

# FINAL TRANSCRIPT

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## **IRBT - Q1 2009 iRobot Corp. Earnings Conference Call**

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## CORPORATE PARTICIPANTS

**Elise Caffrey**  
*iRobot Corporation - IR*

**Colin Angle**  
*iRobot Corporation - Chairman, CEO*

**John Leahy**  
*iRobot Corporation - CFO*

## CONFERENCE CALL PARTICIPANTS

**Jim Ricchiuti**  
*Needham & Company - Analyst*

**Barbara Coffey**  
*Kaufman Brothers - Analyst*

**Paul Coster**  
*JPMorgan - Analyst*

**Charlie Anderson**  
*Dougherty & Company - Analyst*

## PRESENTATION

### Operator

Good day and welcome to the iRobot Corporation First Quarter 2009 Earnings Conference Call. At this time, we are being recorded and for opening remarks and introductions, I would like to turn the call over to your host, Elise Caffrey. Please go ahead.

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**Elise Caffrey** - *iRobot Corporation - IR*

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 provision 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 and operations demand for the company's products and services 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.

During this conference call, we will also discuss various non-GAAP financial measures as defined by SEC regulation G, including adjusted EBITDA, which we define as earnings before interest, taxes, depreciation, amortization and non-cash stock compensation expense. A reconciliation between net loss to a GAAP measures most directly comparable to adjusted EBITDA and adjusted EBITDA loss is provided in the financial tables at the end of the Q1 2009 earnings press release issued last evening, available on our website, [www.irobot.com](http://www.irobot.com).

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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 shortly. In addition, a replay of this conference call will be available through April 30, 2009 and can be accessed by dialing 719-457-0820, access code 5918741.

Please note that beginning with our Second Quarter 2009 Earnings Call in July, we will post a copy of the earnings call script on our website, when we issue the quarterly earnings release the evening before the call.

On today's call, iRobot Chairman and CEO, Colin Angle, will provide a review of our company's operations and achievements for the first quarter of 2009 and our outlook for business for the rest of the year; and John Leahy, Chief Financial Officer, will review our financial results for the first quarter of 2009. Then we will open the call for questions. At this point, I will turn the call over to Colin Angle.

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**Colin Angle** - *iRobot Corporation - Chairman, CEO*

Good morning and thank you for joining us. Last evening, we reported first quarter results that demonstrate the underlying strength of our business, despite tough economic conditions. Revenue of \$57 million was roughly even with last year, and primarily driven by strong international demand in our home robot business. Loss per share of \$0.07 compared favorably with our expectations of a \$0.12 to \$0.18 loss per share and last year's loss per share of \$0.16, and reflects our efforts to manage controllable expenses and improve profitability.

Adjusted EBITDA loss was \$300,000 in Q1, a \$4 million improvement over last year's results, and significantly stronger than our quarterly guidance. This achievement demonstrates our commitment to improved profitability in the first half, when we have historically reported losses.

Given our strong performance in his first quarter, we are reaffirming our full-year expectations despite uncertain economic environment. For 2009, we expect revenues to be in the range of \$290 million to \$310 million, earnings per share of between breakeven and \$0.04, and adjusted EBITDA between \$14 million and \$17 million.

The actions we took in the second half of last year in response to a deepening recession strengthened the company's financial position coming into 2009. We ended the first quarter with nearly \$55 million in cash compared with \$41 million at year-end as a result of aggressive working capital management. We now have generated \$34 million operating cash flow over the past two quarters, and improved our cash position by \$28 million.

Turning now to highlights from the first quarter, in March, we filled a key position in our Home Robots division. Jeff Beck, who brings more than 20 years of high technology leadership, joined us as President and General Manager. Most recently, he served as Senior Vice President and General Manager of the Aerospace and Defense division of Amtech Inc. Jeff's experience as a General Manager and his success in growing businesses has provided him with the tools to successfully lead our Home Robots division, and we are excited to welcome him to the team.

