DIODES INC /DEL/
Form 10-Q
November 09, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended **September 30, 2006**

Or

o 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	**95-2039518**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
3050 East Hillcrest Drive Westlake Village, California	**91362**
(Address of principal executive offices)	(Zip code)

(805) 446-4800
(Registrant's telephone number, including area code)

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 x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one)

Large accelerated filer x Accelerated filer o Non-accelerated filer o

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

The number of shares of the registrant's Common Stock outstanding as of November 3, 2006 was 25,939,514.

PART I - FINANCIAL INFORMATION

Item 1 - Financial Statements

DIODES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED BALANCE SHEET

ASSETS

		December 31, 2005		September 30, 2006 (unaudited)
CURRENT ASSETS				
Cash and cash equivalents	$	73,288,000	$	**53,157,000**
Short-term investments		40,348,000		**56,139,000**
Total cash and short-term investments		113,636,000		**109,296,000**
Accounts receivable				
Customers		48,348,000		**70,049,000**
Related parties		6,804,000		**5,554,000**
		55,152,000		**75,603,000**
Less: Allowance for doubtful receivables		(534,000)		**(675,000)**
		54,618,000		**74,928,000**
Inventories		24,611,000		**45,767,000**
Deferred income taxes, current		2,541,000		**2,565,000**
Prepaid expenses and other current assets		5,326,000		**7,104,000**
Total current assets		200,732,000		**239,660,000**
PROPERTY, PLANT AND EQUIPMENT, at cost, net of accumulated depreciation and amortization		68,930,000		**89,168,000**
DEFERRED INCOME TAXES, non current		8,466,000		**11,043,000**
OTHER ASSETS				
Equity investment		5,872,000		**-**
Goodwill		5,090,000		**24,093,000**
Other		425,000		**2,906,000**
TOTAL ASSETS	$	289,515,000	$	**366,870,000**

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

DIODES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED BALANCE SHEET

LIABILITIES AND STOCKHOLDERS' EQUITY

	December 31, 2005	September 30, 2006 (unaudited)
CURRENT LIABILITIES		
Line of credit	$ 3,000,000	**$ -**
Accounts payable		
Trade	18,619,000	**37,250,000**
Related parties	7,921,000	**13,215,000**
Accrued liabilities	19,782,000	**27,756,000**
Long-term debt, current portion	4,621,000	**1,954,000**
Capital lease obligations, current portion	138,000	**141,000**
Total current liabilities	54,081,000	**80,316,000**
LONG-TERM DEBT, net of current portion	4,865,000	**3,709,000**
CAPITAL LEASE OBLIGATIONS, net of current portion	1,618,000	**1,508,000**
MINORITY INTEREST IN JOINT VENTURE	3,477,000	**4,321,000**
Total liabilities	64,041,000	**89,854,000**
STOCKHOLDERS' EQUITY		
Preferred stock - par value $1.00 per share; 1,000,000 shares authorized; no shares issued and outstanding	-	**-**
Common stock - par value $0.66 2/3 per share; 70,000,000 shares authorized; 25,258,119 and 25,930,914 shares issued at December 31, 2005 and September 30, 2006, respectively	16,839,000	**17,288,000**
Additional paid-in capital	94,664,000	**111,424,000**
Retained earnings	114,659,000	**148,126,000**
	226,162,000	**276,838,000**
Less: Accumulated other comprehensive gain (loss)	(688,000)	**178,000**
Total stockholders' equity	225,474,000	**277,016,000**
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 289,515,000	**$ 366,870,000**

