

DIODES INC /DEL/  
Form 10-K  
February 29, 2008

**United States  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**FORM 10-K**

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended **December 31, 2007**.

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

**Commission file number: 1-5740**

**DIODES INCORPORATED**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of incorporation or  
organization)

**95-2039518**

(I.R.S. Employer Identification  
Number)

**15660 North Dallas Parkway Suite 850**

**Dallas, Texas**

(Address of principal executive offices)

**75248**

(Zip Code)

**Registrant's telephone number, including area code:(972) 385-2810**

**Securities registered pursuant to Section 12(b) of the Act:**

**Title of Each Class**

Common Stock, Par Value \$0.66 2/3

**Name of Each Exchange on Which Registered**

The NASDAQ Stock Market LLC

**Securities registered pursuant to Section 12(g) of the Act: None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Security Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act:

|                         |                                     |                           |                          |
|-------------------------|-------------------------------------|---------------------------|--------------------------|
| Large accelerated filer | <input checked="" type="checkbox"/> | Accelerated filer         | <input type="checkbox"/> |
| Non-accelerated filer   | <input type="checkbox"/>            | Smaller reporting company | <input type="checkbox"/> |

( Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  
Yes o No x

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The aggregate market value of the 30,690,303 shares of Common Stock held by non-affiliates of the registrant, based on the closing price of \$27.85 per share of the Common Stock on the Nasdaq Global Select Market on June 29, 2007, the last business day of the registrant's most recently completed second quarter, was approximately \$854,724,925. The number of shares of the registrant's Common Stock outstanding as of February 26, 2008 was 41,241,391.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's definitive proxy statement to be filed with the Securities and Exchange Commission pursuant to Regulation 14A in connection with the 2008 annual meeting of stockholders are incorporated by reference into Part III of this Report. The proxy statement will be filed with the Securities and Exchange Commission not later than 120 days after the registrant's fiscal year ended December 31, 2007.

## PART I

### Item 1. Business

#### GENERAL

We are a global supplier of application specific standard products within the broad discrete and analog semiconductor markets. These products include diodes, rectifiers, transistors, MOSFET's, protection devices, functional specific arrays, power management devices including DC-DC switching and linear voltage regulators, amplifiers and comparators, Hall effect sensors and silicon wafers used to manufacture these products.

We design, manufacture and market these semiconductors focused on diverse end-use applications in the consumer electronics, computing, industrial, communications and automotive sectors. Semiconductors, which provide electronic signal amplification and switching functions, are basic building-block electronic components that are incorporated into almost every electronic device. We believe that our focus on standard semiconductor products provides us with a meaningful competitive advantage relative to other semiconductor companies that provide a wider range of semiconductor products.

Our product portfolio addresses the design needs of many advanced electronic devices including high-volume consumer devices such as digital audio players, notebook computers, flat-panel displays, mobile handsets, digital cameras and set-top boxes. We believe that we have particular strength in designing innovative surface-mount semiconductors for applications with a critical need to minimize product size while maximizing power efficiency and overall performance, and at a lower cost than alternative solutions. Our product line includes over 4,000 products, and we shipped approximately 10.2 billion units, 14.5 billion units, and 18.1 billion units in 2005, 2006, and 2007, respectively. From 2002 to 2007, our net sales grew from \$115.8 million to \$401.2 million, representing a compound annual growth rate of 28.2%.

We serve over 130 direct customers worldwide, which consist of original equipment manufacturers (OEMs) and electronic manufacturing services (EMS) providers. Additionally, we have approximately 60 distributor customers worldwide, through which we indirectly serve over 10,000 customers. Our customers include: (i) industry leading OEMs, in a broad range of industries, such as Bose Corporation, Honeywell International, Inc., Cisco Systems, Inc., LG Electronics, Inc., Motorola, Inc., Quanta Computer, Inc., Sagem Communication, Samsung Electronics Co., Ltd., Delta Electronics, and Hella, Ltd.; (ii) leading EMS providers such as Celestica, Inc., Flextronics International, Ltd., Hon Hai Precision Industry Co., Ltd., Inventec Corporation, Jabil Circuit, Inc., and Sanmina-SCI Corporation who build end-market products incorporating our semiconductors for companies such as Apple Computer, Inc., Dell, Inc., EMC Corporation, Intel Corporation, Microsoft Corporation, Thompson, Inc., and Roche Diagnostics; and (iii) leading distributors, such as Arrow Electronics, Inc., Avnet, Inc., Future Electronics, Zenitron Corporation, Rutronic and Yosun Industrial Corporation. For 2006 and 2007, our OEM and EMS customers together accounted for 54.2% and 61.1%, respectively, of our net sales.

We were incorporated in 1959 in California and reincorporated in Delaware in 1969. We are headquartered in Dallas, Texas. We have two manufacturing facilities located in Shanghai, China, one analog design facility located in Hsinchu, Taiwan, and our wafer fabrication facility is in Kansas City, Missouri. Our sales, marketing and logistical centers are located in Westlake Village, California; Taipei, Taiwan; Shanghai and Shenzhen, China; and Hong Kong. In 2007, we strengthened our product design centers in Dallas, San Jose, Shanghai and Taiwan to position our design engineers to work more closely with our customers and enable us to deliver a stream of innovative solutions in our targeted product categories. We also have regional sales offices and/or representatives in: Derbyshire, England; Toulouse, France; Frankfurt, Germany; and in various cities throughout the U.S.



The following diagram shows the entities through which we conduct our business and the principal services provided by each entity.

As part of our growth strategy, in December 2005, we announced the acquisition of Anachip Corporation, a fabless Taiwanese semiconductor company focused on analog ICs designed for specific applications, and in November 2006, we acquired the net assets of APD Semiconductor, Inc., a privately held U.S.-based fabless discrete semiconductor company. See “Our Strategy” for more discussion of these acquisitions.

During 2007, we undertook an internal restructuring whereby our foreign subsidiaries were placed under our newly formed, wholly-owned Netherlands holding company, Diodes International B.V. (“Diodes BV”). In addition, Diodes China and Diodes Shanghai were placed under Diodes Hong Kong Holding Company, Ltd., a newly-formed wholly-owned subsidiary of Diodes BV. The primary purpose of this internal restructuring was for treasury management and tax planning functions.

## **SEGMENT REPORTING AND FINANCIAL INFORMATION**

An operating segment is defined as a component of an enterprise about which separate financial information is available that is evaluated regularly by the chief decision maker, or decision-making group, in deciding how to allocate resources and in assessing performance. Our chief decision-making group consists of the President and Chief Executive Officer, Chief Financial Officer, Senior Vice President of Operations, Senior Vice President of Sales and Marketing, Asia President, and Senior Vice President of Finance. For financial reporting purposes, we operate in a single segment, standard semiconductor products, through our various manufacturing and distribution facilities. We aggregated our products since the products are similar and have similar economic characteristics, and the products are similar in production process and share the same customer type.

Our operations include the domestic operations (Diodes Incorporated and Diodes-FabTech) located in the United States and the Asian operations (Diodes-Taiwan, located in Taipei, Taiwan, and Diodes-Anachip located in Hsinchu, Taiwan, Diodes-China and Diodes-Shanghai both located in Shanghai, China, and Diodes-Hong Kong located in Hong Kong, China). For reporting purposes, European operations are consolidated into the domestic (North America) operations. Information about our net revenues, net income, assets and property, plant and equipment is described in our notes to the consolidated financial statements included in Item 8 of this Annual Report on Form 10-K.

## OUR INDUSTRY

Semiconductors are critical components used in the manufacture of an increasing variety of electronic products and systems. Since the invention of the transistor in 1948, continuous improvements in semiconductor processes and design technologies have led to smaller, more complex and more reliable devices at a lower cost per function. The availability of low-cost semiconductors, together with increased customer demand for sophisticated electronic systems, has led to the proliferation of semiconductors in diverse end-use applications in the consumer electronics, computing, industrial, communications and automotive sectors. These factors have also led to an increase in the total number of semiconductor components in individual electronic systems and an increase in value of these components as a percentage of the total cost of the electronic systems in which they are incorporated.

## OUR COMPETITIVE STRENGTHS

We believe our competitive strengths include the following:

**Flexible, scalable and cost-effective manufacturing** - Our manufacturing operations are a core element of our success and we have designed our manufacturing base to allow us to respond quickly to changes in demand trends in the end-markets we serve. For example, we have structured our Shanghai assembly, test and packaging facilities to enable us to rapidly and efficiently add capacity and adjust product mix to meet shifts in customer demand and overall market trends. As a result, for the past several years we have operated our Shanghai facilities at near full capacity, while at the same time significantly expanding that capacity. Additionally, the Shanghai location of our manufacturing operations provides us with access to a highly-skilled workforce at a low overall cost base while enabling us to better serve our leading customers, many of which are located in Asia.

**Integrated packaging expertise** - We believe that we have particular expertise in designing and manufacturing innovative and proprietary packaging solutions that integrate multiple separate discrete elements into a single semiconductor product called an array. Our ability to design and manufacture highly integrated semiconductor solutions provides our customers with products of equivalent functionality with fewer individual parts, and at lower overall cost, than alternative products. For example, one of our leading diode array products integrates eight discrete elements into a single highly miniaturized package that provides four times the functionality, with less than 20% of the space requirements of the previous solution. This combination of integration, functionality and miniaturization makes our products well suited for high-volume consumer applications such as digital audio players, notebook computers and digital cameras.

**Broad customer base and diverse end-markets** - Our customers include leading OEMs such as Bose Corporation, Honeywell International, Inc., LG Electronics, Inc., Cisco Systems, Inc., Motorola, Inc., Quanta Computer, Inc., Sagem Communication, Samsung Electronics Co., Ltd., Delta Electronics, and Hella, Ltd., as well as leading EMS providers such as Celestica, Inc., Flextronics International, Ltd., Hon Hai Precision Industry Co., Ltd., Inventec Corporation, Jabil Circuit, Inc., and Sanmina-SCI Corporation. Overall, we serve over 130 direct customers and over 10,000 additional customers through our distributors, including leading distributors such as Arrow Electronics, Inc., Avnet, Inc., Future Electronics, Zenitron Corporation, Rutronic and Yosun Industrial Corporation. Our products are ultimately used in end-products in a large number of markets served by our broad base of customers, which we believe makes us less dependent on either specific customers or specific end-user applications.

**Customer focused product development** - Effective collaboration with our customers and a high degree of customer service are essential elements of our business. We believe focusing on dependable delivery of semiconductor solutions tailored to specific end-user applications, has fostered deep customer relationships and created a key competitive advantage for us in the highly fragmented discrete and analog semiconductor marketplace. We believe our close relationships with our OEM and EMS customers have provided us with deeper insight into our customers' product needs. This results in differentiation in our product designs and often provides us with insight into additional

opportunities for new design wins in our customers' products.

**Management continuity and experience** - We believe that the continuity of our management team is a critical competitive strength. Five members of our executive management team have an average of over 13 years of service at the Company and the length of their service with us has created significant institutional insight into our markets, our customers and our operations.

In June 2005, we appointed Dr. Keh-Shew Lu as President and Chief Executive Officer. Dr. Lu has served as a director of Diodes since 2001 and has 30 years of relevant industry experience. Dr. Lu began his career at Texas Instruments, Inc. in 1974 and retired in 2001 as Senior Vice President and General Manager of Worldwide Analog, Mixed-Signal and Logic Products. Our Chief Financial Officer, Carl Wertz, has been employed by us since 1993 and has over 20 years of financial experience in manufacturing and distribution industries. Joseph Liu, our Senior Vice President of Operations, joined us in 1990 and has over 30 years of relevant industry experience, having started his career in 1971 at Texas Instruments. Similarly, Mark King, our Senior Vice President of Sales and Marketing, has been employed by us since 1991, as has Steven Ho, our Asia President. In 2006, we strengthened our executive management team with the addition of: Richard White, Senior Vice President of Finance, who brings with him 30 years of senior level finance experience, including 25 years at Texas Instruments; Francis Tang, Vice President of Product Development, promoted from Global Product Manager in May of 2006; and Edmund Tang, Vice President of Corporate Administration, with 30 years of managerial and engineering experience.



## OUR STRATEGY

Our strategy is to continue to enhance our position as a global supplier of standard semiconductor products, and to continue to add other product lines, such as power management products, using our packaging technology capability.

The principal elements of our strategy include the following:

**Continue to rapidly introduce innovative discrete and analog semiconductor products** - We intend to maintain our rapid pace of new product introductions, especially for high-volume, growth applications with short design cycles, such as digital audio players, notebook computers, flat-panel displays, mobile handsets, digital cameras, set-top boxes and other consumer electronics and computing devices. During 2007, we introduced approximately 240 new devices and achieved new design wins at over 100 OEMs. We believe that continued introduction of new and differentiated product solutions is critically important in maintaining and extending our market share in the highly competitive semiconductor marketplace.

Sales of new products (products that have been sold for three years or less) for the years ended December 31, 2005, 2006 and 2007 amounted to 13.9%, 28.2% and 35.1% of total sales, respectively, and this growth includes the contribution of the Anachip acquisition in early 2006 as well as the SBR<sup>â</sup> technology acquired in the APD acquisition in late 2006. New products generally have gross profit margins that are higher than the margins of our standard products. We expect net sales derived from new products to increase in absolute terms, although our net sales of new products as a percentage of our net sales will depend on the demand for our standard products, as well as our product mix. New product revenue in 2007 was driven by products in sub-miniature array, QFN, PowerDI<sup>Ô</sup>323, PowerDI<sup>Ô</sup>123, PowerDI<sup>Ô</sup>5, SBR<sup>â</sup> and Schottky platforms, in both the discrete and analog product lines.

**Expand our available market opportunities** - We intend to aggressively maximize our opportunities in the standard semiconductor market as well as in related markets where we can apply our semiconductor design and manufacturing expertise. A key element of this is leveraging our highly integrated packaging expertise through our Application Specific Multi-Chip Circuit (ASMCC) product platform, which consists of standard arrays, function specific arrays and end-equipment specific arrays. We intend to achieve this by:

- Ø Continuing to focus on increasing packaging integration, particularly with our existing standard array and customer-specific array products, in order to achieve products with increased circuit density, reduced component count and lower overall product cost;
- Ø Expanding existing products and developing new products in our function specific array lines, which combine multiple discrete semiconductor components to achieve specific common electronic device functionality at a low cost; and
- Ø Developing new product lines, which we refer to as end-equipment specific arrays, which combine discrete components with logic and/or standard analog circuits to provide system-level solutions for high-volume, high-growth applications.

**Maintain intense customer focus** - We intend to strengthen and deepen our customer relationships. We believe that continued focus on customer service would increase our net sales, operating performance and overall market share. To accomplish this, we intend to continue to closely collaborate with our customers to design products that meet their specific needs. A critical element of this strategy is to continue to further reduce our design cycle time in order to quickly provide our customers with innovative products. Additionally, to support our customer-focused strategy, we are continuing to expand our sales force and field application engineers, particularly in Asia and Europe.

**Enhance cost competitiveness** - A key element of our success is our overall low-cost base. While we believe that our Shanghai manufacturing facilities are among the most efficient in the industry, we will continue to refine our proprietary manufacturing processes and technology to achieve additional cost efficiencies. Additionally, we intend to continue to operate our facilities at high utilization rates and to increase product yields in order to achieve meaningful economies of scale.

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**Pursue selective strategic acquisitions** - As part of our strategy to expand our standard semiconductor product offerings and to maximize our market opportunities, we may acquire discrete, analog or mixed-signal technologies, product lines or companies in order to support our ASMCC product platform and enhance our standard and new product offerings.

In December 2005, we announced the acquisition of Anachip Corporation, a fabless Taiwanese semiconductor company focused on analog ICs designed for specific applications, and headquartered in the Hsinchu Science Park in Taiwan. This acquisition, which was completed in January 2006, is in line with our long-term strategy. Anachip's main product focus is power management ICs. The analog devices they produce are used in LCD monitor/TV's, wireless LAN 802.11 access points, brushless DC motor fans, portable DVD players, datacom devices, ADSL modems, TV/satellite set-top boxes, and power supplies. Anachip brings a design team with strong capabilities in a range of targeted analog and power management technologies.

On November 3, 2006, we purchased the net assets of APD Semiconductor, Inc., a privately held U.S.-based fabless semiconductor company. APD Semiconductor is headquartered in Redwood City, California, with a sales, application, and administration center in Taipei, Taiwan. APD Semiconductor's main product focus is its patented and trademarked Super Barrier Rectifier ("SBR<sup>®</sup>") technology. Utilizing a low cost IC wafer process, the SBR technology uses a MOS cellular design to replace standard traditional Schottky or PN junction diodes. The SBR<sup>®</sup> technology uses an innovative-patented process technique that allows its key parameters to be easily tuned to optimize any customer applications. This adaptive and scalable technology allows for increased power saving with better efficiency and reliability at higher operating temperatures for end-user applications like digital audio players, DC/DC converters, AC/DC power supplies, LCD monitors, Power-over-Ethernet (POE), Power Factor Correction (PFC) and TV/satellite set-top boxes. The SBR technology offers industry-leading products like the SBR20U100CT, which has the lowest forward voltage and highest efficiency and power saving in its class. The APD acquisition will further strengthen our technology leadership in the discrete semiconductor market and expand our product capabilities across important segments of our end-markets.

## **CONVERTIBLE BONDS OFFERING**

On October 12, 2006, we issued and sold convertible senior notes with an aggregate principal amount of \$230 million due 2026 (the "Notes"), which pay 2.25% interest per annum on the principal amount of the Notes, payable semi-annually in arrears on April 1 and October 1 of each year, beginning on April 1, 2007.

The Notes will be convertible into cash or, at our option, cash and shares of our Common Stock based on an initial conversion rate, subject to adjustment, of 25.6419 shares (split adjusted) per \$1,000 principal amount of Notes (which represents an initial conversion price of \$39.00 per share, split adjusted), in certain circumstances. In addition, following a "make-whole fundamental change" that occurs prior to October 1, 2011, we will, at our option, increase the conversion rate for a holder who elects to convert its Notes in connection with such "make-whole fundamental change," in certain circumstances.

We intend to use the net proceeds for working capital and general corporate purposes, which may include the acquisition of businesses, products, product rights or technologies, strategic investments, or purchases of our own Common Stock.

## **FOLLOW-ON PUBLIC OFFERING**

In October 2005, we sold approximately 3.2 million shares (split adjusted) of our Common Stock in a follow-on public offering, raising approximately \$71.7 million (net of commissions and expenses). We used approximately \$31 million and \$8 million of the proceeds in connection with the Anachip and ADP acquisitions, respectively, and we intend to use the remaining net proceeds from this offering for working capital and other general corporate purposes,

including additional acquisitions.

**OUR PRODUCTS**

Our product portfolio includes over 4,000 products that are designed for use in high-volume consumer devices such as digital audio players, notebook computers, flat-panel displays, mobile handsets, digital cameras and set-top boxes. We target and serve end-equipment market segments that we believe have higher growth rates than other end-market segments served by the overall semiconductor industry.

Our broad product line includes:

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- Ø Discrete semiconductor products, including performance Schottky rectifiers; performance Schottky diodes; Zener diodes and performance Zener diodes, including tight tolerance and low operating current types; standard, fast, super-fast and ultra-fast recovery rectifiers; bridge rectifiers; switching diodes; small signal bipolar transistors; prebiased transistors; MOSFETs; thyristor surge protection devices; and transient voltage suppressors;
- Ø Complex high-density diode, transistor and mixed technology arrays, in multi-pin ultra-miniature surface-mount packages, including customer specific and function specific arrays;
- Ø Silicon wafers used in manufacturing these products; and
- Ø Power management devices and Hall effect sensors through our Anachip acquisition

Our semiconductor products are an essential building-block of electronic circuit design and are available in thousands of permutations varying according to voltage, current, power handling capability and switching speed.

Our complex diode and transistor arrays help bridge the gap between discrete semiconductors and integrated circuits. Arrays consist of multiple discrete semiconductor devices housed in a single package. Our discrete surface-mount devices, which are components that can be attached to the surface of a substrate with solder, target end-equipment categories with critical needs to minimize size while maintaining power efficiency and performance.

The following table lists the end-markets, some of the applications in which our products are used, and the percentage of net sales for each end market for the last three years:

| End Markets          | 2005 | 2006 | 2007 | End product applications                                                                                                             |
|----------------------|------|------|------|--------------------------------------------------------------------------------------------------------------------------------------|
| Consumer Electronics | 38%  | 36%  | 36%  | Set-top boxes, game consoles, digital audio players, digital cameras, mobile handsets, flat-panel displays, personal medical devices |
| Computing            | 34%  | 36%  | 37%  | Notebooks, flat-panel monitors, motherboards, PDAs, multi-function printers, servers, network interface cards, hard disk drives      |
| Communications       | 17%  | 14%  | 15%  | Gateways, routers, switches, hubs, fiber optics, DSL, cable and standard modems, networking (wireless, ethernet, power/phone line)   |
| Industrial           | 7%   | 12%  | 10%  | Ballast lighting, power supplies, DC-DC conversion, security/access systems, motor controls, HVAC                                    |
| Automotive           | 4%   | 2%   | 2%   | Comfort controls, audio/video players, GPS navigation, safety, security, satellite radios, engine controls, HID lighting             |

## PRODUCT PACKAGING

Our device packaging technology primarily includes a wide variety of surface-mount packages. Our focus on the development of smaller, more thermally efficient, and increasingly integrated packaging, is a critical component of our product development. We provide a comprehensive offering of miniature and sub-miniature packaging, enabling us to fit components into smaller and more efficient packages, while maintaining the same device functionality and power handling capabilities. Smaller packaging provides a reduction in the height, weight and board space required for our components, and is well suited for battery-powered, hand-held and wireless consumer applications such as digital audio players, notebook computers, flat-panel displays, mobile handsets, digital cameras and set-top boxes.



## **CUSTOMERS**

We serve over 130 direct customers worldwide, which consist of OEMs and EMS providers. Additionally, we have approximately 60 distributor customers worldwide, through which we indirectly serve over 10,000 customers. Our customers include: (i) industry leading OEMs in a broad range of industries, such as Bose Corporation, Honeywell International, Inc., Cisco Systems, Inc., LG Electronics, Inc., Motorola, Inc., Quanta Computer, Inc., Sagem Communication, Delta Electronics, Hella, Ltd., and Samsung Electronics Co., Ltd.; (ii) leading EMS providers, such as Celestica, Inc., Flextronics International, Ltd., Hon Hai Precision Industry Co., Ltd., Inventec Corporation, Jabil Circuit, Inc., and Sanmina-SCI Corporation, who build end-market products incorporating our semiconductors for companies such as Apple Computer, Inc., Dell, Inc., EMC Corporation, Intel Corporation, Microsoft Corporation, Thompson, Inc. and Roche Diagnostics; and (iii) leading distributors such as Arrow Electronics, Inc., Avnet, Inc., Future Electronics, Yosun Industrial Corporation, Zenitron Corporation and Rutronic. For the years of 2005, 2006 and 2007, our OEM and EMS customers together accounted for 69.5%, 54.2% and 61.1%, respectively, of our net sales. The acquisition of Anachip, which sold products predominantly through distributors, is the primary contributor to the increase in the percentage of our total net sales sold to distributors.

For the years ended December 31, 2005, 2006 and 2007, Lite-On Semiconductor Corporation (LSC), which is also our largest stockholder, (owning approximately 21.6% of our Common Stock as of December 31, 2007), and a member of the Lite-On Group of companies, accounted for approximately 9.6%, 6.5% and 6.2%, respectively, of our net sales. No other customer accounted for 10% or more of our net sales in 2006 and 2007. Also, 14.7%, 13.0% and 11.3% of our net sales were from the subsequent sale of products we purchased from LSC in 2005, 2006 and 2007, respectively. See "Certain Relationships and Related Party Transactions."

We believe that our close relationships with our OEM and EMS customers have provided us with deeper insight into our customers' product needs than other manufacturers who we believe depend to a greater extent on indirect sales through distributors. In addition to seeking to expand relationships with our existing customers, our strategy is to pursue new customers and diversify our customer base by focusing on leading global consumer electronics companies and their EMS providers and distributors.

We generally warrant that products sold to our customers will, at the time of shipment, be free from defects in workmanship and materials and conform to our approved specifications. Subject to certain exceptions, our standard warranty extends for a period of one year from the date of shipment. Warranty expense has not been significant. Generally, our customers may cancel orders on short notice without incurring a significant penalty.

Many of our customers are based in Asia or have manufacturing facilities in Asia. Net sales by country consists of sales to customers assigned to that country based on the country to which the product is shipped. For the year ended December 31, 2007, 38.9%, 25.6%, 20.3%, and 15.2% of our net sales were derived from China, Taiwan, the U.S. and all other markets, respectively, compared to 34.5%, 28.1%, 22.2%, and 15.2% in 2006, respectively. We anticipate the percentage of net sales shipped to customers in Asia to increase as the trend towards manufacturing in Asia continues.

## **SALES AND MARKETING**

We market and sell our products worldwide through a combination of direct sales and marketing personnel, independent sales representatives and distributors. We have direct sales personnel in the United States, United Kingdom, France, Germany, Taiwan and China. We also have independent sales representatives in the United States, Japan, Korea, and Europe. We currently have distributors in the United States, Europe and Asia.

As of December 31, 2007, our direct global sales and marketing organization consisted of approximately 160 employees operating out of 18 offices. We have sales and marketing offices or representatives in Taipei, Taiwan; Shanghai and Shenzhen, China; Hong Kong; Derbyshire, England; Toulouse, France; Frankfurt, Germany; and we

have five regional sales offices in the United States. As of December 31, 2007, we also had approximately 20 independent sales representative firms marketing our products.

Our marketing group focuses on our product strategy, product development road map, new product introduction process, demand assessment and competitive analysis. Our marketing programs include participation in industry tradeshows, technical conferences and technology seminars, sales training and public relations. The marketing group works closely with our sales and research and development groups to align our product development road map. The marketing group coordinates its efforts with our product development, operations and sales groups, as well as with our customers, sales representatives and distributors. We support our customers through our field application engineering and customer support organizations.



To support our global customer-base, our website is language-selectable into English, Chinese, and Korean, giving us an effective marketing tool for worldwide markets. With its extensive online product catalog with advanced search capabilities, our website facilitates quick and easy product selection. Our website provides easy access to our worldwide sales contacts and customer support, and incorporates a distributor-inventory check to provide component inventory availability and a small order desk for overnight sample fulfillment. Our website, [www.diodes.com](http://www.diodes.com), also provides investors access to our financial and corporate governance information.

## **MANUFACTURING OPERATIONS AND FACILITIES**

We operate three manufacturing facilities, two of which are located in Shanghai, China, and the third of which is located in Kansas City, Missouri. Our facilities in Shanghai perform packaging, assembly and testing functions, and our Kansas City facility is a 5-inch wafer foundry. Anachip's main product focus is power management ICs. In 2007, we moved our Taiwan analog probe and testing operations to our China facilities.

For the years ended at December 31, 2006 and 2007, we had invested approximately \$32.3 million and \$41.2 million, respectively, in plant and state-of-the-art equipment in China (\$167.3 million total investment in China from inception). Both of our Chinese factories manufacture product for sale by our U.S. and Asia operations, and also sell to external customers. For the years ended at December 31, 2006 and 2007, we had invested approximately \$4.7 million and \$8.6 million, respectively, in equipment for our wafer foundry. Silicon wafers are received and inspected in a highly controlled "clean room" environment awaiting the assembly operation. At the first step of assembly, the wafers are sawn with very thin, high speed diamond blades into tiny semiconductor "dice," numbering as many as 170,000 per 5-inch diameter wafer. Dice are then loaded onto a handler, which automatically places the dice, one by one, onto lead frames, which are package specific, where they are bonded to the lead-frame pad. Next, automatic wire bonders make the necessary electrical connections from the die to the leads of the lead-frame, using micro-thin gold wire. Our fully automated assembly machinery then molds the epoxy case around the die and lead-frame to produce the desired semiconductor product. After a trim, form, test, mark and re-test operation, the parts are placed into special carrier housings and a cover tape seals the parts in place. The taped parts are then spooled onto reels or placed into other packaging medium and boxed for shipment. In 2007, we began investment in a 6-inch wafer line at our Kansas City wafer foundry and anticipate the completion of the investment in the first half of 2008.

Our manufacturing processes use many raw materials, including silicon wafers, copper lead frames, gold wire and other metals, molding compounds and various chemicals and gases. We have no material agreements with any of our suppliers that impose minimum or continuing supply obligations. From time to time, suppliers may extend lead times, limit supplies or increase prices due to capacity constraints or other factors. Although we believe that supplies of the raw materials we use are currently and will continue to be available, shortages could occur in various essential materials due to interruption of supply or increased demand in the industry.

Our corporate headquarters are located in a leased facility in Dallas, Texas. We also lease or own properties around the world for use as sales offices, research and development labs, warehouses and logistic centers. The size and/or location of these properties can change from time to time based on business requirements. In 2006, we purchased an office building in Taipei, Taiwan for our Taiwan operations for approximately \$6.0 million (see Item 2 - Properties).

## **BACKLOG**

The amount of backlog to be shipped during any period is dependent upon various factors, and all orders are subject to cancellation or modification, usually with no penalty to the customer. Orders are generally booked from one month to greater than twelve months in advance of delivery. The rate of booking of new orders can vary significantly from month to month. We, and the industry as a whole, have been experiencing a trend towards shorter lead-times, and we expect this trend to continue. The amount of backlog at any date depends upon various factors, including the timing of the receipt of orders, fluctuations in orders of existing product lines, and the introduction of any new lines.

Accordingly, we believe that the amount of our backlog at any date is not a particularly useful measure of our future sales. We strive to maintain proper inventory levels to support our customers' just-in-time order expectations.

#### **PATENTS, TRADEMARKS AND LICENSES**

Historically, patents and trademarks have not been material to our operations, but we expect them to become more important, particularly as they relate to our packaging and analog technologies.

Through our APD asset acquisition, we acquired the Super Barrier Rectifier technology (less than 500V) and the SBR<sup>®</sup> trademark. SBR<sup>®</sup> is state-of-the-art integrated circuit wafer processing technology that allows the design and manufacture of a device, which is able to integrate and improve the benefits of the two existing rectifier technologies into a single device. The creation of a finite conduction cellular IC, combined with inherent design uniformity has allowed manufacturing costs to be kept competitive with existing power device technology, and thus produced a breakthrough in rectifier technology.

Currently, our licensing of patents to other companies is not material. We do, however, license certain product technology from other companies, but we do not consider any of the licensed technology to be material in terms of royalties. We believe the duration and other terms of the licenses are appropriate for our current needs.

## **COMPETITION**

Numerous semiconductor manufacturers and distributors serve the discrete and analog semiconductor components market, making competition intense. Some of our larger competitors include Fairchild Semiconductor Corporation, Infineon Technologies A.G., International Rectifier Corporation, ON Semiconductor Corporation, Philips Electronics N.V., Rohm Electronics USA, LLC, Toshiba Corporation and Vishay Intertechnology, Inc., many of which have greater financial, marketing, distribution and other resources than us. Accordingly, in response to market conditions, we from time to time may reposition product lines or decrease prices, which may affect our sales of, and profit margins on, such product lines. The price and quality of the product, and our ability to design products and deliver customer service in keeping with the customers' needs, determine the competitiveness of our products. We believe that our product focus and our flexibility and ability to quickly adapt to customer needs affords us competitive advantages.

## **ENGINEERING AND RESEARCH AND DEVELOPMENT**

Our engineering and research and development groups consist of applications, technical marketing, and product development engineers who assist in determining the direction of our future product lines. Their primary function is to work closely with market-leading customers to further refine, expand and improve our product range within our product types and packages. In addition, customer requirements and acceptance of new package types are assessed and new, higher-density and more energy-efficient packages are developed to satisfy customers' needs. Working with customers to integrate multiple types of technologies within the same package, our applications engineers strive to reduce the required number of components and, thus, circuit board size requirements of a device, while increasing the functionality of the component technology.

Product engineers work directly with our semiconductor wafer design and process engineers who craft die designs needed for products that precisely match our customers' requirements. Direct contact with our manufacturing facilities allows the manufacturing of products that are in line with current technical requirements. We have the capability to capture the customer's customers' electrical and packaging requirements through their product development engineers, and then transfer those requirements to our research and development and engineering department, so that the customers' requirements can be translated, designed, and manufactured with full control, even to the elemental silicon level.

For the years ended December 31, 2005, 2006 and 2007, investment in research and development was \$3.7 million, \$8.3 million and \$13.5 million, respectively. As a percentage of net sales, research and development expense was 1.7%, 2.4% and 3.4% for 2005, 2006 and 2007, respectively. We anticipate research and development to increase in absolute dollars and to be in the range of 3 to 4% of net sales as we continue to develop proprietary technology.

## **EMPLOYEES**

As of December 31, 2007, we employed a total of 2,612 employees, of which 2,266 of our employees were in Asia, 340 were in the United States and six were in Europe. None of our employees is subject to a collective bargaining agreement. We consider our relations with our employees to be satisfactory.

## **ENVIRONMENTAL MATTERS**

We are subject to a variety of U.S. Federal, state, local and foreign governmental laws, rules and regulations related to the use, storage, handling, discharge or disposal of certain toxic, volatile or otherwise hazardous chemicals used in

our manufacturing process both in the United States where our wafer fabrication facility is located, and in China where our assembly, test and packaging facilities are located. Any of these regulations could require us to acquire equipment or to incur substantial other expenses to comply with environmental regulations. As of December 31, 2007, there were no known environmental claims or recorded liabilities.

#### **CERTAIN RELATIONSHIPS AND RELATED PARTY TRANSACTIONS**

We conduct business with one related party company, Lite-On Semiconductor Corporation (“LSC”) (and its subsidiaries and affiliates) and one significant company, Zi Yun International (“Zi Yun”) (formerly Keylink International) (and its affiliates). LSC is our largest stockholder, owning 21.6% of our outstanding Common Stock as of December 31, 2007, and is a member of the Lite-On Group of companies. Zi Yun is our 5% joint venture partner in Diodes-China and Diodes-Shanghai. C.H. Chen, our former President and Chief Executive Officer, and Vice Chairman of our Board of Directors, is also Vice Chairman of LSC. M.K. Lu, a member of our Board of Directors until May 2007, was President of LSC. In addition, Raymond Soong, the Chairman of our Board of Directors, is Chairman of LSC, and is the Chairman of Lite-On Technology Corporation, a significant shareholder of LSC. In connection with our 2005 follow-on public offering, LSC sold 1.7 million shares (split adjusted), reducing its holdings of our Common Stock to approximately 8.7 million shares (split adjusted). We did not receive any of the proceeds from LSC’s sale of our Common Stock, but LSC shared in the expenses of the offering.

