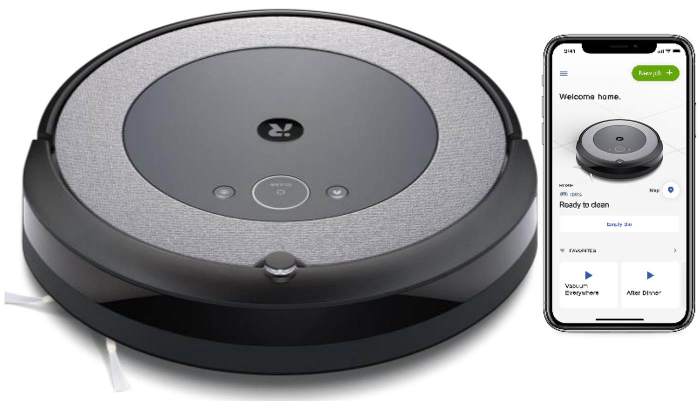
iRobot Q121 Financial Results Conference Call Prepared Remarks



May 4, 2021

iRobot First-Quarter 2021 Conference Call

Operator:

Good day everyone and welcome to the iRobot first-quarter 2021 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 Andrew Kramer of iRobot Investor Relations. Please go ahead.

Andrew:

Thank you operator, and good morning everybody. Joining me on today's are iRobot Chairman & CEO Colin Angle and Executive Vice President and CFO Julie Zeiler.

Before I set the agenda for today's call, I will 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 expressed or implied forward-looking statements relating to the company's financial results, operations and performance, including; expectations regarding market conditions; the introduction of new capabilities and features to our products; our expectations regarding profitability; our expectations regarding revenue, non-GAAP EPS, non-GAAP gross margin, non-GAAP operating profit and margin, non-GAAP operating expenses, non-GAAP operating income, sales & marketing expenses, inventory, non-GAAP tax rate, other expenses, capital expenditures, diluted share count and cash flow; expectations regarding the growth of our direct-to-consumer channel; our expectations regarding the amount and impact of tariffs on goods imported into the United States from China, the potential impact of supply chain limitations due to the global semiconductor chip shortage, and our potential to expand access to semiconductor componentry; our expectations regarding costs for raw materials, air freight and transportation; the impact of our investments; our manufacturing, fulfillment and supply chain diversification and efficiency efforts and the impact of the costs thereof; our plans regarding stock repurchases; our plans to minimize the impact of higher costs; our strategy and the impact thereof; our market opportunity; 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.

Related to our financial disclosures during this conference call, we will reference certain non-GAAP financial measures as defined by SEC Regulation G, including non-GAAP gross margin, non-GAAP operating expense, non-GAAP operating income, profit and margin, non-GAAP effective tax rate, and non-GAAP net income per share. We believe that our non-GAAP financial results help provide additional transparency into iRobot's underlying operating performance and potential. Our definitions of these non-GAAP financial measures, and reconciliations of each of these non-GAAP financial measures to the most directly comparable GAAP measure, are provided at the end of these prepared remarks and in the financial tables at the end of the first-quarter 2021 financial results press release we issued last evening, which is available on our website at www.irobot.com. Also, unless stated otherwise, our first-quarter 2021 financial metrics, as well as financial metrics provided in our outlook, that will be discussed on today's conference call will be on a non-GAAP basis only and all historical comparisons are with the first quarter of 2020.

As a reminder, 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 the telephone conference call will be available for one week through May 11, and can be accessed by dialing 404-537-3406 and using passcode 1792768.

In terms of the agenda for today's call, Colin will briefly review the company's quarterly financial results, discuss major strategic accomplishments and related progress, and share his perspective on our outlook into 2021. Julie will detail our first-quarter financial results, and offer insight into our expectations going forward. Colin will conclude our commentary with some closing remarks. After that, 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. 2021 is off to a very good start. Our first-quarter revenue of $303 million grew 58%, which we converted into operating income of $15 million, an operating profit margin of 5%, and EPS of $0.41. We believe that our first-quarter revenue growth demonstrates that our value proposition is still resonating with consumers around the world. We generated strong top-line growth in each major geographic region as we benefited from stronger-than-expected demand from our distribution partners in EMEA and vibrant retail orders in North America, including certain orders that were previously anticipated for the second quarter. These dynamics were complemented by another quarter of triple-digit growth in our direct-to-consumer (DTC) channel[1].