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

DIODES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED STATEMENTS OF INCOME
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	**2006**	2005	**2006**
Net sales	$ 54,200,000	**$ 92,575,000**	$ 153,398,000	**$ 248,876,000**
Cost of goods sold	35,323,000	**61,879,000**	100,428,000	**166,532,000**
Gross profit	18,877,000	**30,696,000**	52,970,000	**82,344,000**
Selling and general administrative expenses	7,581,000	**11,825,000**	21,469,000	**34,883,000**
Research and development expenses	938,000	**1,941,000**	2,688,000	**5,985,000**
Loss (gain) on disposal of fixed assets	-	**32,000**	(105,000)	**152,000**
Total operating expenses	8,519,000	**13,798,000**	24,052,000	**41,020,000**
Income from operations	10,358,000	**16,898,000**	28,918,000	**41,324,000**
Other income (expense)				
Interest income	23,000	**1,069,000**	66,000	**2,807,000**
Interest expense	(188,000)	**(89,000)**	(465,000)	**(363,000)**
Other	116,000	**(1,563,000)**	95,000	**(1,699,000)**
	(49,000)	**(583,000)**	(304,000)	**745,000**
Income before income taxes and minority interest	10,309,000	**16,315,000**	28,614,000	**42,069,000**
Income tax provision	(1,621,000)	**(3,212,000)**	(4,523,000)	**(7,778,000)**
Income before minority interest	8,688,000	**13,103,000**	24,091,000	**34,291,000**
Minority interest in joint venture earnings	(305,000)	**(333,000)**	(802,000)	**(824,000)**
Net income	$ 8,383,000	**$ 12,770,000**	$ 23,289,000	**$ 33,467,000**
Earnings per share				
Basic	$ 0.38	**$ 0.50**	$ 1.08	**$ 1.31**
Diluted	$ 0.34	**$ 0.45**	$ 0.96	**$ 1.19**
Number of shares used in computation				
Basic	22,010,235	**25,686,913**	21,658,863	**25,520,156**
Diluted	24,731,514	**28,152,592**	24,344,795	**28,055,154**

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

DIODES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30, 2005	**2006**
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 23,289,000	**$ 33,467,000**
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	11,887,000	**14,053,000**
Minority interest earnings	802,000	**824,000**
Share-based compensation	856,000	**5,826,000**
Loss (gain) on disposal of property, plant and equipment	(105,000)	**221,000**
Changes in operating assets:		
Accounts receivable	(5,338,000)	**(9,017,000)**
Inventories	(4,182,000)	**(14,227,000)**
Prepaid expenses and others	297,000	**(1,493,000)**
Deferred income taxes	(1,586,000)	**(2,601,000)**
Changes in operating liabilities:		
Accounts payable	7,685,000	**13,352,000**
Accrued liabilities	1,567,000	**5,038,000**
Income tax payable	2,138,000	**1,040,000**
Net cash provided by operating activities	37,310,000	**46,483,000**
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property, plant and equipment	(14,260,000)	**(34,768,000)**
Proceeds from sale of property, plant and equipment	-	**54,000**
Purchase of available-for-sale securities	(30,002,000)	**(15,791,000)**
Acquisitions, net of cash acquired	-	**(18,411,000)**
Net cash used in investing activities	(44,262,000)	**(68,916,000)**
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayments of line of credit, net	(3,167,000)	**(5,717,000)**
Net proceeds from the issuance of common stock	63,565,000	**4,111,000**
Excess tax benefits	3,116,000	**7,274,000**
Proceeds from long-term debt	4,509,000	**-**
Repayments of long-term debt	(4,875,000)	**(4,125,000)**
Repayments of capital lease obligations	(107,000)	**(107,000)**
Management incentive reimbursement from LSC	375,000	**-**
Net cash provided by financing activities	63,416,000	**1,436,000**
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	(1,221,000)	**866,000**
INCREASE (DECREASE) IN CASH AND EQUIVALENTS	55,243,000	**(20,131,000)**

CASH, BEGINNING OF PERIOD		18,970,000		**73,288,000**
CASH, END OF PERIOD	$	74,213,000	**$**	**53,157,000**

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

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

	Nine Months Ended September 30,	
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION	2005	**2006**
Cash paid during the year for:		
Interest	$ 456,000	**$ 334,000**
Income taxes	$ 2,049,000	**$ 2,142,000**
Non-cash activities:		
Tax benefits related to stock options credited to paid-in capital	$ 3,116,000	**$ 7,274,000**
Property, plant and equipment purchased on accounts payable	$ 1,990,000	**$ (2,699,000)**

The Company purchased 99.81% of capital stock of Anachip Corporation for $31 million (including $5.9 million paid in year 2005).
In conjuction with the acquisition, liabilities were assumed as follows:

Fair value of assets acquired	**$ 46,274,000**
Cash paid for the capital stock	**(28,067,000)**
Decrease in payables for business acquisition	**(2,445,000)**
Liabilities assumed	**$ 15,762,000**

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

DIODES INCORPORATED AND SUBSIDIARIES
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(Unaudited)

NOTE A - Basis of Presentation

Unless the context otherwise requires, the words “Diodes,” “we,” “us” and “our” refer to Diodes Incorporated and its subsidiaries. The accompanying unaudited consolidated condensed financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q. They do not include all information and footnotes necessary for a fair presentation of financial position, results of operations and cash flows in conformity with accounting principles generally accepted in the United States of America for complete financial statements. These consolidated condensed financial statements should be read in conjunction with the consolidated financial statements and related notes contained in our Annual Report on Form 10-K for the year ended December 31, 2005. In the opinion of management, all adjustments (consisting of normal recurring adjustments and accruals) considered necessary for a fair presentation of the results of operations for the period presented have been included in the interim period. Operating results for the three and nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006. The condensed consolidated financial data at December 31, 2005 is derived from audited financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2005.

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

The consolidated financial statements include Diodes-North America and its subsidiaries:

Diodes Taiwan Corporation, Ltd. (“Diodes-Taiwan”) - 100% owned
Diodes Hong Kong Ltd. (“Diodes-Hong Kong”) - 100% owned
Anachip Corporation (Diodes-Anachip) - 99.8% owned
Shanghai KaiHong Electronics Co., Ltd. (“Diodes-China”) - 95% owned
Shanghai KaiHong Technology Co., Ltd. (“Diodes-Shanghai”) - 95% owned
FabTech Incorporated (“FabTech” or “Diodes-FabTech”) - 100% owned

All significant intercompany balances and transactions have been eliminated.

NOTE B - Functional Currencies, Comprehensive Gain/Loss and Foreign Currency Translation

Through our subsidiaries, we maintain operations in Taiwan, Hong Kong and China. We believe the New Taiwan (“NT”) dollar as the functional currency at our Taiwan subsidiaries most appropriately reflects the current economic facts and circumstances of our Taiwan operations. We continue to use the U.S. dollar as the functional currency at our subsidiaries in China and 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.

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities are reported as a separate component of the equity section of the balance sheet, 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 $688,000 and accumulated other comprehensive gain was $178,000 at December 31, 2005 and September 30, 2006, respectively. The $866,000 change was primarily a result of a $1.1 million one-time adjustment to other expense for intercompany foreign currency exchange losses that were incorrectly recorded directly to shareholders' equity via other comprehensive loss, rather than by recording to shareholders' equity through the income statement.

Total comprehensive income for the three and nine months ended September 30, 2005 and 2006 was as follows:

	Three months ended September 30, 2005	Three months ended September 30, 2006	Nine months ended September 30, 2005	Nine months ended September 30, 2006
Net income	$ 8,383,000	**$ 12,770,000**	$ 23,289,000	**$ 33,467,000**
Translation adjustment	(1,449,000)	**429,000**	(1,221,000)	**866,000**
Comprehensive income	$ 6,934,000	**$ 13,199,000**	$ 22,068,000	**$ 34,333,000**

NOTE C - Inventories

Inventories are stated at the lower of cost or market value. Cost is determined principally by the first-in, first-out method.

	December 31, 2005	September 30, 2006
Finished goods	$ 14,722,000	**$ 28,310,000**
Work-in-progress	3,002,000	**8,873,000**
Raw materials	9,534,000	**13,458,000**
	27,258,000	**50,641,000**
Less: reserves	(2,647,000)	**(4,874,000)**
	$ 24,611,000	**$ 45,767,000**

NOTE D - Income Tax Provision

We recognized income tax expense of $3.2 million for the third quarter of 2006, resulting in an effective tax rate of 19.8%, as compared to 15.7% in the same period last year and 19.9% in the second quarter of 2006. Our higher effective tax rate was the result of higher quarterly income in the U.S. at high tax rates, and accrued dividend related taxes in Taiwan. We continue to take advantage of available strategies to optimize our tax rate across the jurisdictions in which we operate. In 2005, we had recorded approximately $1.1 million in deferred taxes for earnings of our foreign subsidiaries, primarily Diodes-Hong Kong. For the nine months ended September 30, 2006, we have accrued an additional $1.6 million for taxes on a future dividend from our foreign subsidiaries to the U.S.