The Audit Committee of our Board of Directors reviews all related party transactions for potential conflict of interest situations on an ongoing basis, in accordance with such procedures as the Audit Committee may adopt from time to time. We believe that all related party transactions are on terms no less favorable to us than would be obtained from unaffiliated third parties.

We sold silicon wafers to LSC totaling 9.6%, 6.5% and 6.2% of total sales for the years ended December 31, 2005, 2006 and 2007, respectively, making LSC our largest customer. Also for the years ended December 31, 2005, 2006 and 2007, 14.7%, 13.0% and 11.3%, respectively, of our net sales were from discrete semiconductor products purchased from LSC for subsequent sale by us, making LSC our largest outside supplier. We also rent warehouse space in Hong Kong from a member of the Lite-On Group, which also provides us with warehousing services at that location. For 2005, 2006 and 2007, we reimbursed this entity in aggregate amounts of \$0.3 million, \$0.5 million and \$0.5 million, respectively, for these services. We believe such transactions are on terms no less favorable to us than could be obtained from unaffiliated third parties.

In December 2000, we acquired a wafer foundry, FabTech, Inc., from LSC for approximately \$6.0 million cash plus \$19.0 million in assumed debt (the debt was due primarily to LSC). As per the terms of the acquisition, we entered into management incentive agreements with several members of FabTech's management. The agreements provided members of FabTech's management with guaranteed annual payments as well as contingent bonuses based on the annual profitability of FabTech, subject to a maximum annual amount. LSC reimbursed us for any portion of the guaranteed and contingent liability paid by FabTech. The final year of the management incentive agreements was 2004, with final payment made on March 31, 2005. LSC reimbursed us \$0.4 million in each of 2003, 2004, and 2005 for amounts paid by us under these management incentive agreements.

We sell product to, and purchase inventory from, companies owned by our 5% Diodes-China and Diodes-Shanghai minority shareholder, Zi Yun. We sold silicon wafers to companies owned by Zi Yun totaling 0.6%, 0.4% and 0.6% of total sales for the years ended December 31, 2005, 2006 and 2007, respectively. Also for the years ended December 31, 2005, 2006 and 2007, 3.0%, 2.3% and 1.5%, respectively, of our net sales were from discrete semiconductor products purchased from companies owned by Zi Yun. In addition, Diodes-China and Diodes-Shanghai lease their manufacturing facilities from, and subcontract a portion of their manufacturing process (metal plating and environmental services) to, Zi Yun. We also pay a consulting fee to Zi Yun. The aggregate amounts for these services for the years ended December 31, 2005, 2006 and 2007 were \$6.6 million, \$7.9 million and \$9.4 million, respectively. We believe such transactions are on terms no less favorable to us than could be obtained from unaffiliated third parties.

In December 2005, we entered into a definitive stock purchase agreement to acquire Anachip Corporation, a Taiwanese fabless analog IC company headquartered in the Hsinchu Science Park in Taiwan. The selling shareholders included LSC (which owned approximately 60% of Anachip's outstanding capital stock), and two Taiwanese venture capital firms (together owning approximately 20% of Anachip's stock), as well as current and former Anachip employees, among others. At December 31, 2005, we had purchased an aggregate of approximately 9.4 million shares (or approximately 18.9%) of the 50 million outstanding shares of the capital stock of Anachip. On January 10, 2006 (the closing date of the acquisition), we purchased an additional approximately 40.5 million shares and therefore, we now hold approximately 99.81% of Anachip's capital stock.

Concurrent with the acquisition, Anachip entered into a wafer purchase agreement with LSC, pursuant to which LSC will sell to Anachip, according to Anachip's requirements, during the two year period ending on December 31, 2007, wafers of the same or similar type, and meeting the same specifications, as those wafers purchased from LSC by Anachip at the time of the acquisition. Anachip would purchase such wafers on terms (including purchase price, delivery schedule, and payment terms) no less favorable to Anachip than those terms on which Anachip purchased such wafers from LSC at the time of the acquisition; provided, however, that the purchase price would be the lower of the current price or the most favorable customer pricing. If the price of raw wafers increases by more than 20% within

any six-month period, Anachip and LSC would renegotiate in good faith the price of wafers to reflect the cost increase.

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**Item 1A. Risk Factors**

Investing in our Common Stock involves a high degree of risk. You should carefully consider the following risks and other information in this report before you decide to buy our Common Stock. Our business, financial condition or operating results may suffer if any of the following risks are realized. Additional risks and uncertainties not currently known to us may also adversely affect our business, financial condition or operating results. If any of these risks or uncertainties occurs, the trading price of our Common Stock could decline and you could lose part or all of your investment.

**RISKS RELATED TO OUR BUSINESS**

***Downturns in the highly cyclical semiconductor industry or changes in end-market demand could affect our operating results and financial condition.***

The semiconductor industry is highly cyclical, and periodically experiences significant economic downturns characterized by diminished product demand, production overcapacity and excess inventory, which can result in rapid erosion in average selling prices. From time to time, the semiconductor industry experiences order cancellations and reduced demand for products, resulting in significant revenue declines, due to excess inventories at computer and telecommunications equipment manufacturers and general economic conditions, especially in the technology sector. The market for semiconductors may experience renewed, and possibly more severe and prolonged downturns in the future, which may harm our results of operations and reduce the value of our business.

In addition, we operate in a narrower market of the broader semiconductor market and, as a result, cyclical fluctuations may affect this segment to a greater extent than they do the broader semiconductor market. This may cause us to experience greater fluctuations in our results of operations than compared to some of our broad line semiconductor manufacturer competitors. In addition, we may experience significant changes in our profitability as a result of variations in sales, changes in product mix, changes in end-user markets and the costs associated with the introduction of new products. The markets for our products depend on continued demand in the consumer electronics, computer, industrial, communications and automotive sectors. These end-user markets also tend to be cyclical and may also experience changes in demand that could adversely affect our operating results and financial condition.

***The semiconductor business is highly competitive, and increased competition may harm our business and our operating results.***

The sectors of the semiconductor industry in which we operate are highly competitive. We expect intensified competition from existing competitors and new entrants. Competition is based on price, product performance, product availability, quality, reliability and customer service. We compete in various markets with companies of various sizes, many of which are larger and have greater resources or capabilities as it relates to financial, marketing, distribution, brand name recognition, research and development, manufacturing and other resources than we have. As a result, they may be better able to develop new products, market their products, pursue acquisition candidates and withstand adverse economic or market conditions. Most of our current major competitors are broad line semiconductor manufacturers who often have a wider range of product types and technologies than we do. In addition, companies not currently in direct competition with us may introduce competing products in the future. Some of our current major competitors are Fairchild Semiconductor Corporation, Infineon Technologies A.G., International Rectifier Corporation, ON Semiconductor Corporation, Philips Electronics N.V., Rohm Electronics USA, LLC, Toshiba Corporation and Vishay Intertechnology, Inc. We may not be able to compete successfully in the future, and competitive pressures may harm our financial condition or our operating results.

***We receive a significant portion of our net sales from a single customer. In addition, this customer is also our largest external supplier and is a related party. The loss of this customer or supplier could harm our business and***

***results of operations.***

In 2006 and 2007, LSC, our largest stockholder and one of our largest customers, accounted for 6.5% and 6.2%, respectively, of our net sales. LSC is also our largest supplier, providing us with discrete semiconductor products for subsequent sale by us, which represented approximately 13.0% and 11.3%, respectively, of our net sales, in 2006 and 2007. The loss of LSC as either a customer or a supplier, or any significant reduction in either the amount of product it supplies to us, or the volume of orders it places with us, could materially harm our business and results of operations.

***Delays in initiation of production at new facilities, implementing new production techniques or resolving problems associated with technical equipment malfunctions could adversely affect our manufacturing efficiencies.***

Our manufacturing efficiency has been and will be an important factor in our future profitability, and we may not be able to maintain or increase our manufacturing efficiency. Our manufacturing and testing processes are complex, require advanced and costly equipment and are continually being modified in our efforts to improve yields and product performance. Difficulties in the manufacturing process can lower yields. Technical or other problems could lead to production delays, order cancellations and lost revenue. In addition, any problems in achieving acceptable yields, construction delays, or other problems in upgrading or expanding existing facilities, building new facilities, problems in bringing other new manufacturing capacity to full production or changing our process technologies, could also result in capacity constraints, production delays and a loss of future revenues and customers. Our operating results also could be adversely affected by any increase in fixed costs and operating expenses related to increases in production capacity if net sales do not increase proportionately, or in the event of a decline in demand for our products.

Our wafer fabrication facility is located in Kansas City, Missouri, while our facilities in Shanghai, China provide assembly, test and packaging capabilities. Any disruption of operations at these facilities could have a material adverse effect on our business, financial condition and results of operations.

***We are and will continue to be under continuous pressure from our customers and competitors to reduce the price of our products, which could adversely affect our growth and profit margins.***

Prices for our products tend to decrease over their life cycle. There is substantial and continuing pressure from customers to reduce the total cost of purchasing our products. To remain competitive and retain our customers and gain new ones, we must continue to reduce our costs through product and manufacturing improvements. We must also strive to minimize our customers' shipping and inventory financing costs and to meet their other goals for rationalization of supply and production. We experienced an annual increase in average selling prices (ASP) for our products of 15.0% and 12.1% for 2005 and 2006, respectively, and an ASP decrease of 6.8% in 2007. At times, we may be required to sell our products at ASP's below our manufacturing cost or purchase price in order to remain competitive. Our growth and the profit margins of our products will suffer if we cannot effectively continue to reduce our costs and keep our product prices competitive.

***Our customer orders are subject to cancellation or modification usually with no penalty. High volumes of order cancellation or reductions in quantities ordered could adversely affect our results of operations and financial condition.***

All of our customer orders are subject to cancellation or modification, usually with no penalty to the customer. Orders are generally made on a purchase order basis, rather than pursuant to long-term supply contracts, and are booked from one to twelve months in advance of delivery. The rate of booking new orders can vary significantly from month to month. We, and the semiconductor industry as a whole, are experiencing a trend towards shorter lead-times, which is the amount of time between the date a customer places an order and the date the customer requires shipment. Furthermore, our industry is subject to rapid changes in customer outlook and periods of excess inventory due to changes in demand in the end markets our industry serves. As a result, many of our purchase orders are revised, and may be cancelled, with little or no penalty and with little or no notice. However, we must still commit production and other resources to fulfilling these orders even though they may ultimately be cancelled. If a significant number of orders are cancelled or product quantities ordered are reduced, and we are unable to timely generate replacement orders, we may build up excess inventory and our results of operations and financial condition may suffer.

***New technologies could result in the development of new products by our competitors and a decrease in demand for our products, and we may not be able to develop new products to satisfy changes in demand, which could result in a decrease in net sales and loss of market share.***

Our product range and new product development program is focused on discrete and analog semiconductor products. Our failure to develop new technologies, or anticipate or react to changes in existing technologies, either within or outside of the semiconductor market, could materially delay development of new products, which could result in a decrease in our net sales and a loss of market share to our competitors. The semiconductor industry is characterized by rapidly changing technologies and industry standards, together with frequent new product introductions. This includes the development of new types of technology or the improvement of existing technologies, such as analog and digital technologies that compete with, or seek to replace discrete semiconductor technology. Our financial performance depends on our ability to design, develop, manufacture, assemble, test, market and support new products and product enhancements on a timely and cost-effective basis. New products often command higher prices and, as a result, higher profit margins. We may not successfully identify new product opportunities or develop and bring new products to market or succeed in selling them into new customer applications in a timely and cost-effective manner.

Products or technologies developed by other companies may render our products or technologies obsolete or noncompetitive and, since we operate primarily in a narrower segment of the broader semiconductor industry, this may have a greater effect on us than it would if we were a broad-line semiconductor manufacturer with a wider range of product types and technologies. Many of our competitors are larger and more established international companies with greater engineering and research and development resources than us. Our failure to identify or capitalize on any fundamental shifts in technologies in our product markets, relative to our competitors, could harm our business, have a material adverse effect on our competitive position within our industry and harm our relationships with our customers. In addition, to remain competitive, we must continue to reduce package sizes, improve manufacturing yields and expand our sales. We may not be able to accomplish these goals, which could harm our business.

***We may be subject to claims of infringement of third-party intellectual property rights or demands that we license third-party technology, which could result in significant expense and reduction in our intellectual property rights.***

The semiconductor industry is characterized by vigorous protection and pursuit of intellectual property rights. From time to time, third parties have asserted, and may in the future assert, patent, copyright, trademark and other intellectual property rights to technologies that are important to our business and have demanded, and may in the future demand, that we license their patents and technology. Any litigation to determine the validity of allegations that our products infringe or may infringe these rights, including claims arising through our contractual indemnification of our customers, or claims challenging the validity of our patents, regardless of its merit or resolution, could be costly and divert the efforts and attention of our management and technical personnel. We may not prevail in litigation given the complex technical issues and inherent uncertainties in intellectual property litigation. If litigation results in an adverse ruling we could be required to:

- Ø pay substantial damages for past, present and future use of the infringing technology;
- Ø cease the manufacture, use or sale of infringing products;
- Ø discontinue the use of infringing technology;
- Ø expend significant resources to develop non-infringing technology;
- Ø pay substantial damages to our customers or end-users to discontinue use or replace infringing technology with non-infringing technology;
- Ø license technology from the third party claiming infringement, which license may not be available on commercially reasonable terms, or at all; or
- Ø relinquish intellectual property rights associated with one or more of our patent claims, if such claims are held invalid or otherwise unenforceable.

***We depend on third-party suppliers for timely deliveries of raw materials, parts and equipment, as well as finished products from other manufacturers, and our results of operations could be adversely affected if we are unable to obtain adequate supplies in a timely manner.***

Our manufacturing operations depend upon obtaining adequate supplies of raw materials, parts and equipment on a timely basis from third parties. Our results of operations could be adversely affected if we are unable to obtain adequate supplies of raw materials, parts and equipment in a timely manner or if the costs of raw materials, parts or equipment were to increase significantly. Our business could also be adversely affected if there is a significant degradation in the quality of raw materials used in our products, or if the raw materials give rise to compatibility or performance issues in our products, any of which could lead to an increase in customer returns or product warranty claims. Although we maintain rigorous quality control systems, errors or defects may arise from a supplied raw material and be beyond our detection or control. Any interruption in, or change in quality of, the supply of raw materials, parts or equipment needed to manufacture our products could adversely affect our business and harm our results of operations and our reputation with our customers.

In addition, we sell finished products from other manufacturers. Our business could also be adversely affected if there is a significant degradation in the quality of these products. From time to time, such manufacturers may extend lead-times, limit supplies or increase prices due to capacity constraints or other factors. We have no long-term purchase contracts with any of these manufacturers and, therefore, have no contractual assurances of continued supply, pricing or access to finished products that we sell, and any such manufacturer could discontinue supplying to us at any time. Additionally, some of our suppliers of finished products or wafers compete directly with us and may in the future choose not to supply products to us.

***If we do not succeed in continuing to vertically integrate our business, we will not realize the cost and other efficiencies we anticipate and our ability to compete, profit margins and results of operations may suffer.***

We are continuing to vertically integrate our business. Key elements of this strategy include continuing to expand the reach of our sales organization, expand our manufacturing capacity, expand our wafer foundry and research and development capability and expand our marketing, product development, package development and assembly/testing operations in company-owned facilities or through the acquisition of established contractors. There are certain risks associated with our vertical integration strategy, including:

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- Ø difficulties associated with owning a manufacturing business, including, but not limited to, the maintenance and management of manufacturing facilities, equipment, employees and inventories and limitations on the flexibility of controlling overhead;
- Ø difficulties in continuing expansion of our operations in Asia and Europe, because of the distance from our U.S. headquarters and differing regulatory and cultural environments;
  - Ø the need for skills and techniques that are outside our traditional core expertise;
  - Ø less flexibility in shifting manufacturing or supply sources from one region to another;
- Ø even when independent suppliers offer lower prices, we would continue to acquire wafers from our captive manufacturing facility, which may result in us having higher costs than our competitors;
  - Ø difficulties developing and implementing a successful research and development team; and
  - Ø difficulties developing, protecting, and gaining market acceptance of, our proprietary technology.

The risks of becoming a fully integrated manufacturer are amplified in an industry-wide slowdown because of the fixed costs associated with manufacturing facilities. In addition, we may not realize the cost, operating and other efficiencies that we expect from continued vertical integration. If we fail to successfully vertically integrate our business, our ability to compete, profit margins and results of operations may suffer.

***Part of our growth strategy involves identifying and acquiring companies with complementary product lines or customers. We may be unable to identify suitable acquisition candidates or consummate desired acquisitions and, if we do make any acquisitions, we may be unable to successfully integrate any acquired companies with our operations.***

A significant part of our growth strategy involves acquiring companies with complementary product lines, customers or other capabilities. For example, (i) in fiscal year 2000, we acquired FabTech, a wafer fabrication company, in order to have our own wafer manufacturing capabilities, (ii) in January 2006, we acquired Anachip as an entry into standard logic markets, and (iii) in November 2006, we acquired the net operating assets of APD. While we do not currently have any agreements or commitments in place with respect to any material acquisitions, we are in various stages of preliminary discussions, and we intend to continue to expand and diversify our operations by making further acquisitions. However, we may be unsuccessful in identifying suitable acquisition candidates, or we may be unable to consummate a desired acquisition. To the extent we do make acquisitions, if we are unsuccessful in integrating these companies or their operations or product lines with our operations, or if integration is more difficult than anticipated, we may experience disruptions that could have a material adverse effect on our business, financial condition and results of operations. In addition, we may not realize all of the benefits we anticipate from any such acquisitions. Some of the risks that may affect our ability to integrate or realize any anticipated benefits from acquisitions that we may make include those associated with:

- Ø unexpected losses of key employees or customers of the acquired company;
- Ø bringing the acquired company's standards, processes, procedures and controls into conformance with our operations;
  - Ø coordinating our new product and process development;
  - Ø hiring additional management and other critical personnel;
  - Ø increasing the scope, geographic diversity and complexity of our operations;
  - Ø difficulties in consolidating facilities and transferring processes and know-how;
    - Ø difficulties in reducing costs of the acquired entity's business;
  - Ø diversion of management's attention from the management of our business; and
  - Ø adverse effects on existing business relationships with customers.

***We are subject to many environmental laws and regulations that could affect our operations or result in significant expenses.***

We are subject to a variety of U.S. Federal, state, local and foreign governmental laws, rules and regulations related to the use, storage, handling, discharge or disposal of certain toxic, volatile or otherwise hazardous chemicals used in our manufacturing process both in the United States where our wafer fabrication facility is located, in China where our assembly, test and packaging facilities are located, and in Taiwan (where our analog products were produced through 2007). Some of these regulations in the United States include the Federal Clean Water Act, Clean Air Act, Resource Conservation and Recovery Act, Comprehensive Environmental Response, Compensation, and Liability Act and similar state statutes and regulations. Any of these regulations could require us to acquire equipment or to incur substantial other expenses to comply with environmental regulations. If we were to incur such additional expenses, our product costs could significantly increase, materially affecting our business, financial condition and results of operations. Any failure to comply with present or future environmental laws, rules and regulations could result in fines, suspension of production or cessation of operations, any of which could have a material adverse effect on our business, financial condition and results of operations. Our operations affected by such requirements include, among others: the disposal of wastewater containing residues from our manufacturing operations through publicly operated treatment works or sewer systems, and which may be subject to volume and chemical discharge limits and may also require discharge permits; and the use, storage and disposal of materials that may be classified as toxic or hazardous. Any of these may result in, or may have resulted in, environmental conditions for which we could be liable.



Some environmental laws impose liability, sometimes without fault, for investigating or cleaning up contamination on, or emanating from, our currently or formerly owned, leased or operated properties, as well as for damages to property or natural resources and for personal injury arising out of such contamination. Such liability may also be joint and several, meaning that we could be held responsible for more than our share of the liability involved, or even the entire liability. In addition, the presence of environmental contamination could also interfere with ongoing operations or adversely affect our ability to sell or lease our properties. Environmental requirements may also limit our ability to identify suitable sites for new or expanded plants. Discovery of contamination for which we are responsible, the enactment of new laws and regulations, or changes in how existing requirements are enforced, could require us to incur additional costs for compliance or subject us to unexpected liabilities.

***Our products may be found to be defective and, as a result, product liability claims may be asserted against us, which may harm our business and our reputation with our customers.***

Our products are typically sold at prices that are significantly lower than the cost of the equipment or other goods in which they are incorporated. For example, our products that are incorporated into a personal computer may be sold for several cents, whereas the computer maker might sell the personal computer for several hundred dollars. Although we maintain rigorous quality control systems, we shipped approximately 10.2 billion, 14.5 billion and 18.1 billion individual semiconductor devices in years ended at December 31, 2005, 2006 and 2007, respectively, to customers around the world, and in the ordinary course of our business, we receive warranty claims for some of these products that are defective, or that do not perform to published specifications. Since a defect or failure in our products could give rise to failures in the end products that incorporate them (and consequential claims for damages against our customers from their customers), we may face claims for damages that are disproportionate to the revenues and profits we receive from the products involved. In addition, our ability to reduce such liabilities may be limited by the laws or the customary business practices of the countries where we do business. Even in cases where we do not believe we have legal liability for such claims, we may choose to pay for them to retain a customer's business or goodwill or to settle claims to avoid protracted litigation. Our results of operations and business could be adversely affected as a result of a significant quality or performance issue in our products, if we are required or choose to pay for the damages that result. Although we currently have product liability insurance, we may not have sufficient insurance coverage, and we may not have sufficient resources, to satisfy all possible product liability claims. In addition, any perception that our products are defective would likely result in reduced sales of our products, loss of customers and harm to our business and reputation.

***We may fail to attract or retain the qualified technical, sales, marketing and management personnel required to operate our business successfully.***

Our future success depends, in part, upon our ability to attract and retain highly qualified technical, sales, marketing and managerial personnel. Personnel with the necessary expertise are scarce and competition for personnel with these skills is intense. We may not be able to retain existing key technical, sales, marketing and managerial employees or be successful in attracting, assimilating or retaining other highly qualified technical, sales, marketing and managerial personnel in the future. For example, we have faced, and continue to face, intense competition for qualified technical and other personnel in Shanghai, China, where our assembly, test and packaging facilities are located. A number of U.S. and multi-national corporations, both in the semiconductor industry and in other industries, have recently established and are continuing to establish factories and plants in Shanghai, China, and the competition for qualified personnel has increased significantly as a result. If we are unable to retain existing key employees or are unsuccessful in attracting new highly qualified employees, our business, financial condition and results of operations could be materially and adversely affected.

***We may not be able to maintain our growth or achieve future growth and such growth may place a strain on our management and on our systems and resources.***

Our ability to successfully grow our business within the discrete and analog semiconductor markets requires effective planning and management. Our past growth, and our targeted future growth, may place a significant strain on our management and on our systems and resources, including our financial and managerial controls, reporting systems and procedures. In addition, we will need to continue to train and manage our workforce worldwide. If we are unable to effectively plan and manage our growth effectively, our business and prospects will be harmed and we will not be able to maintain our profit growth or achieve future growth.

*Our business may be adversely affected by obsolete inventories as a result of changes in demand for our products and change in life cycles of our products.*

The life cycles of some of our products depend heavily upon the life cycles of the end products into which devices are designed. These types of end-market products with short life cycles require us to manage closely our production and inventory levels. Inventory may also become obsolete because of adverse changes in end-market demand. We may in the future be adversely affected by obsolete or excess inventories which may result from unanticipated changes in the estimated total demand for our products or the estimated life cycles of the end products into which our products are designed. In addition, some customers restrict how far back the date of manufacture for our products can be, and therefore some of our products inventory may become obsolete, and thus, adversely affect our results of operations.

***If OEMs do not design our products into their applications, a portion of our net sales may be adversely affected.***

We expect an increasingly significant portion of net sales will come from products we design specifically for our customers. However, we may be unable to achieve these design wins. In addition, a design win from a customer does not necessarily guarantee future sales to that customer. Without design wins from OEMs, we would only be able to sell our products to these OEMs as a second source, which usually means we are only able to sell a limited amount of product to them. Once an OEM designs another supplier's semiconductors into one of its product platforms, it is more difficult for us to achieve future design wins with that OEM's product platform because changing suppliers involves significant cost, time, effort and risk to an OEM. Achieving a design win with a customer does not ensure that we will receive significant revenues from that customer and we may be unable to convert design into actual sales. Even after a design win, the customer is not obligated to purchase our products and can choose at any time to stop using our products, if, for example, its own products are not commercially successful.

***We rely heavily on our internal electronic information and communications systems, and any system outage could adversely affect our business and results of operations.***

All of our operations, other than Diodes-FabTech, operate on a single technology platform. To manage our international operations efficiently and effectively, we rely heavily on our Enterprise Resource Planning (ERP) system, internal electronic information and communications systems and on systems or support services from third parties. Any of these systems are subject to electrical or telecommunications outages, computer hacking or other general system failure. It is also possible that future acquisitions operate on ERP systems different from ours and that we could face difficulties in integrating operational and accounting functions of new acquisitions. Difficulties in upgrading or expanding our ERP system or system-wide or local failures that affect our information processing could have material adverse effects on our business, financial condition, results of operations and cash flows.

***We are subject to interest rate risk that could have an adverse effect on our cost of working capital and interest expenses.***

We have credit facilities with U.S. and Asian financial institutions, as well as other debt instruments, with interest rates equal to LIBOR or similar indices plus a negotiated margin. A rise in interest rates could have an adverse impact upon our cost of working capital and our interest expense. As of December 31, 2007, our outstanding interest-bearing debt was \$237.2 million. An increase of 1.0% in interest rates would increase our annual interest rate expense by approximately \$0.1 million (our \$230 million in convertible notes bear a 2.25% fixed interest rate).

***We had a significant amount of debt following the offering of convertible notes. Our substantial indebtedness could adversely affect our business, financial condition and results of operations and our ability to meet our payment obligations under the notes and or other debt.***

Following the offering of convertible notes in October 2006, we had a significant amount of debt and substantial debt service requirements. As of December 31, 2007, we had \$237.2 million of outstanding debt, including \$230 million senior convertible notes. In addition, \$58.1 million is available for future borrowings under our principal U.S. credit facility, and we are permitted under the terms of our debt agreements to incur substantial additional debt.

This level of debt could have significant consequences on our future operations, including:

- Ø making it more difficult for us to meet our payment and other obligations under the notes and our other outstanding debt;
- Ø resulting in an event of default if we fail to comply with the financial and other restrictive covenants contained in our debt agreements, which event of default could result in all of our debt becoming immediately due and payable and, in the case of an event of default under our secured debt, such as our senior secured credit facility, could permit the lenders to foreclose on our assets securing that debt;
- Ø reducing the availability of our cash flow to fund working capital, capital expenditures, acquisitions and other general corporate purposes, and limiting our ability to obtain additional financing for these purposes;
- Ø subjecting us to the risk of increased sensitivity to interest rate increases on our indebtedness with variable interest rates, including borrowings under senior secured credit facility;
- Ø limiting our flexibility in planning for, or reacting to, and increasing our vulnerability to, changes in our business, the industry in which we operate and the general economy; and
  - Ø placing us at a competitive disadvantage compared to our competitors that have less debt or are less leveraged.

Any of the above-listed factors could have an adverse effect on our business, financial condition and results of operations and our ability to meet our payment obligations under the notes and our other debt.

***We maintain a portfolio of investments, primarily auction rate securities, which are classified as current, available-for-sale investments. Based on current market conditions, it is likely that auctions related to these securities will be unsuccessful in the near term, which will limit liquidity related to these investments, and may cause us to record realized or unrealized losses on our financial statements.***

As of December 31, 2007, we had \$320.7 invested primarily in auction rate securities, which are classified as current, available-for-sale investments. Although the maturities of the securities are over 10 years, management intends to use the funds within one year and does not anticipate holding the investments until maturity; therefore, the securities are classified as short-term and included in short-term investments on our consolidated balance sheets. The carrying values of available-for-sale securities approximates fair value. These investments are primarily in municipal and student loan association bonds that are fully collateralized by AAA rated bonds, and/or insured against loss of principal and interest by AAA rated bond insurers. None of these investments are collateralized mortgage obligations or are any other type of mortgage- or real estate-backed security. Auction rate securities are generally long-term debt instruments that provide liquidity through a Dutch auction process that resets the applicable interest rate at pre-determined calendar intervals. These mechanisms generally allow existing investors to rollover their holdings and continue to own their respective securities or liquidate their holdings by selling their securities at par value.

We generally invest in these securities for short periods of time as part of our cash management program. However, the recent uncertainties in the credit markets have prevented us and other investors from liquidating holdings of auction rate securities in recent auctions occurring subsequent to December 31, 2007, because the amount of securities submitted for sale has exceeded the amount of purchase orders, resulting in our continuing to hold these securities and the issuers paying interest at the maximum contractual rates which are higher than similar securities for which auctions have cleared. Based on current market conditions, it is likely that auctions related to more of these securities will be unsuccessful in the near term. Unsuccessful auctions could result in our holding securities beyond their next scheduled auction reset dates if a secondary market does not develop, thereby limiting the short-term liquidity of these investments. The reported amounts for these securities take into consideration the financial conditions of the issuer and the bond insurers as well as the value of the collateral. If the credit ratings of the issuer, the bond insurers or the collateral deteriorate, we may adjust the carrying value of these investments. Although we are uncertain as to when the liquidity issues relating to these investments will improve, we consider these issues to be only temporary. Any temporary decline, if sustained, would be recognized in other comprehensive income. It is possible that declines in fair value may occur. We continue to monitor the market for auction rate securities and consider its impact (if any) on the fair market value of the investments. If the current market conditions deteriorate further the Company may be required to record unrealized losses in other comprehensive income or impairment charges in 2008.

***If we fail to maintain an effective system of internal controls or discover material weaknesses in our internal controls over financial reporting, we may not be able to report our financial results accurately or detect fraud, which could harm our business and the trading price of our Common Stock.***

Effective internal controls are necessary for us to produce reliable financial reports and are important in our effort to prevent financial fraud. We are required to periodically evaluate the effectiveness of the design and operation of our internal controls. These evaluations may result in the conclusion that enhancements, modifications or changes to our internal controls are necessary or desirable. While management evaluates the effectiveness of our internal controls on a regular basis, these controls may not always be effective. There are inherent limitations on the effectiveness of internal controls including collusion, management override, and failure of human judgment. Because of this, control procedures are designed to reduce rather than eliminate business risks. If we fail to maintain an effective system of internal controls or if management or our independent registered public accounting firm were to discover material weaknesses in our internal controls, we may be unable to produce reliable financial reports or prevent fraud which

could harm our financial condition and results of operations and result in loss of investor confidence and a decline in our stock price.

*Terrorist attacks, or threats or occurrences of other terrorist activities whether in the United States or internationally may affect the markets in which our Common Stock trades, the markets in which we operate and our profitability.*

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Terrorist attacks, or threats or occurrences of other terrorist or related activities, whether in the United States or internationally, may affect the markets in which our Common Stock trades, the markets in which we operate and our profitability. Future terrorist or related activities could affect our domestic and international sales, disrupt our supply chains and impair our ability to produce and deliver our products. Such activities could affect our physical facilities or those of our suppliers or customers. Such terrorist attacks could cause ports or airports to or through which we ship to be shut down, thereby preventing the delivery of raw materials and finished goods to or from our manufacturing facilities in Shanghai, China, Taiwan or Kansas City, Missouri, or to our regional sales offices. Due to the broad and uncertain effects that terrorist attacks have had on financial and economic markets generally, we cannot provide any estimate of how these activities might affect our future results.

## **RISKS RELATED TO OUR INTERNATIONAL OPERATIONS**

*Our international operations subject us to risks that could adversely affect our operations.*

We expect net sales from foreign markets to continue to represent a significant portion of our total net sales. In addition, the majority of our manufacturing facilities are located overseas in China. In 2005, 2006 and 2007, net sales to customers outside the United States represented 74.4%, 77.8% and 79.7%, respectively, of our net sales. There are risks inherent in doing business internationally, and any or all of the following factors could cause harm to our business:

- Ø changes in, or impositions of, legislative or regulatory requirements, including tax laws in the United States and in the countries in which we manufacture or sell our products;
  - Ø compliance with trade or other laws in a variety of jurisdictions;
  - Ø trade restrictions, transportation delays, work stoppages, and economic and political instability;
  - Ø changes in import/export regulations, tariffs and freight rates;
  - Ø difficulties in collecting receivables and enforcing contracts;
    - Ø currency exchange rate fluctuations;
  - Ø restrictions on the transfer of funds from foreign subsidiaries to the United States;
- Ø the possibility of international conflict, particularly between or among China and Taiwan and the United States;
- Ø legal regulatory, political and cultural differences among the countries in which we do business;
  - Ø longer customer payment terms; and
  - Ø changes in U.S. or foreign tax regulations.

*We have significant operations and assets in China, Taiwan and Hong Kong and, as a result, will be subject to risks inherent in doing business in those jurisdictions, which may adversely affect our financial performance.*

We have a significant portion of our assets in mainland China, Taiwan and Hong Kong. Our ability to operate in China, Taiwan and Hong Kong may be adversely affected by changes in those jurisdictions' laws and regulations, including those relating to taxation, import and export tariffs, environmental regulations, land use rights, property and other matters. In addition, our results of operations in China, Taiwan and Hong Kong are subject to the economic and political situation there. We believe that our operations in China, Taiwan and Hong Kong are in compliance with all applicable legal and regulatory requirements. However, the central or local governments of these jurisdictions may impose new, stricter regulations or interpretations of existing regulations that would require additional expenditures and efforts on our part to ensure our compliance with such regulations or interpretations.

