

DIODES INC /DEL/  
Form 10-Q  
November 09, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF  
1934

For the quarterly period ended September 30, 2016

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: 002-25577

DIODES INCORPORATED

(Exact name of registrant as specified in its charter)

Delaware 95-2039518  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification Number)

4949 Hedgcoxe Road, Suite 200

Plano, Texas 75024  
(Address of principal executive offices) (Zip code)

(972) 987-3900

(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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) 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 No

The number of shares of the registrant's Common Stock outstanding as of November 4, 2016 was 48,902,131.

Table of Contents

|  | Page |
|--|------|
| <u>Part I – Financial Information</u>  | 3    |
| <u>Item 1. Financial Statements</u>  | 3    |
| <u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u> | 17   |
| <u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>                            | 26   |
| <u>Item 4. Controls and Procedures</u>   | 26   |
| <u>Part II – Other Information</u>   | 28   |
| <u>Item 1. Legal Proceedings</u>   | 28   |
| <u>Item 1A. Risk Factors</u>   | 28   |
| <u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>                           | 28   |
| <u>Item 3. Defaults Upon Senior Securities</u>   | 29   |
| <u>Item 4. Mine Safety Disclosures</u>   | 29   |
| <u>Item 5. Other Information</u>   | 29   |
| <u>Item 6. Exhibits</u>  | 30   |
| <u>Signatures</u>  | 31   |

## PART I—FINANCIAL INFORMATION

## Item 1. Financial Statements.

## DIODES INCORPORATED AND SUBSIDIARIES

## CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share data)

|  | September<br>30,<br>2016<br>(Unaudited) | December<br>31,<br>2015 |
|--|---|-------------------------|
| <b>Assets</b>  |   |                         |
| Current assets:  |   |                         |
| Cash and cash equivalents  | \$220,526                               | \$218,435               |
| Short-term investments   | 34,766                                  | 64,685                  |
| Accounts receivable, net of allowances of \$2,670 and \$2,625 at<br>September 30, 2016 and December 31, 2015, respectively | 239,278                                 | 218,496                 |
| Inventories  | 204,251                                 | 202,832                 |
| Prepaid expenses and other   | 40,691                                  | 46,103                  |
| Total current assets   | 739,512                                 | 750,551                 |
| Property, plant and equipment, net   | 415,618                                 | 439,340                 |
| Deferred income tax  | 50,702                                  | 45,120                  |
| Goodwill   | 131,661                                 | 132,913                 |
| Intangible assets, net   | 180,232                                 | 196,409                 |
| Other  | 34,715                                  | 34,494                  |
| Total assets   | \$1,552,440                             | \$1,598,827             |
| <b>Liabilities</b>   |   |                         |
| Current liabilities:   |   |                         |
| Accounts payable   | \$90,548                                | \$86,463                |
| Accrued liabilities  | 71,758                                  | 77,801                  |
| Income tax payable   | -                                       | 5,117                   |
| Current portion of long-term debt  | 10,300                                  | 10,282                  |
| Total current liabilities  | 172,606                                 | 179,663                 |
| Long-term debt, net of current portion   | 407,052                                 | 453,738                 |
| Deferred tax liabilities   | 32,219                                  | 32,276                  |
| Other long-term liabilities  | 97,150                                  | 90,153                  |
| Total liabilities  | 709,027                                 | 755,830                 |
| Commitments and contingencies (See Note 8)   |   |                         |
| Stockholders' equity   |   |                         |
| Preferred stock - par value \$1.00 per share; 1,000,000 shares authorized; no<br>shares issued or outstanding              |   |                         |
|  | -                                       | -                       |

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Common stock - par value \$0.66 2/3 per share; 70,000,000 shares authorized;

48,816,264 and 48,148,077, issued and outstanding at September 30, 2016

|  |              |              |
|--|--------------|--------------|
| and December 31, 2015, respectively                                | 32,856       | 32,404       |
| Additional paid-in capital   | 353,539      | 344,086      |
| Retained earnings  | 528,947      | 514,280      |
| Treasury stock, at cost, 466,010 shares held at September 30, 2016 |              |              |
| and December 31, 2015  | (11,009 )    | (11,009 )    |
| Accumulated other comprehensive loss                               | (105,735 )   | (84,416 )    |
| Total stockholders' equity   | 798,598      | 795,345      |
| Noncontrolling interest  | 44,815       | 47,652       |
| Total equity   | 843,413      | 842,997      |
| Total liabilities and stockholders' equity                         | \$ 1,552,440 | \$ 1,598,827 |

