

Non-GAAP Financial Measures

We provide non-GAAP gross margin, non-GAAP net income (loss), and non-GAAP earnings per share to eliminate the impact of items that we do not consider indicative of our overall operating performance. To arrive at our non-GAAP gross margin, we exclude stock-based compensation expense, expenses associated with discontinued products, and non-recurring expenses, if any, from our GAAP gross margin. To arrive at our non-GAAP net income (loss), we exclude all amortization of intangible assets, stock-based compensation expense, non-recurring expenses, unrealized foreign exchange gain (loss), losses from the disposal of idle assets, if any, non-GAAP tax expenses (benefits), and expenses associated with discontinued products, if any, from our GAAP net income (loss). Included in our non-recurring expenses in Q1 2020 and Q1 2019 are certain one-time legal (if any) and consulting fees (if any) and employee severance expenses (if any). In computing our non-GAAP income tax expense (benefit), we have applied an estimate of our annual effective income tax rate and applied it to our net income before income taxes.

Our non-GAAP earnings per share is calculated by dividing our non-GAAP net income by the fully diluted share count (for periods in which non-GAAP net income is positive) or basic share count (for periods in which our non-GAAP net income is negative). We believe that our non-GAAP measures are useful to investors in evaluating our operating performance for the following reasons:

- We believe that elimination of items such as amortization of intangible assets, stock-based compensation expense, non-recurring revenue and expenses, losses from the disposal of idle assets, unrealized foreign exchange gain or loss, unamortized debt issuance costs associated with the extinguishment of debt, and depreciation on certain equipment undergoing reconfiguration is appropriate because treatment of these items may vary for reasons unrelated to our overall operating performance;
- We believe that elimination of expenses associated with discontinued products, including depreciation and inventory obsolescence is appropriate because these expenses are not indicative of our ongoing operations;
- We believe that non-GAAP measures provide better comparability with our past financial performance, period-to-period results and with our peer companies, many of which also use similar non-GAAP financial measures; and
- We anticipate that investors and securities analysts will utilize non-GAAP measures as a supplement to GAAP measures to evaluate our overall operating performance.

A reconciliation of our GAAP net income (loss) and GAAP earnings (loss) per share for Q1 2020 to our non-GAAP net income (loss) and earnings (loss) per share is provided below, together with corresponding reconciliations for the quarter period ended March 31, 2019.

Non-GAAP measures should not be considered as an alternative to net income (loss), earnings (loss) per share, or any other measure of financial performance calculated and presented in accordance with GAAP. Our non-GAAP measures may not be comparable to similarly titled measures of other organizations because other organizations may not calculate such other non-GAAP measures in the same manner. We have not reconciled the non-GAAP measures included in our guidance to the appropriate GAAP financial measures because the GAAP measures are not readily determinable on a forward-looking basis. GAAP measures that impact our non-GAAP financial measures may include stock-based compensation expense, non-recurring expenses, amortization of intangible assets, unrealized exchange loss (gain), asset impairment charges, and loss (gain) from disposal of idle assets. These GAAP measures cannot be reasonably predicted and may directly impact our non-GAAP gross margin, our non-GAAP net income and our non-GAAP fully-diluted earnings per share, although changes with respect to certain of these measures may offset other changes. In addition, certain of these measures are out of our control. Accordingly, a reconciliation of the non-GAAP financial measure guidance to the corresponding GAAP measures is not available without unreasonable effort.

Applied Optoelectronics, Inc.
GAAP to Non-GAAP Reconciliation

(In thousands)