Changes in the political environment or government policies in those jurisdictions could result in revisions to laws or regulations or their interpretation and enforcement, increased taxation, restrictions on imports, import duties or currency revaluations. In addition, a significant destabilization of relations between or among China, Taiwan or Hong Kong and the United States could result in restrictions or prohibitions on our operations or the sale of our products or the forfeiture of our assets in these jurisdictions. There can be no certainty as to the application of the laws and

regulations of these jurisdictions in particular instances. Enforcement of existing laws or agreements may be sporadic and implementation and interpretation of laws inconsistent. Moreover, there is a high degree of fragmentation among regulatory authorities, resulting in uncertainties as to which authorities have jurisdiction over particular parties or transactions. The possibility of political conflict between these countries or with the United States could have an adverse impact upon our ability to transact business in these jurisdictions and to generate profits.



***We are subject to foreign currency risk as a result of our international operations.***

We face exposure to adverse movements in foreign currency exchange rates, primarily Asian currencies and, to a lesser extent, the Euro. For example, many of our employees who are located in China, are paid in the Chinese Yuan and, accordingly, an increase in the value of the Yuan compared to the U.S. dollar could increase our operating expenses. In addition, we sell our products in various currencies and, accordingly, a decline in the value of any such currency against the U.S. dollar, which is our primary functional currency, could create a decrease in our net sales. Our foreign currency risk may change over time as the level of activity in foreign markets grows and could have an adverse impact upon our financial results. These currencies are principally the Chinese Yuan, the Taiwanese dollar, the Japanese Yen, the Euro and the Hong Kong dollar. The Chinese government has recently taken action to permit the Yuan to U.S. dollar exchange rate to fluctuate, which may exacerbate our exposure to foreign currency risk and harm our results of operations. We do not usually employ hedging techniques designed to mitigate foreign currency exposures and, therefore, we could experience currency losses as these currencies fluctuate against the U.S. dollar.

***We may not continue to receive preferential tax treatment in Asia, thereby increasing our income tax expense and reducing our net income.***

As an incentive for establishing our manufacturing subsidiaries in China, we receive preferential tax treatment. In addition, in conjunction with the acquisition of Anachip, we also receive preferential tax treatment in Taiwan. Governmental changes in foreign tax law may cause us not to be able to continue receiving these preferential tax treatments in the future, which may cause an increase in our income tax expense, thereby reducing our net income.

***The distribution of any earnings of our foreign subsidiaries to the United States may be subject to U.S. income taxes, thus reducing our net income.***

As of December 31, 2006, accumulated and undistributed earnings of Diodes-China and Diodes-Shanghai were approximately \$67.0 million (including \$28.5 million of restricted earnings, which are not available for dividends), which we considered as a permanent investment, and we had recorded \$3.3 million in additional U.S. taxes, primarily for earnings of Diodes-Hong Kong.

With the establishment of the holding companies in 2007, the Company now intends to permanently reinvest overseas all of its earnings from its foreign subsidiaries. Accordingly, the \$3.3 million deferred tax liability was reversed during 2007 and U.S. taxes are no longer being recorded on undistributed foreign earnings.

As of December 31, 2007, the Company has undistributed earnings from its non-U.S. operations of approximately \$167 million (including \$28.5 million of restricted earnings which are not available for dividends). Additional Federal and state income taxes of approximately \$40 million would be required should such earnings be repatriated to the U.S. parent.

We may, in the future, plan to distribute earnings of our foreign subsidiaries from Asia to the U.S. We may be required to pay U.S. income taxes on these earnings to the extent we have not previously recorded deferred U.S. taxes on such earnings. Any such taxes would reduce our net income in the period in which these earnings are distributed.

## **RISKS RELATED TO OUR COMMON STOCK**

***Variations in our quarterly operating results may cause our stock price to be volatile.***

We may experience substantial variations in net sales, gross profit margin and operating results from quarter to quarter. We believe that the factors that influence this variability of quarterly results include:

- Ø general economic conditions in the countries where we sell our products;
- Ø seasonality and variability in the computing and communications market and our other end-markets;
  - Ø the timing of our and our competitors' new product introductions;
  - Ø product obsolescence;
- Ø the scheduling, rescheduling and cancellation of large orders by our customers;
  - Ø the cyclical nature of demand for our customers' products;
- Ø our ability to develop new process technologies and achieve volume production at our fabrication facilities;
  - Ø changes in manufacturing yields;
  - Ø changes in gross profit margins due to the Anachip or APD acquisitions;
  - Ø adverse movements in exchange rates, interest rates or tax rates; and
- Ø the availability of adequate supply commitments from our outside suppliers or subcontractors.

Accordingly, a comparison of our results of operations from period to period is not necessarily meaningful to investors and our results of operations for any period do not necessarily indicate future performance. Variations in our quarterly results may trigger volatile changes in our stock price.

***We may enter into future acquisitions and take certain actions in connection with such acquisitions that could affect the price of our Common Stock.***

As part of our growth strategy, we expect to review acquisition prospects that would implement our vertical integration strategy or offer other growth opportunities. While we do not currently have any agreements or commitments in place with respect to any material acquisitions, we are in various stages of preliminary discussions, and we may acquire businesses, products or technologies in the future. In the event of future acquisitions, we could:

- Ø use a significant portion of our available cash;
- Ø issue equity securities, which would dilute current stockholders' percentage ownership;
- Ø incur substantial debt;
- Ø incur or assume contingent liabilities, known or unknown;
- Ø incur amortization expenses related to intangibles; and
- Ø incur large, immediate accounting write-offs.

Such actions by us could harm our results from operations and adversely affect the price of our Common Stock.

***Our directors, executive officers and significant stockholders hold a substantial portion of our Common Stock, which may lead to conflicts with other stockholders over corporate transactions and other corporate matters.***

Our directors, executive officers and our affiliate, LSC, beneficially own approximately 30.4% of our outstanding Common Stock, including options to purchase shares of our Common Stock that are exercisable within 60 days of December 31, 2007. These stockholders, acting together, will be able to influence significantly all matters requiring stockholder approval, including the election of directors and significant corporate transactions such as mergers or other business combinations. This control may delay, deter or prevent a third party from acquiring or merging with us, which could adversely affect the market price of our Common Stock.

LSC, our largest stockholder, owns approximately 21.6% (approximately 8.7 million shares) of our Common Stock. Some of our directors and executive officers may have potential conflicts of interest because of their positions with LSC or their ownership of LSC Common Stock. Some of our directors are LSC directors and officers, and our non-employee Chairman of our Board of Directors is Chairman of the board of LSC. Several of our directors and executive officers own LSC Common Stock and hold options to purchase LSC common stock. Service on our Board of Directors and as a director or officer of LSC, or ownership of LSC common stock by our directors and executive officers, could create, or appear to create, actual or potential conflicts of interest when directors and officers are faced with decisions that could have different implications for LSC and us. For example, potential conflicts could arise in connection with decisions involving the Common Stock owned by LSC, or under the other agreements we may enter into with LSC. LSC was our largest external supplier of discrete semiconductor products for subsequent sale by us. In 2006 and 2007, approximately 13.0% and 11.3%, respectively, of our net sales were from products manufactured by LSC. In addition to being our largest external supplier of finished products in each of these periods, we sold silicon wafers to LSC totaling 6.5% and 6.2%, respectively, of our net sales during such periods, making LSC our largest customer.

We may have difficulty resolving any potential conflicts of interest with LSC, and even if we do, the resolution may be less favorable than if we were dealing with an entirely unrelated third party.



***We were formed in 1959, and our early corporate records are incomplete. As a result, we may have difficulty in assessing and defending against claims relating to rights to our Common Stock purporting to arise during periods for which our records are incomplete.***

We were formed in 1959 under the laws of California and reincorporated in Delaware in 1969. We have had several transfer agents over the past 49 years. In addition, our early corporate records, including our stock ledger, are incomplete. As a result, we may have difficulty in assessing and defending against claims relating to rights to our Common Stock purporting to arise during periods for which our records are incomplete.

***Conversion of our convertible senior notes will dilute the ownership interest of existing stockholders, including holders who had previously converted their notes.***

To the extent we issue Common Stock upon conversion of the notes, the conversion of some or all of the notes will dilute the ownership interests of existing stockholders, including holders who have received Common Stock upon prior conversion of the notes. Any sales in the public market of the Common Stock issuable upon such conversion could adversely affect prevailing market prices of our Common Stock. In addition, the existence of the notes may encourage short selling by market participants because the conversion of the notes could depress the price of our Common Stock.

***The repurchase rights and the increased conversion rate triggered by a make-whole fundamental change could discourage a potential acquirer.***

If a “fundamental change” in accordance with the terms of the senior convertible notes were to occur, the holders of the notes have the right to require us to repurchase the notes. A fundamental change would include a change in control of the Company. In addition, if a make-whole fundamental change were to occur, which may include an acquisition of the Company, the conversion rate for the senior convertible notes will increase. The repurchase rights in our senior convertible notes triggered by a fundamental change and the increased conversion rate triggered by a make-whole fundamental change could discourage a potential acquirer.

***Anti-takeover effects of certain provisions of Delaware law and our Certificate of Incorporation and By-laws.***

Some provisions of Delaware law, our certificate of incorporation and by-laws may be deemed to have an anti-takeover effect and may delay or prevent a tender offer to takeover attempt that a stockholder might consider in its best interest, including those attempts that might result in a premium over the market price for the shares held by stockholders.

### ***Section 203 of Delaware General Corporation Law***

Section 203 of the Delaware General Corporation Law prohibits transactions between a Delaware corporation and an “interested stockholder,” which is defined as a person who, together with any affiliates or associates, beneficially owns, directly or indirectly, 15.0% or more of the outstanding voting shares of a Delaware corporation. This provision prohibits certain business combinations between an interested stockholder and a Delaware corporation for a period of three years after the date the stockholder becomes an interested stockholder, unless:

- (i) either the business combination or the transaction which resulted in the stockholder becoming an interested stockholder is approved by the corporation’s board of directors prior to the date the interested stockholder becomes an interested stockholder;
- (ii) the interested stockholder acquired at least 85.0% of the voting stock of the corporation (other than stock held by directors who are also officers or be certain employee stock plans) in the transaction in which the stockholder became

an interested stockholder; or

(iii) the business combination is approved by a majority of the board of directors and by the affirmative vote of 66.66% of the outstanding voting stock that is not owned by the interested stockholder.

For this purpose, business combinations include mergers, consolidations, sales or other dispositions of assets having an aggregate value in excess of 10.0% of the aggregate market value of the consolidated assets or outstanding stock of the corporation, and certain transactions that would increase the interested stockholder's proportionate share ownership in the corporation.

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*Certificate of Incorporation and Bylaw Provisions*

Provisions of our certificate of incorporation and bylaws may have the effect of making it more difficult for a third party to acquire control of our company. In particular, our bylaws authorize our Board of Directors to issue, without further action by the stockholders, up to 1,000,000 shares of undesignated preferred stock with rights and preferences, including voting rights, designated from time to time by the Board of Directors. The existence of authorized but unissued shares of preferred stock enables our board of directors to render more difficult or to discourage an attempt to obtain control of us by means of a merger, tender offer, proxy contest or otherwise.

**Item 1B. Unresolved Staff Comments**

None

**Item 2. Properties**

Our primary physical properties at December 31, 2007, were as follows:

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\* Size is less than 1,000 square feet and/or monthly rental is less than \$1,000.

We believe our current facilities are adequate for the foreseeable future. See “Property, Plant and Equipment” and “Commitments and Contingencies” in “Notes to Consolidated Financial Statements.”

**Item 3. Legal Proceedings**

We are, from time to time, involved in litigation incidental to the conduct of our business. We do not believe we are currently a party to any material pending litigation.

**Item 4. Submission of Matters to a Vote of Security Holders**

No matter was submitted by us to a vote of security holders during the fourth quarter of 2007.



## PART II

**Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

Our Common Stock is traded on the Nasdaq Global Select Market ("NasdaqGS") under the symbol "DIOD." Until June 19, 2000, our Common Stock was traded on the American Stock Exchange ("AMEX") under the symbol "DIO." In July 2000, November 2003, December 2005 and July 2007, we effected 50% stock dividends in the form of three-for-two stock splits. The following table shows the range of high and low closing sales prices per share, adjusted for the three-for-two stock splits, for our Common Stock for each fiscal quarter from January 1, 2006 as reported by NasdaqGS.

| Calendar Quarter Ended                    | Closing Sales Price of Common Stock |          |
|-------------------------------------------|-------------------------------------|----------|
|                                           | High                                | Low      |
| First quarter (through February 26, 2008) | \$ 29.71                            | \$ 22.68 |
| Fourth quarter 2007                       | 34.71                               | 27.40    |
| Third quarter 2007                        | 32.84                               | 26.31    |
| Second quarter 2007                       | 27.85                               | 23.06    |
| First quarter 2007                        | 26.94                               | 21.89    |
| Fourth quarter 2006                       | 30.23                               | 23.65    |
| Third quarter 2006                        | 30.66                               | 21.71    |
| Second quarter 2006                       | 29.08                               | 21.69    |
| First quarter 2006                        | 27.67                               | 21.64    |

On February 26, 2008, the closing sales price of our Common Stock as reported by NasdaqGS was \$23.92, and there were approximately 500 registered holders of record of our Common Stock.

We have never declared or paid cash dividends on our Common Stock. Our credit agreement permits us to pay dividends to our stockholders to the extent that any such dividends declared or paid in any fiscal year do not exceed an amount equal to 50% of our net profit after taxes for such fiscal year. The payment of dividends is within the discretion of our Board of Directors, and will depend upon, among other things, our earnings, financial condition, capital requirements, and general business conditions. There have been no stock repurchases in our history.

## Performance Graph

Set forth below is a line graph comparing the yearly percentage change in the cumulative total stockholder return of our Common Stock against the cumulative total return of the Nasdaq Composite and the Nasdaq Industrial Index for the five calendar years ending December 31, 2007. The graph is not necessarily indicative of future price performance.

*The graph shall not be deemed incorporated by reference by any general statement incorporating by reference this Annual Report into any filing under the Securities Act of 1933 or under the Securities Exchange Act of 1934, except to the extent that the Company specifically incorporates this information by reference, and shall not otherwise be deemed filed under such Acts.*

Source: CTA Integrated Communications. Data from ReutersBRIDGE Data Networks

The graph assumes \$100 invested on December 31, 2002 in our Common Stock, the stock of the companies in the Nasdaq Composite Index and the Nasdaq Industrial Index, and that all dividends received within a quarter, if any, were reinvested in that quarter.

**Item 6. Selected Financial Data**

The following selected consolidated financial data for the fiscal years ended December 31, 2003 through 2007 is qualified in its entirety by, and should be read in conjunction with, the other information and consolidated financial statements, including the notes thereto, appearing elsewhere herein. Certain amounts as presented in the accompanying consolidated financial statements have been reclassified to conform to 2007 financial statement presentation. These reclassifications had no impact on previously reported net income or stockholders' equity.

| <i>Income Statement Data</i>                                 | Years ended December 31, |            |            |            |            |
|--------------------------------------------------------------|--------------------------|------------|------------|------------|------------|
|                                                              | 2003                     | 2004       | 2005       | 2006       | 2007       |
| Net sales                                                    | \$ 136,905               | \$ 185,703 | \$ 214,765 | \$ 343,308 | \$ 401,159 |
| Gross profit                                                 | 36,528                   | 60,735     | 74,377     | 113,892    | 130,379    |
| Selling, general and administrative expenses                 | 19,586                   | 23,503     | 30,285     | 47,945     | 55,461     |
| Research and development expenses                            | 2,049                    | 3,422      | 3,713      | 8,317      | 13,515     |
| Restructuring costs and impairment loss of long-lived assets | 1,037                    | 14         | (102)      | 152        | 1,003      |
| Income from operations                                       | 13,856                   | 33,796     | 40,481     | 57,478     | 60,400     |
| Interest income (expense), net                               | (860)                    | (637)      | 221        | 4,855      | 11,286     |
| Other Income (expense)                                       | (5)                      | (418)      | 406        | (1,212)    | (225)      |
| Income before taxes and minority interest                    | 12,991                   | 32,741     | 41,108     | 61,121     | 71,461     |
| Income tax provision                                         | 2,460                    | 6,514      | 6,685      | 11,689     | 9,428      |
| Minority interest in joint venture                           | (436)                    | (676)      | (1,094)    | (1,289)    | (2,376)    |
| Net income                                                   | 10,095                   | 25,551     | 33,329     | 48,143     | 59,657     |
| Earnings per share: <sup>(1)</sup>                           |                          |            |            |            |            |
| Basic                                                        | \$ 0.35                  | \$ 0.85    | \$ 0.96    | \$ 1.25    | \$ 1.51    |
| Diluted                                                      | \$ 0.31                  | \$ 0.73    | \$ 0.86    | \$ 1.16    | \$ 1.41    |
| Number of shares used in computation <sup>(1)</sup>          |                          |            |            |            |            |
| Basic                                                        | 28,644                   | 30,160     | 34,752     | 38,443     | 39,601     |

|                                        |            |            |            |            |                   |
|----------------------------------------|------------|------------|------------|------------|-------------------|
| Diluted                                | 32,414     | 34,811     | 38,842     | 41,502     | <b>42,331</b>     |
| <b>As of December 31,</b>              |            |            |            |            |                   |
| <i>Balance Sheet Data</i>              | 2003       | 2004       | 2005       | 2006       | <b>2007</b>       |
| Total assets                           | \$ 123,795 | \$ 167,801 | \$ 289,515 | \$ 622,139 | \$ <b>706,365</b> |
| Working capital                        | 27,154     | 49,571     | 146,651    | 395,354    | <b>451,801</b>    |
| Long-term debt, net of current portion | 6,750      | 7,833      | 4,865      | 237,115    | <b>235,815</b>    |
| Stockholders' equity                   | 71,450     | 112,148    | 225,474    | 294,167    | <b>369,598</b>    |

(1) Adjusted for the effect of 3-for-2 stock splits in November 2003, December 2005 and July 2007.

2006 data included \$5.3 million, or \$0.10 per diluted share, of non-cash, net of tax effect stock option compensation expense as per SFAS No. 123R.

2007 data included \$4.3 million, or \$0.07 per diluted share, of non-cash, net of tax effect stock option compensation expense as per SFAS No. 123R.

## **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

*The following discussion of the Company's financial condition and results of operations should be read together with the consolidated financial statements and the notes to consolidated financial statements included elsewhere in this Form 10-K.*

*The following discussion contains forward-looking statements and information relating to our Company. We generally identify forward-looking statements by the use of terminology such as "may," "will," "could," "should," "potential," "continue," "expect," "intend," "plan," "estimate," "anticipate," "believe," "project," or similar phrases or the negatives of such terms. We base these statements on our beliefs as well as assumptions we made using information currently available to us. Such statements are subject to risks, uncertainties and assumptions, including those identified in "Item 1A. Risk Factors," as well as other matters not yet known to us or not currently considered material by us. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, estimated or projected. Given these risks and uncertainties, prospective investors are cautioned not to place undue reliance on such forward-looking statements. Forward-looking statements do not guarantee future performance and should not be considered as statements of fact.*

*You should not unduly rely on these forward-looking statements, which speak only as of the date of this Annual Report on Form 10-K. Unless required by law, we undertake no obligation to publicly update or revise any forward-looking statements to reflect new information or future events or otherwise. The Private Securities Litigation Reform Act of 1995 (the "Act") provides certain "safe harbor" provisions for forward-looking statements. All forward-looking statements made in this Annual Report on Form 10-K are made pursuant to the Act.*

### **Overview**

We are a global supplier of high-quality, application specific standard products within the broad discrete and analog semiconductor markets. These products include diodes, rectifiers, transistors, MOSFETs, protection devices, functional specific arrays, power management devices including DC-DC switching and linear voltage regulators, amplifiers and comparators, Hall effect sensors, and silicon wafers used to manufacture these products.

We design, manufacture and market these semiconductors focused on diverse end-user applications in the consumer electronics, computing, industrial, communications and automotive sectors. Semiconductors, which provide electronic signal amplification and switching functions, are basic building-block electronic components that are incorporated into almost every electronic device. We believe that our focus on standard semiconductor products provides us with a meaningful competitive advantage relative to other semiconductor companies that provide a wider range of semiconductor products.

We are headquartered in Dallas, Texas. We have two manufacturing facilities located in Shanghai, China, an analog design center located in Hsinchu, Taiwan and a wafer fabrication facility in Kansas City, Missouri. Our sales and marketing and logistical centers are located in Westlake Village, California; Taipei, Taiwan; Shanghai and Shenzhen, China; and Hong Kong. We also have regional sales offices or representatives in: Derbyshire, England; Toulouse, France; Frankfurt, Germany; and various cities in the United States.

In 1998, we began to transform our business from the distribution of discrete semiconductors manufactured by others to the design, manufacture and marketing of discrete semiconductor products using our internal manufacturing capabilities. The key elements of our strategy of transforming our business from a distribution-based model to one primarily based on the design and manufacture of proprietary products are:

Ø

expanding our manufacturing capacity, including establishing integrated state-of-the-art packaging and testing facilities in Asia, in 1998 and 2004, and acquiring a wafer foundry in the U.S. in 2000;

Ø expanding our sales and marketing organization in Asia in order to address the shift of manufacturing of electronics products from the United States to Asia;

Ø establishing our sales and marketing organization in Europe commencing in 2002; and

Ø expanding the number of our field application engineers to design our products into specific end-user applications;

In implementing this strategy, the following factors have affected, and, we believe, will continue to affect, our results of operations:

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- Ø Since 1998, we have experienced increases in the demand for our products, and substantial pressure from our customers and competitors to reduce the selling price of our products. We expect future increases in net income to result primarily from increases in sales volume and improvements in product mix in order to offset reduced average selling prices of our products.
- Ø In 2006 and 2007, 28.2% and 35.1%, respectively, of our net sales were derived from products introduced within the last three years, which we term “new products,” compared to 15.3% in 2005. New products generally have gross profit margins that are significantly higher than the margins of our standard products. We expect net sales derived from new products to increase in absolute terms, although our net sales of new products as a percentage of our net sales will depend on the demand for our standard products, as well as our product mix.
- Ø Our gross profit margin was 32.5% in 2007, compared to 33.2% in 2006 and 34.6% in 2005. Our gross profit margin decrease in 2007 was due to the lower gross margin related to the acquisition of the analog product line. We recently completed the move of our analog product from Taiwan to our China manufacturing facilities to increase the gross margin on this product line. Future gross profit margins will depend primarily on our product mix, cost savings, and the demand for our products.
  - Ø As of December 31, 2007, we had invested approximately \$167.3million in our Asian manufacturing facilities. During 2007, we invested approximately \$41.2 million in our Asian manufacturing facilities and we expect to continue to invest in our manufacturing facilities, although the amount to be invested will depend on product demand and new product developments.
- Ø During 2007, the percentage of our net sales derived from our Asian subsidiaries was 75.4%, compared to 71.9% in 2006 and 65.4% in 2005. We expect our net sales to the Asian market to continue to increase as a percentage of our total net sales for 2008 and beyond as a result of the continuing shift of the manufacture of electronic products from the U.S. to Asia.
- Ø We have increased our investment in research and development from \$8.3 million in 2006 to \$13.5 million in 2007. We continue to seek to hire qualified engineers who fit our focus on proprietary semiconductor processes and packaging technologies. Our goal is to expand research and development expenses to approximately 3 to 4% of net sales, which will enable us to bring additional proprietary devices to the market.

On October 12, 2006, we issued and sold convertible senior notes with an aggregate principal amount of \$230 million due 2026 (“Notes”), which pay 2.25% interest per annum on the principal amount of the Notes, payable semi-annually in arrears on April 1 and October 1 of each year, beginning on April 1, 2007. The Notes will be convertible into cash or, at our option, cash and shares of our Common Stock based on an initial conversion rate, subject to adjustment, of 25.6419 shares (split adjusted) per \$1,000 principal amount of Notes (which represents an initial conversion price of \$39.00 per share, split adjusted), in certain circumstances. In addition, following a “make-whole fundamental change” that occurs prior to October 1, 2011, we will, at our option, increase the conversion rate for a holder who elects to convert its Notes in connection with such “make-whole fundamental change,” in certain circumstances. We intend to use the net proceeds for working capital and general corporate purposes, which may include the acquisition of businesses, products, product rights or technologies, strategic investments, or purchases of our own Common Stock.

During 2005, we sold 4.8 million shares (split adjusted) of our Common Stock in a follow-on public offering, raising approximately \$71.7 million (net of commissions and expenses). We used approximately \$40 million of the net proceeds in connection with the Anachip and APD acquisitions, and we intend to use the remaining net proceeds from this offering for working capital and other general corporate purposes, including additional acquisitions.

As part of our growth strategy, in December 2005, we announced the acquisition of Anachip, a fabless Taiwanese semiconductor company focused on analog ICs designed for specific applications. The \$30.8 million acquisition,

which was completed in January 2006, is in line with our long-term strategy. Anachip's main product focus is power management ICs. The analog devices they produce are used in LCD monitor/TVs, wireless LAN 802.11 access points, brushless DC motor fans, portable DVD players, datacom devices, ADSL modems, TV/satellite set-top boxes, and power supplies. Anachip brings a design team with strong capabilities in a range of targeted analog and power management technologies.

On November 3, 2006, we completed the purchase of the assets of APD Semiconductor, a privately held U.S.-based fabless semiconductor company. APD's main product focus is its patented and trademarked Super Barrier Rectifier™ (SBR®) technology. The purchase price of the acquisition was \$8.4 million in addition to a potential earn-out provision with respect to pre-defined covered products. The APD acquisition will further strengthen our technology leadership in the standard semiconductor market and expand our product capabilities across important segments of our end-markets.



## Net sales

We generate a substantial portion of our net sales through the sale of semiconductor products that are designed and manufactured by third parties or us. We also generate a portion of our net sales from outsourcing our manufacturing capacity to third parties and from the sale of silicon wafers to manufacturers of discrete and analog semiconductor components. We serve customers across diversified industries, including the consumer electronics, computing, industrial, communications and automotive markets.

We recognize revenue from product sales when title to and risk of loss of the product have passed to the customer, there is persuasive evidence of an arrangement, the sale price is fixed or determinable and collection of the related receivable is reasonably assured. These criteria are generally met upon shipment to our customers. Net sales are stated net of reserves for pricing adjustments, discounts, rebates and returns.

The principal factors that have affected or could affect our net sales from period to period are:

- Ø the condition of the economy in general and of the semiconductor industry in particular,
  - Ø our customers' adjustments in their order levels,
- Ø changes in our pricing policies or the pricing policies of our competitors or suppliers,
  - Ø the termination of key supplier relationships,
- Ø the rate of introduction to, and acceptance of new products by, our customers,
  - Ø our ability to compete effectively with our current and future competitors,
- Ø our ability to enter into and renew key corporate and strategic relationships with our customers, vendors and strategic alliances,
  - Ø changes in foreign currency exchange rates,
  - Ø a major disruption of our information technology infrastructure, and
- Ø unforeseen catastrophic events, such as armed conflict, terrorism, fires, typhoons and earthquakes.

## Cost of goods sold

Cost of goods sold includes manufacturing costs for our semiconductors and our wafers. These costs include raw materials used in our manufacturing processes as well as the labor costs and overhead expenses. In addition to costs of raw materials, cost of goods sold is also impacted by yield improvements, capacity utilization and manufacturing efficiencies. In addition, cost of goods sold includes the cost of products that we purchase from other manufacturers and sell to our customers. Cost of goods sold is also affected by inventory obsolescence if our inventory management is not efficient.

## Selling, general and administrative expenses

Selling, general and administrative expenses relate primarily to compensation and associated expenses for personnel in general management, sales and marketing, information technology, engineering, human resources, procurement, planning and finance, and sales commissions, as well as outside legal, accounting and consulting expenses, and other operating expenses. We expect our selling, general and administrative expenses to increase in absolute dollars as we hire additional personnel and expand our sales, marketing and engineering efforts and information technology infrastructure.

## Research and development expenses

Research and development expenses consist of compensation and associated costs of employees engaged in research and development projects, as well as materials and equipment used for these projects. Research and development expenses are primarily associated with our wafer facility in Kansas City, Missouri and our facilities in China and

Taiwan, as well as with our engineers in the U.S. All research and development expenses are expensed as incurred, and we expect our research and development expenses to increase in absolute dollars as we invest in new technologies and product lines.

**Interest income / expense**

Interest income consists of interest earned on our cash and investment balances. Interest expense consists of interest payable on our outstanding credit facilities and other debt instruments including the convertible bonds.

## Income tax provision

Income tax expenses of \$6.7 million, \$11.7 million and \$9.4 million were recorded for the years ended December 31, 2005, 2006, and 2007, respectively, resulting in effective tax rates of 16.3%, 19.1% and 13.2% in the years ended December 31, 2005, 2006 and 2007, respectively. Our lower effective tax rate in 2007 compared with the prior year was the result of lower income in the U.S. and higher income in lower-taxed jurisdictions, as well as a decrease in the amount of estimated repatriation of earnings of our foreign subsidiaries, partially offset by the increased income tax rate at one of our China subsidiaries (Diodes-Shanghai is subject to a 7.5% preferential tax rate from 2007 through 2009, compared to a 0% tax rate in 2006).

Our global presence requires us to pay income taxes in a number of jurisdictions. In general, earnings in the U.S. and Taiwan are currently subject to tax rates of 39.5% and 25.0%, respectively. In addition, Taiwan earnings are subject to an additional 10% retained earnings tax should the Taiwan earnings not be distributed. Earnings of Diodes-Hong Kong are subject to a 17.5% tax for local sales or local source sales; all other Hong Kong sales are not subject to foreign income taxes. Earnings at Diodes-Taiwan and Diodes-Hong Kong are also subject to U.S. taxes with respect to those earnings that are derived from product manufactured by our China subsidiaries and sold to customers outside of Taiwan and Hong Kong, respectively. The U.S. tax rate on this Subpart-F income is computed as the difference between the foreign effective tax rates and the U.S. tax rate. In accordance with U.S. tax law, we receive credit against our U.S. Federal tax liability for income taxes paid by our foreign subsidiaries.

As an incentive for the formation of Anachip, earnings of Anachip are subject to a five-year tax holiday (subject to certain qualifications of Taiwanese tax law). In the third quarter of 2006, we elected to begin this five-year tax holiday as of January 1, 2006. Beginning 2011, Anachip earnings will be subject to statutory Taiwan income tax.

Diodes-China is located in the Songjiang district, where the standard central government tax rate was 24.0% through 2007. However, as an incentive for establishing Diodes-China, the earnings of Diodes-China were subject to a 0% tax rate by the central government from 1996 through 2000, and to a 12.0% tax rate from 2001 through 2007. In addition, due to a \$15.0 million permanent re-investment of Diodes-China earnings in 2004, Diodes-China has received additional preferential tax treatment (earnings will be exempted from central government income tax for two years, and then subject to tax rates in the range of 12.0% to 12.5% for the following three years) on earnings that are generated by this \$15.0 million investment.

In addition, the earnings of Diodes-China would ordinarily be subject to a standard local government tax rate of 3.0%. However, as an incentive for establishing Diodes-China, the local government waived this tax from 1996 through 2006. Management expects this tax to be waived for 2007 as well; however, the local government can re-impose this tax at its discretion at any time.

In 2004, we established our second Shanghai-based manufacturing facility, Diodes-Shanghai, located in the Songjiang Export Zone of Shanghai, China. In the Songjiang Export Zone, the central government standard tax rate is 15.0%, and there is no local government tax. As an incentive for establishing Diodes-Shanghai, the 2005 and 2006 earnings of Diodes-Shanghai were exempted from central government income tax, and for the years 2007 through 2009 its earnings will be subject to tax rates in the range of 7.5% to 10.0%.

The recent China government income tax reform terminates some existing tax incentives for foreign enterprises doing business in China. The central government tax rate in China will increase to 25.0% beginning in 2008; however we believe Diodes-China may qualify for a “high-technology” preferential tax treatment that could reduce the tax rate to 15.0%. It is unclear to what extent our China subsidiaries will continue to receive preferential tax treatment.

We file income tax returns in the U.S. Federal jurisdiction and various state and foreign jurisdictions. We are no longer subject to U.S. Federal income tax examinations by tax authorities for tax years before 2004. With respect to

state and local jurisdictions and countries outside of the U.S., with limited exceptions, we are no longer subject to income tax audits for years before 2001. Although the outcome of tax audits is always uncertain, we believe that adequate amounts of tax, interest and penalties, if any, have been provided for in our FIN48 reserve for any adjustments that may result from future tax audits. We recognize accrued interest and penalties, if any, related to unrecognized tax benefits in income tax expense.

We adopted the provisions of FASB interpretation (FIN) No. 48, "Accounting for Uncertainty in Income Taxes" (FIN48) effective January 1, 2007. As a result of the implementation of FIN48, we increased our liability for unrecognized tax benefits, primarily related to our foreign subsidiaries, by approximately \$2.0 million during the first quarter of 2007, which was accounted for as a reduction to the January 1, 2007 balance of retained earnings. Accordingly, as of January 1, 2007 and December 31, 2007, approximately \$3.2 million and \$4.1 million, respectively, of unrecognized tax benefits, if recognized, would affect the effective tax rate.

It is reasonably possible that the amount of the unrecognized benefit with respect to certain of our unrecognized tax positions will significantly increase or decrease within the next 12 months. These changes may be the result of settlement of ongoing audits or competent authority proceedings. At this time, an estimate of the range of the reasonably possible outcomes cannot be made.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

The preparation of financial statements in accordance with Generally Accepted Accounting Principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an on-going basis, we evaluate our estimates, including those related to revenue recognition, allowance for doubtful accounts, inventory reserves and income taxes, among others. Our estimates are based upon historical experiences, market trends and financial forecasts and projections, and upon various other assumptions that management believes to be reasonable under the circumstances and at that certain point in time. Actual results may differ, significantly at times, from these estimates under different assumptions or conditions.

We believe the following critical accounting policies and estimates affect the significant estimates and judgments we use in the preparation of our consolidated financial statements, and may involve a higher degree of judgment and complexity than others.

### **Revenue recognition**

We recognize revenue when there is persuasive evidence that an arrangement exists, when delivery has occurred, when our price to the buyer is fixed or determinable and when collectibility of the receivable is reasonably assured. These elements are met when title to the products is passed to the buyers, which is generally when our product is shipped to our customers.