Based on our strong Q1 performance and favorable consumer demand tailwinds, we see continued growth ahead and we have raised our full-year revenue outlook. We also reaffirmed our 2021 profitability and EPS expectations as we have adjusted our spending plans to offset expected gross margin pressure from transitory supply chain challenges. As we move forward, we are optimistic about our potential to deliver upside to our updated 2021 targets.

Strategic Progress: Q121 and Recent Accomplishments and Highlights

I'll discuss our outlook in more detail shortly, but first I'd like to highlight our progress in executing each element of our strategy. As a reminder, our strategy remains focused on driving greater customer engagement in ways that lead to more customers transacting directly with us more often.

Differentiate the iRobot Experience

The first element of our strategy is to differentiate the iRobot experience for consumers. In a competitive market like robotic floor care, this means continued investment in AI, home understanding and machine vision technologies so that our floor cleaning robots

[1] Refers to transactions made on irobot.com, the iRobot Home App and on certain third-party websites outside the U.S. in which iRobot is directly involved in order management and fulfilment.

can be tightly integrated into the customer's lifestyle and clean with unprecedented levels of thoughtfulness, reliability, control and support. We are pleased with our recent progress on this front:

- During the first quarter of 2021, we upgraded our iRobot Genius Home Intelligence Platform, adding several compelling new features including "estimated clean time," which helps customers know when a new cleaning job may be finished and "clean while I am away," which uses a smart phone's location services to tell the robot to start cleaning once you leave the house.
- The unique functionality of our Genius platform is helping drive sales of our mid-tier and premium robots. By pushing innovation across more of our product line and making certain pricing adjustments, we are reinvigorating the mid-tier[2] of our portfolio and generated strong first-quarter revenue growth from these robots.
- We believe that solid execution on this element of our strategy played an important role in enabling Roomba to occupy 7 of the top 10 best-selling RVC models in the U.S., EMEA and Japan in the first quarter.

Build Stronger, Enduring Relationships with Consumers Worldwide

The second element of our strategy is to build stronger, more enduring consumer relationships. Our connected customer base grew by 74% over 2020's first quarter to 10.7 million customers who have opted-in to our digital communications. It has also been gratifying to see how the high-value features and functionality within the Genius platform are delighting our customers. As iRobot's customer community expands, we are enhancing all points of the consumer's journey with us – from the moment they purchase a product from us and then unbox it to when they complete their first cleaning mission and at various points over the months and years that follow.

Nurturing Value

The third strategic pillar is nurturing the lifetime value of our customer relationships to expand existing customer revenue. This involves accelerating the replacement cycle, upselling and cross-selling, helping customers properly maintain their robots, offering

[2] Defined as floor cleaning robots with an MSRP between $300 and $499. For the first quarter of 2021, this included the Roomba i3, 900 Series, e5 and the Braava Jet m Series.

complementary products and developing new services including new purchasing options to drive recurring revenue and higher margins. Since the start of the year, we accomplished several important milestones:

- In early April, we introduced our new iRobot h1 handheld vacuum as a complement to Roomba and Braava robots. Many of you have heard me say that the future of vacuuming is a Roomba and a cordless vacuum for areas that robots can't easily clean. Now our customers can get both products directly from us.
- We also made tangible progress with new services that provide customers with greater purchase protection and flexibility. Consumers who purchase their robots directly from us can also add an extended warranty, and we've been very pleased with the attachment rates thus far. In addition, customer feedback on our iRobot Select robot-as-a-service membership program has been very positive as those pilots have progressed. Moving forward, we plan to optimize the value proposition for iRobot Select and prepare to further scale this program as well as advance testing of a premium care-as-a-service offering.
- Overall, our direct-to-consumer sales grew 146% in the first quarter and generated 12% of Q1 revenue. Accessories represent another opportunity to drive existing customer revenue growth through our DTC channel. We generated very healthy Q1 growth in accessory sales, which includes filters, rollers, batteries, bags, mopping pads and mopping solution. We expect to build on this momentum over the coming quarters as we further upgrade the buying experience on irobot.com and our Home App, and implement world-class digital marketing systems, tools and campaigns that will enable us to present our customers with the right offers for the right products at the right time.

