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 income, non-GAAP non-operating income, net, non-GAAP net income, non-GAAP earnings per diluted share 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. In this press release, Cree also presents its target for non-GAAP expenses, which are expenses less expenses in the various categories described below. 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:

Contract manufacturer dispute related expenses. In fiscal 2016, the Company recognized charges associated with a dispute with a former Lighting Products contract manufacturer, whom Cree ceased utilizing as of the end of 2014. Because these charges relate to amounts from prior fiscal years, Cree does not consider these charges to be reflective of ongoing operating results.

T8 product recall charges. In fiscal 2016, the Company recognized charges associated with the product recall of its Linear LED T8 Replacement Lamps and the associated discontinuance of this product line. Because these charges relate to the exit from a market segment, Cree does not consider these charges to reflective of ongoing operating results.

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.

LED business restructuring charges or gains. In June 2015, Cree's board of directors approved a plan to restructure the LED business. The restructuring, which was completed during fiscal 2016, reduced excess capacity and overhead in order to improve the cost structure moving forward. The components of the restructuring included the planned sale or abandonment of certain manufacturing equipment, facility consolidation and the elimination of certain positions. Because these charges relate to assets which have been retired prior to the end of their estimated useful lives and severance costs for eliminated positions, Cree does not consider these charges to be reflective of ongoing operating results. Similarly, Cree does not consider realized gains on the sale of assets relating to the restructuring to be reflective of ongoing operating results.

Changes in the 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.

Recognition of deferred IPO (Initial Public Offering) costs. In fiscal 2016, the Company recognized an expense for previously deferred IPO costs due to the delay in the anticipated timing of the planned initial public offering of Wolfspeed, as required by SEC guidance. Cree excludes the impact of this expense as Cree does not consider this charge to be reflective of ongoing operating results.

Transaction costs and termination fee associated with the terminated sale of the Wolfspeed business. The Company has incurred transaction costs in conjunction with the previously proposed sale of its Wolfspeed business to Infineon. In addition, as a result of the termination of the agreement to sell the Wolfspeed business, Infineon paid a termination fee to the Company. Because these costs were incurred, and the termination fee received, relative to a portion of the business which was previously reported as discontinued operations in fiscal 2017, Cree does not consider these amounts to be reflective of ongoing operating results.

Income tax effects of the foregoing non-GAAP items. This amount is used to present each of the amounts described above on an after-tax basis consistent with the presentation of non-GAAP net income. Non-GAAP net income is presented using a non-GAAP tax rate. The Company’s non-GAAP tax rate represents a recalculation of the GAAP tax rate reflecting the exclusion of the non-GAAP items.

Cree expects to incur many 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 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 thousands, except per share amounts and percentages)
(unaudited)

Non-GAAP Gross Margin

	Three Months Ended		Year Ended	
	June 25, 2017	**June 26, 2016**	**June 25, 2017**	**June 26, 2016**
GAAP gross profit	$98,001	$113,023	$434,572	$487,074
GAAP gross margin percentage	27.3%	29.1%	29.5%	30.1%
Adjustments:				
Contract manufacturer dispute related expenses	—	2,108	—	2,108
T8 product recall charges	—	1,349	—	1,349
Stock-based compensation expense	2,415	3,170	10,427	12,394
Non-GAAP gross profit	$100,416	$119,650	$444,999	$502,925
Non-GAAP gross margin percentage	28.0%	30.8%	30.2%	31.1%

Non-GAAP Operating Income

	Three Months Ended		Year Ended	
	June 25, 2017	**June 26, 2016**	**June 25, 2017**	**June 26, 2016**
GAAP operating loss	($13,067)	($4,791)	($18,672)	($10,471)
GAAP operating income percentage	(3.6)%	(1.2)%	(1.3)%	(0.6)%
Adjustments:				
Contract manufacturer dispute related expenses	—	2,108	—	2,108
T8 product recall charges	—	1,349	—	1,349
Stock-based compensation expense:				
Cost of revenue, net	2,415	3,170	10,427	12,394
Research and development	2,151	3,289	10,619	13,842
Sales, general and administrative	4,741	7,952	26,679	32,492
Total stock-based compensation expense	9,307	14,411	47,725	58,728
Amortization or impairment of acquisition-related intangibles	6,792	7,290	27,499	28,732
Costs associated with LED business restructuring	—	133	15	17,710
Recognition of deferred IPO costs	—	—	—	1,810
Transaction costs related to the terminated sale of the Wolfspeed business	121	1,041	11,947	1,745
Wolfspeed transaction termination fee	—	—	(12,500)	—
Total adjustments to GAAP operating loss	16,220	26,332	74,686	112,182
Non-GAAP operating income	$3,153	$21,541	$56,014	$101,711
Non-GAAP operating income percentage	0.9 %	5.5 %	3.8 %	6.3 %

Non-GAAP Non-Operating Income, net

	Three Months Ended		Year Ended	
	June 25, 2017	June 26, 2016	June 25, 2017	June 26, 2016
GAAP non-operating income (loss), net	$9,057	$1,040	$14,008	($13,035)
Adjustment:				
Net changes in the fair value of Lextar investment	(7,607)	(59)	(10,203)	15,832
Non-GAAP non-operating income, net	$1,450	$981	$3,805	$2,797

Non-GAAP Net Income

	Three Months Ended		Year Ended	
	June 25, 2017	June 26, 2016	June 25, 2017	June 26, 2016
GAAP net loss	($5,890)	($10,641)	($98,118)	($21,536)
Adjustments:				
Contract manufacturer dispute related expenses	—	2,108	—	2,108
T8 product recall charges	—	1,349	—	1,349
Stock-based compensation expense	9,307	14,411	47,725	58,728
Amortization or impairment of acquisition-related intangibles	6,792	7,290	27,499	28,732
Costs associated with LED business restructuring	—	133	15	17,710
Recognition of deferred IPO costs	—	—	—	1,810
Transaction costs related to the terminated sale of the Wolfspeed business	121	1,041	11,947	1,745
Wolfspeed transaction termination fee	—	—	(12,500)	—
Net changes in the fair value of Lextar investment	(7,607)	(59)	(10,203)	15,832
Total adjustments to GAAP net loss before provision for income taxes	8,613	26,273	64,483	128,014
Income tax effect *	1,102	3,286	83,353	(18,937)
Non-GAAP net income	$3,825	$18,918	$49,718	$87,541
Income per share				
Non-GAAP diluted net income per share	$0.04	$0.19	$0.50	$0.86
Shares used in diluted net income per share calculation				
Non-GAAP shares used	97,548	100,663	98,487	101,783

*Estimated income tax effect is based upon the Company's overall consolidated effective tax rate for the given period.

Free Cash Flow

	Three Months Ended		Year Ended	
	June 25, 2017	June 26, 2016	June 25, 2017	June 26, 2016
Cash flow from operations	$52,746	$64,553	$215,900	$203,316
Less: PP&E spending	(30,033)	(20,326)	(86,928)	(120,018)
Less: Patents spending	(3,529)	(3,409)	(12,405)	(14,443)
Total free cash flow	$19,184	$40,818	$116,567	$68,855

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