We reduce revenue in the period of sale for estimates of product returns, distributor price adjustments and other allowances, the majority of which are related to our U.S. operations. Our reserve estimates are based upon historical data as well as projections of revenues, distributor inventories, price adjustments, average selling prices and market conditions. Actual returns and adjustments could be significantly different from our estimates and provisions, resulting in an adjustment to revenues.

### **Inventories**

Inventories are stated at the lower of cost or market value. Cost is determined principally by the first-in, first-out method. On an on-going basis, we evaluate our inventory, both finished goods and raw material, for obsolescence and slow-moving items. This evaluation includes analysis of sales levels, sales projections, and purchases by item, as well as raw material usage related to our manufacturing facilities. If our review indicates a reduction in utility below carrying value, we reduce our inventory to a new cost basis. If future demand or market conditions are different than our current estimates, an inventory adjustment may be required, and would be reflected in cost of goods sold in the period the revision is made.

### **Accounting for income taxes**

As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes in each of the tax jurisdictions in which we operate. This process involves using an asset and liability approach whereby deferred tax assets and liabilities are recorded for differences in the financial reporting bases and tax bases of our assets and liabilities. Significant management judgment is required in determining our provision for income taxes,

deferred tax assets and liabilities. In assessing the realizability of the deferred tax assets, the Company considered whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the existence of, or generation of, taxable income during the periods in which those temporary differences become deductible. Based upon the available evidence, the Company does not believe it is more likely than not that all of the deferred tax assets will be realized. Accordingly, the Company established a valuation allowance of approximately \$5 million in 2007 to offset foreign tax credits that are considered more likely than not to expire before the Company is able to utilize the tax benefit. The Company considered the scheduled reversal of deferred tax liabilities and projected future taxable income in making this assessment. To the extent that the Company is unable to generate adequate taxable income, the Company may be required to increase the valuation allowance.

### **Allowance for doubtful accounts**

Management evaluates the collectability of our accounts receivable based upon a combination of factors, including the current business environment and historical experience. If we are aware of a customer's inability to meet its financial obligations to us, we record an allowance to reduce the receivable to the amount we reasonably believe we will be able to collect from the customer. For all other customers, we record an allowance based upon the amount of time the receivables are past due. If actual accounts receivable collections differ from these estimates, an adjustment to the allowance may be necessary with a resulting effect on operating expense.

### **Impairment of goodwill and long-lived assets**

As of December 31, 2007, goodwill was \$25.1 million. We account for goodwill in accordance with SFAS No. 142 ("Goodwill and Other Intangible Assets"), for which goodwill is tested for impairment at least annually. Our impairment review process is based upon (i) an income approach from a discounted cash flow analysis, which uses our estimates of revenues, costs and expenses, as well as market growth rates, and (ii) a market multiples approach which measures the value of an asset through an analysis of recent sales or offerings or comparable public entities. If ever the carrying value of the goodwill is determined to be less than the fair value of the reporting unit net assets, a write-down of the goodwill will be required, with the resulting expense charged in the period that the impairment is determined. No impairment of goodwill has been identified.

We assess the impairment of long-lived assets on an on-going basis and whenever events or changes in circumstances indicate that the carrying value may not be recoverable. We evaluate long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." We assess the recoverability of our long-lived and intangible assets by determining whether the unamortized balances can be recovered through undiscounted future net cash flows of the related assets. If such asset is considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the asset exceeds its fair market value using a discounted cash flow analysis.

### **Share-Based Compensation**

Prior to January 1, 2006, we accounted for the share-based payments under the recognition and measurement provisions of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* ("APB No. 25"), and related Interpretations, as permitted by Financial Accounting Standards Board Statement ("SFAS") No. 123, *Accounting for Stock-Based Compensation* ("SFAS No. 123"). No stock-based compensation expense related to employee stock option awards was recognized in the consolidated statement of operations for the year ended December 31, 2005 as all options granted under our stock option plans had an exercise price equal to the market value of the underlying common stock on the date of grant.

We adopted SFAS No. 123R, ("Share-Based Payments"), using the modified prospective method. No modifications were made to any outstanding share-options prior to the adoption of SFAS 123R. The adoption of SFAS 123R requires us to value stock options prior to our adoption of SFAS 123 under the fair value method and expense these amounts over the stock options' remaining vesting period. This resulted in an expense of \$6.5 million and \$5.6 million in the years ended December 31, 2006 and 2007, respectively, which was recorded within cost of goods sold, general and administrative expense, and research and development expense in our condensed consolidated income statement. In addition, SFAS 123R requires us to reflect any tax savings resulting from tax deductions in excess of expense reflected in our financial statements as a financing cash inflow in its statement of cash flows rather than as an operating cash flow as in prior periods. We have changed our primary award type from stock options to stock awards as an improved method of reward and retention. In general, for new grants, we also extended the vesting period from three years to four years, and reduced the number of shares subject to the award.

The amount of compensation expense recognized using the fair value method requires us to exercise judgment and make assumptions relating to the factors that determine the fair value of our stock option grants. We use the Black-Scholes-Merton model to estimate the fair value of our option grants. The fair value calculated by this model is a function of several factors, including grant price, the risk-free interest rate, the estimated term of the option and the estimated future volatility of the option. The estimated term and estimated future volatility of the options require our judgment. We have provided pro forma disclosures in the notes to the consolidated financial statements of our net income and net income per share for the year ended December 31, 2005 as if we used the fair value method under FAS 123.



We have approximately 1.0 million restricted stock grants outstanding as of December 31, 2007. Compensation expense is recognized for restricted stock grants over the requisite service period based on the grant date fair value of the award. As of December 31, 2007, there was \$12.9 million of total unrecognized compensation cost related to non-vested restricted stock awards. This cost is expected to be recognized over a weighted-average period of 2.8 years. In addition to the expense, the effects of the restricted stock grants are included in the diluted shares outstanding calculation (see “Note 15 - Share-based Compensation”).

## Results of Operations

The following table sets forth, for the periods indicated, the percentage that certain items in the statement of income bear to net sales and the percentage dollar increase (decrease) of such items from period to period.

|                                           | Percent of Net sales<br>Year Ended December 31, |        |        |        |        | Percentage Dollar Increase (Decrease)<br>Year Ended Decemeber 31, |           |           |           |
|-------------------------------------------|-------------------------------------------------|--------|--------|--------|--------|-------------------------------------------------------------------|-----------|-----------|-----------|
|                                           | 2003                                            | 2004   | 2005   | 2006   | 2007   | 03 to '04                                                         | 04 to '05 | 05 to '06 | 06 to '07 |
| Net sales                                 | 100%                                            | 100%   | 100%   | 100%   | 100%   | 35.6%                                                             | 15.6%     | 59.9%     | 16.9%     |
| Cost of goods sold                        | (73.3)                                          | (67.3) | (65.4) | (66.8) | (67.5) | 24.5                                                              | 12.3      | 63.4      | 18.0      |
| Gross profit                              | 26.7                                            | 32.7   | 34.6   | 33.2   | 32.5   | 66.3                                                              | 22.5      | 53.1      | 14.5      |
| Operating expenses                        | (16.6)                                          | (14.5) | (15.8) | (16.4) | (17.4) | 18.8                                                              | 25.8      | 66.4      | 24.0      |
| Income (loss) from operations             | 10.1                                            | 18.2   | 18.8   | 16.8   | 15.1   | 143.9                                                             | 19.8      | 42.0      | 5.1       |
| Interest income (expense)                 | (0.6)                                           | (0.3)  | 0.1    | 1.4    | 2.8    | (25.9)                                                            | (134.7)   | 2096.8    | 132.5     |
| Other income (expense)                    | (0.0)                                           | (0.2)  | 0.2    | (0.4)  | (0.1)  | (8260.0)                                                          | 197.1     | 398.5     | 81.4      |
| Income before taxes and minority interest | 9.5                                             | 17.6   | 19.1   | 17.8   | 17.8   | 152.0                                                             | 25.6      | 48.7      | 16.9      |
| Income tax benefit (provision)            | (1.8)                                           | (3.5)  | (3.1)  | (3.4)  | (2.4)  | 164.8                                                             | 2.6       | 74.9      | (19.3)    |
| Minority interest                         | (0.3)                                           | (0.4)  | (0.5)  | (0.4)  | (0.6)  | 54.9                                                              | 61.8      | 17.8      | 84.3      |
| Net income                                | 7.4                                             | 13.8   | 15.5   | 14.0   | 14.9   | 153.1                                                             | 30.4      | 44.4      | 23.9      |

The following discussion explains in greater detail the consolidated financial condition of the Company. This discussion should be read in conjunction with the consolidated financial statements and notes thereto appearing elsewhere herein. All per share amounts have been adjusted to reflect the three-for-two stock splits in November 2003, December 2005, and July 2007.

### Year 2007 Compared to Year 2006

|                  | 2006       | 2007       |
|------------------|------------|------------|
| <u>Net sales</u> | \$ 343,308 | \$ 401,159 |

Net sales for 2007 increased \$57.9 million to \$401.2 million from \$343.3 million for 2006. The 16.9% increase was due primarily to a 25.4% increase in units sold, offset by a 6.8% decrease in average selling prices (ASP). The decrease in ASP was due to the price pressure on our product lines. The following table sets forth the geographic breakdown of our net sales for the periods indicated based on the country to which the product is shipped:

|               | Net sales for the year<br>ended December 31 |            | Percentage of<br>net sales |        |
|---------------|---------------------------------------------|------------|----------------------------|--------|
|               | 2006                                        | 2007       | 2006                       | 2007   |
| China         | \$ 118,303                                  | \$ 156,183 | 34.5%                      | 38.9%  |
| Taiwan        | 96,401                                      | \$ 102,562 | 28.1%                      | 25.6%  |
| United States | 76,357                                      | \$ 81,408  | 22.2%                      | 20.3%  |
| All Others    | 52,247                                      | \$ 61,006  | 15.2%                      | 15.2%  |
| Total         | \$ 343,308                                  | \$ 401,159 | 100.0%                     | 100.0% |

|                                              | <b>2006</b> | <b>2007</b>       |
|----------------------------------------------|-------------|-------------------|
| <b><u>Cost of goods sold</u></b>             | \$ 229,416  | <b>\$ 270,780</b> |
| <b><u>Gross profit</u></b>                   | \$ 113,892  | <b>\$ 130,379</b> |
| <b><u>Gross profit margin percentage</u></b> | 33.2%       | <b>32.5%</b>      |

Cost of goods sold increased \$41.4 million, or 18.0%, for 2007 compared to \$229.4 million in 2006. As a percent of sales, cost of goods sold increased from 66.8% for 2006 to 67.5% for 2007. Our average unit cost (AUP) for discrete devices decreased approximately 2.4% from 2006, AUPs for analog products decreased approximately 12.8%, and AUPs for wafer products decreased approximately 1.6%. As per SFAS 123R, included in cost of goods sold for 2006 and 2007 were \$0.5 million and \$0.3 million, respectively, of non-cash, stock option compensation expenses related to our manufacturing facilities.

Gross profit for 2007 increased 14.5% to \$130.4 million from \$113.9 million for 2006. Gross margin as a percentage of net sales was 32.5% for 2007, compared to 33.2% for 2006. The decreased gross margin was primarily due to product mix changes.

|                                                                         | <b>2006</b> | <b>2007</b>     |
|-------------------------------------------------------------------------|-------------|-----------------|
| <b><u>Selling, general and administrative expenses (“SG&amp;A”)</u></b> | \$ 47,945   | <b>\$55,461</b> |

Selling, general and administrative expenses for 2007 increased approximately \$7.5 million, or 15.7%, to \$55.5 million, compared to \$47.9 million in 2006, due primarily to (i) an approximately \$1.6 million increase associated with non-cash, share-based compensation expense related to options and share grants, (ii) \$4.2 million higher sales commissions, wages and marketing expenses associated with the increased marketing and operating activities, and (iii) \$0.8 million increase in audit expenses associated with Sarbanes-Oxley Act compliance. SG&A, as a percentage of net sales, was 13.8% in 2007, compared to 14.0% in 2006.

|                                                             | <b>2006</b> | <b>2007</b>     |
|-------------------------------------------------------------|-------------|-----------------|
| <b><u>Research and development expenses (“R&amp;D”)</u></b> | \$ 8,317    | <b>\$13,515</b> |

Research and development expenses for 2007 increased \$5.2 million to \$13.5 million, or 3.4% of net sales, from \$8.3 million, or 2.4% of net sales, in 2006. R&D expenses are primarily related to new product development at the silicon wafer level and at the packaging level. We continue to seek to hire qualified engineers who fit our focus on next-generation processes and packaging technologies. Our current goal is to maintain R&D at 3 to 4% of revenue as we continue to bring proprietary technology and advanced devices to the market.

|                                                                       | <b>2006</b> | <b>2007</b>     |
|-----------------------------------------------------------------------|-------------|-----------------|
| <b><u>Restructuring costs and impairment of long-lived assets</u></b> | \$ 152      | <b>\$ 1,003</b> |

In the year ended December 31, 2007, we recorded approximately \$1.1 million in restructuring costs related to the consolidation of our analog wafer probe and final test operations from Hsinchu, Taiwan to our manufacturing facilities in Shanghai, China. The expense primarily consisted of approximately \$0.8 million in termination and severance costs and approximately \$0.3 million in impairment of fixed assets and others.



|                               | <b>2006</b> | <b>2007</b>      |
|-------------------------------|-------------|------------------|
| <b><u>Interest income</u></b> | \$ 6,699    | <b>\$ 18,117</b> |

Interest income for 2007 was \$18.1 million, compared to \$6.7 million in 2006, due primarily to interest income earned on short-term investment securities purchased with the proceeds from the \$230 million convertible bonds.

|                                | <b>2006</b> | <b>2007</b>     |
|--------------------------------|-------------|-----------------|
| <b><u>Interest expense</u></b> | \$ 1,844    | <b>\$ 6,831</b> |

Interest expense for 2007 was \$6.8 million, compared to \$1.8 million in the same period 2006, due primarily to \$4.1 million increase in interest expense related to the 2.25% convertible bonds (\$5.2 million in 2007, compared to \$1.1 million in 2006), and to a lesser extent, \$1.1 million increase in amortization related convertible bonds issuance costs relating to the full year 2007 amortization expense.

|                          | <b>2006</b> | <b>2007</b>   |
|--------------------------|-------------|---------------|
| <b><u>Other loss</u></b> | \$ 1,212    | <b>\$ 225</b> |

Other loss for 2007 was \$0.2 million, compared to \$1.2 million in 2006. The \$1.0 million decrease in other loss was due primarily to \$1.1 million one time adjustment for currency exchange losses in the third quarter of 2006 and \$0.1 million decrease in currency exchange loss in 2007.

|                                    | <b>2006</b> | <b>2007</b>     |
|------------------------------------|-------------|-----------------|
| <b><u>Income tax provision</u></b> | \$ 11,689   | <b>\$ 9,428</b> |

We recognized income tax expense of \$9.4 million for 2007, resulting in an effective tax rate of 13.2%, as compared to 19.1% in 2006. Our lower effective tax rate compared with the same period last year was the result of lower income in the U.S and higher income in low-taxed foreign jurisdictions, as well as a decrease in the amount of estimated repatriation of earnings of our foreign subsidiaries, partially offset by the increased income tax rate at one of our China subsidiaries (Diodes-Shanghai is subject to a range of 7.5% to 10% preferential tax rate from 2007 through 2009, compared to a 0% tax rate in 2006). For 2008, we anticipate our full-year effective tax rate to be in the mid-teen range as we continue to take advantage of available strategies to optimize our tax rate across the jurisdictions in which we operate.

|                                 | <b>2006</b> | <b>2007</b>     |
|---------------------------------|-------------|-----------------|
| <b><u>Minority interest</u></b> | \$ 1,289    | <b>\$ 2,376</b> |

Minority interest in joint venture earnings primarily represented the minority investor's share of the earnings of our China and Tawian subsidiaries for the period. The joint venture investments were eliminated in the consolidations of our financial statements, and the activities of Diodes-China, Diodes-Shanghai and Diodes-Anachip were included therein. As of December 31, 2006 and 2007, we had 95% controlling interests in Diodes-China and Diodes-Shanghai, and a 99.81% controlling interest in Diodes-Anachip.

|                          | <b>2006</b> | <b>2007</b>      |
|--------------------------|-------------|------------------|
| <b><u>Net income</u></b> | \$ 48,143   | <b>\$ 59,657</b> |

Net income increased 23.9% to \$59.7 million (or \$1.51 basic earnings per share and \$1.41 diluted earnings per share) for the twelve months ended December 31, 2007, compared to \$48.1 million (or \$1.25 basic earnings per share and \$1.16 diluted earnings per share) for the same period in 2006, due primarily to increased revenue, higher net interest income from short-term investments and a lower effective tax rate.



*Year 2006 Compared to Year 2005*

|                         |             |             |
|-------------------------|-------------|-------------|
|                         | <b>2005</b> | <b>2006</b> |
| <b><u>Net sales</u></b> | \$ 214,765  | \$ 343,308  |

Net sales for 2006 increased \$128.5 million to \$343.3 million from \$214.8 million for 2005. The 59.9% increase was due primarily to a 42.6% increase in units sold combined with a 12.1% increase in average selling prices (ASP). The increase in ASP was due to the product lines related to the Anachip and APD acquisitions. The following table sets forth the geographic breakdown of our net sales for the periods indicated based on the country to which the product is shipped:

|               | Net sales for the year<br>ended December 31 |                   | Percentage of<br>net sales |               |
|---------------|---------------------------------------------|-------------------|----------------------------|---------------|
|               | 2005                                        | 2006              | 2005                       | 2006          |
| China         | \$ 68,050                                   | \$ 118,303        | 31.7%                      | 34.5%         |
| Taiwan        | 59,838                                      | 96,401            | 27.9%                      | 28.1%         |
| United States | 54,981                                      | 76,357            | 25.6%                      | 22.2%         |
| All Others    | 31,896                                      | 52,247            | 14.8%                      | 15.2%         |
| <b>Total</b>  | <b>\$ 214,765</b>                           | <b>\$ 343,308</b> | <b>100.0%</b>              | <b>100.0%</b> |

|                                                  |             |             |
|--------------------------------------------------|-------------|-------------|
|                                                  | <b>2005</b> | <b>2006</b> |
| <b><u>Cost of goods sold</u></b>                 | \$ 140,388  | \$ 229,416  |
| <b><u>Gross profit</u></b>                       | \$ 74,377   | \$ 113,892  |
| <b><u>Gross profit margin<br/>percentage</u></b> | 34.6%       | 33.2%       |

Cost of goods sold increased \$89.0 million, or 63.4%, for 2006 compared to \$140.4 million in 2005. As a percent of sales, cost of goods sold increased from 65.4% for 2005 to 66.8% for 2006. Our average unit cost (AUP) for discrete devices decreased approximately 4.4% from 2005, and AUPs for wafer products increased approximately 6.0%. As per SFAS 123R, included in cost of goods sold for 2006 was \$0.5 million of non-cash, stock option compensation expense related to our manufacturing facilities.

Gross profit for 2006 increased 53.1% to \$113.9 million from \$74.4 million for 2005. Gross margin as a percentage of net sales was at 33.2% for the year of 2006, down from 34.6% for the year of 2005. The decreased gross margin was primarily due to the lower margin product line related to the Anachip acquisition.

|                                                                                 |             |             |
|---------------------------------------------------------------------------------|-------------|-------------|
|                                                                                 | <b>2005</b> | <b>2006</b> |
| <b><u>Selling, general and<br/>administrative expenses<br/>("SG&amp;A")</u></b> | \$ 30,285   | \$ 47,945   |

Selling, general and administrative expenses for 2006 increased approximately \$17.7 million, or 58.3%, compared to \$30.3 million in 2005, due primarily to (i) an approximately \$5.4 million increase associated with non-cash, share-based compensation expense due to our adoption of SFAS 123R, (ii) higher sales commissions, wages and marketing expenses associated with the acquisition of Anachip, and (iii) audit and legal expenses associated with Sarbanes-Oxley Act compliance. SG&A, as a percentage of net sales, was 14.0% in 2006, compared to 14.1% in 2005. Included in SG&A for the year ended December 31, 2006 was an approximate \$0.6 million one-time adjustment due to an overstatement of restricted share grant expense recorded in 2005. For comparable purposes, excluding the \$5.4 million of share-based compensation related to options, SG&A for the year ended December 31, 2006 would



have improved to 12.4% of total sales.

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|                                                             | <b>2005</b>     | <b>2006</b>    |
|-------------------------------------------------------------|-----------------|----------------|
| <b><u>Research and development expenses (“R&amp;D”)</u></b> | <b>\$ 3,713</b> | <b>\$8,317</b> |

Research and development expenses in 2006 increased \$4.6 million to \$8.3 million, or 2.4% of net sales from \$3.7 million, or 1.7% of net sales, in 2005. R&D expenses are primarily related to new product development at the silicon wafer level, and, to a lesser extent, at the packaging level. We continue to seek to hire qualified engineers who fit our focus on next-generation processes and packaging technologies.

|                                | <b>2005</b>   | <b>2006</b>     |
|--------------------------------|---------------|-----------------|
| <b><u>Interest income</u></b>  | <b>\$ 819</b> | <b>\$ 6,699</b> |
| <b><u>Interest expense</u></b> | <b>\$ 598</b> | <b>\$ 1,844</b> |

Net interest income for 2006 was \$4.9 million compared to net interest income of \$0.2 million in 2005, due primarily to interest income earned on proceeds from the offering of convertible notes, as well as to a reduction in our bank loans from \$10.7 million at December 31, 2005 to \$8.5 million at December 31, 2006. Our interest income is generated from interest earned on our \$48.9 million cash balances and \$291.0 million short-term investments. Our interest expense is primarily the \$1.1 million interest payable for \$230 million convertible notes.

|                                   | <b>2005</b>     | <b>2006</b>     |
|-----------------------------------|-----------------|-----------------|
| <b><u>Other (income) loss</u></b> | <b>\$ (406)</b> | <b>\$ 1,212</b> |

Other loss for the year ended December 31, 2006 was \$1.2 million, compared to other income \$0.4 million for the same period of 2005. Included in other expense for the year ended December 31, 2006, was an approximate \$1.1 million one-time, non-cash, prior periods adjustment due to the understatement of intercompany currency exchange losses at our Taiwan subsidiary.

|                                    | <b>2005</b>     | <b>2006</b>      |
|------------------------------------|-----------------|------------------|
| <b><u>Income tax provision</u></b> | <b>\$ 6,685</b> | <b>\$ 11,689</b> |

We recognized income tax expense of \$11.7 million for 2006, resulting in an effective tax rate of 19.1%, as compared to \$6.7 million or 16.3% for the same period in 2005, due primarily to higher income in the U.S. at higher tax rates and accrued dividend related taxes for our foreign subsidiaries.

|                                 | <b>2005</b>     | <b>2006</b>     |
|---------------------------------|-----------------|-----------------|
| <b><u>Minority interest</u></b> | <b>\$ 1,094</b> | <b>\$ 1,289</b> |

Minority interest in joint venture earnings primarily represented the minority investor's share of the earnings of our China subsidiaries for the period. The joint venture investments were eliminated in the consolidations of our financial statements, and the activities of Diodes-China, Diodes-Shanghai and Diodes-Anachip were included therein. As of December 31, 2005 and 2006, we had 95% controlling interests in Diodes-China and Diodes-Shanghai, and a 99.81% controlling interest in Diodes-Anachip.

|                          | <b>2005</b>      | <b>2006</b>      |
|--------------------------|------------------|------------------|
| <b><u>Net income</u></b> | <b>\$ 33,329</b> | <b>\$ 48,143</b> |

Net income increased 44.4% to \$48.1 million (or \$1.25 basic earnings per share and \$1.16 diluted earnings per share) for the twelve months ended December 31, 2006, compared to \$33.3 million (or \$0.96 basic earnings per share and \$0.86 diluted earnings per share) for the same period in 2005, primarily as a result of an increase in net sales. For comparison purposes, excluding \$5.3 million net of tax stock option expenses, pro forma net income was \$53.4

million (or \$1.39 basic earnings per share and \$1.26 diluted earnings per share) for the twelve months ended December 31, 2006, as compared to \$33.3 million (or \$0.96 basic earnings per share and \$0.86 diluted earnings per share) for the same period in 2005.

## **Financial Condition**

### ***Liquidity and Capital Resources***

Our primary sources of liquidity are cash, funds from operations and borrowings under our credit facilities. Our primary liquidity requirements have been to meet our inventory and capital expenditure needs. For 2005, 2006 and 2007, our working capital was \$146.7 million, \$395.4 million, and \$451.8 million, respectively. We anticipate our working capital position will be sufficient for at least the next 12 months.

During 2005, we sold 4.8 million (split adjusted) shares of our Common Stock in a follow-on public offering, raising approximately \$72 million (net of commissions and expenses). We used approximately \$31 million of the net proceeds in connection with the Anachip acquisition, and we intend to use the remaining net proceeds from this offering for working capital and other general corporate purposes, including additional acquisitions.

On October 12, 2006, we issued and sold convertible senior notes with an aggregate principal amount of \$230 million due 2026 ("Notes"), which pay 2.25% interest per annum on the principal amount of the Notes, payable semi-annually in arrears on April 1 and October 1 of each year, beginning on April 1, 2007. We intend to use the net proceeds for working capital and general corporate purposes, which may include the acquisition of businesses, products, product rights or technologies, strategic investments, or purchases of our own Common Stock.

In connection with the issuance of the Notes, we incurred approximately \$6.2 million of issuance costs, which primarily consisted of investment banker fees, legal and accounting fees. These costs are classified within Other Assets and are being amortized as a component of interest expense using the straight-line method over the life of the Notes from issuance through October 12, 2011.

On July 10, 2007, we declared a three-for-two stock split in the form of a 50% stock dividend payable on July 30, 2007 to stockholders of record on July 20, 2007. Under the terms of this stock dividend, our stockholders received one additional share for every two shares held on the record date. The dividend was paid in authorized but unissued shares of Common Stock. Fractional shares created by the stock dividend were paid in cash based upon the closing price of our Common Stock on the record date. The par value of our stock is not affected by the dividend and remains at \$0.66 2/3 per share. The outstanding shares stated on the statement of stockholders' equity, the balance sheet and the consolidated condensed statement of income and disclosures have been adjusted to reflect the effects of the stock split.

In 2005, 2006 and 2007, our capital expenditures were \$24.7 million, \$45.1 million and \$54.2 million, respectively. Our capital expenditures for these periods were primarily related to manufacturing expansion in our facilities in China and, to a lesser extent, our wafer fabrication facility in the U.S., and an office building in Taiwan. The capital expenditures for 2007 were approximately 13.5% of revenue.

As of December 31, 2007, we had \$320.7 million invested primarily in auction rate securities, which are classified as current, available-for-sale investments. Although the maturities of the securities are over 10 years, management expects to convert these securities into cash within one year and does not anticipate holding the investments until maturity; therefore, the securities are classified as short-term and included in short-term investments on our consolidated balance sheets. The carrying values of available-for-sale securities approximates fair value. These investments are primarily in municipal and student loan association bonds that are fully collateralized by AAA rated bonds and/or insured against loss of principal and interest by AAA rated bond insurers. None of these investments are collateralized mortgage obligations or are any other type of mortgage- or real estate-backed security.

Auction rate securities are generally long-term debt instruments that provide liquidity through a Dutch auction process that resets the applicable interest rate at pre-determined calendar intervals. These mechanisms generally allow existing

investors to rollover their holdings and continue to own their respective securities or liquidate their holdings by selling their securities at par value.

We generally invest in these securities for short periods of time as part of our cash management program. However, the recent uncertainties in the credit markets have prevented us and other investors from liquidating holdings of auction rate securities in recent auctions occurring subsequent to December 31, 2007, because the amount of securities submitted for sale has exceeded the amount of purchase orders, resulting in our continuing to hold these securities and the issuers paying interest at the maximum contractual rates which are higher than similar securities for which auctions have cleared. Based on current market conditions, it is likely that auctions related to more of these securities will be unsuccessful in the near term. Unsuccessful auctions could result in our holding securities beyond their next scheduled auction reset dates if a secondary market does not develop, thereby limiting the short-term liquidity of these investments.

*Discussion of cash flows*

Cash and short-term investments have increased from \$113.6 million at December 31, 2005, to \$339.9 million at December 31, 2006, to \$379.7 million at December 31, 2007. The increase from 2005 to 2006 was primarily due to the proceeds from the \$230 million convertible bond offering. During 2007, we increased short-term investments to \$323.5 million from \$291.0 million in 2006 from the proceeds of the convertible bond offering (see Note 3).

*Operating activities*

(Amounts in thousands)

| <b>Years ended December 31,</b>                                                   | <b>2005</b> | <b>2006</b> | <b>2007</b> |
|-----------------------------------------------------------------------------------|-------------|-------------|-------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                                       |             |             |             |
| Net income                                                                        | \$ 33,329   | \$ 48,143   | \$ 59,657   |
| Adjustments to reconcile net income to net cash provided by operating activities: |             |             |             |
| Depreciation and amortization                                                     | 16,228      | 20,443      | 26,245      |
| Minority interest earnings                                                        | 1,094       | 1,289       | 2,377       |
| Share-based compensation                                                          | 1,814       | 8,272       | 9,864       |
| Amortization of acquired intangibles                                              | -           | 360         | 836         |
| Amortization of convertible bond issuance costs                                   | -           | 262         | 1,252       |
| Loss (gain) on disposal of property, plant and equipment                          | (102)       | 152         | (16)        |
| Adjustment of other comprehensive income                                          | -           | 1,071       | -           |
| Changes in operating assets:                                                      |             |             |             |
| Accounts receivable                                                               | (11,037)    | (11,320)    | (11,874)    |
| Inventories                                                                       | (2,373)     | (16,283)    | (4,662)     |
| Prepaid expenses and other current assets                                         | 696         | (2,792)     | (3,667)     |
| Deferred income taxes                                                             | (3,482)     | 929         | 1,664       |
| Changes in operating liabilities:                                                 |             |             |             |
| Accounts payable                                                                  | 5,330       | 14,534      | 2,996       |
| Accrued liabilities                                                               | 2,770       | 4,957       | 4,608       |
| Other liabilities                                                                 | -           | 101         | 3,192       |
| Income taxes payable                                                              | 3,390       | 1,963       | (1,701)     |
| Net cash provided by operating activities                                         | 47,657      | 72,081      | 90,771      |

Net cash provided by operating activities during 2007 was \$90.8 million, resulting primarily from \$59.7 million of net income in this period. Net cash provided by operating activities was \$72.1 million for 2006 and \$47.7 million for 2005.

Net cash provided by operations increased by \$18.7 million from 2006 to 2007. This increase resulted primarily from a \$11.5 million increase in our net income (from \$48.1 million in 2005 to \$59.7 million in 2006), \$1.6 million increase in non-cash, share-based compensation expense, and \$7.3 million increase in depreciation and amortization expense, partially offset by \$1.5 million changes in net working capital. We continue to closely monitor our credit terms with our customers, while at times providing extended terms, primarily required by our customers in Asia and Europe.

Net cash provided by operations increased by \$24.4 million from 2005 to 2006. This increase resulted primarily from a \$14.8 million increase in our net income (from \$33.3 million in 2005 to \$48.1 million in 2006), \$6.5 million increase in non-cash, share-based compensation expense, and \$4.8 million increase in depreciation and amortization expense, partially offset by increases in inventories, resulting from slower inventory turns, and increases in accounts receivable

and prepaid expenses and other assets. We continue to closely monitor our credit terms with our customers, while at times providing extended terms, primarily required by our customers in Asia and Europe.

**Investing activities**

(Amounts in thousands)

| <b>Years ended December 31,</b>                      | <b>2005</b> | <b>2006</b> | <b>2007</b> |
|------------------------------------------------------|-------------|-------------|-------------|
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>          |             |             |             |
| Purchases of property, plant and equipment           | (19,583)    | (45,656)    | (56,101)    |
| Purchases of short-term investments                  | (40,348)    | (250,660)   | (32,464)    |
| Acquisitions, net of cash acquired                   | (5,872)     | (29,433)    | -           |
| Proceeds from sales of property, plant and equipment | -           | 54          | 202         |
| Net cash used by investing activities                | (65,803)    | (325,695)   | (88,363)    |

Net cash used by investing activities for 2007 was \$88.4 million resulting from capital expenditures of \$56.1 million, and \$32.5 million increase in short-term investments of municipal bonds.

Net cash used by investing activities for 2006 was \$325.7 million resulting from capital expenditures of \$45.7 million, including the \$6 million office building purchase in Taiwan, \$250.7 million short-term investments of municipal bonds and \$29.4 million used for acquisitions including the final acquisition payment for Anachip of \$21.0 million (net of cash acquired) and the \$8.4 million APD acquisition payment.

**Financing activities**

(Amounts in thousands)

| <b>Years ended December 31,</b>                | <b>2005</b> | <b>2006</b> | <b>2007</b> |
|------------------------------------------------|-------------|-------------|-------------|
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>    |             |             |             |
| Repayments on line of credit                   | (3,167)     | (5,758)     | -           |
| Net proceeds from the issuance of common stock | 76,367      | 4,327       | 7,573       |
| Excess tax benefits                            | 2,898       | 6,655       | -           |
| Management incentive reimbursement from LSC    | 375         | -           | -           |
| Proceeds from long-term debt                   | 5,890       | 228,569     | -           |
| Repayments of long-term debt                   | (7,750)     | (4,666)     | (2,758)     |
| Minority shareholder investment in subsidiary  | -           | -           | -           |
| Repayments of capital lease obligations        | (136)       | (138)       | (141)       |
| Dividend to minority shareholder               | (750)       | -           | -           |
| Net cash provided by financing activities      | 73,727      | 228,989     | 4,674       |

Net cash provided by financing activities for 2007 was \$4.7 million, resulting primarily from \$7.6 million from stock option exercises in 2007 and repayments of long-term debt and offset by \$2.8 million in repayments of long-term debt.