Jon Elordi, who has served as interim general manager will resume full-time responsibility for our high-growth Home Robots international businesses. Our international business continues to demonstrate the strength we anticipated going into the year. Many of our existing customers are expanding into new stores because of the success they have had with Roomba 500.

In addition, we are participating in an affinity program in Europe with a new customer, which is proving to be very successful. We are wary of overseas economies, particularly in Western Europe, but demand at this point seems to be outpacing the negative recessionary impact.

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Home robot revenue in the first quarter was \$33 million compared with \$30 million in 2008. International revenue grew 69% in the first quarter to \$18 million and comprised more than 50% of home robot revenue this year compared with 35% last year. At this point, our expectations at home robot have not changed, since we shared our expectations in February.

We continue to expect growth in international to partially offset recession-driven weakness in our domestic retail and direct channels. We feel good about the home robot business. We have made tremendous progress in the international markets, and see continued opportunities overseas.

The domestic market will recover with the economy and still has very low penetration. We're continuing to make strategic investments in Home Robots consistent with our long-term plan to develop new home robot products, and we have found an accomplished leader for the division.

In the government and industrial division, we generated \$24 million in Q1 revenue, primarily as a result of delivering PackBot FasTac robots that compares with \$27 million a year ago. Based on the backlog going into the quarter, the decrease is consistent with our expectations and does not negatively impact our G&I outlook for the year.

The recent announcement from Defense Secretary Gates regarding the strategic reshaping of the Department of Defense spending to fund development of technologies and products that address the challenges of irregular warfare appear at the present to be positive for iRobot. With respect to the Future Combat Systems Program, Gates reaffirmed that he plans to retain and accelerate the initial increment of the program to spin out technology enhancements to all combat brigades.

Our small unmanned ground vehicle, the SUGV, is part of this initial increment of the program. The budget details surrounding the army's procurement of the SUGVs are still forthcoming. However, the Secretary of Defense, clearly communicated that spin out one of FCS will be both accelerated and expanded. That means that SUGVs will be procured for all combat brigades rather than just for FCS battalions. We expect the increased revenue from the shift to be material beginning in 2010, and extend for the next three to five years. Also, funding for robots will transfer into the core budget from programs currently funded by supplemental bills.

In addition, we expect international sales opportunities to begin in 2010 and extend well beyond the initial DOD buy. To date, we have had positive field and test results as well as user pull on our robots. Restructuring the program has the potential to free funds to accelerate slightly further. There is some risk, however, that contracts and our funding will be delayed, while the Defense Department sorts out its new direction.

When we spoke to you last quarter, we anticipated an FCS SUGV production decision in orders in late 2009. At this point, we are uncertain about that timing. Based on the conversations with our customers, however, we expect to receive additional 2009 orders for SUG variants such as the \$17 million contract for the mini-EOD that the iRobot Boeing team won in February, as well as more orders for the PackBot 510 than we had originally anticipated for 2009.

The military shift in focus from Iraq to Afghanistan positively impacts our expectations of sales to the military as the rough terrain and lack of urban transport requires a lighter, more mobile robot. Both Iraq and Afghanistan employ our robots in detecting and diffusing roadside bombs or providing situational awareness for the troops in urban settings or clearing caves.

Our robots provide a low-cost solution for the current state of a regular warfare. In addition to supplying robots to the US Government, we are gaining traction in international markets. In the first quarter, international revenue increased to \$2.8 million or 17% of G&I product revenue compared with \$800,000 or 4% last year. We delivered robots to seven countries outside of the United States, and expect the rest of the year to continue to be strong internationally, as we pursue additional orders in Europe, Asia and Latin America.

Iraqi government sales are a particular focus for us as the US troop levels are ramped down, and the Iraqi needs to ramp up the take over for these departing US forces. In March, we participated in the National Defense Industry Association's Ground Robotics

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Capabilities Conference. This is one of the most important industry conferences for us as it is focused on unmanned ground vehicles and is attended by general officers, war fighters, and all major players in the industry.