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 39.0% and 35.0%, respectively. Earnings of Diodes-Hong Kong are currently subject to a 17.5% tax for local sales or local source sales; all other Hong Kong sales are foreign income tax-free. 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 these earnings 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.

Diodes-China is located in the Songjiang district, where the standard central government tax rate is 24.0%. 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 2005. For 2006 and future years, Diodes-China's earnings will continue to be subject to a 12.0% tax rate provided it exports at least 70.0% of its net sales. We currently intend to maintain this volume of exports in the future.

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 the third quarter of 2006. Management expects this tax to be waived for at least the remainder of 2006; however, the local government can re-impose this tax at any time in its discretion.

In 2004, we established Diodes-Shanghai located in the Songjiang Export Zone of Shanghai, China. In the Songjiang Export Zone, the central government's standard tax rate is 15.0%. There is no local government tax in this zone.

As an incentive for establishing Diodes-Shanghai, for 2005 and 2006, the earnings of Diodes-Shanghai are exempted from central government income tax, and for the years 2007 through 2009 its earnings will be subject to a 7.5% tax rate. From 2010 onward, provided that Diodes-Shanghai exports over 70.0% of its net sales, the earnings will be subject to a 10.0% tax rate. We currently intend to maintain this volume of exports in the future.

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.

NOTE E - 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. The plans are described more fully in Note 9 of our audited financial statements included in the Annual Report on Form 10-K for the year ended December 31, 2005.

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 Statement of Financial Accounting Standards (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 three and nine months ended September 30, 2006, operating income decreased by $1.6 million and $5.0 million, respectively, net income decreased by $1.4 million and $4.3 million, respectively, and diluted earnings per share were reduced by $0.04 and $0.13, respectively. For the three and nine months ended September 30, 2006, stock-based compensation expense associated with the Company's stock options recognized in the income statement is as follows:

	September 30, 2006			
	Three Months Ended		Nine Months Ended	
Selling and administrative expense	$	1,355,000	$	4,112,000
Reseach and development expense	$	146,000	$	438,000
Cost of sales	$	133,000	$	398,000

Total share-based compensation expense	**$**	**1,634,000**	**$**	**4,948,000**

Share-based compensation expense for the three and nine months ended September 30, 2006 for stock options granted during the quarter was calculated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions:

	September 30, 2006	
	Three Months Ended	**Nine Months Ended**
Expected volatility	56.03%	53.85%
Expected term (in years)	6.57	5.86
Risk-free interest rate	5.07%	4.70%
Expected forfeitures	2.56%	2.56%

Expected volatility. The Company estimates expected volatility using historical volatility. Public trading volume on options in the Company's stock is not material. As a result, the Company determined that utilizing an implied volatility factor would not be appropriate. The Company calculates historical volatility for the period that is commensurate with the option's expected term assumption.

Expected term. The Company has evaluated expected term based on history and exercise patterns across its demographic population. The Company believes that this historical data is the best estimate of the expected term of a new option. The expected term for officers and Directors is 6.57 years, while the expected term for all other employees is 5.88 years.

Risk free interest rate. The Company estimated the risk-free interest rate based on zero-coupon U.S. Treasury securities for a period that is commensurate with the expected term assumption.

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. The Company has applied an annual forfeiture rate of 2.56% to all unvested options as of September 30, 2006. This analysis will be re-evaluated at least annually, and the forfeiture rate will be adjusted as necessary.

Dividend yield. The Company historically has not paid a cash dividend; therefore this input is not applicable.

For the three and nine months ended September 30, 2006, the Company granted stock options to purchase 10,000 and 265,780 shares of the Company's 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. Options granted in the three and nine months ended September 30, 2006 had a weighted-average grant date fair value of $25.12 and $18.95, respectively.

The total intrinsic value (actual gain) of options exercised during the nine months ended September 30, 2006 was approximately $21.7 million.

At September 30, 2006, un-amortized compensation expense related to unvested options, net of forfeitures, was approximately $11.0 million. The weighted average period over which share-based compensation expense related to these options will be recognized is 2.2 years.