Net cash provided by financing activities for 2006 was \$229.0 million, resulting primarily from \$224.0 million in net proceeds from the offering of convertible notes and \$4.8 million loan proceeds in Taiwan secured by land and building, offset by \$10.4 million debt repayment. In addition, we received \$4.3 million from stock option exercises in 2006 and \$6.7 million in excess tax benefits related to stock option exercise.

Net cash provided by financing activities for 2005 was \$73.7 million, resulting primarily from \$71.7 million in net proceeds from the offering of equity securities, offset by \$10.9 million in debt repayment. In addition, we received \$4.2 million from stock option exercises in 2005 and \$2.9 million in excess tax benefits related to stock option exercise.





### *Debt instruments*

On October 12, 2006, we issued and sold convertible senior Notes with an aggregate principal amount of \$230 million due 2026, which pay 2.25% interest per annum on the principal amount of the Notes, payable semi-annually in arrears on April 1 and October 1 of each year, beginning on April 1, 2007. Interest will accrue on the Notes from and including October 12, 2006 or from and including the last date in respect of which interest has been paid or provided for, as the case may be, to, but excluding, the next interest payment date or maturity date, as the case may be. Commencing with the six-month period beginning October 1, 2011, and for each six-month period thereafter, we will, on the interest payment date for such interest period, pay contingent interest to the holders of the Notes under certain circumstances and in amounts described in the indenture. For U.S. Federal income tax purposes, we will treat, and each holder of the Notes will agree under the indenture to treat, the Notes as contingent payment debt instruments governed by special tax rules and to be bound by our application of those rules to the Notes.

Under our U.S. credit arrangements with Union Bank of California, N.A. (Union Bank), we now have available a revolving credit commitment of up to \$20.0 million, including a \$5.0 million letter of credit sub-facility. In addition, one of our subsidiaries, Diodes-FabTech, has a term note in the principal amount of \$5.0 million.

The revolving credit commitment expires on August 29, 2008. The Diodes-FabTech term loan, which amortizes monthly, matures on August 29, 2010. As of December 31, 2007, we had no amounts outstanding under our revolving credit facility, and \$2.7 million was outstanding under the Diodes-FabTech term loan. Loans to us under our credit facility are guaranteed by Diodes-FabTech, and in turn, the Diodes-FabTech term loan is guaranteed by us. The purpose of the revolving credit facility is to provide cash for domestic working capital purposes, and to fund permitted acquisitions.

All loans under the credit facility and the Diodes-FabTech term loan are collateralized by all of our U.S. accounts, instruments, chattel paper, documents, general intangibles, inventory, equipment, furniture and fixtures, pursuant to security agreements entered into by us in connection with these credit arrangements.

Any amounts borrowed under the revolving credit facility and the Diodes-FabTech term loan bear interest at LIBOR plus 1.15%. At December 31, 2007, the effective rate under both the credit agreement and the Diodes-FabTech term loan was LIBOR plus 1.15%, or approximately 6.0%.

The credit agreement contains covenants that require us to maintain a leverage ratio not greater than 3.25 to 1.0, an interest expense coverage ratio of not less than 2.0 to 1 and a current ratio of not less than 1.0 to 1. It also requires us to achieve a net profit before taxes, as of the last day of each fiscal quarter, for the two consecutive fiscal quarters ending on that date of not less than \$1. The credit agreement permits us to pay dividends to our stockholders to the extent that any such dividends declared or paid in any fiscal year do not exceed an amount equal to 50% of our net profit after taxes for such fiscal year. However, it limits our ability to dispose of assets, incur additional indebtedness, engage in liquidation or merger, acquisition, partnership or other combination (except permitted acquisitions). The credit agreement also contains customary representations, warranties, affirmative and negative covenants and events of default. As of December 31, 2007, we were in compliance with the bank covenants.

The agreements governing the FabTech term loan do not contain any financial or negative covenants. However, they provide that a default under our credit agreement will cause a cross-default under the FabTech term loan.

As of December 31, 2005, FabTech had paid down \$3.75 million, to pay in full a note in favor of LSC, which debt was incurred in connection with our acquisition of FabTech from LSC in 2000. This note matured on June 30, 2006 and amortized monthly. The obligations under this note were subordinated to the obligations under our U.S. credit agreement with Union Bank.

As of December 31, 2007, our Asia subsidiaries have available lines of credit of up to an aggregate of \$38.1 million with a number of Chinese and Taiwanese financial institutions. These lines of credit, except for one Taiwanese credit facility, are collateralized by its premises, are unsecured, uncommitted and, in some instances, may be repayable on demand. Loans under these lines of credit bear interest at LIBOR or similar indices plus a specified margin.

As of December 31, 2007, Diodes-Taiwan owed \$4.5 million under a term loan agreement with a commercial bank in Taiwan, secured by land and building. At December 31, 2007, the effective rate was approximately 3.7%.

## Off-Balance Sheet Arrangements

We do not have any transactions, arrangements and other relationships with unconsolidated entities that will affect our liquidity or capital resources. We have no special purpose entities that provided off-balance sheet financing, liquidity or market or credit risk support, nor do we engage in leasing, hedging or research and development services, that could expose us to liability that is not reflected on the face of our financial statements.

## Contractual Obligations

The following table represents our contractual obligations as of December 31, 2007:

| Contractual Obligations  | Payments due by period (in thousands) |                 |                 |                 |                   |
|--------------------------|---------------------------------------|-----------------|-----------------|-----------------|-------------------|
|                          | Total                                 | Less than       | 1-3             | 3-5             | More than         |
|                          |                                       | 1 year          | years           | years           | 5 years           |
| Long-term debt           | \$ 237,160                            | \$ 1,345        | \$ 2,353        | \$ 732          | \$ 232,730        |
| Capital leases           | 1,477                                 | 145             | 290             | 290             | 752               |
| Operating leases         | 14,981                                | 4,512           | 5,186           | 3,791           | 1,492             |
| Purchase obligations     | 1,771                                 | 1,771           | 0               | 0               | 0                 |
| <b>Total obligations</b> | <b>\$ 255,389</b>                     | <b>\$ 7,773</b> | <b>\$ 7,829</b> | <b>\$ 4,813</b> | <b>\$ 234,974</b> |

The \$230 million convertible Notes, classified as long-term debt, are redeemable beginning in 2011 (see Note 8).

## Recently Issued Accounting Pronouncements and Proposed Accounting Changes

In December 2007, the Financial Accounting Standards Board (FASB) issued SFAS No. 141R, "Business Combinations," which changes how business acquisitions are accounted. SFAS No. 141R requires the acquiring entity in a business combination to recognize all (and only) the assets acquired and liabilities assumed in the transaction and establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed in a business combination. Among the more significant changes in the accounting for acquisitions are the following: i) Transaction costs will generally be expensed. Certain such costs are presently treated as costs of the acquisition; ii) In-process research and development ("IPR&D") will be accounted for as an asset, with the cost recognized as the research and development is realized or abandoned. IPR&D is presently expensed at the time of the acquisition; iii) Contingencies, including contingent consideration, will generally be recorded at fair value with subsequent adjustments recognized in operations. Contingent consideration is presently accounted for as an adjustment of purchase price; and iv) Decreases in valuation allowances on acquired deferred tax assets will be recognized in operations. Such changes previously were considered to be subsequent changes in consideration and were recorded as adjustments to goodwill. SFAS No. 141R is effective for business combinations and adjustments to an acquired entity's deferred tax asset and liability balances occurring after December 31, 2008. The Company is currently evaluating the future impacts and disclosures of this standard.

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51," which establishes new standards governing the accounting for and reporting of noncontrolling interests (NCIs) in partially owned consolidated subsidiaries and the loss of control of subsidiaries. Certain provisions of this standard indicate, among other things, that NCIs (previously referred to as minority interests) be treated as a separate component of equity, not as a liability; that increases and decrease in the parent's ownership interest, that leave control intact, be treated as equity transactions, rather than as step acquisitions or

dilution gains or losses; and that losses of a partially owned consolidated subsidiary be allocated to the NCI even when such allocation might result in a deficit balance. This standard also requires changes to certain presentation and disclosure requirements. SFAS No. 160 is effective beginning January 1, 2009. The provisions of the standard are to be applied to all NCIs prospectively, except for the presentation and disclosure requirements, which are to be applied retrospectively to all periods presented. After adoption, noncontrolling interests (\$4.8 million and \$7.2 million at December 31, 2006 and 2007, respectively) will be classified as shareowners' equity, a change from its current classification between liabilities and shareowners' equity. The Company is currently evaluating the future impacts and disclosures of this standard.

In December 2007, the FASB ratified the EITF consensus on EITF Issue No. 07-1, "Accounting for Collaborative Arrangements" that discusses how parties to a collaborative arrangement (which does not establish a legal entity within such arrangement) should account for various activities. The consensus indicates that costs incurred and revenues generated from transactions with third parties (i.e. parties outside of the collaborative arrangement) should be reported by the collaborators on the respective line items in their income statements pursuant to EITF Issue No. 99-19, "Reporting Revenue Gross as a Principal Versus Net as an Agent." Additionally, the consensus provides that income statement characterization of payments between the participants in a collaborative arrangement should be based upon existing authoritative pronouncements; analogy to such pronouncements if not within their scope; or a reasonable, rational, and consistently applied accounting policy election. EITF Issue No. 07-1 is effective for the Company beginning January 1, 2009 and is to be applied retrospectively to all periods presented for collaborative arrangements existing as of the date of adoption. The Company is currently evaluating the impacts and disclosures of this standard.

In June 2007, the FASB's EITF reached a consensus on EITF Issue No. 07-3, "Accounting for Nonrefundable Advance Payments for Goods or Services to Be Used in Future Research and Development Activities" that would require nonrefundable advance payments made by the Company for future R&D activities to be capitalized and recognized as an expense as the goods or services are received by the Company. EITF Issue No. 07-3 is effective for the Company with respect to new arrangements entered into beginning January 1, 2008. The Company is currently evaluating the impacts and disclosures of this standard.

In February 2007, FASB issued FAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities - Including an amendment of FASB Statement No. 115" ("FAS 159"). This Statement permits entities to choose to measure many financial instruments and certain other items at fair value and report unrealized gains and losses on these instruments in earnings. FAS 159 is effective as of January 1, 2008. At the effective date, an entity may elect the fair value option for eligible items that exist at that date. The entity shall report the effect of the first re-measurement to fair value as a cumulative-effect adjustment to the opening balance of retained earnings. The Company has not elected the fair value option for eligible items that existed as of January 1, 2008.

In September 2006, FASB issued SFAS 157, "Fair Value Measurements" ("FAS 157"). SFAS 157 clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. Under the standard, fair value measurements would be separately disclosed by level within the fair value hierarchy. FAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years, with early adoption permitted. We have not yet determined the effect, if any, that the implementation of FAS 157 will have on our results of operations or financial condition.

#### **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

**Foreign Currency Risk.** We face exposure to adverse movements in foreign currency exchange rates, primarily in Asia. Our foreign currency risk may change over time as the level of activity in foreign markets grows and could have an adverse impact upon our financial results. Certain of our assets, including certain bank accounts and accounts receivable, and liabilities exist in non-U.S. dollar denominated currencies, which are sensitive to foreign currency exchange fluctuations. These currencies are principally the Chinese Yuan and the Taiwanese dollar and, to a lesser extent, the Japanese Yen, the Euro and the Hong Kong dollar. Because of the relatively small size and nature of each individual currency exposure, we do not regularly employ hedging techniques designed to mitigate foreign currency exposures. If the Chinese Yuan and the Taiwanese dollar were to strengthen or weaken by 1.0% against the U.S. dollar, we would experience currency loss of approximately \$0.1 million and currency gain of approximately \$0.1 million, respectively. In the future, we may enter into hedging arrangements designed to mitigate foreign currency fluctuations.

The Chinese government has begun to permit the Chinese Yuan to float more freely compared to other world currencies. Should the Chinese government allow a significant Chinese Yuan appreciation, and we do not take appropriate means to offset this exposure, the effect could have an adverse impact upon our financial results.

**Interest Rate Risk.** We have credit facilities with U.S. and Asian financial institutions as well as other debt instruments with interest rates equal to LIBOR or similar indices plus a negotiated margin. A rise in interest rates could have an adverse impact upon our cost of working capital and our interest expense. As a matter of policy, we do not enter into derivative transactions for trading or speculative purposes. As of December 31, 2007, our outstanding debt under our interest-bearing credit agreements was \$237.2 million, including \$230 million convertible notes with a fixed interest rate of 2.25%. Based on an increase or decrease in interest rates by 1.0% for the year, our annual interest rate expense would increase or decrease by approximately \$0.1 million.

**Political Risk.** We have a significant portion of our assets in mainland China and Taiwan. The possibility of political conflict between the two countries or with the U.S. could have an adverse impact upon our ability to transact business through these important business segments and to generate profits. See “Risk Factors - Foreign Operations.”

**Liquidity Risk.** As of December 31, 2007, we had \$320.7 million invested primarily in auction rate securities, which are classified as current, available-for-sale investments. Although the maturities of the securities are over 10 years, management expects to convert these securities into cash within one year and does not anticipate holding the investments until maturity; therefore within one year and does not anticipate holding the investments until maturity; therefore, the securities are classified as short-term and included in short-term investments on our consolidated balance sheets. The carrying values of available-for-sale securities approximates fair value. These investments are primarily in municipal and student loan association bonds that are fully collateralized by AAA rated bonds and/or insured against loss of principal and interest by AAA rated bond insurers. None of these investments are collateralized mortgage obligations or are any other type of mortgage- or real estate-backed security.

Auction rate securities are generally long-term debt instruments that provide liquidity through a Dutch auction process that resets the applicable interest rate at pre-determined calendar intervals. These mechanisms generally allow existing investors to rollover their holdings and continue to own their respective securities or liquidate their holdings by selling their securities at par value.

We generally invest in these securities for short periods of time as part of our cash management program. However, the recent uncertainties in the credit markets have prevented us and other investors from liquidating holdings of auction rate securities in recent auctions occurring subsequent to December 31, 2007, because the amount of securities submitted for sale has exceeded the amount of purchase orders, resulting in our continuing to hold these securities and the issuers paying interest at the maximum contractual rates which are higher than similar securities for which auctions have cleared. Based on current market conditions, it is likely that auctions related to more of these securities will be unsuccessful in the near term. Unsuccessful auctions could result in our holding securities beyond their next scheduled auction reset dates if a secondary market does not develop, thereby limiting the short-term liquidity of these investments.

**Inflation Risk.** Inflation did not have a material effect on net sales or net income in fiscal years 2005 through 2007. A significant increase in inflation could affect future performance.

## **Item 8. Financial Statements and Supplementary Data**

See “Item 15. Exhibits and Financial Statement Schedules” for the Company’s Consolidated Financial Statements and the notes and schedules thereto filed as part of this Annual Report on Form 10-K.

## **Item 9. Changes In and Disagreements With Accountants on Accounting and Financial Disclosure**

Not Applicable.

## **Item 9A. Controls and Procedures**

### **Disclosure Controls and Procedures**

The Company's Chief Executive Officer, Dr. Keh-Shew Lu, and Chief Financial Officer, Carl C. Wertz, with the participation of the Company's management, carried out an evaluation of the effectiveness of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-15(e). Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer believe that, as of the end of the period covered by this report, the Company's disclosure controls and procedures are effective to provide reasonable assurance that material information



relating to the Company (including its consolidated subsidiaries) required to be included in this report is made known to them.

Disclosure controls and procedures, no matter how well designed and implemented, can provide only reasonable assurance of achieving an entity's disclosure objectives. The likelihood of achieving such objectives is affected by limitations inherent in disclosure controls and procedures. These include the fact that human judgment in decision-making can be faulty and that breakdowns in internal control can occur because of human failures such as simple errors, mistakes or intentional circumvention of the established processes.

## **Management's Annual Report on Internal Control Over Financial Reporting**

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed by, or under the supervision of, the Company's Chief Executive Officer and the Chief Financial Officer and implemented by the Company's Board of Directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles in the United States of America.

The Company's internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles in the United States of America, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision and with the participation from management, including our Chief Executive Officer and the Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework and criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). This evaluation included review of the documentation of controls, testing of operating effectiveness of controls and a conclusion on this evaluation. Based on this evaluation, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2007. Moss Adams LLP, an independent registered public accounting firm, has audited and reported on the consolidated financial statements of Diodes Incorporated and on the effectiveness of our internal controls over financial reporting. The reports of Moss Adams LLP are contained in this Annual Report.

## **Changes in Internal Control over Financial Reporting**

There was no change in our internal control over financial reporting, known to the Chief Executive Officer or the Chief Financial Officer, that occurred during the last fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## **Item 9B. Other Information**

None.

## **PART III**

## **Item 10. Directors, Executive Officers and Corporate Governance**

The information concerning the directors, executive officers and corporate governance of the Company is incorporated herein by reference from the section entitled "Proposal One - Election of Directors" contained in the

definitive proxy statement of the Company to be filed pursuant to Regulation 14A within 120 days after the Company's fiscal year end of December 31, 2007, for its annual stockholders' meeting for 2008 (the "Proxy Statement").

We have adopted a code of ethics that applies to our Chief Executive Officer and senior financial officers. The code of ethics has been posted on our website under the Corporate Governance portion of the Investor Relations section at [www.diodes.com](http://www.diodes.com). We intend to satisfy disclosure requirements regarding amendments to, or waivers from, any provisions of our code of ethics on our website.

**Item 11. Executive Compensation**

The information concerning executive compensation is incorporated herein by reference from the section entitled "Proposal One - Election of Directors" contained in the Proxy Statement.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

The information concerning the security ownership of certain beneficial owners and management and related stockholder matters is incorporated herein by reference from the section entitled “General Information - Security Ownership of Certain Beneficial Owners and Management” and “Proposal One - Election of Directors” contained in the Proxy Statement.

**Item 13. Certain Relationships, Related Transactions and Director Independence**

The information concerning certain relationships, related transactions and director independence is incorporated herein by reference from the section entitled “Proposal One - Election of Directors - Certain Relationships, Related Transactions and Director Independence” and “Proposal One - Elections of Directors” contained in the Proxy Statement.

**Item 14. Principal Accountant Fees and Services**

The information concerning the Company’s principal accountant’s fees and services is incorporated herein by reference from the section entitled “Ratification of the Appointment of Independent Registered Public Accounting Firm” in the Proxy Statement.

**PART IV****Item 15. Exhibits and Financial Statement Schedules****(a) Financial Statements and Schedules****(1) Financial statements:**

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**(2) Schedules:**

None

Schedules not listed above have been omitted because the information required to be set forth therein is not applicable or is shown in the financial statements and note thereto.

(b) **Exhibits**

The exhibits listed on the Index to Exhibits at page 89 are filed as exhibits or incorporated by reference to this Annual Report on Form 10-K.

(c) **Financial Statements of Unconsolidated Subsidiaries and Affiliates**

Not Applicable.

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Stockholders  
Diodes Incorporated and Subsidiaries

We have audited the accompanying consolidated balance sheets of Diodes Incorporated and Subsidiaries (the “Company”) as of December 31, 2006 and 2007 and the related consolidated statements of income, stockholders' equity and cash flows for each of the years in the three-year period ended December 31, 2007. We also have audited the Company's internal control over financial reporting as of December 31, 2007, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on these consolidated financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also include performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Diodes Incorporated and Subsidiaries as of December 31, 2006 and 2007, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2007, in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, Diodes Incorporated and Subsidiaries, maintained, in all material respects, effective internal control over financial

reporting as of December 31, 2007, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

As discussed in Notes 1 and 15 to the consolidated financial statements, effective January 1, 2006, the Company changed its method of accounting for share-based payment arrangements to conform to Statement of Financial Accounting Standards (FASB) No. 123(R), "Share-Based Payment". As discussed in Notes 1 and 13 to the consolidated financial statements, effective January 1, 2007, the Company adopted FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB No. 109."

/s/ Moss Adams LLP

Los Angeles, California  
February 28, 2008

**DIODES INCORPORATED AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**

(Amounts in thousands)

| <b>December 31,</b>                       | <b>2006</b>       | <b>2007</b>       |
|-------------------------------------------|-------------------|-------------------|
| <b>ASSETS</b>                             |                   |                   |
| <b>CURRENT ASSETS</b>                     |                   |                   |
| Cash and cash equivalents                 | \$ 48,888         | \$ 56,179         |
| Short-term investments                    | 291,008           | 323,472           |
| Total cash and short-term investments     | 339,896           | 379,651           |
| Accounts receivable                       |                   |                   |
| Trade customers                           | 72,175            | 84,638            |
| Related parties                           | 6,147             | 5,405             |
|                                           | 78,322            | 90,043            |
| Allowance for doubtful accounts           | (617)             | (465)             |
| Accounts receivable, net of allowances    | 77,705            | 89,578            |
| Inventories                               | 48,202            | 53,031            |
| Deferred income taxes, current            | 4,650             | 5,173             |
| Prepaid expenses and other                | 8,393             | 10,576            |
| <b>Total current assets</b>               | <b>478,846</b>    | <b>538,009</b>    |
| <b>PROPERTY, PLANT AND EQUIPMENT, net</b> | <b>95,469</b>     | <b>123,407</b>    |
| <b>DEFERRED INCOME TAXES, non-current</b> | <b>5,428</b>      | <b>3,241</b>      |
| <b>OTHER ASSETS</b>                       |                   |                   |
| Intangible assets, net                    | 10,669            | 9,643             |
| Goodwill                                  | 25,030            | 25,135            |
| Other                                     | 6,697             | 6,930             |
| <b>Total assets</b>                       | <b>\$ 622,139</b> | <b>\$ 706,365</b> |

*The accompanying notes are an integral part of these consolidated financial statements.*



**DIODES INCORPORATED AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS (Continued)**

(Amounts in thousands, except share data)

| December 31,                                                       | 2006              | 2007              |
|--------------------------------------------------------------------|-------------------|-------------------|
| <b>LIABILITIES AND STOCKHOLDERS'</b>                               |                   |                   |
| <b>EQUITY</b>                                                      |                   |                   |
| <b>CURRENT LIABILITIES</b>                                         |                   |                   |
| Line of credit                                                     | \$ -              | \$ -              |
| Accounts payable                                                   |                   |                   |
| Trade                                                              | 40,029            | 42,010            |
| Related parties                                                    | 12,120            | 13,135            |
| Accrued liabilities                                                | 24,967            | 27,841            |
| Income tax payable                                                 | 3,433             | 1,732             |
| Current portion of long-term debt                                  | 2,802             | 1,345             |
| Current portion of capital lease obligations                       | 141               | 145               |
| <b>Total current liabilities</b>                                   | <b>83,492</b>     | <b>86,208</b>     |
| <b>LONG-TERM DEBT, net of current portion</b>                      |                   |                   |
| 2.25% convertible senior notes due 2026                            | 230,000           | 230,000           |
| Others                                                             | 7,115             | 5,815             |
| <b>CAPITAL LEASE OBLIGATIONS, net of current portion</b>           | <b>1,477</b>      | <b>1,331</b>      |
| <b>OTHER LONG TERM LIABILITIES</b>                                 | <b>1,101</b>      | <b>6,249</b>      |
| <b>Total liabilities</b>                                           | <b>323,185</b>    | <b>329,603</b>    |
| <b>MINORITY INTEREST IN JOINT VENTURES</b>                         | <b>4,787</b>      | <b>7,164</b>      |
| <b>COMMITMENTS AND CONTINGENCIES</b>                               |                   |                   |
| <b>STOCKHOLDERS' EQUITY</b>                                        |                   |                   |
| Preferred stock - par value \$1.00 per share;                      |                   |                   |
| 1,000,000 shares authorized; no shares issued or outstanding       | -                 | -                 |
| Common stock - par value \$0.66 2/3 per share;                     |                   |                   |
| 70,000,000 shares authorized; 38,941,901 and 40,172,491            |                   |                   |
| issued and outstanding at December 31, 2006 and December 31, 2007, |                   |                   |
| respectively                                                       | 25,962            | 26,782            |
| Additional paid-in capital                                         | 104,795           | 121,412           |
| Retained earnings                                                  | 162,802           | 220,504           |
| Accumulated other comprehensive gain                               | 608               | 900               |
| <b>Total stockholders' equity</b>                                  | <b>294,167</b>    | <b>369,598</b>    |
| <b>Total liabilities and stockholders' equity</b>                  | <b>\$ 622,139</b> | <b>\$ 706,365</b> |

*The accompanying notes are an integral part of these consolidated financial statements.*

**DIODES INCORPORATED AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**

(Amounts in thousands, except per share data)

| <b>Years ended December 31,</b>                              | <b>2005</b> | <b>2006</b> | <b>2007</b> |
|--------------------------------------------------------------|-------------|-------------|-------------|
| <b>NET SALES</b>                                             | \$ 214,765  | \$ 343,308  | \$ 401,159  |
| <b>COST OF GOODS SOLD</b>                                    | 140,388     | 229,416     | 270,780     |
| Gross profit                                                 | 74,377      | 113,892     | 130,379     |
| <b>OPERATING EXPENSES</b>                                    |             |             |             |
| Selling, general and administrative                          | 30,285      | 47,945      | 55,461      |
| Research and development                                     | 3,713       | 8,317       | 13,515      |
| Restructuring costs and impairment loss of long-lived assets | (102)       | 152         | 1,003       |
| Total operating expenses                                     | 33,896      | 56,414      | 69,979      |
| Income from operations                                       | 40,481      | 57,478      | 60,400      |
| <b>OTHER INCOME (EXPENSES)</b>                               |             |             |             |
| Interest income                                              | 819         | 6,699       | 18,117      |
| Interest expense                                             | (598)       | (1,844)     | (6,831)     |
| Other                                                        | 406         | (1,212)     | (225)       |
| Total other income (expenses)                                | 627         | 3,643       | 11,061      |
| Income before income taxes and minority interest             | 41,108      | 61,121      | 71,461      |
| <b>INCOME TAX PROVISION</b>                                  | (6,685)     | (11,689)    | (9,428)     |
| Income before minority interest                              | 34,423      | 49,432      | 62,033      |
| Minority interest in earnings of joint venture               | (1,094)     | (1,289)     | (2,376)     |
| <b>NET INCOME</b>                                            | \$ 33,329   | \$ 48,143   | \$ 59,657   |
| <b>EARNINGS PER SHARE</b>                                    |             |             |             |
| Basic                                                        | \$ 0.96     | \$ 1.25     | \$ 1.51     |
| Diluted                                                      | \$ 0.86     | \$ 1.16     | \$ 1.41     |
| Number of shares used in computation                         |             |             |             |
| Basic                                                        | 34,752      | 38,443      | 39,601      |
| Diluted                                                      | 38,842      | 41,502      | 42,331      |

*The accompanying notes are an integral part of these consolidated financial statements.*

**DIODES INCORPORATED AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**

(Amounts in thousands)

Years ended December 31, 2005, 2006, and 2007

|                                                                          | Common stock             |         |                          |                                   | Additional<br>paid-in<br>capital | Retained<br>earnings | Accumulated<br>other<br>comprehensive<br>gain (loss) | Total      |
|--------------------------------------------------------------------------|--------------------------|---------|--------------------------|-----------------------------------|----------------------------------|----------------------|------------------------------------------------------|------------|
|                                                                          | Shares<br>in<br>Treasury | Shares  | Amount<br>in<br>treasury | Common<br>stock<br>in<br>treasury |                                  |                      |                                                      |            |
| BALANCE,<br>December 31, 2004                                            | 35,467                   | 3,630   | \$ 23,645                | \$(2,673)                         | \$ 9,272                         | \$ 81,330            | \$ 575                                               | \$ 112,148 |
| Comprehensive income, net of tax:                                        |                          |         |                          |                                   |                                  |                      |                                                      |            |
| Net income for the year<br>ended December 31, 2005                       |                          |         |                          |                                   |                                  | 33,329               |                                                      | 33,329     |
| Translation adjustments                                                  |                          |         |                          |                                   |                                  |                      | (1,263)                                              | (1,263)    |
| Total comprehensive income                                               |                          |         |                          |                                   |                                  |                      |                                                      | 32,066     |
| Management fee from LSC                                                  |                          |         |                          |                                   | 180                              |                      |                                                      | 180        |
| Exercise of stock options<br>including \$2,898,000 income<br>tax benefit | 1,181                    |         | 788                      |                                   | 6,761                            |                      |                                                      | 7,548      |
| Common stock issued for share-based plans                                | 88                       |         | 59                       |                                   | 1,756                            |                      |                                                      | 1,814      |
| Follow-on offering                                                       | 4,781                    |         | 3,189                    |                                   | 68,529                           |                      |                                                      | 71,718     |
| Treasury share retirement                                                | (3,630)                  | (3,630) | (2,421)                  | 2,673                             | (252)                            | -                    | -                                                    | -          |
| BALANCE,<br>December 31, 2005                                            | 37,887                   | -       | \$ 25,259                | \$ -                              | \$ 86,245                        | \$ 114,659           | \$ (688)                                             | \$ 225,474 |
| Comprehensive income, net of tax:                                        |                          |         |                          |                                   |                                  |                      |                                                      |            |
| Net income for the year<br>ended December 31, 2006                       |                          |         |                          |                                   |                                  | 48,143               |                                                      | 48,143     |
| Translation adjustments                                                  |                          |         |                          |                                   |                                  |                      | 1,296                                                | 1,296      |
| Total comprehensive income                                               |                          |         |                          |                                   |                                  |                      |                                                      | 49,439     |
| Common stock issued for share-based plans                                | 1,055                    |         | 704                      |                                   | 3,624                            |                      |                                                      | 4,327      |
| Excess tax benefits                                                      |                          |         |                          |                                   | 6,655                            |                      |                                                      | 6,655      |

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|                                                  |        |   |           |    |       |            |            |                   |
|--------------------------------------------------|--------|---|-----------|----|-------|------------|------------|-------------------|
| Share-based compensation                         | -      | - | -         | -  | 8,272 | -          | -          | 8,272             |
| <b>BALANCE,</b>                                  |        |   |           |    |       |            |            |                   |
| December 31, 2006                                | 38,942 | - | \$ 25,962 | \$ | -     | \$ 104,795 | \$ 162,802 | \$ 608 \$ 294,167 |
| <b>Comprehensive income, net of tax:</b>         |        |   |           |    |       |            |            |                   |
| <b>Net income for the year</b>                   |        |   |           |    |       |            |            |                   |
| ended December 31, 2007                          |        |   |           |    |       | 59,657     |            | 59,657            |
| <b>Translation adjustments</b>                   |        |   |           |    |       |            |            |                   |
|                                                  |        |   |           |    |       |            | 292        | 292               |
| <b>Total comprehensive income</b>                |        |   |           |    |       |            |            |                   |
|                                                  |        |   |           |    |       |            |            | 59,949            |
| <b>Common stock issued for share-based plans</b> |        |   |           |    |       |            |            |                   |
|                                                  | 1,231  |   | 820       |    | 6,753 |            |            | 7,573             |
| <b>Share-based compensation</b>                  |        |   |           |    |       |            |            |                   |
|                                                  |        |   |           |    | 9,864 |            |            | 9,864             |
| <b>Liability for unrecognized tax benefits</b>   |        |   |           |    |       |            |            |                   |
|                                                  | -      | - | -         | -  | -     | (1,955)    | -          | (1,955)           |
| <b>BALANCE,</b>                                  |        |   |           |    |       |            |            |                   |
| December 31, 2007                                | 40,172 | - | \$ 26,782 | \$ | -     | \$ 121,412 | \$ 220,504 | \$ 900 \$ 369,598 |

*The accompanying notes are an integral part of these consolidated financial statements.*

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**DIODES INCORPORATED AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Amounts in thousands)

| <b>Years ended December 31,</b>                                                   | <b>2005</b> | <b>2006</b> | <b>2007</b> |
|-----------------------------------------------------------------------------------|-------------|-------------|-------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                                       |             |             |             |
| Net income                                                                        | \$ 33,329   | \$ 48,143   | \$ 59,657   |
| Adjustments to reconcile net income to net cash provided by operating activities: |             |             |             |
| Depreciation and amortization                                                     | 16,228      | 20,443      | 26,245      |
| Minority interest earnings                                                        | 1,094       | 1,289       | 2,377       |
| Share-based compensation                                                          | 1,814       | 8,272       | 9,864       |
| Amortization of acquired intangibles                                              | -           | 360         | 836         |
| Amortization of convertible bond issuance costs                                   | -           | 262         | 1,252       |
| Loss (gain) on disposal of property, plant and equipment                          | (102)       | 152         | (16)        |
| Adjustment of other comprehensive income                                          | -           | 1,071       | -           |
| Changes in operating assets:                                                      |             |             |             |
| Accounts receivable                                                               | (11,037)    | (11,320)    | (11,874)    |
| Inventories                                                                       | (2,373)     | (16,283)    | (4,662)     |
| Prepaid expenses and other current assets                                         | 696         | (2,792)     | (3,667)     |
| Deferred income taxes                                                             | (3,482)     | 929         | 1,664       |
| Changes in operating liabilities:                                                 |             |             |             |
| Accounts payable                                                                  | 5,330       | 14,534      | 2,996       |
| Accrued liabilities                                                               | 2,770       | 4,957       | 4,608       |
| Other liabilities                                                                 | -           | 101         | 3,192       |
| Income taxes payable                                                              | 3,390       | 1,963       | (1,701)     |
| Net cash provided by operating activities                                         | 47,657      | 72,081      | 90,771      |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                                       |             |             |             |
| Purchases of property, plant and equipment                                        | (19,583)    | (45,656)    | (56,101)    |
| Purchases of short-term investments                                               | (40,348)    | (250,660)   | (32,464)    |
| Acquisitions, net of cash acquired                                                | (5,872)     | (29,433)    | -           |
| Proceeds from sales of property, plant and equipment                              | -           | 54          | 202         |
| Net cash used by investing activities                                             | (65,803)    | (325,695)   | (88,363)    |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                                       |             |             |             |
| Repayments on line of credit                                                      | (3,167)     | (5,758)     | -           |
| Net proceeds from the issuance of common stock                                    | 76,367      | 4,327       | 7,573       |
| Excess tax benefits                                                               | 2,898       | 6,655       | -           |
| Management incentive reimbursement from LSC                                       | 375         | -           | -           |
| Proceeds from long-term debt                                                      | 5,890       | 228,569     | -           |
| Repayments of long-term debt                                                      | (7,750)     | (4,666)     | (2,758)     |
| Repayments of capital lease obligations                                           | (136)       | (138)       | (141)       |
| Dividend to minority shareholder                                                  | (750)       | -           | -           |
| Net cash provided by financing activities                                         | 73,727      | 228,989     | 4,674       |
| <b>EFFECT OF EXCHANGE RATE CHANGES</b>                                            |             |             |             |
| <b>ON CASH AND CASH EQUIVALENTS</b>                                               | (1,263)     | 225         | 209         |
| <b>INCREASE (DECREASE) IN CASH</b>                                                | 54,318      | (24,400)    | 7,291       |

|                                                      |           |           |                  |
|------------------------------------------------------|-----------|-----------|------------------|
| <b>CASH AND CASH EQUIVALENTS</b> , beginning of year | 18,970    | 73,288    | <b>48,888</b>    |
| <b>CASH AND CASH EQUIVALENTS</b> , end of year       | \$ 73,288 | \$ 48,888 | \$ <b>56,179</b> |

*The accompanying notes are an integral part of these consolidated financial statements.*

**DIODES INCORPORATED AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)**

(Amounts in thousands)

**Years ended December 31,** **2005** **2006** **2007**

**SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION**

Cash paid during the year for:

|              |    |       |    |       |    |              |
|--------------|----|-------|----|-------|----|--------------|
| Interest     | \$ | 633   | \$ | 1,771 | \$ | <b>7,595</b> |
| Income taxes | \$ | 3,443 | \$ | 3,377 | \$ | <b>6,921</b> |

Non-cash activities:

|                                                                             |    |       |    |       |    |              |
|-----------------------------------------------------------------------------|----|-------|----|-------|----|--------------|
| Tax benefit related to stock options credited to additional paid-in capital | \$ | 2,898 | \$ | 6,655 | \$ | -            |
| Property, plant and equipment purchased on accounts payable                 | \$ | 5,061 | \$ | 878   | \$ | <b>1,733</b> |

The Company purchased 99.81% of the capital stock of Anachip Corporation and purchased the net assets of APD semiconductor for total \$35.2 million, net of \$3.9 million cash acquired (and \$5.8 million was paid in year 2005). In conjunction with the acquisition, liabilities were assumed as follows:

|                                |    |   |    |          |    |   |
|--------------------------------|----|---|----|----------|----|---|
| Fair value of assets acquired  | \$ | - | \$ | 56,896   | \$ | - |
| Liabilities assumed            |    | - |    | (17,737) |    | - |
| Cash acquired                  |    | - |    | (3,888)  |    | - |
| Cash paid for the acquisitions | \$ | - | \$ | 35,271   | \$ | - |

*The accompanying notes are an integral part of these consolidated financial statements.*

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

*(Amounts in thousands except share data)*

**NOTE 1 - SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES**

**Nature of operations** - Diodes Incorporated and its subsidiaries manufacture and distribute high-quality application specific standard semiconductor products to manufacturers in the communications, computing, consumer electronics, industrial, and automotive markets. Our products include diodes, rectifiers, transistors, MOSFETs, protection devices, functional specific arrays, power management devices including DC-DC switching and linear voltage regulators, amplifiers and comparators, Hall effect sensors, and silicon wafers. The products are sold primarily throughout North America, Asia and Europe.

