

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 net income, non-GAAP earnings per diluted share, non-GAAP gross margin, non-GAAP operating expenses 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 operating expenses, which is operating expenses less stock-based compensation expense, charges for amortization or impairment of acquired intangibles, acquisition finished goods inventory step-up, and acquisition costs.

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 stock-based compensation expense or amortization or impairment of acquired intangible assets, and the income taxes associated with the foregoing, and also do not include acquisition finished goods inventory step-up or acquisition costs. Cree's management also uses non-GAAP measures, in addition to the corresponding GAAP measures, in reviewing the company's financial results.

The Consolidated GAAP Gross Profit includes amounts that are excluded for non-GAAP measures in the "Unallocated Costs" in the Segment Reporting. The Company does not consider these costs when evaluating segment performance and allocating resources.

As described above, 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 and employee stock purchases through its Employee Stock Purchase Plan (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 acquired intangible assets. Cree incurs amortization or impairments of acquired intangible assets in connection with acquisitions. Cree excludes these items because they arise from Cree's prior acquisitions and have no direct correlation to the current operating results of Cree's business.

Ruud Lighting Finished Goods Inventory Step-up. The inventory purchased as part of the Ruud Lighting acquisition was recorded at fair value at the time of the acquisition. In particular, the finished goods inventory was valued at the anticipated customer sales price less cost to sell, which is higher than the

cost to produce the finished goods. Cree refers to the difference between the fair value and cost to produce as the Ruud Lighting finished goods inventory step-up. Cree excludes this inventory step-up item as Cree does not believe this step-up value is reflective of ongoing operating results.

Ruud Lighting Acquisition Cost. Cree incurred expenses directly related the acquisition of Ruud Lighting. These expenses include auditor fees, investment banking fees, legal fees and other consulting fees incurred to conclude the acquisition. Cree excludes these expenses as they bear no direct correlation to the current operating results and are not reflective of the 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.

Cree expects to incur stock-based compensation expense and amortization of acquired intangible assets in future periods, including income taxes associated with the foregoing. In addition to the non-GAAP measures discussed above, Cree also uses free cash flow as a measure of operating performance. Free cash flow represents operating cash flows less net purchases of property and equipment and payments for patent and licensing rights. Cree considers free cash flow to be 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, 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 financial performance is that it does not represent the total increase or decrease in the company's cash balance for the period.

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		Six Months Ended	
	December 30, 2012	December 25, 2011	December 30, 2012	December 25, 2011
GAAP gross profit	\$ 133,476	\$ 105,118	\$ 249,525	\$ 203,146
GAAP gross margin percentage	38.5%	34.6%	37.7%	35.4%
Adjustment:				
Stock-based compensation expense	\$ 2,257	\$ 1,615	\$ 4,541	\$ 3,329
Ruud Lighting finished goods inventory step-up	—	503	—	1,482
Non-GAAP gross profit	<u>\$ 135,733</u>	<u>\$ 107,236</u>	<u>\$ 254,066</u>	<u>\$ 207,957</u>
Non-GAAP gross margin percentage	39.2%	35.3%	38.4%	36.3%

Non-GAAP Operating Income

	Three Months Ended		Six Months Ended	
	December 30, 2012	December 25, 2011	December 30, 2012	December 25, 2011
GAAP operating income	\$ 25,092	\$ 12,192	\$ 42,381	\$ 25,579
GAAP operating income percentage	7.2%	4.0%	6.4%	4.5%
Adjustments				
Stock-based compensation expense	14,544	11,195	27,029	22,635
Amortization of acquisition-related intangible assets	7,719	7,367	15,389	11,292
Ruud Lighting acquisition costs	—	—	—	3,069
Ruud Lighting finished goods inventory step-up	—	503	—	1,482
Total adjustments to GAAP operating income	22,263	19,065	42,418	38,478
Non-GAAP operating income	\$ 47,355	\$ 31,257	\$ 84,799	\$ 64,057
Non-GAAP operating income percentage	13.7%	10.3%	12.8%	11.2%

Non-GAAP Net Income

	Three Months Ended		Six Months Ended	
	December 30, 2012	December 25, 2011	December 30, 2012	December 25, 2011
GAAP net income	\$ 20,403	\$ 12,078	\$ 36,526	\$ 24,897
Adjustments				
Stock-based compensation expense	14,544	11,195	27,029	22,635
Amortization of acquisition-related intangible assets	7,719	7,367	15,389	11,292
Ruud Lighting acquisition costs	—	—	—	3,069
Ruud Lighting finished goods inventory step-up	—	503	—	1,482
Total adjustments to GAAP income before provision for income taxes	22,263	19,065	42,418	38,478
Income tax effect *	(5,788)	(2,478)	(10,308)	(6,772)
Non-GAAP net income	\$ 36,878	\$ 28,665	\$ 68,636	\$ 56,603

Earnings per Share

Non-GAAP diluted net income per share	\$ 0.32	\$ 0.25	\$ 0.59	\$ 0.50
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Shares used in diluted net income per share calculation

Non-GAAP shares used	116,410	115,883	116,249	114,239
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* Based on effective tax rate calculated using forecasted non-GAAP income

Free Cash Flow

	Three Months Ended		Six Months Ended	
	December 30, 2012	December 25, 2011	December 30, 2012	December 25, 2011
Cash flow from operations	\$ 92,608	\$ 80,592	\$ 178,294	\$ 122,237
Less: PP&E CapEx spending	(17,833)	(19,076)	(30,430)	(53,038)
Less: Patents spending	(4,473)	(3,884)	(10,021)	(8,043)
Total free cash flow	\$ 70,302	\$ 57,632	\$ 137,843	\$ 61,156