We demonstrated the Warrior, SUGV, FasTac, and PackBot 510 to a broad range of customers, and identified a range of new opportunities. Probably the most important information at the conference was the army's thinking about autonomous systems. The army articulated a system for more autonomy in the robots, which marks a significant change in their thinking. Generals and war fighters spoke passionately about having increased autonomy.

iRobot's sophisticated Aware operating system, which enables the development of increased autonomy, differentiates our robots and provides a barrier of entry for low-end companies and competitors.

New autonomous requirements for robots identified by the military include automated route clearance, convoy operations, persistent surveillance, and formation wingmen. iRobot has the platforms and leading technology that will be useful in addressing these new requirements.

The customer's increased focus on autonomy is a positive development for the industry as a whole, and for iRobot in particular as it supports our long-term strategy to develop and produce increasingly autonomous robotic systems.

We also experienced a bit of local excitement here in Massachusetts during the quarter, when the State Bomb Squad equipped with the PackBot First Responder successfully removed and destroyed suspicious packages in two local towns. The events received widespread media coverage, and the company had significant exposure as a result. Robots already play a central role in the military, but they have received -- they have recently taken center stage, alongside state and local police.

They have great utility in hostage situations, chemical and biological hazards, and even domestic disputes. They can be used by responders, where they need to understand the risks of a situation, without being physically present.

I'm very encouraged by our results for the quarter, and expect that the rest of 2009 will be challenging due to the current state of the economy and uncertainties around the timing of actions from Secretary Gates' proposed DOD budget. We will continue to tightly manage the business and drive EBITDA and operating cash flow. I will now turn the call over to John to review our first quarter financial results.

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**John Leahy** - *iRobot Corporation - CFO*

Thanks Colin. First quarter revenue of \$57 million was about even with last year, despite challenges in both divisions. Higher international home robot sales offset lower domestic sales, while revenues in G&I were generated by sales of PackBot FasTacs.

Loss per share for the quarter was \$0.07 compared with a loss of \$0.16 per share in 2008. Adjusted EBITDA loss for Q1 was \$300,000 compared with an adjusted EBITDA loss of \$4.4 million a year ago. Revenue, EPS and EBITDA all exceeded our Q1 expectations.

As a reminder, the Linens 'N Things bankruptcy last year adversely impacted revenue by \$1.8 million and EPS by \$0.05 in the first quarter a year ago. In the Home Robots division, shipments of 183,000 units generated \$33 million in revenue compared to 169,000 units and \$30 million in revenue a year ago.

International revenue increased 69% in the quarter year-over-year, and comprised more than 50% of home robot revenue. Domestic revenue, including direct, declined 22% year-over-year. In the G&I division, total revenue declined 11% to \$24 million in the quarter largely due to order timing.

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Revenue was driven by fulfillment of several orders for the PackBot FasTac. Contract revenue increased 9% in the quarter due to funding for Warrior development in various PackBot sensor programs. G&I product revenue was \$17 million in the first quarter compared to \$20 million a year ago due to the timing of orders from the government. Product life-cycle revenue was \$4 million or 26% of G&I product revenue compared with 16% of product revenue in Q1 last year.

For the total company, gross margin for the first quarter was 28.5%, up from 26.8% last year. Home Robot gross margin increased 4.2 percentage points in Q1, largely due to the impact of Linens 'N Things last year, while G&I gross margin decreased 1.8 points mostly due to lower overhead absorption and decreased revenue.

Operating expenses improved \$2.5 million year-over-year in Q1. Expenses totaled 34.6% of revenue, down from 38.8% last year. The overall reduction in operating expense was driven by a reduction in selling and marketing, as we aggressively managed our expenses.

We generated \$14.3 million of operating cash flow for the quarter compared with breakeven in Q1 last year. The improvement this year is the result of our focus on inventory management and strong receivables collection. We have now generated \$34 million in operating cash flow over the past two quarters. At the end of the first quarter, we had cash and investments totaling \$55 million, compared with \$41 million at the end of December.

