the fourth quarter was excellent once again with revenue reaching the highest quarterly level in our history. Earnings per share, Adjusted EBITDA and cash flow all exceeded our expectations. Revenue of **$131** million was up **15%** for the quarter driven by growth in both businesses. We have now had nine consecutive quarters of double digit revenue growth.

Earnings per share for the quarter and full year were **$0.38** and **$1.44** compared with **$0.26** and **$0.96** in Q4 and full year 2010, respectively. EPS included the impact of a **$3.5** million tax benefit in 2011, and a **$2.3** million tax benefit in 2010. Excluding the impact of these tax benefits, EPS for the year would have been **$1.32**, compared with **$0.88** in 2010**.** Adjusted EBITDA for Q4 was **$21** million, and our full year Adjusted EBITDA of **$73** million increased nearly **50%** over 2010. Operating cash flow of **$56** million drove our cash position to **$184** million, up **$62** million from the end of last year.

Our return on invested capital, or ROIC, is now in the high teens. Our cash position and ROIC are the highest in the company's history.

In the Home Robot division, revenue of **$74** million increased **7%** in Q4 from our record-setting Q4 2010. International revenue increased **13%** in the quarter year over year and comprised **67%** of Home Robot revenue. Home Robot gross margins improved **340** basis points in the quarter and **500** basis points for the full year, primarily due to product and channel mix.

In the G&I Division, Q4 revenue was **$56** million compared with **$45** million a year ago, up **27%**. Product lifecycle revenue was **$11** million or **23%** of G&I product revenue. Full year PLR was **29%** of G&I product revenue. This strong revenue performance was delivered despite the disruption of the BCTM research contract.

For the total company, gross margin was **43%** for the quarter and **41%** for the year, up **300** and **500** basis points respectively. The year over year increases were driven primarily by favorable revenue mix in home robots and higher overhead absorption in G&I. Gross margins have been the key drivers of our improved profitability, increasing more than **1,000** basis points from two years ago.

Q4 operating expenses improved to **31%** of revenue from **33%** in Q4 last year. Full year spending on marketing programs increased **16%** while investments in iR&D were up **47%** for the full year. As we communicated in our call reviewing Q3 results, we also absorbed approximately **$1** million in costs for the reduction in force implemented in early October.

Q4 operating cash flow was **$37** million. For the full year, operating cash flow was **$56** million, or **12%** of revenue. This was higher than we expected as we received **$10** million in accounts receivable payments in Q4 that we had anticipated in Q1 2012. Our Q1 and full year 2012 OCF will be impacted accordingly.

Now I'd like to provide you with additional detail and some of the underlying assumptions for our 2012 financial expectations. The outlook for our home robot business remains very strong with growth drivers identified for the next couple of years. For our government business, we don't have the visibility to plan for growth for the division in 2012. U.S. budget pressures coupled with a presidential election increase our uncertainty for this year.

Therefore, for 2012, we expect full year revenue of **$465** to **$485** million comprised of Home Robot revenue of **$320** to **$325** million and G&I revenue of **$145** to **$165** million. We expect Q1 revenue to be down year over year but to increase in each of the subsequent quarters resulting in nearly **60**% of 2012 revenue in the second half.

In Home Robots, growth will be driven by further penetration of long time overseas markets, coupled with expansion into new geographies and wider distribution of new products. Expanded retail distribution of the Roomba 700 series and Scooba 230 in the U.S. market will drive domestic growth.

We expect roughly half of G&I product unit revenue to come from SUGV sales, **25%** to come from PackBot and the balance to come from FirstLook™ and Warrior sales. Contract revenue is expected to be between **$25** and **$30** million and product lifecycle revenue is expected to total approximately **25%** of product revenue. SUGVs and PLR will drive our revenue in 2012. We anticipate more than **70%** of G&I revenue to come in the second half of the year.

We once again expect positive EBITDA in each quarter this year, increasing sequentially throughout the year. Investments in ir&d for Ava and other product development, as well as increased marketing spend to promote expanded distribution of new home robot products will continue throughout the year. Operating expense will be approximately **31%** of revenue for the full year. Operating cash flow will be **$30-35** million, largely driven by net income gains.

We are also assuming:

- Stock comp expense of roughly **$11** million
- Depreciation and amortization expense of approximately $**11** million and;
- Diluted share count of **28.5** million shares

We are estimating a tax rate of **35%** for 2012 – much higher than 2011 when we benefited from several one-time tax events. Also, we have not assumed in our rate the investment tax credit for R&D which has not yet been approved by Congress for 2012.

Finally, as Colin mentioned we are raising our three-year profit target from mid-teens to high-teens Adjusted EBITDA. We expect this to be driven by both gross margin gains and expense leverage. We expect gross margins of mid **40s** and operating expense in the low **30s** as a percent of revenue.

I'll now turn the call back to Colin.

Colin

In addition to delivering record setting results this year and meeting our 3-year financial goals a full year ahead of our target, we delivered new products, and entered new geographical markets that will fuel our growth for years to come,
Over the next three years we are committing to achieve:

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

There is a gap between our 2012 expectations and these goals. While our home robot division will deliver robust 2012 results throughout the year, our lack of near term visibility in our government business negatively impacts our first half and full year expectations. However, we expect continued demand from the warfighters and support from military leadership for our products to drive higher revenue in the second half and position us well for future growth.

We have tremendous emerging opportunities to pursue. The robot world is changing quickly. Two years ago I said that tablet computers were going to change the way we interact with robots by providing intuitive touch screen interfaces, voice and video over IP, and powerful development tools. Last year, the video game industry provided another change agent, the Kinetic xBox sensor giving us a gestural interface and an ideal indoor object sensor. And this year, led by Siri, the true power of the Cloud is becoming apparent. Algorithms that require vast memory and processing power to work are delivered as a nearly free service to any connected device - things like face recognition and speaker independent natural language recognition.

The power of these new technologies, coupled with our maturing software technology to build and use maps of a robot's environment, create opportunities to build valuecreating robots, the likes of which the world has never seen, for both our current markets and new ones. There has never been a better time to be positioned as we are.

Today iRobot is truly a global technology company with a portfolio of products meeting the needs of customers worldwide and our exceptional results reflect the increasing diversification of the company. We are successfully meeting the challenges of international economic uncertainty, and continuing unresolved U.S. budget issues by delivering multiple products into multi-billion dollar automated home maintenance and remote presence global markets.

With that we'll take your questions.

Following Q&A

Colin

That concludes our fourth quarter and full year 2011 earnings call. We appreciate your support and look forward to talking with you again in April to discuss our Q1 results.

Operator

That concludes the call. Participants may now disconnect.