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

-3-

## DIODES INCORPORATED AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(In thousands, except per share data)

|  | Three Months Ended<br>September 30, |           | Nine Months Ended<br>September 30, |           |
|--|-------------------------------------|-----------|------------------------------------|-----------|
|  | 2016                                | 2015      | 2016                               | 2015      |
| Net sales  | \$250,694                           | \$208,888 | \$710,077                          | \$634,522 |
| Cost of goods sold                                       | 170,071                             | 147,252   | 490,417                            | 439,536   |
| Gross profit   | 80,623                              | 61,636    | 219,660                            | 194,986   |
| Operating expenses                                       |                                     |           |                                    |           |
| Selling, general and administrative                      | 38,321                              | 34,669    | 119,165                            | 98,282    |
| Research and development                                 | 17,088                              | 13,745    | 52,247                             | 40,644    |
| Amortization of acquisition related intangible assets    | 5,117                               | 1,828     | 15,379                             | 5,630     |
| Other operating expenses                                 | 144                                 | 1,421     | 184                                | 1,556     |
| Total operating expenses                                 | 60,670                              | 51,663    | 186,975                            | 146,112   |
| Income from operations                                   | 19,953                              | 9,973     | 32,685                             | 48,874    |
| Other income (expense)                                   |                                     |           |                                    |           |
| Interest income  | 321                                 | 153       | 1,075                              | 695       |
| Interest expense   | (3,684 )                            | (781 )    | (9,880 )                           | (2,602 )  |
| Loss on securities carried at fair value                 | -                                   | (91 )     | -                                  | (145 )    |
| Other income (expense)                                   | (959 )                              | 974       | (1,494 )                           | 626       |
| Total other income (expense)                             | (4,322 )                            | 255       | (10,299 )                          | (1,426 )  |
| Income before income taxes and noncontrolling interest   | 15,631                              | 10,228    | 22,386                             | 47,448    |
| Income tax provision                                     | 4,097                               | 6,593     | 5,941                              | 16,179    |
| Net income   | 11,534                              | 3,635     | 16,445                             | 31,269    |
| Less net income attributable to noncontrolling interest  | (886 )                              | (798 )    | (1,778 )                           | (2,222 )  |
| Net income attributable to common stockholders           | \$10,648                            | \$2,837   | \$14,667                           | \$29,047  |
| Earnings per share attributable to common stockholders:  |                                     |           |                                    |           |
| Basic  | \$0.22                              | \$0.06    | \$0.30                             | \$0.60    |
| Diluted  | \$0.21                              | \$0.06    | \$0.30                             | \$0.59    |
| Number of shares used in earnings per share computation: |                                     |           |                                    |           |
| Basic  | 48,814                              | 48,586    | 48,496                             | 48,114    |
| Diluted  | 49,922                              | 49,564    | 49,565                             | 49,351    |

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



## DIODES INCORPORATED AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

(In thousands)

|   | Three Months  |               | Nine Months Ended |           |
|---|---------------|---------------|-------------------|-----------|
|   | Ended         |               | September 30,     |           |
|   | September 30, | September 30, | 2016              | 2015      |
|   | 2016          | 2015          | 2016              | 2015      |
| Net income  | \$11,534      | \$3,635       | \$16,445          | \$31,269  |
| Foreign currency translation adjustment                               | 1,546         | (11,954)      | (6,246 )          | (13,205 ) |
| Unrealized (loss) gain on defined benefit plan, net of tax            | (9,571 )      | 1,852         | (14,732 )         | 4,487     |
| Unrealized foreign currency loss, net of tax                          | (359 )        | (343 )        | (342 )            | (444 )    |
| Comprehensive income (loss)   | 3,150         | (6,810 )      | (4,875 )          | 22,107    |
| Less: Comprehensive income attributable to noncontrolling interest    | (886 )        | (798 )        | (1,778 )          | (2,222 )  |
| Total comprehensive income (loss) attributable to common stockholders | \$2,264       | \$(7,608 )    | \$(6,653 )        | \$19,885  |