Preliminary Unaudited

	1Q18	2Q18	3Q18	4Q18	CY2018	1Q19	2Q19	3Q19	4Q19	CY2019	1Q20
GAAP revenue	65,239	87,822	56,386	58,018	267,465	52,719	43,411	46,084	48,658	190,872	40,467
Non-recurring customer credit	-	-	-	891	891	-	-	-	-	-	-
Non-GAAP revenue	65,239	87,822	56,386	58,909	268,356	52,719	43,411	46,084	48,658	190,872	40,467
GAAP total gross profit	25,836	33,863	17,537	10,537	87,773	12,351	10,538	11,976	11,336	46,201	6,338
Non-recurring customer credit	-	-	-	891	891	-	-	-	-	-	-
Share-based compensation expense	177	211	205	202	795	189	199	197	189	774	246
Non-recurring expense	7	-	-	43	50	-	-	-	-	-	970
Expenses associated with discontinued products	71	1,432	1,412	2,852	5,767	925	1,067	1,117	1,891	5,000	354
Non-GAAP income from gross profit	26,091	35,506	19,154	14,525	95,276	13,465	11,804	13,290	13,416	51,975	7,908
GAAP research and development expense	11,736	12,645	14,180	11,342	49,903	11,185	11,151	10,466	10,597	43,399	10,558
Share-based compensation expense	576	676	623	544	2,419	640	657	647	614	2,558	688
Non-recurring expense	-	43	-	13	56	-	-	-	-	-	212
Non-cash expenses associated with discontinued products	751	1,004	859	273	2,887	-	-	-	-	-	-
Non-GAAP research and development expense	10,409	10,922	12,698	10,512	44,541	10,545	10,494	9,819	9,983	40,841	9,658
GAAP sales and marketing expense	2,474	2,377	2,370	1,920	9,141	2,595	2,331	2,518	2,615	10,059	2,936
Share-based compensation expense	227	261	181	256	925	271	279	274	245	1,069	291
Non-recurring expense	-	-	-	-	-	-	-	-	-	-	18
Non-GAAP sales and marketing expense	2,247	2,116	2,189	1,664	8,216	2,324	2,052	2,244	2,370	8,990	2,627
GAAP general and administrative expense	9,456	9,898	10,591	9,552	39,497	10,440	10,884	9,988	10,178	41,490	10,638
Share-based compensation expense	1,588	1,752	1,885	1,758	6,983	1,843	1,885	1,860	1,816	7,404	2,013
Amortization expense	126	127	125	128	506	130	133	137	140	540	141
Non-recurring expense	284	287	685	1,121	2,377	69	813	568	94	1,544	301
Non-cash expenses associated with discontinued products	-	-	-	-	-	1,017	1,115	1,114	1,067	4,313	1,025
Non-GAAP general and administrative expense	7,458	7,732	7,896	6,545	29,631	7,381	6,938	6,309	7,062	27,690	7,158
GAAP total operating expense	23,666	24,920	27,141	22,814	98,541	24,220	24,366	22,972	23,390	94,948	24,132
Share-based compensation expense	2,391	2,689	2,689	2,558	10,327	2,754	2,821	2,781	2,676	11,032	2,992
Amortization expense	126	127	125	128	506	130	133	137	140	540	141
Non-recurring expense	284	330	685	1,134	2,433	69	813	568	94	1,544	531
Non-cash expenses associated with discontinued products	751	1,004	859	273	2,887	1,017	1,115	1,114	1,067	4,313	1,025
Non-GAAP total operating expense	20,114	20,770	22,783	18,721	82,388	20,250	19,484	18,372	19,414	77,520	19,443
GAAP operating income (loss)	2,170	8,943	(9,604)	(12,277)	(10,768)	(11,869)	(13,828)	(10,996)	(12,054)	(48,747)	(17,794)
Non-recurring customer credit	-	-	-	891	891	-	-	0	0	0	-
Share-based compensation expense	2,569	2,900	2,894	2,757	11,120	2,943	3,020	2,978	2,864	11,805	3,238
Amortization expense	126	127	125	128	506	130	133	137	140	540	141
Non-recurring expense	290	330	685	1,180	2,485	69	813	568	94	1,544	1,501
Expenses associated with discontinued products	71	1,432	1,412	2,852	5,767	925	1,067	1,117	1,891	5,000	354
Non-cash expenses associated with discontinued products	751	1,004	859	273	2,887	1,017	1,115	1,114	1,067	4,313	1,025
Non-GAAP operating income (loss)	5,977	14,736	(3,629)	(5,087)	11,997	(6,785)	(7,680)	(5,082)	(5,999)	(25,546)	(11,535)
GAAP other income (loss)	(1,046)	1,387	578	71	990	(1,079)	(729)	276	(1,109)	(2,641)	(1,052)
Loss (gain) from disposal of idle assets	-	-	-	8	8	-	-	-	-	-	-
Unrealized exchange loss (gain)	(203)	(911)	506	7	(601)	(227)	56	(65)	79	(157)	(169)
Non-recurring expense	0	0	0	0	0	173	-	-	-	173	-
Non-GAAP other income (loss)	(1,249)	476	1,084	86	397	(1,133)	(673)	211	(1,030)	(2,625)	(1,221)

Applied Optoelectronics, Inc.
GAAP to Non-GAAP Reconciliation

(In thousands)