Outlook

With a strong Q1 behind us, we move forward with solid category momentum, a compelling value proposition, a fast-growing and rapidly maturing DTC channel, excellent retailer relationships and healthy channel inventory positions. Our year-to-date sell-through growth through week 15 is, not surprisingly, substantially better than the same period one year ago, which was dramatically impacted by the early days of the pandemic. Nevertheless, we recognize that it is still early in the year. The pandemic continues to weigh heavily on the macroeconomic landscape and limit our visibility. Additionally, our business is not immune to the semiconductor chip shortage that is disrupting a wide range of industries. To that end, certain component suppliers recently notified us of potential volume limitations. We have already made good progress in our efforts to mitigate those constraints although additional work lies ahead on this front. Taking all of these dynamics into consideration, we have raised our full-year revenue expectations to range from $1.67 billion to $1.71 billion.

From a profitability perspective, the semiconductor chip shortage is resulting in higher costs for these components. At the same time, we are now grappling with rising costs for raw materials, air freight and transportation. While these transitory costs are likely to remain elevated for the next several quarters, we expect that over time they will revert to more normalized levels as market forces adjust. Nevertheless, to offset their near-term impact on our anticipated 2021 gross margin, we have recalibrated our spending over the coming quarters. As a result, we have reaffirmed our 2021 operating income, operating income margin and EPS targets.

With two-thirds of the year still ahead of us, we are optimistic about our potential for further upside, especially if current demand trends remain healthy and we successfully expand access to the semiconductor componentry that will enable us to increase production beyond what's embedded in our current expectations.

That concludes my initial commentary. I will now turn the call over to Julie.

Julie:

Thank you Colin. As Andy mentioned earlier, my review of our financial results and outlook will be done on a non-GAAP basis, so unless stated otherwise, each mention of gross margin, operating expense, operating income and operating profit margin, effective tax rate and net income per share will mean the corresponding non-GAAP metric. All quarterly comparisons are against the first quarter of 2020 unless otherwise noted.

As Colin noted, our Q1 performance represents a strong start to 2021. Total Q1 revenue grew 58% to $303 million and exceeded our original targets due primarily to stronger-than-expected orders from distributors in EMEA and U.S. retailers including over $5 million in orders that were originally expected in the second quarter. Geographically, revenue grew 40% in the U.S. with international revenue up 70% due primarily to 74% growth in EMEA and a 53% increase in Japan. From a product mix perspective, Roomba robots and accessories represented 89% of our Q1 revenue mix with Braava making up the remainder. Since the start of the pandemic over a year ago, more consumers are buying our products online. We estimate that approximately 56% of total first-quarter revenue came from e-commerce, which comprises our own website and app, dedicated e-commerce websites and the online arms of traditional brick and mortar retailers.

Our gross margin of 40.7% in Q1 was largely unchanged from the prior year's first quarter. Changes in pricing and promotion, higher air freight fees and higher costs to procure certain components were essentially offset by leverage from higher sales, lower tariff costs, favorable channel mix and the timing of one-time write-offs associated with pausing certain product activities in the first quarter of 2020 that did not recur in the first quarter. Tariffs on RVCs imported into the U.S. from China were reinstated on January 1, 2021. Taking advantage of the non-tariffed inventory that was in place at the end of 2020 helped us limit our first-quarter tariff costs to just $3.4 million. Our gross and operating profit margin would have been 1.1 percentage points higher without tariffs.

First-quarter 2021 operating expenses of $109 million increased by 17% and represented 36% of revenue. The increase primarily reflects higher personnel-related expenses and increased working media spending to drive sales growth. Our Q121 operating income was $15 million, or 5% of revenue.

Our Q1 2021 effective tax rate was 19.2%, which was in line with our plans. Our net income per share was $0.41.

We ended Q1 with $501 million in cash and short-term investments, an increase of $17 million from year-end. The increase primarily reflects the company's fundamental operating performance plus favorable changes in working capital. It should also be noted that the reduction in short-term investments since the end of 2020 primarily reflects the sale of our Teladoc stock early in the first quarter once the restriction on selling those shares lapsed.