Over the past two quarters, we have improved our cash position by \$28 million, and our cash balance is at its highest level in almost two years. We expect our cash balance to decrease at the end of the second and third quarters, as we build inventory for the holiday season before growing again in Q4.

Day sales outstanding were 42 days, up from 38 at the end of the fourth quarter, and 39 last year. At the end of the quarter, inventory was \$31 million, down from \$35 million at the end of the fourth quarter and down from \$46 million a year ago.

To summarize, we exceeded expectations in a difficult environment and continue to strengthen the company's financial position. The remainder of the year promises to be challenging, but we will continue to aggressively manage the key drivers of valuation, EBITDA, working capital, and operating cash flow. Now I would like to turn the call back to Colin.

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**Colin Angle** - *iRobot Corporation - Chairman, CEO*

Thank you John. We had a very good first quarter at both the top and bottom lines and outperformed expectations, however, there is uncertainty moving forward. In summary, we generated more than \$14 million in operating cash flow at the end of the first quarter with nearly \$55 million in cash and reported a \$4 million improvement in adjusted EBITDA year-over-year.

Our international home robot business continues to offset the recession-driven domestic decline. We believe the Defense Secretary Gates' statement regarding the strategic reshaping of the DOD spending is very positive for iRobot, but the details and timing are uncertain.

Net-net, we need to continue to manage the business aggressively, but are well positioned for strong operating performance in the future. Before we take your questions, I like to provide you with our financial expectations for the second quarter.

We are expecting revenues to be in the range of \$57 million to \$62 million. For Q2 we expect a loss per share of \$0.10 to \$0.14, and we expect adjusted EBITDA loss for Q2 to be between \$1 million and \$4 million. We're reaffirming our full-year expectations. For 2009, we anticipate revenues to be in the range of \$290 million to \$310 million, earnings per share to be between breakeven and \$0.04, and adjusted EBITDA to be between \$14 million and \$17 million. With that we will open the call to your questions. Thank you.

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## QUESTIONS AND ANSWERS

### Operator

Thank you. (Operator Instructions). And we will take our first question from Jim Ricchiuti with Needham & Company.

### Jim Ricchiuti - Needham & Company - Analyst

Yes, good morning. I wonder with respect to the guidance, the full-year guidance you've given for revenues, has the mix of that business changed at all. It sounds -- it appears that the home robot business at least internationally remains very strong and looks like there are some moving parts to the G&I business. I'm just wondering as you look out at the balance of the year how you see the mix of business.

### Colin Angle - iRobot Corporation - Chairman, CEO

I think you've got that right. The home robot side of revenue is consistent with our prior expectations, and on the government and industrial side we are seeing some push out of the FCS SUGV revenue replaced by stronger PackBot 510 revenue. So there are moving parts but we like the math.

### Jim Ricchiuti - Needham & Company - Analyst

John, how would you characterize your visibility for the G&I business this year? Has it -- versus, say, three months ago?

### John Leahy - iRobot Corporation - CFO

It continues to improve. We are at 42% for the year, as we like to say sort of in the bag where we can either -- we either have signed contracts, have services already rendered and -- or existing backlog under contract. So that is a figure that we have talked about before and that has improved over the last year, and then we have more revenue coming that is in less certain buckets. So we feel good about it.

### Jim Ricchiuti - Needham & Company - Analyst

Okay, and if I can and may, one follow-up, is there any color you could provide on the strength of the international business, specifically the countries where you are seeing very strong demand for the products?

### Colin Angle - iRobot Corporation - Chairman, CEO

Well, on the home robots side, the strongest areas right now are in Europe, and as we mentioned that -- well, we understand that the economies in the rest of the world, and particularly Europe are weakening. We are operating off a smaller base and we see expansion of demand for the product outpacing the recessionary impact. So, certainly we will be doing better with the economy stronger. About 80% of our international sales are currently coming from Europe.

### Jim Ricchiuti - Needham & Company - Analyst

Okay, thank you.

