Cree, Inc.
Non-GAAP Measures of Financial Performance

To supplement the Company's consolidated financial statements presented in accordance with generally accepted accounting principles, or GAAP, Cree uses non-GAAP measures of certain components of financial performance. These non-GAAP measures include non-GAAP gross margin, non-GAAP operating (loss) income, non-GAAP non-operating income (expense), net, non-GAAP net (loss) income, non-GAAP diluted (loss) earnings per share from continuing operations and free cash flow.

Reconciliation to the nearest GAAP measure of all historical non-GAAP measures included in this press release can be found in the tables included with this press release. Both our GAAP targets and non-GAAP targets do not include any estimated changes in the fair value of our Lextar investment.

Non-GAAP measures presented in this press release are not in accordance with or an alternative to measures prepared in accordance with GAAP and may be different from non-GAAP measures used by other companies. In addition, these non-GAAP measures are not based on any comprehensive set of accounting rules or principles. Non-GAAP measures have limitations in that they do not reflect all of the amounts associated with Cree's results of operations as determined in accordance with GAAP. These non-GAAP measures should only be used to evaluate Cree's results of operations in conjunction with the corresponding GAAP measures.

Cree believes that these non-GAAP measures, when shown in conjunction with the corresponding GAAP measures, enhance investors' and management's overall understanding of the Company's current financial performance and the Company's prospects for the future, including cash flows available to pursue opportunities to enhance shareholder value. In addition, because Cree has historically reported certain non-GAAP results to investors, the Company believes the inclusion of non-GAAP measures provides consistency in the Company's financial reporting.

For its internal budgeting process, and as discussed further below, Cree's management uses financial statements that do not include the items listed below and the income tax effects associated with the foregoing. Cree's management also uses non-GAAP measures, in addition to the corresponding GAAP measures, in reviewing the Company's financial results.

Cree excludes the following items from one or more of its non-GAAP measures when applicable:

Stock-based compensation expense. This expense consists of expenses for stock options, restricted stock, performance stock awards and employee stock purchases through its ESPP. Cree excludes stock-based compensation expenses from its non-GAAP measures because they are non-cash expenses that Cree does not believe are reflective of ongoing operating results.

Amortization or impairment of acquisition-related intangibles. Cree incurs amortization or impairment of acquisition-related intangibles in connection with acquisitions. Cree excludes these items because they arise from Cree's prior acquisitions and have no direct correlation to the ongoing operating results of Cree's business.

Factory optimization restructuring. In May 2019, the Company started a significant, multi-year factory optimization plan ("factory optimization plan") to be anchored by a state-of-the-art, automated 200mm silicon carbide fabrication facility. In September 2019, the Company announced the intent to build the new fabrication facility in Marcy, New York to complement the factory expansion underway at its U.S. campus headquarters in Durham, North Carolina. As part of the plan, the Company will incur restructuring costs associated with the movement of equipment as well as disposals on certain long-lived assets. Because these charges relate to assets which had been retired prior to the end of their estimated useful lives, Cree does not believe these costs are reflective of ongoing operating results. Similarly, Cree does not consider the realized losses on sale of assets relating to the restructuring to be reflective of ongoing operating results.

Severance and other restructuring. For the six months ended December 29, 2019, these costs relate to the Company realigning its sales resources as part of the Company's transition to a more focused semiconductor company. For the six months ended December 30, 2018, these costs relate to the Company realigning the Company's cost base with a long-range business strategy that was announced in February 2018. Cree does not believe these costs are reflective of ongoing operating results.

Project, transformation and transaction costs. The Company has incurred professional services fees and other costs associated with acquisitions and divestitures, as well as for internal transformation programs designed to improve its operating margins and change the manner in which business is conducted. Cree excludes these items because Cree believes they are not reflective of the ongoing operating results of Cree's business.

Factory optimization start-up costs. The Company has incurred and will incur start-up costs as part of the factory optimization plan. Cree does not believe these costs are reflective of ongoing operating results.

Non-restructuring related executive severance. The Company has incurred costs in conjunction with the termination of key executive personnel. Cree excludes these items because Cree believes they have no direct correlation to the ongoing operating results of Cree's business.