First-quarter DSOs were 20 days, a two-day increase against the same period one year ago. Q1 ending inventory was $233 million, or 118 days, compared with $147 million, or 118 days, at the same time last year.

Outlook

With the quarterly review complete, let's move on to our 2021 outlook.

2021 Revenue

As Colin outlined, we now expect 2021 revenue in the range of $1.67 billion to $1.71 billion. Our updated outlook assumes very strong sequential revenue growth, which implies a split between the first and second halves of 2021 that approaches our historical 40/60 split. As a reminder, our revenue expectations contemplate Yen and Euro exchange rates roughly in line with current rates, plus or minus 5%.

2021 Gross Margin

Colin outlined several recent developments involving our supply chain that are resulting in higher-than-expected costs including constrained availability of semiconductor componentry, rising raw material costs and increased air freight and transportation fees.

In addition, we expect slightly higher 2021 tariff costs in the range of $43 to $45 million[3]. As a result, we now expect a full-year 2021 gross margin of approximately 39%. We anticipate a Q2 gross margin that is in line with our full-year target, which reflects the timing of promotional activities as well as incrementally higher supply chain costs.

Many of the other factors shaping our 2021 gross margin are unchanged. Since the pandemic began, our operations organization has been outstanding in keeping key initiatives on course while moving with urgency and decisiveness to address unanticipated supply chain challenges. Our plan to substantially increase our production in Malaysia over the course of this year is progressing well even with a tight labor market. We are also fortunate to have a strong balance sheet, which will help us secure longer lead time and increasingly scarce componentry.

2021 Operating Costs & Operating Profitability

In terms of our 2021 operating costs, we have adjusted our full-year spending plans to offset the anticipated gross margin pressure. We are now targeting full-year operating costs in the range of $535 million to $555 million, or approximately 32% of sales. As a result, we still expect an operating profit margin of 7% with anticipated operating income between $110 and $120 million.

While we expect relatively nominal increases in our Q2 R&D & G&A spending versus first-quarter 2021 levels, we plan to significantly ramp up our Q2 sales and marketing activity as we continue to invest in scaling our DTC operations and activate our working media programs to support major holiday and other seasonal events. Although we expect our Q2 operating profit margin will decline from the first quarter, we anticipate that the substantially higher second-half revenue will support a meaningful improvement in our profitability in the second half of the year.

[3] Original FY21 tariff costs were expected to range from $41 million to $43 million.

Other Assumptions & EPS

In terms of other major modeling assumptions for 2021, we now expect other expense to be between $2 and $3 million, and we still anticipate an effective tax rate ranging from 18% to 19%. We still expect our full-year EPS to range from $3.00 to $3.25 with an anticipated diluted share count of approximately 29 million shares.

We continue to expect our 2021 capital spending will be in the low $50 million range. On the use of capital front, our previously authorized $200 million stock repurchase plan had $175 million available entering the second quarter. Earlier this month, we disclosed our intention to repurchase up to $50 million of our common stock under a 10b5-1 plan that began on April 12 and is expected to end on or before September 5. As a reminder, our 2021 expectations do not assume any repurchase activity.

On the inventory front, we expect that inventory, both in terms of absolute dollars and DII, may fluctuate meaningfully from quarter to quarter over the remainder of the year as we navigate a challenging and fluid supply chain environment.

In summary, Q1 was a good way to begin the year. We move forward focused on executing against our plans as we look to capitalize on the exciting opportunities we see and overcome the challenges that lie ahead. That concludes my commentary. I'll now turn the call back to Colin for some closing thoughts.

Colin:

Closing Thoughts

Thank you Julie. We are nearing the midway point of a multi-year strategic plan to transform iRobot into a more defensible, more profitable business capable of sustaining solid growth with the scale, channels, and offerings to address the evolving needs of an expansive and expanding global customer base. Our recent accomplishments and progress – from driving innovation in robotic floor cleaning and introducing complementary cleaning products to offering extended warranties, advancing promising new high-value services and selling more accessories – all illustrate the importance of our investments to build out our e-commerce and digital marketing capabilities. They also highlight our potential to grow existing customer revenue and further improve the profitability of our enterprise in the process.