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**Operator**

We will take our next question from Barbara Coffey with Kaufman.

**Barbara Coffey** - Kaufman Brothers - Analyst

Yes, good morning. Can you speak a bit about the consumer side of what you're seeing from the direct of your own website sales versus what sort of the profile of the companies you are selling through or the Bed Bath & Beyond, it shifting at all through a different profile.

**Colin Angle** - iRobot Corporation - Chairman, CEO

The profile we are seeing is roughly consistent. We haven't seen the recessionary impact drive a fundamental change in customer buying behavior. We are basically domestically down all over by similar percentages. So, I don't think people are being forced or driven to the web or driven to retail. It's just consistent across the board impact.

**Barbara Coffey** - Kaufman Brothers - Analyst

Are you seeing greater traction with lower-priced home robots or is that consistent as well.

**Colin Angle** - iRobot Corporation - Chairman, CEO

We are seeing some impact on that front but on the web, the higher priced units have always been our strong sellers. So, I think that we may see some stratification where people are either going low-end or high-end on the web, and if the center price points are suffering a bit, but it is, you know, it's subtle.

**Barbara Coffey** - Kaufman Brothers - Analyst

Thank you.

**Operator**

We will take our next question from Paul Coster with JPMorgan.

**Paul Coster** - JPMorgan - Analyst

Yes, thank you. Colin, the international sales were obviously excellent. Can you just talk a little bit about the pricing of international product relative to domestic products, and also sell in to the channel versus sell through and how that will evolve as the year progresses?

**Colin Angle** - iRobot Corporation - Chairman, CEO

Sure. We managed to keep our pricing strategy for international consistent with what we did last year. We haven't -- you know, we did not do all our transactions denominated in dollars. So the (inaudible) of the dollar has put some pressure on our international distributors, but it has been consistent.



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As far as sell in versus sell through, the international distributors have been doing some channel expansion based on the strength of sales, but as we look at it, the vast majority of the improvement we've seen year-over-year is coming from improvements in the sell through. We are not opening up substantial percentages of new stores so that -- which could artificially increase sales. So we feel good about that.

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**Paul Coster** - JPMorgan - Analyst

Do you have any sense of the demographics of use in Europe? Is it young people, sort of you know, well to do people. How is it working out there? You are getting any feedback?

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**Colin Angle** - iRobot Corporation - Chairman, CEO

Something that we do look at, not something that we're going to share on this call, but it is not something that is surprising or radically different from what we are seeing domestically. So the strength of our market is in the age ranges between 25 and 50, it skews slightly female, maybe 60/40, that type of skew, but it is quite consistent with domestic.

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**Paul Coster** - JPMorgan - Analyst

Okay, on the G&I front, you've obviously got a number of some newish kind of products, you got R-Gator and Warrior and, I know you had a DARPA project that you are doing, and if you bought the underwater business. Can you just talk a little bit about all of above and whether there is any sort of significant revenue opportunities associated with them in the next, let's say, next year?

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**Colin Angle** - iRobot Corporation - Chairman, CEO

Well the -- we have talked a bit about the emergence of SUGV, and we've got -- and the back half is going to be materially driven by these SUGV variants, although not the FCS version of the SUGV. So that program is on track and ramping very nicely. The back half of the year is also going to be impacted by the beginning of sales of the Warrior robot, although it's not going to be tremendously material in 2009, but we're going to start to see the revenue build on the Warrior side.

The -- our Maritime Systems group is selling Seaglidors. This is our long-range high endurance robot. We've closed contracts this week with -- for three of these robots with a University in UK. We have a strong backlog of perspective customers on that front. So those are starting to move and they carry a good price point. So that that is going to contribute.

And the other products that you referenced, the Ranger robot is going to be associated with some contract revenue in the back half, but not product revenue in the back half of the year. So certainly it is true that the numbers of revenue generating military robots is expanding strongly in the back half, and we'll see that momentum continuing into 2010.