**Principles of consolidation** - The consolidated financial statements include Diodes-North America and the following:

**Holding companies**

Diodes International B.V. ("Diodes-International") 100% owned (2007)

Diodes Hong Kong Holding Company, Ltd. 100% owned (2007)

**Subsidiaries**

Diodes Taiwan Corporation, Ltd. 100% owned  
("Diodes-Taiwan")

Diodes Hong Kong Ltd. ("Diodes-Hong Kong") 100% owned

Anachip Corporation ("Anachip") 99.81% owned  
("Diodes-Anachip")

Shanghai KaiHong Electronics Co., Ltd. 95% owned  
("Diodes-China")

Shanghai KaiHong Technology Co., Ltd. 95% owned  
("Diodes-Shanghai")

FabTech Incorporated ("FabTech") 100% owned  
("Diodes-FabTech")

Diodes United Kingdom, Ltd. 100% owned (2007)

Diodes Korea Incorporated 100% owned (2007)

Diodes Germany GmbH 100% owned (2007)

All significant intercompany balances and transactions have been eliminated.

During 2007, we undertook an internal restructuring whereby our foreign subsidiaries were placed under our newly formed, wholly-owned Netherlands holding company, Diodes International B.V. ("Diodes BV"). In addition, Diodes China and Diodes Shanghai were placed under Diodes Hong Kong Holding Company, Ltd., a newly-formed wholly-owned subsidiary of Diodes BV. The primary purpose of this internal restructuring was for treasury management and tax planning functions.

**Revenue recognition** - Revenue is recognized when there is persuasive evidence that an arrangement exists, when delivery has occurred, when our price to the buyer is fixed or determinable, and when collectibility of the receivable is reasonably assured. These elements are met when title to the products is passed to the buyers, which is generally when our product is shipped to our customers. We reduce revenue in the period of sale for estimates of product returns and other allowances.



**Product warranty** - We generally warrant our products for a period of one year from the date of sale. Historically, warranty expense has not been significant.

**Cash and cash equivalents** - We consider all highly liquid investments with maturity of three months or less at the date of purchase to be cash equivalents. We currently maintain substantially all of our day-to-day operating cash balances with major financial institutions.

**Short-term investments** - Our short-term investments consist primarily of auction rate securities, all of which are classified as available-for-sale. Available-for-sale securities are recorded at fair value, and unrealized holding gains and losses are recorded, net of tax, as a separate component of accumulated other comprehensive income. Available-for-sale securities with remaining maturities of less than one year, and those identified by management at time of purchase for funding operations in less than one year are classified as short-term. Unrealized losses are charged against net earnings when a decline in fair value is determined to be other than temporary (see Note 3).

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 - SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES**

(Continued)

**Allowance for doubtful accounts** - Management evaluates the collectability of our accounts receivable based upon a combination of factors, including the current business environment and historical experience. If we are aware of a customer's inability to meet its financial obligations to us, we record an allowance to reduce the receivable to the amount we reasonably believe we will be able to collect from the customer. For all other customers, we record an allowance based upon the amount of time the receivables are past due. If actual accounts receivable collections differ from these estimates, an adjustment to the allowance may be necessary with a resulting effect on operating expense. Accounts receivable are presented net of a valuation allowance indicated in the following table:

**Inventories** - Inventories are stated at the lower of cost or market value. Cost is determined principally by the first-in, first-out method. Cost includes materials, labor, and manufacturing overhead related to the purchase and production of inventories. The write-down of inventory to the lower of cost or market at the close of a fiscal period creates a new cost basis that subsequently would not be marked up based on changes in underlying facts and circumstances. On an on-going basis, both finished goods inventory and raw material inventory are evaluated for obsolescence and estimated utility. This evaluation includes analysis of sales levels, sales projections, and purchases by item, as well as raw material usage related to our manufacturing facilities. If our review indicates a reduction in utility below carrying value, we reduce our inventory to a new cost basis.

**Property, plant and equipment** - Property, plant and equipment are depreciated using straight-line methods over the estimated useful lives, which range from 20 to 55 years for buildings and 3 to 10 years for machinery and equipment. The estimated lives of leasehold improvements range from 3 to 5 years, and are amortized over the shorter of the remaining lease term or their estimated useful lives (see Note 5).

**Goodwill and other intangible assets** - Goodwill is tested for impairment on an annual basis as of December 31, and between annual tests if indicators of potential impairment exist, using a fair-value-based approach. No impairment of goodwill has been identified during any of the periods presented. Intangible assets are amortized on a straight-line basis over their estimated period of benefit. All of our intangible assets are subject to amortization. We evaluate the recoverability of intangible assets periodically and take into account events or circumstances that warrant revised estimates of useful lives or that indicate that impairment exists. No impairments of intangible assets have been identified during any of the periods presented. (see Note 6).

**Debt issuance costs** - Debt issuance costs of \$6.2 million related to the convertible bond were capitalized and are amortized over 5 years using the straight-line method. Amortization of debt issuance costs is included in interest expense while the un-amortized balance is included in other assets. Un-amortized debt issuance costs were \$4.7 million at December 31, 2007.

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 - SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES**

(Continued)

**Impairment of long-lived assets** - Certain of our long-lived assets are reviewed at least annually as to whether their carrying values have become impaired in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". Management considers assets to be impaired if the carrying value exceeds the undiscounted projected cash flows from operations. If impairment exists, the assets are written down to fair value or to the projected discounted cash flows from related operations. As of December 31, 2007, we expect the remaining carrying value of assets to be recoverable.

**Income taxes** - Income taxes are accounted for using an asset and liability approach whereby deferred tax assets and liabilities are recorded for differences in the financial reporting bases and tax bases of our assets and liabilities. If it is more likely than not that some portion of deferred tax assets will not be realized, a valuation allowance is recorded.

In July 2006, the FASB issued FASB interpretation (FIN) No. 48, "Accounting for Uncertainty in Income Taxes" which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, "Accounting for Income Taxes." FIN 48 prescribes a comprehensive model for how companies should recognize, measure, present, and disclose in their financial statements uncertain tax positions taken or expected to be taken on a tax return. Under FIN 48, tax positions shall initially be recognized in the financial statements when it is more likely than not the position will be sustained upon examination by the tax authorities. Such tax positions shall initially and subsequently be measured as the largest amount of tax benefit that is greater than 50% likely of being realized upon ultimate settlement with the tax authority assuming full knowledge of the position and all relevant facts. FIN 48 is effective for fiscal years beginning after December 15, 2006. The cumulative effects of adopting FIN 48 was recorded as an adjustment to retained earnings as of the beginning of the period of adoption. (see Note 13).

**Research and development costs** - Research and development costs are expensed as incurred.

**Shipping and handling costs** - Shipping and handling costs, which are included in selling, general and administrative expenses, were \$0.8 million, \$1.7 million and \$2.4 million for the years ended December 31, 2005, 2006 and 2007.

**Concentration of credit risk** - Financial instruments, which potentially subject us to concentrations of credit risk, include trade accounts receivable. Credit risk is limited by the dispersion of our customers over various geographic areas, operating primarily in the electronics manufacturing and distribution. We perform on-going credit evaluations of our customers, and generally require no collateral. Historically, credit losses have not been significant.

We currently maintain substantially all of our day-to-day cash balances with major financial institutions. Cash balances are usually in excess of Federal and/or foreign deposit insurance limits.

**Valuation of financial instruments** - The carrying value of our financial instruments, including cash and cash equivalents, accounts receivable, accounts payable, working capital line of credit, and long-term debt approximate fair value due to their current market conditions, maturity dates and other factors. Short-term investments classified as available-for-sale are recorded at market value with unrealized gains or losses reflected in other accumulated comprehensive income or loss.

**Treasury shares** - In December 2005, the Board of Directors canceled the 2,420,262 shares held in treasury. The cancellation has no net impact on stockholders' equity, shares outstanding, or shares used to compute earnings per

share.

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**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 - SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES**

(Continued)

**Equity investment** - On December 20, 2005, we acquired an 18.87% equity interest of Anachip Corporation, a private-held Taiwanese fabless analog IC company, for approximately \$5.9 million. The investment was accounted for under the equity method as required by APB No. 18, "The Equity Method of Accounting for Investments in Common Stock". However, we did not record income from the investment on the consolidated financial statements for the ten days ending December 31, 2005, as the amount was not material. In January 2006, we increased our equity ownership of Anachip Corporation to 99.81%. As a result, Anachip was consolidated beginning the first fiscal quarter of 2006.

**Stock split** - On both December 1, 2005 and July 30, 2007, we affected three-for-two stock splits in the form of 50% stock dividends. All share and per-share amounts in the accompanying consolidated financial statements and footnotes disclosures have been retroactively adjusted to reflect the effect of these stock splits.

**Use of estimates** - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires that management make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ materially from those estimates.

**Earnings per share** - Earnings per share are based upon the weighted average number of shares of common stock and common stock equivalents outstanding, including those related to share-based compensation and convertible bonds. Earnings per share are computed using the "treasury stock method" under Financial Accounting Standards Board (FASB) Statement No. 128. The convertible bonds include a net share settlement feature which requires us to redeem the par amount of the bond in cash and any remaining value, assuming the bond is in-the-money, in incremental shares, cash, or a combination thereof. The net-share settled convertible, as structured, is defined in EITF 90-19, instrument C, which allows us to use the treasury stock method of calculating diluted earnings per share. The incremental value of the shares will be determined based on the average price of our common stock over the reporting period. There are no shares in the earnings per share calculation related to the convertible bonds as our average stock price did not exceed the conversion price and, therefore, there is no conversion spread.

For the years ended December 31, 2005, 2006 and 2007, options and share grants outstanding for 1.0 million shares, 0.2 million shares and 0.6 million shares, respectively, of common stock have been excluded from the computation of diluted earnings per share because their effect was anti-dilutive.

|                                                                         | <b>Year Ended December 31</b> |             |             |
|-------------------------------------------------------------------------|-------------------------------|-------------|-------------|
|                                                                         | <b>2005</b>                   | <b>2006</b> | <b>2007</b> |
| Net income for earnings<br>per share computation                        | \$ 33,329                     | \$ 48,143   | \$ 59,657   |
| <b>Basic</b>                                                            |                               |             |             |
| Weighted average number of common<br>shares outstanding during the year | 34,752                        | 38,443      | 39,601      |
| <b>Basic earnings per share</b>                                         | \$ 0.96                       | \$ 1.25     | \$ 1.51     |
| <b>Diluted</b>                                                          |                               |             |             |
| Weighted average number of common                                       |                               |             |             |

|                                                                                               |         |         |                |
|-----------------------------------------------------------------------------------------------|---------|---------|----------------|
| shares outstanding used in calculating<br>basic earnings per share                            | 34,752  | 38,443  | <b>39,601</b>  |
| Add: incremental shares upon stock option exercise<br>and non-vested stock awards             | 4,090   | 3,059   | <b>2,730</b>   |
| Weighted average number of common<br>shares used in calculating<br>diluted earnings per share | 38,842  | 41,502  | <b>42,331</b>  |
| <b>Diluted earnings per share</b>                                                             | \$ 0.86 | \$ 1.16 | <b>\$ 1.41</b> |

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**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 - SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES**

(Continued)

**Stock-based compensation** - Effective January 1, 2006, we adopted SFAS No. 123R, (“Share-Based Payments”), using the modified prospective method. We are required to select a valuation technique or option-pricing model that meets the criteria as stated in the standard, which includes a binomial model and the Black-Scholes model. At the present time, we continue to use the Black-Scholes model, consistent with prior period valuations under SFAS 123. No modifications were made to any outstanding share-options prior to the adoption of SFAS 123R.

Under the modified prospective transition method share-based compensation cost is measured at the grant date based on the estimated fair value of the award and is recognized as expense over the employee’s requisite service period for all unvested share-based awards outstanding as of January 1, 2006. Prior to January 1, 2006, the Company accounted for its share-based awards under the recognition and measurement principles of APB 25 “Accounting for Stock issued to Employees” (APB 25) and its related interpretations and adopted the disclosure only provision of SFAS 123, “Accounting for Stock-Based Compensation” (SFAS 123). Accordingly, for fiscal years ending prior to January 1, 2006, no compensation cost was recognized for the employee stock option plan under the fair value recognition provisions of SFAS 123. In addition, SFAS 123R requires us to reflect any tax savings resulting from tax deductions in excess of expense reflected in our financial statements as a financing cash inflow in its statement of cash flows rather than as an operating cash flow as in prior periods (See “Note 15 - Share-based Compensation” for details).

We have approximately 1.0 million restricted stock grants outstanding as of December 31, 2007. Compensation expense is recognized for restricted stock grants on a straight-line basis over the requisite service period. As of December 31, 2007, there was \$12.9 million of total unrecognized compensation cost related to non-vested share-based compensation (See “Note 15 - Share-based Compensation”). In addition to the recognition of compensation expense, non-vested restricted stock grants are included in the diluted shares outstanding calculation.

**Functional currencies and foreign currency translation** - Through our subsidiaries, we maintain foreign operations in Taiwan, Hong Kong and China. We believe the New Taiwan (“NT”) dollar as the functional currency at Diodes-Taiwan and Diodes-Anachip most appropriately reflects the current economic facts and circumstances of the operations. Assets and liabilities recorded in NT dollar are translated at the exchange rate on the balance sheet date. Income and expense accounts are translated at the average monthly exchange rate during the period. Resulting translation adjustments are recorded as a separate component of accumulated other comprehensive income or loss.

We use the U.S. dollar as the functional currency in Diodes-China, Diodes-Shanghai and Diodes-Hong Kong, as substantially all monetary transactions are made in that currency, and other significant economic facts and circumstances currently support that position. As these factors may change in the future, we will periodically assess our position with respect to the functional currency of our foreign subsidiaries. Included in net income are foreign exchange gains of \$0.1 million for the year ended December 31, 2005, and exchange losses of \$1.8 million and \$0.6 million for the years ended December 31, 2006, and December 31, 2007, respectively.

**Comprehensive income** - Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities are reported as a separate component of stockholders’ equity, such items, along with net income, are components of comprehensive income. The components of other comprehensive income include foreign currency translation adjustments. Accumulated other comprehensive loss was \$0.7 million at December 31, 2005, and accumulated other comprehensive gain was \$0.6 million and \$0.9 million at December 31, 2006 and December 31, 2007, respectively.





**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 - SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES**

(Continued)

**Total Comprehensive Income**

|                        | <b>Twelve Months Ended December 31,</b> |           |                  |
|------------------------|-----------------------------------------|-----------|------------------|
|                        | 2005                                    | 2006      | <b>2007</b>      |
| Net income             | \$ 33,329                               | \$ 48,143 | \$ <b>59,657</b> |
| Translation adjustment | (1,263)                                 | 1,296     | <b>292</b>       |
| Comprehensive income   | \$ 32,066                               | \$ 49,439 | \$ <b>59,949</b> |

**Recently issued accounting pronouncements and proposed accounting changes** - In December 2007, the FASB issued SFAS No. 141R, "Business Combinations," which changes how business acquisitions are accounted. SFAS No. 141R requires the acquiring entity in a business combination to recognize all (and only) the assets acquired and liabilities assumed in the transaction and establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed in a business combination. Among the more significant changes in the accounting for acquisitions are the following: i) Transaction costs will generally be expensed. Certain such costs are presently treated as costs of the acquisition; ii) In-process research and development (IPR&D) will be accounted for as an asset, with the cost recognized as the research and development is realized or abandoned. IPR&D is presently expensed at the time of the acquisition; iii) Contingencies, including contingent consideration, will generally be recorded at fair value with subsequent adjustments recognized in operations. Contingent consideration is presently accounted for as an adjustment of purchase price; and iv) Decreases in valuation allowances on acquired deferred tax assets will be recognized in operations. Such changes previously were considered to be subsequent changes in consideration and were recorded as adjustments to goodwill. SFAS No. 141R is effective for business combinations and adjustments to an acquired entity's deferred tax asset and liability balances occurring after December 31, 2008. The Company is currently evaluating the future impacts and disclosures of this standard.

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51," which establishes new standards governing the accounting for and reporting of noncontrolling interests (NCIs) in partially owned consolidated subsidiaries and the loss of control of subsidiaries. Certain provisions of this standard indicate, among other things, that NCIs (previously referred to as minority interests) be treated as a separate component of equity, not as a liability; that increases and decreases in the parent's ownership interest, that leave control intact, be treated as equity transactions, rather than as step acquisitions or dilution gains or losses; and that losses of a partially owned consolidated subsidiary be allocated to the NCI even when such allocation might result in a deficit balance. This standard also requires changes to certain presentation and disclosure requirements. SFAS No. 160 is effective beginning January 1, 2009. The provisions of the standard are to be applied to all NCIs prospectively, except for the presentation and disclosure requirements, which are to be applied retrospectively to all periods presented. After adoption, noncontrolling interests (\$4.8 million and \$7.2 million at December 31, 2006 and 2007, respectively) will be classified as shareowners' equity, a change from its current classification between liabilities and shareowners' equity. The Company is currently evaluating the future impacts and disclosures of this standard.

In December 2007, the FASB ratified the EITF consensus on EITF Issue No. 07-1, "Accounting for Collaborative Arrangements" that discusses how parties to a collaborative arrangement (which does not establish a legal entity within such arrangement) should account for various activities. The consensus indicates that costs incurred and revenues

generated from transactions with third parties (i.e. parties outside of the collaborative arrangement) should be reported by the collaborators on the respective line items in their income statements pursuant to EITF Issue No. 99-19, "Reporting Revenue Gross as a Principal Versus Net as an Agent." Additionally, the consensus provides that income statement characterization of payments between the participants in a collaborative arrangement should be based upon existing authoritative pronouncements; analogy to such pronouncements if not within their scope; or a reasonable, rational, and consistently applied accounting policy election. EITF Issue No. 07-1 is effective for the Company beginning January 1, 2009 and is to be applied retrospectively to all periods presented for collaborative arrangements existing as of the date of adoption. The Company is currently evaluating the impacts and disclosures of this standard.

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 - SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES**

(Continued)

In June 2007, the FASB's EITF reached a consensus on EITF Issue No. 07-3, "Accounting for Nonrefundable Advance Payments for Goods or Services to Be Used in Future Research and Development Activities" that would require nonrefundable advance payments made by the Company for future R&D activities to be capitalized and recognized as an expense as the goods or services are received by the Company. EITF Issue No. 07-3 is effective for the Company with respect to new arrangements entered into beginning January 1, 2008. The Company is currently evaluating the impacts and disclosures of this standard.

In February 2007, the Financial Accounting Standards Board (FASB) issued FAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities - Including an amendment of FASB Statement No. 115" ("SFAS 159"). This Statement permits entities to choose to measure many financial instruments and certain other items at fair value and report unrealized gains and losses on these instruments in earnings. SFAS 159 is effective as of January 1, 2008. At the effective date, an entity may elect the fair value option for eligible items that exist at that date. The entity shall report the effect of the first re-measurement to fair value as a cumulative-effect adjustment to the opening balance of retained earnings. The Company has not elected the fair value option for eligible items that existed as of January 1, 2008.

In September 2006, FASB issued SFAS 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. Under the standard, fair value measurements would be separately disclosed by level within the fair value hierarchy. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years, with early adoption permitted. We have not yet determined the effect, if any, that the implementation of SFAS 157 will have on our results of operations or financial condition.

**Reclassifications** - In the first quarter of 2006, we adopted SFAS No. 123R, "Share-Based Payments," using the modified prospective method. SFAS 123R requires that the excess tax benefit associated with an individual share-based payment award be included in the statement of cash flows as a cash inflow from financing activities and a cash outflow from operating activities. The amounts presented in the accompanying financial statements for year 2005 have been reclassified to conform to year 2006 and year 2007 financial statement presentation. These reclassifications had no impact on previously reported net income or stockholders' equity.

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 2 - BUSINESS ACQUISITIONS**

**Anachip acquisition** - On December 20, 2005, we announced the signing of a definitive stock purchase agreement to acquire Anachip Corporation, a Taiwanese fabless analog IC company.

Headquartered in the Hsinchu Science Park in Taiwan, Anachip's main product focus is power management ICs. Anachip's products are widely used in LCD monitor/TV's, wireless 802.11 LAN access points, brushless DC motor fans, portable DVD players, datacom devices, ADSL modems, TV/satellite set-top boxes, and power supplies.

The selling shareholders of Anachip stock included Lite-On Semiconductor Corporation (which owned approximately 60% of Anachip's outstanding capital stock), and two Taiwanese venture capital firms (together owning approximately 20% of Anachip's stock), as well as current and former Anachip employees, among others.

At December 31, 2005, we had purchased an aggregate of approximately 9.4 million shares (or approximately 18.9%) of the 50 million outstanding shares of the capital stock of Anachip. On January 10, 2006, (the closing date of the acquisition) we purchased an additional approximately 40.5 million shares and therefore, we hold approximately 99.81% of the Anachip capital stock. At December 31, 2005, the investment in Anachip is recorded under the equity method; however, we did not record income from the investment on the consolidated financial statements for the ten days ending December 31, 2005, as the amount was not material. As of result of the additional Anachip interest acquired during 2006, Anachip was consolidated beginning the first fiscal quarter of 2006.

The purchase price of the acquisition was NT\$20 per share (approximately US\$31 million as of the transaction date). The following table summarizes management's fair value of the assets acquired and liabilities assumed at the date of acquisition.

|                                  | Original<br>Amount<br>Disclosed in<br>2005 Form<br>10-K<br>(unaudited) | Purchase<br>Adjustments | <b>Total<br/>Allocation</b> |
|----------------------------------|------------------------------------------------------------------------|-------------------------|-----------------------------|
| Current assets                   | \$ 23,752                                                              | \$ (1,254)              | \$ 22,498                   |
| Fixed assets/non-current         | 2,291                                                                  | (11)                    | 2,280                       |
| Patents and trademarks           | 2,269                                                                  | 161                     | 2,430                       |
| Goodwill                         | 19,541                                                                 | 399                     | 19,940                      |
| <b>Total assets acquired</b>     | <b>47,853</b>                                                          | <b>(705)</b>            | <b>47,148</b>               |
| Current liabilities              | (16,829)                                                               | 1,132                   | (15,697)                    |
| Non-current liabilities          | (655)                                                                  | (45)                    | (700)                       |
| <b>Total liabilities assumed</b> | <b>(17,484)</b>                                                        | <b>1,087</b>            | <b>(16,397)</b>             |
| <b>Total purchase price</b>      | <b>\$ 30,369</b>                                                       | <b>\$ 382</b>           | <b>\$ 30,751</b>            |

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 2 - BUSINESS ACQUISITIONS** (Continued)

Purchase adjustments primarily relate to acquisition costs and refinement to estimated fair values of assets acquired and liabilities assumed. The acquired intangible assets include patents and trademarks of \$2.4 million with an approximately 10-year weighted-average useful life.

The following unaudited table summarizes the supplemental consolidated pro forma information for the year ended December 31, 2005 as though the acquisition had been completed as of the beginning of that reporting period. The consolidated pro forma information is presented for illustrative purposes and is not indicative of future performance.

|                    | <b>Twelve months ended December</b> |                  |
|--------------------|-------------------------------------|------------------|
|                    | <b>31, 2005</b>                     |                  |
|                    | <b>As reported</b>                  | <b>Pro forma</b> |
| Revenue            | \$ 214,765                          | \$ 265,083       |
| Net income         | \$ 33,329                           | \$ 32,934        |
| Earnings per share |                                     |                  |
| Basic              | \$ 0.96                             | \$ 0.95          |
| Diluted            | \$ 0.86                             | \$ 0.85          |

**APD acquisition** - On October 24, 2006, we signed an agreement to purchase the net assets of APD Semiconductor, a privately held U.S.-based fabless discrete semiconductor company. The assets related to the business of manufacturing, marketing, selling and distribution of discrete semiconductor products. The initial purchase price of the acquisition was \$8.4 million in addition to a potential earn-out provision with respect to pre-defined covered products. The acquisition was completed on November 3, 2006.

As of December 31, 2007, contingent consideration has been recorded as a liability approximating \$1 million. When the contingency is resolved and the consideration is distributable, any excess of the fair value of the contingent consideration payable over the amount that was recognized as a liability shall be recognized as an additional cost of the acquired entity. If the amount initially recognized as a liability exceeds the consideration payable, that excess shall be allocated as a pro rata reduction of the amounts assigned to assets acquired.

The following table summarizes management's estimates of the fair values of the assets acquired and liabilities assumed at the date of acquisition.

| Assets acquired     | <b>Total Allocation</b> |
|---------------------|-------------------------|
| Accounts receivable | \$ 299                  |
| Inventory           | 754                     |
| Fixed assets        | 125                     |
| Patents             | 8,569                   |
| Liabilities assumed |                         |

|                     |    |         |
|---------------------|----|---------|
| Accounts payable    |    | (339)   |
| Accrued liabilities |    | (1,000) |
| Net assets acquired | \$ | 8,408   |

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 3 - SHORT-TERM INVESTMENTS**

Short-term investments were as follows:

| <b>As of December 31, 2007</b>                           | Cost Basis        | Unrealized Gains | Unrealized Losses | Recorded Basis    |
|----------------------------------------------------------|-------------------|------------------|-------------------|-------------------|
| Available for sale investment in auction rate securities | \$ 320,700        | \$ -             | \$ -              | <b>\$ 320,700</b> |
| Money market mutual funds                                | 2,772             | -                | -                 | <b>\$ 2,772</b>   |
| <b>Total short-term investments</b>                      | <b>\$ 323,472</b> | <b>\$ -</b>      | <b>\$ -</b>       | <b>\$ 323,472</b> |

| As of December 31, 2006                                  | Cost Basis        | Unrealized Gains | Unrealized Losses | Recorded Basis    |
|----------------------------------------------------------|-------------------|------------------|-------------------|-------------------|
| Available for sale investment in auction rate securities | \$ 290,796        | \$ -             | \$ -              | 290,796           |
| Money market mutual funds                                | 212               | -                | -                 | \$ 212            |
| <b>Total short-term investments</b>                      | <b>\$ 291,008</b> | <b>\$ -</b>      | <b>\$ -</b>       | <b>\$ 291,008</b> |

As of December 31, 2007, we had \$320.7 million invested primarily in auction rate securities, which are classified as current, available-for-sale investments. Although the maturities of the securities are over 10 years, management intends to use the funds within one year and does not anticipate holding the investments until maturity; therefore, the securities are classified as short-term and included in short-term investments on our consolidated balance sheets. The carrying values of available-for-sale securities approximates fair value. These investments are primarily in municipal and student loan association bonds that are fully collateralized by AAA rated bonds and/or insured against loss of principal and interest by AAA rated bond insurers. None of these investments are collateralized mortgage obligations or are any other type of mortgage- or real estate-backed security.

Auction rate securities are generally long-term debt instruments that provide liquidity through a Dutch auction process that resets the applicable interest rate at pre-determined calendar intervals. These mechanisms generally allow existing investors to rollover their holdings and continue to own their respective securities or liquidate their holdings by selling their securities at par value.

We generally invest in these securities for short periods of time as part of our cash management program. However, the recent uncertainties in the credit markets have prevented us and other investors from liquidating holdings of auction rate securities in recent auctions occurring subsequent to December 31, 2007, because the amount of securities submitted for sale has exceeded the amount of purchase orders, resulting in our continuing to hold these securities and the issuers paying interest at the maximum contractual rates which are higher than similar securities for which auctions have cleared. Based on current market conditions, it is likely that auctions related to more of these securities will be unsuccessful in the near term. Unsuccessful auctions could result in our holding securities beyond their next scheduled auction reset dates if a secondary market does not develop, thereby limiting the short-term liquidity of these investments.

The reported amounts for these securities take into consideration the financial conditions of the issuer and the bond insurers as well as the value of the collateral. If the credit ratings of the issuer, the bond insurers or the collateral deteriorate, we may adjust the carrying value of these investments. Although we are uncertain as to when the liquidity

issues relating to these investments will improve, we consider these issues to be only temporary. Any temporary decline, if sustained, would be recognized in other comprehensive income. It is possible that declines in fair value may occur. We continue to monitor the market for auction rate securities and consider its impact (if any) on the fair market value of the investments. If the current market conditions deteriorate further the Company may be required to record unrealized losses in other comprehensive income or impairment charges in 2008.



**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 4 - INVENTORIES**

Inventories, stated at the lower of cost or market value, at December 31 were:

|                  |    | <b>2006</b> |    | <b>2007</b>   |
|------------------|----|-------------|----|---------------|
| Finished goods   | \$ | 24,473      | \$ | 21,245        |
| Work-in-progress |    | 10,265      |    | 11,868        |
| Raw materials    |    | 13,464      |    | 19,918        |
|                  | \$ | 48,202      | \$ | <b>53,031</b> |

**NOTE 5 - PROPERTY, PLANT AND EQUIPMENT**

Property, plant and equipment at December 31 were:

|                                                 |    | <b>2006</b> |    | <b>2007</b>     |
|-------------------------------------------------|----|-------------|----|-----------------|
| Buildings and leasehold improvements            | \$ | 8,117       | \$ | <b>9,287</b>    |
| Construction in-progress                        |    | 6,619       |    | <b>8,968</b>    |
| Machinery and equipment                         |    | 148,716     |    | <b>196,559</b>  |
|                                                 |    | 163,452     |    | <b>214,814</b>  |
| Less: Accumulated depreciation and amortization |    | (72,612)    |    | <b>(96,060)</b> |
|                                                 |    | 90,840      |    | <b>118,754</b>  |
| Land                                            |    | 4,629       |    | <b>4,653</b>    |
|                                                 | \$ | 95,469      | \$ | <b>123,407</b>  |

Depreciation and amortization of property, plant and equipment was \$16.2 million, \$20.4 million and \$26.2 million for the years ended December 31, 2005, 2006 and 2007, respectively.

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 - INTANGIBLE ASSETS SUBJECT TO AMORTIZATION**

Intangible assets subject to amortization at December 31 were as follows:

| Amortized Intangible Assets | Useful life | As of December 31, 2007 |                          |                             |                 | Net |
|-----------------------------|-------------|-------------------------|--------------------------|-----------------------------|-----------------|-----|
|                             |             | Gross Carrying Amount   | Accumulated Amortization | Currency exchange and other |                 |     |
| APD:                        |             |                         |                          |                             |                 |     |
| Patents                     | 15 years    | \$ 8,401                | \$ 638                   | \$ -                        | \$ 7,763        |     |
| Anachip:                    |             |                         |                          |                             |                 |     |
| Patents and trademarks      | 3-10 years  | 2,430                   | 556                      | 6                           | 1,880           |     |
| <b>Total</b>                |             | <b>\$ 10,831</b>        | <b>\$ 1,194</b>          | <b>\$ 6</b>                 | <b>\$ 9,643</b> |     |

| Amortized Intangible Assets | Useful life | As of December 31, 2006 |                          |                             |                  | Net |
|-----------------------------|-------------|-------------------------|--------------------------|-----------------------------|------------------|-----|
|                             |             | Gross Carrying Amount   | Accumulated Amortization | Currency exchange and other |                  |     |
| APD:                        |             |                         |                          |                             |                  |     |
| Patents                     | 15 years    | \$ 8,569                | \$ 79                    | \$ -                        | \$ 8,490         |     |
| Anachip:                    |             |                         |                          |                             |                  |     |
| Patents and trademarks      | 3-10 years  | 2,430                   | 281                      | 30                          | 2,179            |     |
| <b>Total:</b>               |             | <b>\$ 10,999</b>        | <b>\$ 360</b>            | <b>\$ 30</b>                | <b>\$ 10,669</b> |     |

Amortization expense related to intangible assets subject to amortization was \$0, \$0.4 million and \$0.8 million for the years ended December 31, 2005, 2006 and 2007, respectively.