A summary of the stock option plans as of September 30, 2006 follows:

Stock options	Shares (000)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (yrs)	Aggregate Intrinsic Value ($000)
Outstanding at December 31, 2005	4,095	$ 10.45		
Granted	266	34.33		
Exercised	(673)	6.11		
Forfeited or expired	(54)	24.05		
Outstanding at September 30, 2006	3,634	$ 12.51	6.5	$ 110,453
Exercisable at September 30, 2006	2,646	$ 8.88	5.8	$ 90,712

Prior to our adoption of SFAS 123R, Statement of Financial Accounting Standards 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 Statement of Financial Accounting Standards No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure" (SFAS 148).

Had the Company 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, the Company's earnings per common share, basic and diluted, for the three and nine months ended September 30, 2005, would have approximated the following:

	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2005
Net income, as reported	**$ 8,383,000**	**$ 23,289,000**
Deduct: Total stock-based compensation expense determined under fair value based method for all awards, net of tax benefits	(824,000)	(1,907,000)
Pro forma net income	**$ 7,559,000**	**$ 21,382,000**
Earnings per share:		
Basic		
- as reported	$ 0.38	$ 1.08
- pro forma	$ 0.35	$ 0.99
Diluted		
- as reported	$ 0.34	$ 0.96
- pro forma	$ 0.29	$ 0.88

Share Grants. Restricted stock awards and restricted stock units generally vest in equal annual installments over a four-year period.

A summary of the status of the Company's non-vested share grants as of September 30, 2005 and September 30, 2006 are presented below:

Nonvested Shares	Shares (000)	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2005	—	—
Granted	330	$ 17.30
Vested	—	—
Forfeited	—	—
Nonvested at September 30, 2005	330	$ 17.30

Nonvested Shares	Shares (000)	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2006	330	$ 17.30
Granted	204	33.96
Vested	—	—
Forfeited	—	—
Nonvested at September 30, 2006	534	$ 23.66

During the nine months ended September 30, 2006 and September 30, 2005, there were $878,000 and $856,000 of total recognized share-based compensation expense related to non-vested stock award arrangements granted under the plans, respectively.

The total of unrecognized share-based compensation expense as of September 30, 2006 and September 30, 2005 was $9.8 million and $4.9 million, respectively.

NOTE F -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 Finance, Senior Vice President of Sales and Marketing, and Senior Vice President of Operations. We operate in a single segment, semiconductor devices, through our various manufacturing and distribution facilities.

Our operations include the domestic operations (Diodes-North America and Diodes-FabTech) located in the United States, and the Far East operations (Diodes-Taiwan located in Taipei, Taiwan; Anachip Corporation 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 3.2% and 3.5% of total sales for the three and nine months ended September 30, 2006, respectively (2.7% for the third quarter of 2005, and 2.6% for the nine months ended September 30, 2005), are consolidated into the domestic (North America) operations.

The accounting policies of the operations 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.

Three Months Ended September 30, 2005	Far East	North America	Consolidated Segments
Total sales	$ 62,622,000	$ 23,229,000	$ 85,851,000
Inter-company sales	(26,460,000)	(5,191,000)	(31,651,000)
Net sales	$ 36,162,000	$ 18,038,000	$ 54,200,000
Property, plant and equipment	$ 53,601,000	$ 11,279,000	$ 64,880,000
Assets	$ 155,330,000	$ 109,237,000	$ 264,567,000

Three Months Ended September 30, 2006	Far East	North America	Consolidated Segments
Total sales	**$ 113,717,000**	**$ 30,636,000**	**$ 144,353,000**
Inter-company sales	**(46,559,000)**	**(5,219,000)**	**(51,778,000)**
Net sales	**$ 67,158,000**	**$ 25,417,000**	**$ 92,575,000**
Property, plant and equipment	**$ 76,161,000**	**$ 13,007,000**	**$ 89,168,000**
Assets	**$ 227,454,000**	**$ 139,416,000**	**$ 366,870,000**