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**Paul Coster** - JPMorgan - Analyst

Okay, last question. Any update on the roadmap for home robots?

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**Colin Angle** - iRobot Corporation - Chairman, CEO

If you're asking for new product announcements, you're going to be once again disappointed. We are not announcing anything on this call. So, we continue to invest in new product development, and as you know, we will let you guys know as soon as it's ready and fit for launch, and that will be around the same time you're reading about it in the newspapers.

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**Paul Coster** - JPMorgan - Analyst

Well then, thanks Collin.

**Operator**

We will take our next question from Jeff Evanson with Dougherty & Company.

**Charlie Anderson** - Dougherty & Company - Analyst

Great, this is actually Charlie for Jeff. How are you guys today?

**Colin Angle** - iRobot Corporation - Chairman, CEO

Good.

**Charlie Anderson** - Dougherty & Company - Analyst

Good. Just a question on, you know, international, you guys obviously saw really strong in Q1 on consumer. When you look at the guidance it's a little bit more tame, you are not carrying it through. So I just wonder if you see any sort of a slow down there, and you feel that can be consistent throughout the year on the international.

**John Leahy** - iRobot Corporation - CFO

Really what you are seeing in our guidance is the fact that we continue to be in recessionary time. We have this potential very positive news coming out of the DOD with uncertain timing, and, you know, I think it would be foolhardy to say that we are bullish and optimistic with these types of risk factors out there, and so that certainly the first quarter was positive, but there is a lot to follow through and get done in this year. So, I think that we are comfortable with the guidance that we've provided and are willing to stand behind that.

**Charlie Anderson** - Dougherty & Company - Analyst

Next question is about the SUGV variants; obviously you guys got the mini-EOD order. What are some of the other variants you're anticipating there? And then also, you know, on the mini-EOD itself, were you guys recognizing any revenue from that in the quarter and is that you know, completely sort of a 2009 event that contract?

**Colin Angle** - iRobot Corporation - Chairman, CEO

So the mini-EOD contract, a very small amount of revenue is recognized in the second quarter. The bulk of that extends through the balance of the year, and as far as other revenue, we are -- we do have a non FCS variant that we are marketing, and believe will be driving some real revenue in the back half. So it is officially in our product line and in our bag of things to deliver to customers.

**Charlie Anderson** - Dougherty & Company - Analyst

Is that in that bag category the SUGV variants, the 42%?

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**Colin Angle** - *iRobot Corporation - Chairman, CEO*

No that is not in the 42%. 42%, we are very conservative on that number. That is things that are actually under contract or already shipped. So that is in the other bag to be nailed down.

**Charlie Anderson** - *Dougherty & Company - Analyst*

Got it. Thanks a lot guys.

**Colin Angle** - *iRobot Corporation - Chairman, CEO*

You bet.

**Operator**

We will take a follow-up question from Jim Ricchiuti with Needham & Company.

**Jim Ricchiuti** - *Needham & Company - Analyst*

The international portion of the G&I business seems to be growing nicely, and I wonder if you have a target in mind as to what you would like to see that represent over the long term as a percent of G&I.

**John Leahy** - *iRobot Corporation - CFO*

Jim in Q1 for G&I, international was about 17%. For the rest of this year, we are probably looking in the range of about 15% of product revenue being international for G&I, but as Colin mentioned in his remarks, it is an area of growing focus for us. We've put more resource behind selling overseas. So, we expect over time that we would have a percentage of revenue of 20% or greater coming internationally for the G&I business.

**Colin Angle** - *iRobot Corporation - Chairman, CEO*

All right. Well, thank you very much. That concludes our first quarter earnings call. We very much appreciate your support. I look forward to talking with you again following our second quarter.

**Operator**

Thank you and at this time I would like to turn the conference back over to Colin Angle for any additional comments.

**Colin Angle** - *iRobot Corporation - Chairman, CEO*

Thanks again and good-bye.

**Operator**

That does conclude today's conference call. Thank you for joining us and have a wonderful day.

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