Preliminary Unaudited

	1Q18	2Q18	3Q18	4Q18	CY2018	1Q19	2Q19	3Q19	4Q19	CY2019	1Q20
GAAP net income (loss)	2,120	8,034	(3,732)	(8,568)	(2,146)	(10,474)	(11,366)	(8,780)	(35,430)	(66,049)	(16,797)
Non-recurring customer credit				891	891	-	-	-	-	-	-
Amortization of intangible assets	126	127	125	128	506	130	133	137	140	540	141
Share-based compensation expense	2,569	2,900	2,894	2,757	11,120	2,943	3,020	2,978	2,864	11,804	3,238
Non Recurring charges	290	330	685	1,180	2,485	242	812	568	94	1,716	1,501
Expenses associated with discontinued products	71	1,432	1,412	2,852	5,767	925	1,067	1,117	1,891	5,000	354
Non-cash expenses associated with discontinued products	751	1,004	859	273	2,887	1,017	1,116	1,114	1,067	4,314	1,025
Loss (gain) from disposal of idle assets	-	-	-	8	8	-	-	-	-	-	-
Unrealized exchange loss (gain)	(203)	(911)	506	7	(601)	(227)	56	(65)	79	(157)	(169)
Non-GAAP Tax Benefit	(114)	(48)	-	-	(162)	-	-	-	25,736	25,736	1,915
Non-GAAP net income (loss)	5,610	12,868	2,749	(472)	20,755	(5,444)	(5,162)	(2,931)	(3,559)	(17,096)	(8,792)
GAAP net income (loss)	2,120	8,034	(3,732)	(8,568)	(2,146)	(10,474)	(11,366)	(8,780)	(35,430)	(66,049)	(16,797)
Non-recurring customer credit				891	891	-	-	-	-	-	-
Amortization of intangible assets	126	127	125	128	506	130	133	137	140	540	141
Share-based compensation expense	2,569	2,900	2,894	2,757	11,120	2,943	3,020	2,978	2,864	11,804	3,238
Depreciation expense	6,837	7,202	7,391	7,762	29,192	5,817	5,883	5,872	5,887	23,459	5,657
Non-recurring charges	290	330	685	1,180	2,485	242	812	568	94	1,716	1,501
Expenses associated with discontinued products	71	1,432	1,412	1,603	4,518	925	1,067	1,117	1,891	5,000	354
Loss (gain) from disposal of idle assets	-	-	-	8	8	-	-	-	-	-	-
Unrealized exchange loss (gain)	(203)	(911)	506	7	(601)	(227)	56	(65)	79	(157)	(169)
Interest (income) expense, net	19	194	188	423	824	752	1,181	1,170	1,206	4,309	1,308
Tax (benefit) expense related to the above	(996)	2,296	(5,294)	(3,638)	(7,632)	(2,474)	(3,191)	(1,940)	22,267	14,662	(2,048)
Adjusted EBITDA	\$10,833	\$21,604	\$4,175	\$2,553	\$39,165	(2,366)	(2,405)	\$1,057	(1,003)	(4,717)	(6,815)
GAAP diluted net income (loss) per share	\$ 0.11	\$ 0.40	\$ (0.19)	\$ (0.43)	\$ (0.11)	\$ (0.53)	\$ (0.57)	\$ (0.44)	\$ (1.76)	\$ (3.31)	\$ (0.83)
Non-recurring customer credit				0.05	0.04	-	-	-	-	-	-
Amortization of intangible assets	0.01	0.01	0.01	0.01	0.03	0.01	0.01	0.01	0.01	0.03	0.01
Share-based compensation expense	0.13	0.14	0.14	0.15	0.56	0.15	0.15	0.15	0.14	0.59	0.16
Non Recurring charges	0.01	0.02	0.03	0.06	0.12	0.01	0.04	0.03	0.00	0.09	0.07
Expenses associated with discontinued products	0.00	0.07	0.07	0.14	0.29	0.05	0.05	0.06	0.09	0.25	0.02
Non-cash expenses associated with discontinued products	0.04	0.05	0.04	0.01	0.14	0.05	0.06	0.05	0.05	0.22	0.05
Loss (gain) from disposal of idle assets	-	-	-	0.00	0.00	-	-	-	-	-	-
Unrealized exchange loss (gain)	(0.01)	(0.05)	0.04	(0.01)	(0.03)	(0.01)	0.00	(0.01)	0.00	(0.01)	(0.01)
Non-GAAP Tax Benefit	(0.01)	(0.00)	-	0.01	(0.00)	-	-	-	1.29	1.30	0.09
Non-GAAP diluted net income (loss) per share	\$ 0.28	\$ 0.64	\$ 0.14	\$ (0.02)	\$ 1.04	\$ (0.27)	\$ (0.26)	\$ (0.15)	\$ (0.18)	\$ (0.86)	\$ (0.44)
Shares used to compute diluted earnings per share	19,989	20,080	20,185	19,793	20,027	19,863	19,932	20,023	20,109	19,982	20,208