Amortization of intangible assets through 2012 is as follows:

| Years | Anachip | APD    | Total amortization of Intangible assets |
|-------|---------|--------|-----------------------------------------|
| 2008  | \$ 282  | \$ 560 | \$ 842                                  |
| 2009  | 282     | 560    | 842                                     |
| 2010  | 282     | 560    | 842                                     |

|      |     |     |     |
|------|-----|-----|-----|
| 2011 | 244 | 560 | 804 |
| 2012 | 207 | 560 | 767 |

**NOTE 7 - GOODWILL**

Changes in goodwill for the years ended December 31 were as follows:

|                | 2006                     |                                                        |                                   |                            | 2007                  |                                                        |                                   |                            |
|----------------|--------------------------|--------------------------------------------------------|-----------------------------------|----------------------------|-----------------------|--------------------------------------------------------|-----------------------------------|----------------------------|
|                | Balance,<br>January<br>1 | Acquisitions/<br>purchase<br>accounting<br>adjustments | Currency<br>exchange<br>and other | Balance,<br>December<br>31 | Balance,<br>January 1 | Acquisitions/<br>purchase<br>accounting<br>adjustments | Currency<br>exchange<br>and other | Balance,<br>December<br>31 |
| Diodes-China   | \$ 881                   | \$ -                                                   | \$ -                              | \$ 881                     | \$ 881                | \$ -                                                   | \$ -                              | \$ 881                     |
| -              |                          |                                                        |                                   |                            |                       |                                                        |                                   |                            |
| Diodes-FabTech | 4,209                    | -                                                      | -                                 | 4,209                      | 4,209                 | -                                                      | -                                 | 4,209                      |
| -              |                          |                                                        |                                   |                            |                       |                                                        |                                   |                            |
| Diodes-Anachip | -                        | 19,675                                                 | 265                               | 19,940                     | 19,940                | -                                                      | 105                               | 20,045                     |
| Total          | \$ 5,090                 | \$ 19,675                                              | \$ 265                            | \$ 25,030                  | \$ 25,030             | \$ -                                                   | \$ 105                            | \$ 25,135                  |

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 8 - BANK CREDIT AGREEMENTS AND LONG-TERM DEBT**

**Credit facilities** - We maintain credit facilities with several financial institutions through our entities in the U.S. and Asia totaling \$68 million. The credit unused and available under the various facilities as of December 31, 2007, was \$58.1 million, as follows:

| 2007<br>Credit Facility | Terms                                                                                               | Outstanding at December 31, |             |
|-------------------------|-----------------------------------------------------------------------------------------------------|-----------------------------|-------------|
|                         |                                                                                                     | 2006                        | 2007        |
| \$ 20,000               | Revolving, collateralized by all assets, variable interest, LIBOR plus variable margin, due monthly | \$ -                        | \$ -        |
| \$ 27,000               | Unsecured, interest at LIBOR plus margin, due quarterly                                             | -                           | -           |
| \$ 11,100               | Unsecured, variable interest plus margin due monthly                                                | \$ -                        | \$ -        |
| <b>\$ 58,100</b>        |                                                                                                     | <b>\$ -</b>                 | <b>\$ -</b> |

**Long-term debt** - The balances as of December 31, consist of the following:

|                                                                                                                                                                                                                                                                    | 2006              | 2007              |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------|-------------------|
| <b>Convertible bond</b> with aggregate principal amount \$230 million of convertible senior notes due 2026. The notes mature October 1, 2026. Interest, at 2.25%, is payable semi-annually in arrears on April 1 and October 1 of each year, beginning 2007.       | \$ 230,000        | \$ 230,000        |
| <b>Notes payable</b> to Taiwan bank, principal amount of NT\$158 million, variable interest (approximately 3.7% as of December 31, 2007), of which NT\$132 million matures on July 6, 2021, and NT\$26 million matures July 6, 2013, secured by land and building. | 4,790             | 4,480             |
| <b>Term note portion</b> due to unrelated customer, unsecured and interest-free repaid in quarterly price concessions, paid in full December 2007.                                                                                                                 | 1,441             | -                 |
| <b>Note payable</b> to U.S. bank, collateralized by all assets, due in aggregate monthly principal payments of \$83,000 plus interest (approximately 6.0% at December 31, 2007).                                                                                   | 3,686             | 2,680             |
|                                                                                                                                                                                                                                                                    | 239,917           | 237,160           |
| Less: Current portion                                                                                                                                                                                                                                              | (2,802)           | (1,345)           |
| <b>Long-term debt, net of current portion</b>                                                                                                                                                                                                                      | <b>\$ 237,115</b> | <b>\$ 235,815</b> |



**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 8 - BANK CREDIT AGREEMENTS AND LONG-TERM DEBT (Continued)**

The U.S. credit facility includes a revolving credit commitment of up to \$20.0 million, including a \$5.0 million letter of credit sub-facility. As of December 31, 2007, there was no amount outstanding. The credit facilities contain certain covenants and restrictions, which, among other matters, require the maintenance of certain financial ratios and attainment of certain financial results.

The annual contractual maturities of long-term debt at December 31, 2007 are as follows:

|                             |           |                |
|-----------------------------|-----------|----------------|
| 2008                        | \$        | 1,345          |
| 2009                        |           | 1,339          |
| 2010                        |           | 1,014          |
| 2011                        |           | 359            |
| 2012                        |           | 372            |
| Thereafter                  |           | 232,731        |
| <b>Total long-term debt</b> | <b>\$</b> | <b>237,160</b> |

**Convertible bond** - On October 12, 2006, we issued and sold convertible senior notes with an aggregate principal amount of \$230 million due 2026 (the “Notes”), which pay 2.25% interest per annum on the principal amount of the Notes, payable semi-annually in arrears on April 1 and October 1 of each year, beginning on April 1, 2007. Interest will accrue on the Notes from and including October 12, 2006 or from and including the last date in respect of which interest has been paid or provided for, as the case may be, to, but excluding, the next interest payment date or maturity date, as the case may be. Commencing with the six-month period beginning October 1, 2011, and for each six-month period thereafter, we will, on the interest payment date for such interest period, pay contingent interest to the holders of the Notes under certain circumstances and in amounts described in the indenture. For U.S. Federal income tax purposes, we will treat, and each holder of the Notes will agree under the indenture to treat, the Notes as contingent payment debt instruments governed by special tax rules and to be bound by our application of those rules to the Notes.

The Notes will be convertible into cash or, at our option, cash and/or shares of our common stock based on an initial conversion rate, subject to adjustment, of 25.6419 shares per \$1,000 principal amount of Notes, which represents an initial conversion price of \$39.00 per share (split adjusted), in certain circumstances. In addition, following a “make-whole fundamental change” that occurs prior to October 1, 2011, we will, at our option, increase the conversion rate for a holder who elects to convert its Notes in connection with such “make-whole fundamental change,” in certain circumstances.

Note holders may convert their Notes prior to stated maturity only under the following circumstances: (i) during any calendar quarter after the calendar quarter ending December 31, 2006, if the closing sale price of our common stock for each of 20 or more trading days in a period of 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter exceeds 120% of the conversion price in effect on the last trading day of the immediately preceding calendar quarter; (ii) during the five consecutive business days immediately after any five consecutive trading day period (we refer to this five consecutive trading day period as the “note measurement period”) in which the average trading price per \$1,000 principal amount of Notes was equal to or less than 98% of the average conversion value of the Notes during the note measurement period; (iii) upon the occurrence of specified corporate transactions; (iv) if we have called the Notes for redemption; and (v) at any time from, and including, September 1, 2011 to, and including, October 1, 2011 and at any time on or after October 1, 2024. Upon conversion, holders will receive cash, or at our option, cash and shares of our common stock based on the conversion payment terms described

in the Note. The conversion obligation is based on the sum of the “daily settlement amounts” described in the prospectus for the 20 consecutive trading days that begin on, and include, the second trading day after the day the Notes are tendered for conversion.

On or after October 1, 2011, we may, from time to time, at our option, redeem the Notes, in whole or in part, for cash, at a redemption price equal to 100% of the principal amount of the Notes we redeem, plus any accrued and unpaid interest to, but excluding, the redemption date.

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 8 - BANK CREDIT AGREEMENTS AND LONG-TERM DEBT (Continued)**

On each of October 1, 2011, October 1, 2016 and October 1, 2021, holders may require us to purchase all or a portion of their Notes at a purchase price in cash equal to 100% of the principal amount of the Notes to be purchased, plus any accrued and unpaid interest to, but excluding, the purchase date.

Note holders may require us to repurchase all or a portion of their Notes upon a fundamental change, as described in this prospectus, at a repurchase price in cash equal to 100% of the principal amount of the Notes to be repurchased, plus any accrued and unpaid interest to, but excluding, the fundamental change repurchase date. Future minimum interest payments related to the Notes as of December 31, 2007 are \$5.2 million for each year from 2008 through 2012. Future minimum payments related to the Notes as of December 31, 2007 for 2012 and thereafter include \$72.3 million in interest and \$230 million in principal for a total of \$302.3 million.

We have evaluated the terms of the call feature, redemption feature, and the conversion feature under applicable accounting literature, including SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," and EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock," and concluded that none of these features should be separately accounted for as derivatives.

We intend to use the net proceeds for working capital and general corporate purposes, which may include the acquisition of businesses, products, product rights or technologies, strategic investments, or purchases of own common stock.

In connection with the issuance of the Notes, we incurred approximately \$6.2 million of issuance costs, which primarily consisted of investment banker fees, legal and accounting fees. These costs are classified within Other Assets and are amortized as a component of interest expense using the straight-line method from issuance through October 12, 2011.

**NOTE 9 - CAPITAL LEASE OBLIGATIONS**

Future minimum lease payments under capital lease agreements are summarized as follows:

For years ending December 31,

|                                         |    |       |
|-----------------------------------------|----|-------|
| 2008                                    | \$ | 185   |
| 2009                                    |    | 185   |
| 2010                                    |    | 185   |
| 2011                                    |    | 185   |
| Thereafter                              |    | 942   |
|                                         |    | 1,682 |
| Less: Interest                          |    | (206) |
| Present value of minimum lease payments |    | 1,476 |
| Less: Current portion                   |    | (145) |
| Long-term portion                       | \$ | 1,331 |

At December 31, 2007, property under capital leases had a cost of \$2.4 million, and the related accumulated



depreciation was \$1.0 million. Depreciation of assets held under capital lease is included in depreciation expenses.

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**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 10 - ACCRUED LIABILITIES**

Accrued liabilities at December 31 were:

|                                | 2006      | 2007      |
|--------------------------------|-----------|-----------|
| Compensation and payroll taxes | \$ 9,746  | \$ 10,517 |
| Equipment purchases            | 6,195     | 4,462     |
| Accrued interest               | 1,121     | 1,294     |
| Other                          | 7,905     | 11,568    |
|                                | \$ 24,967 | \$ 27,841 |

**NOTE 11 - STOCKHOLDERS' EQUITY**

On July 10, 2007, we declared a three-for-two stock split in the form of a 50% stock dividend payable on July 30, 2007 to stockholders of record on July 20, 2007. Under the terms of this stock dividend, our stockholders received one additional share for every two shares held on the record date. The dividend was paid in authorized but unissued shares of common stock. Fractional shares created by the stock dividend were paid in cash based upon the closing price of our common stock on the record date. The par value of our stock is not affected by the dividend and remains at \$0.66 2/3 per share. The outstanding shares stated on the statement of stockholders' equity, the balance sheet and the consolidated condensed statement of income and disclosures have been adjusted to reflect the effects of the stock split.

As of December 31, 2007, we had approximately 40.2 million outstanding common shares. During 2007, shares outstanding increased by approximately 1.2 million shares, due to approximately 1.1 million shares issued in conjunction with stock option exercises and 0.1 million shares issued in conjunction with vested restricted stock units.

Additional paid-in capital increased approximately \$16.6 million in the year ended December 31, 2007, primarily due to \$5.6 million in stock option expense, \$4.3 million in share grant expense, and \$6.7 million in conjunction with stock option exercises and vested restricted stock units.

We adopted the provisions of FASB Interpretation No. 48 (FIN48) effective January 1, 2007. As a result of the implementation of FIN48, during the first quarter of 2007, we increased our liability for unrecognized tax benefits by approximately \$2.0 million, primarily related to our foreign subsidiaries, which was accounted for as a reduction to the January 1, 2007 retained earnings balance.

**NOTE 12 - RESTRUCTURING COSTS**

In the year ended December 31, 2007, we recorded approximately \$1.1 million in restructuring costs related to the consolidation of our analog wafer probe and final test operations from Hsinchu, Taiwan to our manufacturing facilities in Shanghai, China. The expense primarily consisted of approximately \$0.8 million in termination and severance costs and approximately \$0.3 million in impairment of fixed assets and other. The restructuring has been completed as of December 31, 2007.



**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 13 - INCOME TAXES**

The components of the income tax provision are as follows:

|                            | 2005     | 2006      | 2007     |
|----------------------------|----------|-----------|----------|
| Current tax provision      |          |           |          |
| Federal                    | \$ 3,013 | \$ 9,106  | \$ -     |
| Foreign                    | 4,546    | 6,555     | 6,355    |
| State                      | 547      | 641       | 230      |
|                            | 8,106    | 16,302    | 6,585    |
| Deferred tax expense       | (1,421)  | (4,613)   | 2,843    |
| Total income tax provision | \$ 6,685 | \$ 11,689 | \$ 9,428 |

Reconciliation between the effective tax rate and the statutory tax rates for the years ended December 31, 2005, 2006, and 2007 is as follows:

|                                                        | 2005      |                            | 2006      |                            | 2007      |                            |
|--------------------------------------------------------|-----------|----------------------------|-----------|----------------------------|-----------|----------------------------|
|                                                        | Amount    | Percent of pretax earnings | Amount    | Percent of pretax earnings | Amount    | Percent of pretax earnings |
| Federal tax                                            | \$ 14,388 | 35.0                       | \$ 21,392 | 35.0                       | \$ 25,011 | 35.0                       |
| State income taxes, net of Federal tax benefit         | 1,891     | 4.6                        | 2,506     | 4.1                        | 231       | 0.3                        |
| Foreign income taxed at lower tax rates                | (11,079)  | (27.0)                     | (16,993)  | (27.8)                     | (21,063)  | (29.5)                     |
| Subpart F income                                       | 1,520     | 3.7                        | 2,614     | 4.3                        | 1,185     | 1.7                        |
| U.S. tax on undistributed foreign earnings             | 1,116     | 2.7                        | 2,270     | 3.7                        | (3,339)   | (4.7)                      |
| Valuation allowance - foreign tax credit carryforwards | -         | -                          | -         | -                          | 5,044     | 7.1                        |
| Liability for unrecognized tax benefits                | -         | -                          | -         | -                          | 1,185     | 1.7                        |
| Other                                                  | (1,151)   | (2.8)                      | (100)     | (0.2)                      | 1,174     | 1.6                        |
| Income tax provision                                   | \$ 6,685  | 16.3                       | \$ 11,689 | 19.1                       | \$ 9,428  | 13.2                       |

Our global presence requires us to pay income taxes in a number of jurisdictions. In general, earnings in the U.S. and Taiwan are currently subject to tax rates of 39.5% and 25.0%, respectively. In addition, Taiwan earnings are subject to an additional 10% retained earnings tax should the Taiwan earnings not be distributed. Earnings of Diodes-Hong Kong are subject to a 17.5% tax for local sales or local source sales; all other Hong Kong sales are not subject to foreign income taxes. Earnings at Diodes-Taiwan and Diodes-Hong Kong are also subject to U.S. taxes with respect to those earnings that are derived from product manufactured by our China subsidiaries and sold to customers outside

of Taiwan and Hong Kong, respectively. The U.S. tax rate on this Subpart-F income is computed as the difference between the foreign effective tax rates and the U.S. tax rate. In accordance with U.S. tax law, we receive credit against our U.S. Federal tax liability for income taxes paid by our foreign subsidiaries.

As an incentive for the formation of Anachip, earnings of Diodes-Anachip are subject to a five-year tax holiday (subject to certain qualifications of Taiwanese tax law). In the third quarter of 2006, we elected to begin this five-year tax holiday as of January 1, 2006. Beginning 2011, Diodes-Anachip earnings will be subject to statutory Taiwan income tax.

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 13 - INCOME TAXES** (Continued)

Diodes-China is located in the Songjiang district, where the standard central government tax rate was 24.0% through 2007. However, as an incentive for establishing Diodes-China, the earnings of Diodes-China were subject to a 0% tax rate by the central government from 1996 through 2000, and to a 12.0% tax rate from 2001 through 2007. In addition, due to a \$15.0 million permanent re-investment of Diodes-China earnings in 2004, Diodes-China has received additional preferential tax treatment (earnings will be exempted from central government income tax for two years, and then subject to tax rates in the range of 12.0% to 12.5% for the following three years) on earnings that are generated by this \$15.0 million investment.

In addition, the earnings of Diodes-China would ordinarily be subject to a standard local government tax rate of 3.0%. However, as an incentive for establishing Diodes-China, the local government waived this tax from 1996 through 2006. Management expects this tax to be waived for 2007 as well; however, the local government can re-impose this tax at its discretion at any time.

In 2004, we established our second Shanghai-based manufacturing facility, Diodes-Shanghai, located in the Songjiang Export Zone of Shanghai, China. In the Songjiang Export Zone, the central government standard tax rate is 15.0%, and there is no local government tax. As an incentive for establishing Diodes-Shanghai, the 2005 and 2006 earnings of Diodes-Shanghai were exempted from central government income tax, and for the years 2007 through 2009 its earnings will be subject to tax rates in the range of 7.5% to 10.0%.

The recent China government income tax reform terminates some existing tax incentives for foreign enterprises doing business in China. The central government tax rate in China will increase to 25.0% beginning in 2008; however we believe Diodes-China may qualify for a “high-technology” preferential tax treatment that could reduce the tax rate to 15.0%. It is unclear to what extent our China subsidiaries will continue to receive preferential tax treatment.

We file income tax returns in the U.S. Federal jurisdiction and various state and foreign jurisdictions. We are no longer subject to U.S. Federal income tax examinations by tax authorities for tax years before 2004. With respect to state and local jurisdictions and countries outside of the U.S., with limited exceptions, we are no longer subject to income tax audits for years before 2001. Although the outcome of tax audits is always uncertain, we believe that adequate amounts of tax, interest and penalties, if any, have been provided for in our FIN48 reserve for any adjustments that may result from future tax audits. We recognize accrued interest and penalties, if any, related to unrecognized tax benefits in income tax expense.

We adopted the provisions of FIN48 effective January 1, 2007. As a result of the implementation of FIN48, we increased our liability for unrecognized tax benefits, primarily related to our foreign subsidiaries, by approximately \$2.0 million during the first quarter of 2007, which was accounted for as a reduction to the January 1, 2007 balance of retained earnings. Accordingly, as of January 1, 2007 and December 31, 2007, approximately \$3.2 million and \$4.1 million, respectively, of unrecognized tax benefits, if recognized, would affect the effective tax rate.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

|                                  |          |
|----------------------------------|----------|
| Balance at<br>January 1,<br>2007 | \$ 3,200 |
| Additions<br>based on tax        | 1,185    |

positions  
related to the  
current year

|                                                   |       |
|---------------------------------------------------|-------|
| Reductions for<br>tax positions of<br>prior years | (263) |
|---------------------------------------------------|-------|

|                                             |                 |
|---------------------------------------------|-----------------|
| <b>Balance at<br/>December 31,<br/>2007</b> | <b>\$ 4,122</b> |
|---------------------------------------------|-----------------|

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**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 13 - INCOME TAXES (Continued)**

It is reasonably possible that the amount of the unrecognized benefit with respect to certain of our unrecognized tax positions will significantly increase or decrease within the next 12 months. These changes may be the result of settlement of ongoing audits or competent authority proceedings. At this time, an estimate of the range of the reasonably possible outcomes cannot be made.

At December 31, 2006 and 2007, our deferred tax assets and liabilities are comprised of the following items:

|                                              | 2006            | 2007            |
|----------------------------------------------|-----------------|-----------------|
| <b>Deferred tax assets, current</b>          |                 |                 |
| Inventory cost                               | \$ 728          | \$ 1,229        |
| Accrued expenses and accounts receivable     | 1,074           | 1,085           |
| Foreign tax credit                           | 1,100           | -               |
| Net operating loss carryforwards and other   | 1,294           | 1,200           |
| Share based compensation and others          | 454             | 1,659           |
| Total deferred tax assets, current           | \$ 4,650        | \$ 5,173        |
| <b>Deferred tax assets, non-current</b>      |                 |                 |
| Plant, equipment and intangible assets       | \$ 2,050        | \$ 544          |
| Foreign tax credit                           | 6,506           | 7,976           |
| Research and development tax credit          | 1,434           | 1,868           |
| Net operating loss carryforwards             | 4,549           | 1,887           |
| Share based compensation and others          | (2,108)         | 4,078           |
|                                              | 12,431          | 16,353          |
| Valuation allowance                          | -               | (5,043)         |
| Total deferred tax assets, non-current       | \$ 12,431       | \$ 11,310       |
| <b>Deferred tax liabilities, non-current</b> |                 |                 |
| Step up in basis - acquisition               | (2,366)         | (2,284)         |
| Convertible debt interest                    | (1,298)         | (5,785)         |
| U.S. tax on undistributed foreign earnings   | (3,339)         | -               |
| Total deferred tax liabilities, non-current  | \$ (7,003)      | \$ (8,069)      |
| <b>Net deferred tax assets, non-current</b>  | <b>\$ 5,428</b> | <b>\$ 3,241</b> |



**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 13 - INCOME TAXES** (Continued)

Funds repatriated from foreign subsidiaries to the U.S. may be subject to Federal and state income taxes. On October 22, 2004, the President of the United States signed the American Jobs Creation Act (AJCA) into law. Originally intended to repeal the extraterritorial income (ETI) exclusion, which had triggered tariffs by the European Union, the AJCA expanded to cover a wide range of business tax issues. Among other items, the AJCA establishes a phased repeal of the ETI, a new incentive tax deduction for U.S. corporations to repatriate cash from foreign subsidiaries at a reduced tax rate (a deduction equal to 85% of cash dividends received in the year elected that exceeds a base-period amount) and significantly revises the taxation of U.S. companies doing business abroad. Under the guidelines of the AJCA, we developed a required domestic reinvestment plan, covering items such as U.S. bank debt repayment, U.S. capital expenditures and U.S. research and development activities, among others, to cover the dividend repatriation. During 2005, we repatriated \$24.0 million from our foreign subsidiaries under the AJCA guidelines.

At of December 31, 2006, accumulated and undistributed earnings of Diodes-China and Diodes-Shanghai were approximately \$67.0 million (including \$28.5 million of restricted earnings, which are not available for dividends), which we considered as a permanent investment, and we had recorded \$3.3 million in additional U.S. taxes, primarily for earnings of Diodes-Hong Kong.

With the establishment of the holding companies in 2007, the Company now intends to permanently reinvest overseas all of its earnings from its foreign subsidiaries. Accordingly, the \$3.3 million deferred tax liability was reversed during 2007 and U.S. taxes are no longer being recorded on undistributed foreign earnings.

As of December 31, 2007, the Company has undistributed earnings from its non-U.S. operations of approximately \$167 million (including \$28.5 million of restricted earnings which are not available for dividends). Additional Federal and state income taxes of approximately \$40 million would be required should such earnings be repatriated to the U.S. parent.

For the years ended December 31, 2005 and 2006, we recorded tax benefits related to the exercise of non-qualified stock options and the disqualified disposition of incentive stock options, which were recorded as a credit to additional paid-in capital in the amount of \$2.9 million and \$6.7 million, respectively. No tax benefit was recorded for the tax year ended December 31, 2007.

At December 31, 2007, we had Federal and state net operating loss (NOL) carryforwards of approximately \$39.0 million and \$37.0 million, respectively, available to offset future regular and alternative minimum taxable income. The Federal NOL carryforwards will begin to expire in 2017 and the state NOL carryforwards will begin to expire in 2013. Furthermore, the tax benefits of approximately \$22.8 million of NOLs related to stock option exercises in 2007 will be credited to additional paid-in capital when realized.

At December 31, 2007, we had Federal and state tax credit carryforwards of approximately \$9.8 million and \$0.4 million, respectively, available to offset future regular income and partially offset alternative minimum taxable income. During the year ended December 31, 2007, the Company determined that it was more likely than not that a portion of the Federal tax credit carryforwards would expire before they could be utilized. Accordingly, the Company recorded a \$5.0 million valuation allowance during the twelve months ended December 31, 2007. The Federal credit carryforwards will begin to expire in 2009 and the state credit carryforwards will begin to expire in 2020.

**NOTE 14 - EMPLOYEE BENEFIT PLANS**

We maintain a 401(k) retirement plan (the Plan) for the benefit of qualified employees at our U.S. locations. Employees who participate may elect to make salary deferral contributions to the Plan up to 100% of the employees' eligible payroll subject to annual Internal Revenue Code maximum limitations. We make a matching contribution of \$1 for every \$2 contributed by the participant up to 6% (3% maximum matching) of the participant's eligible payroll. In addition, we may make a discretionary contribution to the entire qualified employee pool, in accordance with the Plan.

As stipulated by the regulations of the People's Republic of China, we maintain a retirement plan pursuant to the local municipal government for the employees in China. We are required to make contributions to the retirement plan at a rate of 22.5% of the employee's eligible payroll. Pursuant to the Taiwan Labor Standard Law and Factory Law, we maintain a retirement plan for the employees in Taiwan. We make contributions at a rate of 6% of the employee's eligible payroll.

For the years ended December 31, 2005, 2006, and 2007, total amounts expensed under these plans were approximately \$1.8 million, \$2.6 million and \$2.9 million, respectively.

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 15 - SHARE-BASED COMPENSATION**

We maintain share-based compensation plans for our Board of Directors (“Directors”), officers, and key employees, which provide for stock options and stock awards under our 1993 ISO Plan, 1993 NQO Plan, and 2001 Omnibus Equity Incentive Plan.

**Stock Options** - Through March 31, 2006, substantially all stock options granted vest in equal annual installments over a three-year period and expire ten years after the grant date. Beginning April 1, 2006, substantially all stock options granted vest in equal annual installments over a four-year period and expire ten years after the grant date.

Beginning in fiscal year 2006, we adopted SFAS No. 123R, “Share-Based Payments” (SFAS 123R), on a modified prospective transition method to account for our employee stock options. Under the modified prospective transition method, fair value of new and previously granted but unvested stock options are recognized as compensation expense in the income statement, and prior period results are not restated, and thus do not include the additional compensation expense. In the year ended December 31, 2006, operating income decreased by \$6.5 million, net income decreased by \$5.4 million (net of tax benefits recognized \$1.1 million), and diluted earnings per share were reduced by approximately \$0.10. In the year ended December 31, 2007, operating income decreased by \$5.6 million, net income decreased by \$4.3 million (net of tax benefits recognized \$1.3 million), and diluted earnings per share were reduced by approximately \$0.07. For the years ended December 31, 2006 and 2007, share-based compensation expense associated with our stock options are as follows:

|                                               | 2006            | 2007            |
|-----------------------------------------------|-----------------|-----------------|
| Selling, general and administrative expense   | \$ 5,394        | \$ 4,824        |
| Research and development expense              | 603             | 463             |
| Cost of goods sold                            | 469             | 273             |
| <b>Total share-based compensation expense</b> | <b>\$ 6,466</b> | <b>\$ 5,560</b> |

Share-based compensation expense for stock options granted during 2005, 2006 and 2007 were calculated on the date of grant using the following weighted-average forfeiture rates, and the Black-Scholes option-pricing model using the following weighted-average assumptions:

|                         | 2005   | 2006   | 2007   |
|-------------------------|--------|--------|--------|
| Expected volatility     | 60.00% | 54.34% | 54.52% |
| Expected term (years)   | 5.00   | 5.88   | 6.63   |
| Risk free interest rate | 3.85%  | 4.73%  | 4.91%  |
| Forfeiture rate         | 2.54%  | 2.56%  | 2.50%  |
| Dividend yield          | N/A    | N/A    | N/A    |

Expected volatility - We estimate expected volatility using historical volatility. Public trading volume on options in our stock is not material. As a result, we determined that utilizing an implied volatility factor would not be appropriate. We calculate historical volatility for the period that is commensurate with the option's expected term assumption.

Expected term - We have evaluated expected term based on history and exercise patterns across its demographic population. We believe that this historical data is the best estimate of the expected term of a new option. The expected term for officers and Directors is 6.94 years, while the expected term for all other employees is 4.66 years.

Risk free interest rate - We estimate the risk-free interest rate based on zero-coupon U.S. treasury securities for a period that is commensurate with the expected term assumption.

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 15 - SHARE-BASED COMPENSATION (Continued)**

Forfeiture rate - The amount of stock-based compensation recognized during a period is based on the value of the portion of the awards that are ultimately expected to vest as SFAS 123R requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The term “forfeitures” is distinguished from “cancellations” or “expirations” and represents only the unvested portion of the surrendered option. We have applied an annual forfeiture rate of 2.54%, 2.56%, and 2.50% to all unvested options as of December 31, 2005, 2006, and 2007, respectively. This analysis will be re-evaluated at least annually, and the forfeiture rate will be adjusted as necessary.

Dividend yield - We historically have not paid a cash dividend; therefore this input is not applicable.

Discount for post vesting restrictions - This input is not applicable.

For the years ended December 31, 2005, 2006 and 2007, we granted stock options to purchase 1.2 million, 0.4 million and 0.3 million shares of our common stock, respectively, which vest in equal annual installments over a three or four-year period and expire ten years from the date of grant. The weighted-average grant-date fair value of options granted during 2005, 2006 and 2007 was \$8.1, \$13.0, and \$14.7, respectively. The total intrinsic value (actual gain) of options exercised during 2005, 2006 and 2007 was approximately \$11.9 million, \$23.2 million, and \$26.7 million, respectively.

At December 31, 2007, un-amortized compensation expense related to unvested options, net of estimated forfeitures, was approximately \$7.3 million. The weighted average period over which share-based compensation expense related to these options will be recognized is 2.5 years.

A summary of our stock option plans as of December 31 is as follows:

| Stock options                           | Shares       | Weighted<br>Average<br>Exercise<br>Price | Weighted Average<br>Remaining Contractual<br>Term (years) | Aggregate<br>Intrinsic<br>Value |
|-----------------------------------------|--------------|------------------------------------------|-----------------------------------------------------------|---------------------------------|
| Outstanding at January 1, 2005          | 6,163        | \$ 4.73                                  | 6.70                                                      | \$ 20,727                       |
| Granted                                 | 1,250        | 14.89                                    |                                                           |                                 |
| Exercised                               | (1,182)      | 3.51                                     |                                                           | 11,902                          |
| Forfeited or expired                    | (92)         | 8.74                                     |                                                           |                                 |
| <b>Outstanding at December 31, 2005</b> | <b>6,139</b> | <b>6.97</b>                              | <b>6.74</b>                                               | <b>84,277</b>                   |
| Outstanding at January 1, 2006          | 6,139        | 6.97                                     |                                                           |                                 |
| Granted                                 | 365          | 23.05                                    |                                                           |                                 |
| Exercised                               | (1,055)      | 4.14                                     |                                                           | 23,164                          |
| Forfeited or expired                    | (81)         | 16.03                                    |                                                           |                                 |
| <b>Outstanding at December 31, 2006</b> | <b>5,368</b> | <b>8.49</b>                              | <b>6.36</b>                                               | <b>81,396</b>                   |
| <b>Exercisable at December 31, 2006</b> | <b>3,910</b> | <b>5.97</b>                              | <b>5.57</b>                                               | <b>69,161</b>                   |
| Outstanding at January 1, 2007          | 5,368        | 8.49                                     |                                                           |                                 |
| Granted                                 | 265          | 24.96                                    |                                                           |                                 |
| Exercised                               | (1,260)      | 6.04                                     |                                                           | 26,722                          |

|                                         |                 |              |                |               |
|-----------------------------------------|-----------------|--------------|----------------|---------------|
| Forfeited or expired                    | (105)           | 19.53        |                |               |
| <b>Outstanding at December 31, 2007</b> | <b>4,268 \$</b> | <b>10.06</b> | <b>5.95 \$</b> | <b>85,393</b> |
| <b>Exercisable at December 31, 2007</b> | <b>3,411 \$</b> | <b>7.55</b>  | <b>5.36 \$</b> | <b>76,814</b> |

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**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 15 - SHARE-BASED COMPENSATION** (Continued)

Prior to our adoption of SFAS 123R, SFAS No. 123, "Accounting for Stock-Based Compensation" (SFAS 123) provided an alternative to APB Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25), in accounting for stock-based compensation issued to employees. SFAS 123 provided for a fair value based method of accounting for employee stock options and similar equity instruments. However, companies that continued to account for stock-based compensation arrangements under APB 25 were required by SFAS 123 to disclose, in the notes to financial statements, the pro forma effects on net income and net income per share as if the fair value based method prescribed by SFAS 123 had been applied. Prior to our adoption of SFAS 123R, we accounted for stock-based compensation using the provisions of APB 25 and presented the pro forma information required by SFAS 123 as amended by SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure" (SFAS 148).