We expect more progress on these and other related fronts over the coming quarters. On our Q4 call in February, we shared our preliminary thoughts on what our business may look like in 2022. That view remains unchanged, regardless of the short-term supply chain turbulence we've recently encountered. Over the past several quarters, we've made good progress in refining our long-range strategic plan. As we finalize this activity, we have started our planning process for a virtual Investor Day event that we plan to hold later this year. We believe this will be an important opportunity for analysts and investors to fully appreciate why we are so enthusiastic about our prospects. We expect to finalize the timing for this event soon and will share those details with you accordingly.

That concludes our comments. Operator, we will take questions now.

iRobot Corporation
Explanation of Non-GAAP Measures

In addition to disclosing financial results in accordance with U.S. GAAP, this earnings release contains references to the non-GAAP financial measures described below. We use non-GAAP measures to internally evaluate and analyze financial results. We believe these non-GAAP financial measures provide investors with useful supplemental information about the financial performance of our business, enable comparison of financial results between periods where certain items may vary independent of business performance, and enable comparison of our financial results with other public companies, many of which present similar non-GAAP financial measures.

Our non-GAAP financial measures reflect adjustments based on the following items. These non-GAAP financial measures should not be considered a substitute for, or superior to, financial measures calculated in accordance with GAAP, and the financial results calculated in accordance with GAAP and reconciliations from these results should be carefully evaluated.

Amortization of acquired intangible assets: Amortization of acquired intangible assets consists of amortization of intangible assets including completed technology, customer relationships, and reacquired distribution rights acquired in connection with business combinations. Amortization charges for our acquisition-related intangible assets are inconsistent in size and are significantly impacted by the timing and valuation of our acquisitions. We exclude these charges from our non-GAAP measures to facilitate an evaluation of our current operating performance and comparisons to our past operating performance.

Net Merger, Acquisition and Divestiture (Income) Expense: Net merger, acquisition and divestiture (income) expense primarily consists of transaction fees, professional fees, and transition and integration costs directly associated with mergers, acquisitions and divestitures. It also includes business combination adjustments including adjustments after the measurement period has ended. The occurrence and amount of these costs will vary depending on the timing and size of these transactions. We exclude these charges from our non-GAAP measures to facilitate an evaluation of our current operating performance and comparisons to our past operating performance.

Stock-Based Compensation: Stock-based compensation is a non-cash charge relating to stock-based awards. We exclude this expense as it is a non-cash expense, and we assess our internal operations excluding this expense and believe it facilitates comparisons to the performance of other companies.

IP Litigation Expense, Net: IP litigation expense, net relates to legal costs incurred to litigate patent, trademark, copyright and false advertising infringements, or to oppose or defend against interparty actions related to intellectual property. Any settlement payment or proceeds resulting from these infringements are included or netted against the costs. We exclude these costs from our non-GAAP measures as we do not believe these costs have a direct correlation to the operations of our business and may vary in size depending on the timing and results of such litigations and settlements.

Gain/Loss on Strategic Investments: Gain/loss on strategic investments includes fair value adjustments, realized gains and losses on the sales of these investments and losses on the impairment of these investments. We exclude these items from our non-GAAP measures because we do not believe they correlate to the performance of our core business and may vary in size based on market conditions and events. We believe that the exclusion of these gains or losses provides investors with a supplemental view of our operational performance.

Income tax adjustments: Income tax adjustments include the tax effect of the non-GAAP adjustments, calculated using the appropriate statutory tax rate for each adjustment. We reassess the need for any valuation allowance recorded based on the non-GAAP profitability and have eliminated the effect of the valuation allowance recorded in the U.S. jurisdiction. We also exclude certain tax items, including impact from stock-based compensation windfalls/shortfalls, that are not reflective of income tax expense incurred as a result of current period earnings. We believe disclosure of the income tax provision before the effect of such tax items is important to permit investors' consistent earnings comparison between periods.

iRobot Corporation
Supplemental Reconciliation of GAAP Actuals to Non-GAAP Actuals
(in thousands, except per share amounts)
(unaudited)