Transition service agreement costs. As a result of the sale of the Lighting Products business unit, the Company is providing certain IT services under a transition services agreement which will not be reimbursed. Cree excludes the costs of these services because Cree believes they are not reflective of the ongoing operating results of Cree's business.

Asset impairment. The Company incurred impairment charges in conjunction with the factory optimization plan. Cree excludes these items because Cree believes they are not reflective of the ongoing operating results of Cree's business.

Net changes in fair value of our Lextar investment. The Company's common stock ownership investment in Lextar Electronics Corporation is accounted for utilizing the fair value option. As such, changes in fair value are recognized in income, including fluctuations due to the exchange rate between the New Taiwan Dollar and the United States Dollar. Cree excludes the impact of these gains or losses from its non-GAAP measures because they are non-cash impacts that Cree does not believe are reflective of ongoing operating results. Additionally, Cree excludes the impact of dividends received on its Lextar investment as Cree does not believe it is reflective of ongoing operating results.

Accretion on convertible notes. In August 2018, the Company issued $575 million in convertible notes resulting in interest accretion on the convertible notes' issue costs and discount. Management considers these items as either limited in term or having no impact on the Company's cash flows, and therefore has excluded such items to facilitate a review of current operating performance and comparisons to our past operating performance.

Income tax adjustment. This amount reconciles GAAP tax expense (benefit) to a calculated non-GAAP tax expense (benefit) utilizing a non-GAAP tax rate. The non-GAAP tax rate estimates an appropriate tax rate if the listed non-GAAP items were excluded. This reconciling item adjusts non-GAAP net (loss) income to the amount it would be if the calculated non-GAAP tax rate was applied to non-GAAP (loss) income before taxes.

Cree may incur some of these same expenses, including income taxes associated with these expenses, in future periods. In addition to the non-GAAP measures discussed above, Cree also uses free cash flow as a measure of operating performance and liquidity. Free cash flow represents operating cash flows from continuing operations less net purchases of property and equipment and patent and licensing rights. Cree considers free cash flow to be an operating performance and a liquidity measure that provides useful information to management and investors about the amount of cash generated by the business after the purchases of property and equipment, a portion of which can then be used to, among other things, invest in Cree's business, make strategic acquisitions, strengthen the balance sheet and repurchase stock. A limitation of the utility of free cash flow as a measure of operating performance and liquidity is that it does not represent the residual cash flow available to the company for discretionary expenditures, as it excludes certain mandatory expenditures such as debt service.

CREE, INC.
Reconciliation of GAAP to Non-GAAP Measures
(in millions of U.S. Dollars, except per share amounts and percentages)
(unaudited)

Non-GAAP Gross Margin

	Three months ended		Six months ended	
	December 29, 2019	**December 30, 2018**	**December 29, 2019**	**December 30, 2018**
GAAP gross profit	$61.9	$103.5	$136.1	$201.8
GAAP gross margin percentage	26 %	37 %	28 %	36 %
Adjustments:				
Stock-based compensation expense	2.5	1.8	4.7	3.4
Project, transformation and transaction	—	—	—	1.2
Non-GAAP gross profit	$64.4	$105.3	$140.8	$206.4
Non-GAAP gross margin percentage	27 %	38 %	29 %	37 %

Non-GAAP Operating (Loss) Income

	Three months ended		Six months ended	
	December 29, 2019	**December 30, 2018**	**December 29, 2019**	**December 30, 2018**
GAAP operating (loss) income from continuing operations	($56.4)	$10.0	($95.3)	$20.8
GAAP operating (loss) income percentage	(24)%	4 %	(20)%	4 %
Adjustments:				
Stock-based compensation expense:				
Cost of revenue, net	2.5	1.8	4.7	3.4
Research and development	2.4	2.2	4.8	3.7
Sales, general and administrative	8.1	7.0	20.4	13.9
Total stock-based compensation expense	13.0	11.0	29.9	21.0
Amortization or impairment of acquisition-related intangibles	3.6	3.9	7.2	7.8
Factory optimization restructuring	1.2	—	2.4	—
Severance and other restructuring	—	—	0.8	2.6
Project, transformation and transaction costs	10.8	0.2	13.4	1.8
Factory optimization start-up costs	1.5	—	2.9	—
Non-restructuring related executive	0.3	—	1.5	—
Transition service agreement costs	5.2	—	8.2	—
Asset impairment	—	—	0.2	—
Non-GAAP operating (loss) income	($20.8)	$25.1	($28.8)	$54.0
Non-GAAP operating (loss) income	(9)%	9 %	(6)%	10 %