Had we accounted for stock-based compensation plans using the fair value based accounting method described by SFAS 123R for the periods prior to fiscal year 2006, our earnings per share for 2005 would have approximated the following:

|                                                                                                                             | 2005             |
|-----------------------------------------------------------------------------------------------------------------------------|------------------|
| <b>Net income, as reported</b>                                                                                              | \$ 33,329        |
| Deduct: Total stock-based compensation expense determined under fair value based method for all awards, net of tax benefits | (2,805)          |
| <b>Pro forma net income</b>                                                                                                 | <b>\$ 30,524</b> |
| <b>Earnings per share:</b>                                                                                                  |                  |
| <b>Basic</b>                                                                                                                |                  |
| - As reported                                                                                                               | \$ 0.96          |
| - Pro forma                                                                                                                 | \$ 0.88          |
| <b>Diluted</b>                                                                                                              |                  |
| - As reported                                                                                                               | \$ 0.86          |
| - Pro forma                                                                                                                 | \$ 0.79          |

As of December 31, 2007, approximately 3.4 million of the 4.3 million outstanding stock options were exercisable. The following table summarizes information about stock options outstanding at December 31, 2007:

| Plan | Range of exercise prices | Number outstanding | Weighted average remaining contractual life (years) | Weighted average exercise price |
|------|--------------------------|--------------------|-----------------------------------------------------|---------------------------------|
| '93  |                          |                    |                                                     |                                 |
| NQQ  | \$ 1.33-7.09             | 377                | 2.19                                                | \$ 4.73                         |
|      | 1.85-7.09                | 329                | 2.93                                                | 5.22                            |

'93

ISO

'01

|      |            |       |      |       |
|------|------------|-------|------|-------|
| Plan | 2.47-28.45 | 3,562 | 6.62 | 11.08 |
|------|------------|-------|------|-------|

|       |               |       |      |          |
|-------|---------------|-------|------|----------|
| Total | \$ 1.33-28.45 | 4,268 | 5.95 | \$ 10.06 |
|-------|---------------|-------|------|----------|

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**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 15 - SHARE-BASED COMPENSATION (Continued)**

The following summarizes information about stock options exercisable at December 31, 2007:

| Plan     | Range of exercise prices | Number outstanding | Weighted average remaining contractual life (years) | Weighted average exercise price |
|----------|--------------------------|--------------------|-----------------------------------------------------|---------------------------------|
| '93 NQQ  | \$ 1.33-7.09             | 377                | 2.19                                                | \$ 4.73                         |
| '93 ISO  | 1.85-7.09                | 329                | 2.93                                                | 5.22                            |
| '01 Plan | 2.47-28.45               | 2,705              | 6.08                                                | 8.23                            |
| Total    | \$ 1.33-28.45            | 3,411              | 5.36                                                | \$ 7.55                         |

**Share Grants** - Restricted stock awards and restricted stock units generally vest in equal annual installments over a four-year period. A summary of our non-vested share grants in 2005, 2006 and 2007 are presented below:

| Restricted Stock Grants               | Shares       | Weighted-Average Grant-Date Fair Value |
|---------------------------------------|--------------|----------------------------------------|
| Nonvested at January 1, 2005          | -            | \$ -                                   |
| Granted                               | 495          | 11.53                                  |
| Vested                                | -            | -                                      |
| Forfeited                             | -            | -                                      |
| <b>Nonvested at December 31, 2005</b> | <b>495</b>   | <b>\$ 11.53</b>                        |
| Nonvested at January 1, 2006          | 495          | \$ 11.53                               |
| Granted                               | 364          | 23.26                                  |
| Vested                                | -            | -                                      |
| Forfeited                             | (7)          | 23.31                                  |
| <b>Nonvested at December 31, 2006</b> | <b>852</b>   | <b>\$ 16.45</b>                        |
| Nonvested at January 1, 2007          | 852          | \$ 16.45                               |
| Granted                               | 297          | 26.00                                  |
| Vested                                | (84)         | 23.19                                  |
| Forfeited                             | (47)         | 23.73                                  |
|                                       | <b>1,018</b> | <b>\$ 18.34</b>                        |

**Nonvested at  
December 31, 2007**

For each of the years ended December 31 of 2005, 2006 and 2007, there were \$0, \$1.8 million and \$4.3 million of total recognized share-based compensation expense related to restricted stock arrangements granted under the plans. The total of unrecognized share-based compensation expense as of December 31 of 2005, 2006 and 2007 was \$3.9 million, \$10.2 million and \$12.9 million, respectively. This cost is expected to be recognized over a weighted average period of 2.8 years.

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**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 16 - RELATED PARTY TRANSACTIONS**

We conduct business with one related party company, Lite-On Semiconductor Corporation (“LSC”) (and its subsidiaries and affiliates) and one significant company, Zi Yun International (Zi Yun) (formerly Keylink International) (and its subsidiaries and affiliates). LSC is our largest stockholder and owns 21.6% of our outstanding Common Stock as of December 31, 2007. Zi Yun is our 5% joint venture partner in Diodes-China and Diodes-Shanghai. C.H. Chen, our former President and Chief Executive Officer, and current Vice Chairman of our Board of Directors, is also Vice Chairman of LSC. M.K. Lu, a member of our Board of Directors until May 2007, served as President of LSC until May 2007, while Raymond Soong, the Chairman of our Board of Directors, is the Chairman of LSC as well as Chairman of Lite-On Technology Corporation, a significant shareholder of LSC. L.P. Hsu, a member of our Board since May 2007 serves as a consultant to LSC. We consider our relationship with LSC, a member of the Lite-On Group of companies, to be mutually beneficial and we plan to continue our strategic alliance together as we have since 1991.

The Audit Committee of our Board of Directors conducts an appropriate review of all related party transactions for potential conflict of interest situations on an ongoing basis, all in accordance with such procedures as the Audit Committee may adopt from time to time. We believe that all related party transactions are on terms no less favorable to us than would be obtained from unaffiliated third parties.

**Lite-On Semiconductor Corporation (LSC) -** We sold silicon wafers to LSC totaling 9.6%, 6.5% and 6.2% of total sales for the years ended December 31, 2005, 2006 and 2007, respectively, making LSC our largest customer. Also for the years ended December 31, 2005, 2006 and 2007, 14.7%, 13.0% and 11.3%, respectively, of our net sales were from discrete semiconductor products purchased from LSC for subsequent sale by us, making LSC our largest outside supplier. We also rent warehouse space in Hong Kong from a member of the Lite-On Group, which also provides us with warehousing services at that location. For 2005, 2006 and 2007, we reimbursed this entity in aggregate amounts of \$0.3 million, \$0.5 million and \$0.5 million, respectively, for these items. We believe such transactions are on terms no less favorable to us than could be obtained from unaffiliated third parties.

Net sales to, and purchases from, LSC were as follows for years ended December 31:

|           | 2005      | 2006      | 2007      |
|-----------|-----------|-----------|-----------|
| Net sales | \$ 20,608 | \$ 22,374 | \$ 24,809 |
| Purchases | \$ 22,289 | \$ 48,778 | \$ 49,224 |

In December 2000, we acquired FabTech, Inc. from LSC for approximately \$6.0 million cash plus \$19.0 million in assumed debt (the debt was due primarily to LSC). As per the terms of the acquisition, we entered into several management incentive agreements with members of FabTech's management, which provided FabTech's management with guaranteed annual payments as well as contingent bonuses based on the annual profitability of FabTech, subject to a maximum annual amount. Any portion of the guaranteed and contingent liability paid by FabTech was reimbursed by LSC. The final year of the management incentive agreements was 2004, with final payment made on March 31, 2005. LSC reimbursed us \$0.4 million in 2003, 2004, and 2005 for each of 2002, 2003 and 2004, for amounts paid by us under these management incentive agreements.

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 16 - RELATED PARTY TRANSACTIONS (Continued)**

**Zi Yun International Pte. Ltd. (Zi Yun)** - We sell product to, and purchase inventory from, companies owned by our 5% Diodes-China and Diodes-Shanghai minority shareholder. We sold silicon wafers to companies owned by Zi Yun totaling 0.6%, 0.4% and 0.6% of total sales for the years ended December 31, 2005, 2006 and 2007, respectively. Also for the years ended December 31, 2005, 2006 and 2007, 3.0%, 2.3% and 1.5%, respectively of our net sales were from discrete semiconductor products purchased from companies owned by Zi Yun. In addition, Diodes-China and Diodes-Shanghai lease their manufacturing facilities from, and subcontract a portion of their manufacturing process (metal plating and environmental services) to, Zi Yun. We also pay a consulting fee to Zi Yun. The aggregate amounts for these services for the years ended December 31, 2005, 2006 and 2007 were \$6.6 million, \$7.9 million and \$9.4 million, respectively. We believe such transactions are on terms no less favorable to us than could be obtained from unaffiliated third parties.

Net sales to, and purchases from, companies owned by Zi Yun were as follows for years ended December 31st:

|           | 2005     | 2006     | 2007            |
|-----------|----------|----------|-----------------|
| Net sales | \$ 1,336 | \$ 1,481 | \$ <b>2,586</b> |
| Purchases | \$ 3,882 | \$ 5,973 | \$ <b>6,005</b> |

Accounts receivable from, and accounts payable to, LSC and Zi Yun were as follows as of December 31st:

|                      | 2006            | 2007             |
|----------------------|-----------------|------------------|
| Accounts receivable  |                 |                  |
| LSC                  | \$ 4,848        | \$ 3,526         |
| Zi Yun International | 1,299           | 1,879            |
|                      | \$ <b>6,147</b> | \$ <b>5,405</b>  |
| Accounts payable     |                 |                  |
| LSC                  | \$ 8,646        | \$ 8,906         |
| Zi Yun International | 3,474           | 4,229            |
|                      | \$ 12,120       | \$ <b>13,135</b> |

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 17 - SEGMENT INFORMATION**

An operating segment is defined as a component of an enterprise about which separate financial information is available that is evaluated regularly by the chief decision maker, or decision-making group, in deciding how to allocate resources and in assessing performance. Our chief decision-making group consists of the President and Chief Executive Officer, Chief Financial Officer, Senior Vice President of Operations, Senior Vice President of Sales and Marketing, Asia President, and Senior Vice President of Finance. For financial reporting purposes, we operate in a single segment, standard semiconductor products, through our various manufacturing and distribution facilities. We aggregated our products since the products are similar and have similar economic characteristics, and the products are similar in production process and share the same customer type.

Our operations include the domestic operations (Diodes Incorporated and Diodes-FabTech) located in the U.S. and the Asia operations (Diodes-Taiwan located in Taipei, Taiwan, Diodes-Anachip located in Hsinchu, Taiwan, Diodes-China and Diodes-Shanghai both located in Shanghai, China, and Diodes-Hong Kong located in Hong Kong, China). For reporting purposes, European operations, which accounted for approximately 2.6%, 3.3% and 4.2% of total sales for the years ended December 31, 2005, 2006 and 2007, respectively, are consolidated into the domestic (North America) operations.

| <b>2007</b>            | <b>Asia</b> | <b>U.S.A.</b> | <b>Consolidated</b> |
|------------------------|-------------|---------------|---------------------|
| Total Sales            | \$ 514,195  | \$ 122,274    | \$ <b>636,469</b>   |
| Inter-company sales    | (211,913)   | (23,397)      | <b>(235,310)</b>    |
| Net sales              | \$ 302,282  | \$ 98,877     | \$ <b>401,159</b>   |
| Long-lived assets, net | \$ 105,100  | \$ 27,950     | \$ <b>133,050</b>   |
| Assets                 | \$ 240,196  | \$ 466,169    | \$ <b>706,365</b>   |
| <b>2006</b>            | <b>Asia</b> | <b>U.S.A.</b> | <b>Consolidated</b> |
| Total Sales            | \$ 405,002  | \$ 117,867    | \$ 522,869          |
| Inter-company sales    | (158,131)   | (21,430)      | (179,561)           |
| Net sales              | \$ 246,871  | \$ 96,437     | \$ 343,308          |
| Long-lived assets, net | \$ 105,020  | \$ 26,148     | \$ 131,168          |
| Assets                 | \$ 241,979  | \$ 380,160    | \$ 622,139          |
| <b>2005</b>            | <b>Asia</b> | <b>U.S.A.</b> | <b>Consolidated</b> |
| Total Sales            | \$ 238,825  | \$ 90,707     | \$ 329,532          |
| Inter-company sales    | (98,427)    | (16,340)      | (114,767)           |
| Net sales              | \$ 140,398  | \$ 74,367     | \$ 214,765          |

|             |    |         |    |         |            |
|-------------|----|---------|----|---------|------------|
| Long-lived  |    |         |    |         |            |
| assets, net | \$ | 58,283  | \$ | 15,737  | \$ 74,020  |
| Assets      | \$ | 139,863 | \$ | 149,652 | \$ 289,515 |

The accounting policies of the operating entities are the same as those described in the summary of significant accounting policies. Revenues are attributed to geographic areas based on the location of the market producing the revenues.

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 17 - SEGMENT INFORMATION** (Continued)

**Geographic Information**

Revenues were derived from (shipped to) customers located in the following countries. "All Others" represents countries with less than 10% of total revenues each (in thousands):

| 2007          | Revenue           | % of Total<br>Revenue |
|---------------|-------------------|-----------------------|
| China         | \$ 156,183        | 38.9%                 |
| Taiwan        | 102,562           | 25.6%                 |
| United States | 81,408            | 20.3%                 |
| All Others    | 61,006            | 15.2%                 |
| <b>Total</b>  | <b>\$ 401,159</b> | <b>100.0%</b>         |

| 2006          | Revenue           | % of<br>Total<br>Revenue |
|---------------|-------------------|--------------------------|
| China         | \$ 118,303        | 34.5%                    |
| Taiwan        | 96,401            | 28.1%                    |
| United States | 76,357            | 22.2%                    |
| All Others    | 52,247            | 15.2%                    |
| <b>Total</b>  | <b>\$ 343,308</b> | <b>100.0%</b>            |

| 2005          | Revenue           | % of<br>Total<br>Revenue |
|---------------|-------------------|--------------------------|
| China         | \$ 68,050         | 31.7%                    |
| Taiwan        | 59,838            | 27.9%                    |
| United States | 54,981            | 25.6%                    |
| All Others    | 31,896            | 14.8%                    |
| <b>Total</b>  | <b>\$ 214,765</b> | <b>100.0%</b>            |

**Major customers** - In 2007, we sold finished goods and silicon wafers to LSC totaling 6.2% (6.5% in 2006 and 9.6% in 2005) of our total net sales, thus LSC is our largest customer. No customer accounted for 10% or greater of our total net sales in 2005, 2006, and 2007.

**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 18- COMMITMENTS AND CONTINGENCIES**

**Operating leases** - We lease offices, manufacturing plants and warehouses under operating lease agreements expiring through December 2012. Rental expense amounted to approximately \$3.7 million, \$4.0 million and \$4.3 million for the years ended December 31, 2005, 2006, and 2007, respectively.

Future minimum lease payments under non-cancelable operating leases at December 31, 2007 are:

|                     |           |
|---------------------|-----------|
| 2008                | \$ 4,512  |
| 2009                | 3,027     |
| 2010                | 2,159     |
| 2011                | 2,151     |
| 2012 and thereafter | 3,132     |
|                     | \$ 14,981 |

**Purchase commitments** - We have entered into non-cancelable purchase contracts for capital expenditures, primarily for manufacturing equipment in China, for approximately \$1.8 million at December 31, 2007.

**Legal proceedings** - The Company is involved, from time to time, in claims, proceedings and litigation arising in the normal course of business. The Company believes that, to the extent that it exists, any pending or threatened litigation involving the Company or its properties will not likely have a material adverse effect on the Company's financial condition or results of operations.



**DIODES INCORPORATED AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 19 - SELECTED QUARTERLY FINANCIAL DATA (Unaudited)**

|                           | March 31  | Quarter Ended |            | Dec. 31    |
|---------------------------|-----------|---------------|------------|------------|
|                           |           | June 30       | Sept. 30   |            |
| <b>Fiscal 2007</b>        |           |               |            |            |
| <b>Net sales</b>          | \$ 92,020 | \$ 96,283     | \$ 105,264 | \$ 107,591 |
| <b>Gross profit</b>       | 29,524    | 30,678        | 34,152     | 36,024     |
| <b>Net income</b>         | 13,009    | 12,249        | 16,101     | 18,298     |
| <b>Earnings per share</b> |           |               |            |            |
| <b>Basic</b>              | \$ 0.33   | \$ 0.31       | \$ 0.40    | \$ 0.46    |
| <b>Diluted</b>            | 0.31      | 0.29          | 0.38       | 0.43       |

|                           | March 31  | Quarter Ended |           | Dec. 31   |
|---------------------------|-----------|---------------|-----------|-----------|
|                           |           | June 30       | Sept. 30  |           |
| <b>Fiscal 2006</b>        |           |               |           |           |
| <b>Net sales</b>          | \$ 73,589 | \$ 82,712     | \$ 92,575 | \$ 94,432 |
| <b>Gross profit</b>       | 24,214    | 27,433        | 30,696    | 31,549    |
| <b>Net income</b>         | 9,312     | 11,385        | 12,770    | 14,675    |
| <b>Earnings per share</b> |           |               |           |           |
| <b>Basic</b>              | \$ 0.25   | \$ 0.30       | \$ 0.33   | \$ 0.38   |
| <b>Diluted</b>            | 0.23      | 0.27          | 0.30      | 0.35      |

|                           | March 31  | Quarter Ended |           | Dec. 31   |
|---------------------------|-----------|---------------|-----------|-----------|
|                           |           | June 30       | Sept. 30  |           |
| <b>Fiscal 2005</b>        |           |               |           |           |
| <b>Net sales</b>          | \$ 48,600 | \$ 50,598     | \$ 54,200 | \$ 61,367 |
| <b>Gross profit</b>       | 16,596    | 17,496        | 18,877    | 21,407    |
| <b>Net income</b>         | 7,240     | 7,665         | 8,383     | 10,041    |
| <b>Earnings per share</b> |           |               |           |           |
| <b>Basic</b>              | \$ 0.23   | \$ 0.23       | \$ 0.25   | \$ 0.27   |
| <b>Diluted</b>            | 0.21      | 0.21          | 0.23      | 0.24      |

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

D I O D E S  
INCORPORATED  
(Registrant)

By: /s/ Keh-ShewFebruary  
Lu 29, 2008  
KEH-SHEW LU  
President and Chief  
Executive Officer  
( P r i n c i p a l  
Executive Officer)

By: /s/ Carl C. February  
Wertz 29, 2008  
CARL C. WERTZ  
Chief Financial  
Officer, Treasurer,  
and Secretary  
(Principal Financial  
and Accounting  
Officer)

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below hereby constitutes and appoints Dr. Keh-Shew Lu, President and Chief Executive Officer and Carl C. Wertz, Chief Financial Officer, Treasurer, and Secretary, his true and lawful attorneys-in-fact and agents, with full power of substitution, to sign and execute on behalf of the undersigned and any and all amendments to this report, and to perform any acts necessary in order to file the same, with all exhibits thereto and other documents in connection therewith with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents full power and authority to do and perform each and every act and thing requested and necessary to be done in connection therewith, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorney-in-fact and agents, or their or his or her substitutes, shall do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on February 29, 2008.

/s/ Keh-Shew,  
Lu  
KEH-SHEW  
LU  
President and  
C h i e f  
E x e c u t i v e  
Officer

(Principal  
Executive  
Officer)

By: /s/ Carl  
C. Wertz  
C A R L C .  
W E R T Z  
C h i e f  
F i n a n c i a l  
O f f i c e r ,  
T r e a s u r e r ,  
a n d S e c r e t a r y  
(Principal  
Financial and  
Accounting  
Officer)

|                                                                                      |                                                    |
|--------------------------------------------------------------------------------------|----------------------------------------------------|
| /s/ Raymond<br>Soong<br>RAYMOND<br>SOONG<br>Chairman of<br>the Board of<br>Directors | /s/ C.H.<br>Chen<br>C . H .<br>C H E N<br>Director |
|--------------------------------------------------------------------------------------|----------------------------------------------------|

|                                                                    |                                         |
|--------------------------------------------------------------------|-----------------------------------------|
| /s/ Michael R.<br>Giordano<br>MICHAEL<br>R<br>GIORDANO<br>Director | /s/ L.P.<br>Hsu<br>L.P. HSU<br>Director |
|--------------------------------------------------------------------|-----------------------------------------|

|                                                  |                                                      |
|--------------------------------------------------|------------------------------------------------------|
| /s/ Keh-Shew<br>Lu<br>KEH-SHEW<br>LU<br>Director | /s/ John M.<br>Stich<br>JOHN M.<br>STICH<br>Director |
|--------------------------------------------------|------------------------------------------------------|

/s/ Shing Mao  
SHING MAO  
Director

## INDEX TO EXHIBITS

### Number Description

- 2.1 Stock Purchase Agreement dated as of December 20, 2005, by and among DII Taiwan Corporation Ltd., Anachip Corporation, Lite-On Semiconductor Corporation, Shin Sheng Investment Limited and Sun Shining Investment Corp.<sup>(1)</sup>
- 2.2 Asset Purchase Agreement dated as of October 18, 2006, by and among DII Taiwan Corporation Ltd., APD Semiconductor, Inc. and Certain Shareholders Thereof, and entered into by the parties on October 19, 2006 <sup>(2)</sup>
- 2.3 Amendment to the Asset Purchase Agreement, dated October 18, 2006, by and among Diodes Incorporated, DII Taiwan Corporation Ltd., APD Semiconductor, Inc. and APD Semiconductor (Asia) Inc., and entered into by the parties on October 19, 2006 <sup>(3)</sup>
- 2.4 Second Amendment to Asset Purchase Agreement dated as of October 31, 2006, by and among Diodes Incorporated, DII Taiwan Corporation Ltd., APD Semiconductor, Inc. and APD Semiconductor (Asia) Inc<sup>(4)</sup>
- 3.1 Certificate of Incorporation, as amended <sup>(5)</sup>
- 3.2 Amended By-laws of the Company dated July 19, 2007 <sup>(6)</sup>
- 4.1 Form of Certificate for Common Stock, par value \$0.66 2/3 per share <sup>(7)</sup>
- 4.2 Form of Convertible Senior Notes due 2026 <sup>(8)</sup>
- 4.3 Form of Indenture for the Convertible Senior Notes due 2026 <sup>(9)</sup>
- 10.1 \* Company's 401(k) Plan - Adoption Agreement<sup>(10)</sup>
- 10.2 \* Company's 401(k) Plan - Basic Plan Documentation #03<sup>(10)</sup>
- 10.3 \* Company's Incentive Bonus Plan<sup>(11)</sup>
- 10.4 \* Company's 1993 Non-Qualified Stock Option Plan<sup>(11)</sup>
- 10.5 \* Company's 1993 Incentive Stock Option Plan<sup>(10)</sup>
- 10.6 KaiHong Compensation Trade Agreement for SOT-23 Product <sup>(12)</sup>
- 10.7 KaiHong Compensation Trade Agreement for MELF Product <sup>(13)</sup>
- 10.8 Lite-On Power Semiconductor Corporation Distributorship Agreement <sup>(14)</sup>
- 10.9 Loan Agreement between the Company and FabTech Incorporated <sup>(15)</sup>
- 10.10 KaiHong Joint Venture Agreement between the Company and Mrs. J.H. Xing <sup>(15)</sup>
- 10.11 Quality Assurance Consulting Agreement between LPSC and Shanghai KaiHong Electronics Company, Ltd. <sup>(16)</sup>
- 10.12 Guaranty Agreement between the Company and Shanghai KaiHong Electronics Co., Ltd. <sup>(17)</sup>
- 10.13 Guaranty Agreement between the Company and Xing International, Inc. <sup>(17)</sup>
- 10.14 Bank Guaranty for Shanghai KaiHong Electronics Co., LTD <sup>(18)</sup>
- 10.15 Consulting Agreement between the Company and J.Y. Xing <sup>(19)</sup>
- 10.16 Diodes-Taiwan Relationship Agreement for FabTech Wafer Sales <sup>(20)</sup>
- 10.17 Volume Purchase Agreement dated as of October 25, 2000, between FabTech, Inc. and Lite-On Power Semiconductor Corporation <sup>(21)</sup>
- 10.18 Diodes Incorporated Building Lease - Third Amendment <sup>(22)</sup>
- 10.19\* 2001 Omnibus Equity Incentive Plan <sup>(23)</sup>
- 10.20 Sale and Leaseback Agreement between the Company and Shanghai Ding Hong Company, Ltd. <sup>(24)</sup>
- 10.21 Lease Agreement between the Company and Shanghai Ding Hong Company, Ltd. <sup>(24)</sup>
- 10.22 Lease Agreement for Plant #2 between the Company and Shanghai Ding Hong Electronic Equipment Limited <sup>(25)</sup>
- 10.23 \$5 Million Term Note with Union Bank <sup>(25)</sup>
- 10.24 First Amendment To Amended And Restated Credit Agreement <sup>(25)</sup>
- 10.25 Covenant Agreement between Union Bank and FabTech, Inc. <sup>(25)</sup>

- 10.26 Amendment to The Sale and Lease Agreement dated as January 31, 2002 with Shanghai Ding Hong Electronic Co., Ltd. <sup>(25)</sup>
- 10.27 Lease Agreement between Diodes Shanghai and Shanghai Yuan Hao Electronic Co., Ltd. <sup>(25)</sup>
- 10.28 Supplementary to the Lease agreement dated as September 30, 2003 with Shanghai Ding Hong Electronic Co., Ltd. <sup>(25)</sup>
- 10.29 Second Amendment to Amended and Restated Credit Agreement dated as of August 29, 2005, between Diodes Incorporated and Union Bank of California, N.A. <sup>(26)</sup>
- 10.30 Covenant Agreement dated as of August 29, 2005, between FabTech, Inc. and Union Bank of California, N.A. <sup>(26)</sup>
- 10.31 Revolving Note dated as of August 29, 2005, of Diodes Incorporated payable to Union Bank of California, N.A. <sup>(26)</sup>
- 10.32 Term Note dated as of August 29, 2005, of FabTech, Inc. payable to Union Bank of California, N.A. <sup>(26)</sup>
- 10.33 Security Agreement dated as of February 27, 2003, between the Company and Union Bank of California, N.A. <sup>(26)</sup>
- 10.34 Security Agreement dated as of February 27, 2003, between FabTech, Inc. and Union Bank of California, N.A. <sup>(26)</sup>
- 10.35 Continuing Guaranty dated as of December 1, 2000, between the Company and Union Bank of California, N.A. <sup>(26)</sup>

- 10.36 Continuing Guaranty dated as of December 1, 2000, between FabTech, Inc. and Union Bank of California, N.A. <sup>(26)</sup>
- 10.37\* Employment agreement between Diodes Incorporated and Dr. Keh-Shew Lu dated August 29, 2005<sup>(27)</sup>
- 10.38\* Employment agreement between Diodes Incorporated and Joseph Liu, dated August 29, 2005. <sup>(27)</sup>
- 10.39\* Employment agreement between Diodes Incorporated and Mark King, dated August 29, 2005. <sup>(27)</sup>
- 10.40\* Employment agreement between Diodes Incorporated and Carl Wertz, dated August 29, 2005. <sup>(27)</sup>
- 10.41\* Form of Indemnification Agreement between Diodes and its directors and executive officers.<sup>(27)</sup>
- 10.42 Wafer purchase Agreement dated January 10, 2006 between Diodes Incorporated Taiwan Co., Ltd and Lite-on Semiconductor Corporation<sup>(28)</sup>
- 10.43 Supplementary to the Lease Agreement dated on September 5, 2004 with Shanghai Ding Hong Electronic Co., Ltd. <sup>(29)</sup>
- 10.44 Supplementary to the Lease Agreement dated on June 28, 2004 with Shanghai Yuan Hao Electronic Co., Ltd. <sup>(29)</sup>
- 10.45 Agreement on Application, Construction and Transfer of Power Facilities, dated as of March 15, 2006, between the Company and Shanghai Yahong Electronic Co., Ltd <sup>(29)</sup>
- 10.46\* Amendment of 1993 Non-Qualified Stock Option Plan, the 1993 Incentive Stock Option Plan and the 2001 Equity Incentive Plan of the Company dated as of September 22, 2006<sup>(30)</sup>
- 10.47 Amended and Restated Lease Agreement dated as of September 1, 2006, between Diodes FabTech, Inc. with Townsend Summit, LLC<sup>(31)</sup>
- 10.48 Agreement on purchase of office building located in Taiwan dated April 14, 2006, between Diodes Taiwan and First International Computer, Inc. <sup>(31)</sup>
- 10.49\* Deferred Compensation Plan effective January 1, 2007 <sup>(32)</sup>
- 10.50 A Supplement dated January 1, 2007 to the Lease Agreement on Disposal of Waste and Scraps between Diodes Shanghai and Shanghai Yuan Hao Electronic Co., Ltd.
- 10.51 A Supplement dated January 1, 2007 to the Lease Agreement on Disposal of Waste and Scraps between Diodes China and Shanghai Ding Hong Electronic Co., Ltd
- 10.52 Plating Process Agreement made and entered into among Diodes China, Diodes Shanghai, Shanghai Ding Hong Electronic Co., Ltd. and Shanghai Micro-Surface Co., Ltd.
- 10.53 Supplementary Agreement dated December 31, 2007 to the Lease Agreement dated June, 28, 2004 for Leasing Diodes Shanghai New Building's Fourth and Fifth Floor between Diodes Shanghai and Shanghai Yuan Hao Electronic Co., Ltd.
- 10.54 Accommodation Building Fourth and Fifth Floor Lease Agreement dated December 31, 2007 between Diodes Shanghai and Shanghai Ding Hong Electronic Co., Ltd.
- 10.55 Consulting Agreement between the Company and Mr. M.K. Lu.
- 14 Code of Ethics for Chief Executive Officer and Senior Financial Officers <sup>(33)</sup>
- 21 Subsidiaries of the Registrant
- 23.1 Consent of Independent Registered Public Accounting Firm
- 31.1 Certification Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1933, adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1933, adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification Pursuant to 18 U.S.C. adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification Pursuant to 18 U.S.C. adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

- (1) Previously filed with Company's Form 8-K, filed with the Commission on December 21, 2005, which is hereby incorporated by reference.
- (2) Previously filed with Company's Form 8-K, filed with the Commission on October 24, 2006 which is hereby incorporated by reference.
- (3) Previously filed with Company's Form 8-K, filed with the Commission on October 24, 2006 which is hereby incorporated by reference.
- (4) Previously filed with Company's Form 8-K, filed with the Commission on November 7, 2006 which is hereby incorporated by reference.
- (5) Previously filed as Exhibit 3.1 of Amendment No. 1 to the Company's Registration Statement on Form S-3 (File No. 333-127833) filed on September 8, 2005, which is hereby incorporated by reference.
- (6) Previously filed with Company's Form 8-K, filed with the Commission on July 23, 2007, which is hereby incorporated by reference.
- (7) Previously filed as Exhibit 4.1 of the Company's Registration Statement on Form S-3 (Registration No. 333-127833 filed on August 25, 2005, which is hereby incorporated by reference.
- (8) Previously filed as Exhibit 4.1 of the Company's Registration Statement on Form S-3 (Registration No. 333-137803) filed on October 4, 2006, which is hereby incorporated by reference.

- (9) Previously filed as Exhibit 4.3 of the Company's Registration Statement on Form S-3 (Registration No. 333-137803) filed on October 4, 2006, which is hereby incorporated by reference.
- (10) Previously filed with Company's Form 10-K, filed with the Commission on March 31, 1995, which is hereby incorporated by reference.
- (11) Previously filed with Company's Form S-8, filed with the Commission on May 9, 1994, which is hereby incorporated by reference.
- (12) Previously filed as Exhibit 10.2 to Form 10-Q/A, filed with the Commission on October 27, 1995, which is hereby incorporated by reference.
- (13) Previously filed as Exhibit 10.3 to Form 10-Q/A, filed with the Commission on October 27, 1995, which is hereby incorporated by reference.
- (14) Previously filed as Exhibit 10.4 to Form 10-Q, filed with the Commission on July 27, 1995, which is hereby incorporated by reference.
- (15) Previously filed with Company's Form 10-K, filed with the Commission on April 1, 1996, which is hereby incorporated by reference.
- (16) Previously filed with Company's Form 10-Q, filed with the Commission on May 15, 1996, which is hereby incorporated by reference.
- (17) Previously filed with Company's Form 10-K, filed with the Commission on March 26, 1997, which is hereby incorporated by reference.
- (18) Previously filed with Company's Form 10-Q, filed with the Commission on August 11, 1998, which is hereby incorporated by reference.
- (19) Previously filed with Company's Form 10-Q, filed with the Commission on November 11, 1998, which is hereby incorporated by reference.
- (20) Previously filed with Company's Form 10-Q, filed with the Commission on August 10, 1999, which is hereby incorporated by reference.
- (21) Previously filed with Company's Form 8-K, filed with the Commission on December 14, 2000, which is hereby incorporated by reference.
- (22) Previously filed with Company's Form 10-Q, filed with the Commission on November 2, 2001, which is hereby incorporated by reference.
- (23) Previously filed with Company's Definitive Proxy Statement, filed with the Commission on April 27, 2001, which is hereby incorporated by reference.
- (24) Previously filed with Company's Form 10-Q, filed with the Commission on May 15, 2002, which is hereby incorporated by reference.
- (25)



Previously filed with Company's Form 10-Q, filed with the Commission on August 9, 2004, which is hereby incorporated by reference.

- (26) Previously filed with Company's Form 8-K, filed with the Commission on September 2, 2005, which is hereby incorporated by reference.
- (27) Previously filed with Company's Form 8-K, filed with the Commission on September 2, 2005, which is hereby incorporated by reference.
- (28) Previously filed with Company's Form 8-K, filed with the Commission on January 12, 2006.
- (29) Previously filed with Company's Form 10-Q, filed with the Commission on May 10, 2006 which is hereby incorporated by reference.
- (30) Previously filed with Company's Form 8-K, filed with the Commission on September 26, 2006 which is hereby incorporated by reference.
- (31) Previously filed with Company's Form 8-K, filed with the Commission on October 11, 2006 which is hereby incorporated by reference.
- (32) Previously filed with Company's Form 8-K, filed with the Commission on January 8, 2007.
- (33) Provided in the Corporate Governance portion of the Investor Relations section of the Company's website at <http://www.diodes.com>.

\* Constitute management contracts, or compensatory plans or arrangements, which are required to be filed pursuant to Item 601 of Regulation S-K.