	For the three months ended	
	April 3, 2021	March 28, 2020
GAAP Revenue	$ 303,261	$ 192,535
GAAP Gross Profit	$ 122,944	$ 77,955
Amortization of acquired intangible assets	225	285
Stock-based compensation	362	527
Non-GAAP Gross Profit	$ 123,531	$ 78,767
Non-GAAP Gross Margin	40.7%	40.9%
GAAP Operating Expenses	$ 116,555	$ 98,180
Amortization of acquired intangible assets	(205)	(254)
Stock-based compensation	(6,420)	(4,664)
Net merger, acquisition and divestiture income	-	500
IP litigation expense, net	(1,140)	(615)
Restructuring and other	(213)	-
Non-GAAP Operating Expenses	$ 108,577	$ 93,147
Non-GAAP Operating Expenses as a % of Non-GAAP Revenue	35.8 %	48.4 %
GAAP Operating Income (Loss)	$ 6,389	$ (20,225)
Amortization of acquired intangible assets	430	539
Stock-based compensation	6,782	5,191
Net merger, acquisition and divestiture income	-	(500)
IP litigation expense, net	1,140	615
Restructuring and other	213	-
Non-GAAP Operating Income (Loss)	$ 14,954	$ (14,380)
Non-GAAP Operating Margin	4.9 %	(7.5)%
GAAP Income Tax Benefit	$ (1,214)	$ (2,109)
Tax effect of non-GAAP adjustments	1,398	(1,831)
Other tax adjustments	2,653	(1,384)
Non-GAAP Income Tax Expense (Benefit)	$ 2,837	$ (5,324)

iRobot Corporation
Supplemental Reconciliation of GAAP Actuals to Non-GAAP Actuals – Continued
(in thousands, except per share amounts)
(unaudited)

	For the three months ended	
	April 3, 2021	March 28, 2020
GAAP Net Income (Loss)	$ 7,443	$ (18,135)
Amortization of acquired intangible assets	430	539
Stock-based compensation	6,782	5,191
Net merger, acquisition and divestiture income	-	(500)
IP litigation expense, net	1,140	615
Restructuring and other	213	-
Gain on strategic investments	(38)	(87)
Income tax effect	(4,051)	3,215
Non-GAAP Net Income (Loss)	$ 11,919	$ (9,162)
GAAP Net Income (Loss) Per Diluted Share	$ 0.26	$ (0.64)
Amortization of acquired intangible assets	0.01	0.02
Stock-based compensation	0.23	0.19
Net merger, acquisition and divestiture income	-	(0.02)
IP litigation expense, net	0.04	0.02
Restructuring and other	0.01	-
Income tax effect	(0.14)	0.11
Non-GAAP Net Income (Loss) Per Diluted Share	$ 0.41	$ (0.32)
Number of shares used in diluted per share calculation	29,086	28,297
Section 301 Tariff Costs		
Section 301 tariff costs	$ 3,383	$ 6,609
Impact of Section 301 tariff costs to gross and operating margin (GAAP & non-GAAP)	(1.1)%	(3.4)%
Impact of Section 301 tariff costs to net income (loss) per diluted share (GAAP & non-GAAP)	$ (0.12)	$ (0.23)
Supplemental Information		
Days sales outstanding	20	18
Days in inventory	118	118

iRobot Corporation
Supplemental Reconciliation of Fiscal Year 2021 GAAP to Non-GAAP Guidance
(unaudited)

	FY-21
GAAP Gross Profit	$642 - $672 million
Amortization of acquired intangible assets	~$1 million
Stock-based compensation	~$2 million
Total adjustments	~$3 million
Non-GAAP Gross Profit	$645 - $675 million

	FY-21
GAAP Operating Income	$69 - $79 million
Amortization of acquired intangible assets	~$1 million
Stock-based compensation	~$32 million
IP litigation expense, net	~$8 million
Total adjustments	~$41 million
Non-GAAP Operating Income	$110 - $120 million

	FY-21
GAAP Net Income Per Diluted Share	$1.85 - $2.10
Amortization of acquired intangible assets	~ $0.03
Stock-based compensation	~ $1.10
IP litigation expense, net	~ $0.27
Income tax effect	~ ($0.25)
Total adjustments	~ $1.15
Non-GAAP Net Income Per Diluted Share	$3.00 - $3.25
Number of shares used in diluted per share calculations	~ 29.2 million