Non-GAAP Non-Operating Income (Expense), net

	Three months ended		Six months ended	
	December 29, 2019	December 30, 2018	December 29, 2019	December 30, 2018
Non-operating income (expense), net	$5.1	($5.6)	$6.7	($15.3)
Adjustments:				
Net changes in the fair value of Lextar investment	(7.8)	1.8	(11.2)	9.1
Accretion on convertible notes	5.8	5.4	11.4	7.2
Non-GAAP non-operating income, net	$3.1	$1.6	$6.9	$1.0

Non-GAAP Net (Loss) Income

	Three months ended		Six months ended	
	December 29, 2019	December 30, 2018	December 29, 2019	December 30, 2018
GAAP net loss from continuing operations	($52.5)	($0.2)	($90.3)	($1.0)
Net income attributable to noncontrolling interest	$0.3	$—	$0.3	$—
GAAP net loss from continuing operations attributable to controlling interest	($52.8)	($0.2)	($90.6)	($1.0)
Adjustments:				
Stock-based compensation expense	13.0	11.0	29.9	21.0
Amortization or impairment of acquisition-related intangibles	3.6	3.9	7.2	7.8
Factory optimization restructuring	1.2	—	2.4	—
Severance and other restructuring	—	—	0.8	2.6
Project, transformation and transaction costs	10.8	0.2	13.4	1.8
Factory optimization start-up costs	1.5	—	2.9	—
Non-restructuring related executive severance	0.3	—	1.5	—
Transition service agreement costs	5.2	—	8.2	—
Asset impairment	—	—	0.2	—
Net changes in the fair value of Lextar investment	(7.8)	1.8	(11.2)	9.1
Accretion on convertible notes	5.8	5.4	11.4	7.2
Total adjustments to GAAP net loss from continuing operations attributable to controlling interest before provision for income taxes	33.6	22.3	66.7	49.5
Income tax adjustment - benefit (expense)	8.8	(0.2)	9.8	(3.4)
Non-GAAP net (loss) income from continuing operations attributable to controlling interest	($10.4)	$21.9	($14.1)	$45.1
Non-GAAP diluted (loss) earnings per share from continuing operations attributable to controlling interest	($0.10)	$0.21	($0.13)	$0.44
Non-GAAP weighted average shares (in thousands)	107,925	102,871	107,519	102,396

Free Cash Flow

	Three months ended		Six months ended	
	December 29, 2019	**December 30, 2018**	**December 29, 2019**	**December 30, 2018**
Net cash provided by (used in) operating activities of continuing operations	$8.2	$68.7	($11.8)	$109.8
Less: PP&E spending	(59.0)	(32.2)	(101.0)	(63.2)
Less: Patents spending	(2.2)	(1.4)	(3.3)	(3.8)
Total free cash flow	($53.0)	$35.1	($116.1)	$42.8

CREE, INC.
Business Outlook Unaudited GAAP to Non-GAAP Reconciliation

(in millions of U.S. Dollars)	**Three Months Ended March 29, 2020**
GAAP net loss outlook range	($68) to ($62)
Adjustments:	
Stock-based compensation expense	13
Amortization or impairment of acquisition-related intangibles	4
Factory optimization restructuring and start-up costs	6
Accretion on convertible notes	6
Project, transformation, transaction and transition costs	13
Total adjustments to GAAP net loss before provision for income taxes	42
Income tax adjustment	10
Non-GAAP net loss outlook range	($16) to ($10)

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Source: Cree, Inc.