Nine Months Ended September 30, 2005	Far East	North America	Consolidated Segments
Total sales	$ 171,425,000	$ 66,153,000	$ 237,578,000
Inter-company sales	(71,108,000)	(13,072,000)	(84,180,000)
Net sales	$ 100,317,000	$ 53,081,000	$ 153,398,000
Property, plant and equipment	$ 53,601,000	$ 11,279,000	$ 64,880,000
Assets	$ 155,330,000	$ 109,237,000	$ 264,567,000

Nine Months Ended September 30, 2006	Far East	North America	Consolidated Segments
Total sales	**$ 287,102,000**	**$ 89,248,000**	**$ 376,350,000**
Inter-company sales	**(110,825,000)**	**(16,649,000)**	**(127,474,000)**
Net sales	**$ 176,277,000**	**$ 72,599,000**	**$ 248,876,000**
Property, plant and equipment	**$ 76,161,000**	**$ 13,007,000**	**$ 89,168,000**
Assets	**$ 227,454,000**	**$ 139,416,000**	**$ 366,870,000**

Geographic Information

Revenues were derived from (invoiced to) customers located in the following countries. "All Others" represents countries with less than 20% of total revenues each.

	Net Sales for the three months ended September 30,				Percentage of net sales	
	2005		2006		2005	2006
	(Dollars in thousands)					
Taiwan	$	16,383	$	35,014	30.2%	37.8%
China		17,318		24,840	32.0%	26.8%
United States		13,377		20,038	24.7%	21.6%
All Others		7,122		12,683	13.1%	13.8%
Total	**$**	**54,200**	**$**	**92,575**	**100.0%**	**100.0%**

	Net Sales for the nine months ended September 30,				Percentage of net sales	
	2005		2006		2005	2006
	(Dollars in thousands)					
China	$	42,854	$	78,209	27.9%	31.4%
Taiwan		49,989		73,993	32.6%	29.7%
United States		38,534		57,600	25.1%	23.1%
All Others		22,021		39,074	14.4%	15.8%
Total	**$**	**153,398**	**$**	**248,876**	**100.0%**	**100.0%**

NOTE G - Business Acquisition

On December 20, 2005, the Company 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, 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 ("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.

At December 31, 2005, the Company had purchased an aggregate of 9,433,613 shares (or approximately 18.9%) of the 50,000,000 outstanding shares of the capital stock of Anachip. On January 10, 2006, (the closing date of the acquisition) the Company purchased an additional 40,470,212 shares and therefore, the Company holds approximately 99.81% of the Anachip capital stock. At December 31, 2005, the investment in Anachip is recorded under the equity method; however, the Company 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 a 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). The following table summarizes management's preliminary estimates of the fair values of the assets acquired and liabilities assumed at the date of acquisition. The allocation of the purchase price is subject to refinement for final determination of fair value.

	Original Amount Disclosed in 2005 Form 10-K (unaudited)	Purchase Adjustments	Total Allocation
Current assets	$ 23,752,000	$ (1,121,000)	$ 22,631,000
Fixed assets/non-current	2,045,000	(46,000)	1,999,000
Intangible assets			0
Patents and trademarks	2,269,000	125,000	2,394,000
Computer cost	246,000	0	246,000
Goodwill	19,541,000	(537,000)	19,004,000
Total assets acquired	**47,853,000**	**(1,579,000)**	**46,274,000**
Current liabilities	(16,829,000)	1,369,000	(15,460,000)
Non-current liabilities	(655,000)	353,000	(302,000)
Total liabilities assumed	**(17,484,000)**	**1,722,000**	**(15,762,000)**
Total purchase price	**$ 30,369,000**	**$ 143,000**	**$ 30,512,000**

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, and computer costs of $246,000 with a weighted-average useful life of approximately 3-7 years. The recorded goodwill was assigned primarily to the analog IC segment.

The following unaudited table summarizes the supplemental pro forma information for the three months and nine months ended September 30, 2005 as though the acquisition had been completed as of the beginning of that reporting period. The pro forma information is presented for illustrative purposes and is not indicative of future performance.

	Three months ended September 30, 2005	
	As reported	Pro forma
Revenue	$ 54,200,000	$ 67,737,000
Net income	8,383,000	9,575,000
Earnings per share		
Basic	$ 0.38	$ 0.44
Diluted	$ 0.34	$ 0.39

Nine months ended September 30, 2005