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

## DIODES INCORPORATED AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(In thousands)

|  | Nine Months Ended<br>September 30, |             |
|--|------------------------------------|-------------|
|  | 2016                               | 2015        |
| Cash flows from operating activities                         | \$74,935                           | \$98,453    |
| Cash flows from investing activities                         |                                    |             |
| (Increase) decrease in restricted cash                       | (311 )                             | 527         |
| Purchases of property, plant and equipment                   | (47,054 )                          | (94,994 )   |
| Proceeds from sales of property, plant, and equipment        | 84                                 | 129         |
| Purchase of equity securities                                | -                                  | (4,553 )    |
| Proceeds from sales of equity securities                     | -                                  | 3,968       |
| Purchases of short-term investments                          | (17,482 )                          | (36,784 )   |
| Proceeds from maturity of short-term investments             | 46,352                             | 23,156      |
| Purchase of TF Semiconductor Solutions, net of cash acquired | -                                  | (1,033 )    |
| Other  | (1,400 )                           | 304         |
| Net cash and cash equivalents used in investing activities   | (19,811 )                          | (109,280)   |
| Cash flows from financing activities                         |                                    |             |
| Advances on lines of credit and short-term debt              | 9,000                              | 1,713       |
| Taxes paid related to net share settlement                   | (2,528 )                           | -           |
| Repayments on lines of credit and short-term debt            | (9,000 )                           | (2,512 )    |
| Debt issuance costs  | (435 )                             | (1,158 )    |
| Proceeds from long-term debt                                 | 23,500                             | -           |
| Repayments of long-term debt                                 | (70,714 )                          | (47,216 )   |
| Net proceeds from issuance of common stock                   | 5                                  | 9,906       |
| Repayment of capital lease obligation and other              | (4,116 )                           | (178 )      |
| Net cash and cash equivalents used in financing activities   | (54,288 )                          | (39,445 )   |
| Effect of exchange rate changes on cash and cash equivalents | 1,255                              | (3,973 )    |
| Increase (decrease) in cash and cash equivalents             | 2,091                              | (54,245 )   |
| Cash and cash equivalents, beginning of period               | 218,435                            | 243,000     |
| Cash and cash equivalents, end of period                     | \$220,526                          | \$188,755   |
| Supplemental disclosure                                      |                                    |             |
| Non-cash financing activities:                               |                                    |             |
| Property, plant and equipment purchased on accounts payable  | \$7,459                            | \$(24,907 ) |
| Acquisition of TF Semiconductor Solutions:                   |                                    |             |
| Total assets acquired  | \$-                                | \$8,697     |
| Total liabilities assumed                                    | \$-                                | \$86        |

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

DIODES INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1 – Nature of Operations, Basis of Presentation and Recently Issued Accounting Pronouncements

Nature of Operations

Diodes Incorporated, together with its subsidiaries (collectively, the “Company,” “we” or “our”), (Nasdaq: DIOD), is a leading global manufacturer and supplier of high-quality, application-specific standard products within the broad discrete, logic, analog and mixed-signal semiconductor markets. We serve the consumer electronics, computing, communications, industrial, and automotive markets. Our products include diodes, rectifiers, transistors, MOSFETs, protection devices, function-specific arrays, single gate logic, amplifiers and comparators, Hall-effect and temperature sensors, power management devices, including LED drivers, AC-DC converters and controllers, DC-DC switching and linear voltage regulators, and voltage references along with special function devices, such as USB power switches, load switches, voltage supervisors, and motor controllers. Our corporate headquarters and Americas’ sales office are located in Plano, Texas and Milpitas, California. Design, marketing, and engineering centers are located in Plano; Milpitas; Taipei; Taoyuan City and Zhubei City, Taiwan; Manchester, England; and Neuhaus, Germany. Our wafer fabrication facilities are located in Kansas City, Missouri and Manchester, with an additional facility located in Shanghai, China. We have assembly and test facilities located in Shanghai, Jinan, Chengdu, and Yangzhou, China, as well as in Hong Kong, Neuhaus and Taipei. Additional engineering, sales, warehouse, and logistics offices are located in Taipei; Hong Kong; Manchester; Shanghai; Shenzhen, China; Seongnam-si, South Korea; and Munich, Germany, with support offices throughout the world. On November 24, 2015, we completed our acquisition of Pericom Semiconductor Corporation (“Pericom”). Pericom is not included in the Company’s 2015 results presented in this Form 10-Q.

Basis of Presentation

The condensed consolidated financial data at December 31, 2015 is derived from audited financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2015 filed with the Securities and Exchange Commission (“SEC”) on March 11, 2016 (“Form 10-K”). The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with United States Generally Accepted Accounting Principles (“GAAP”) 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, operating results and cash flows in conformity with GAAP for complete financial statements. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes contained in our Form 10-K. All significant intercompany balances and transactions have been eliminated in consolidation. In the opinion of management, all adjustments (consisting of normal recurring adjustments and accruals) considered necessary for a fair presentation of the operating results for the period presented have been included in the interim period. Operating results for the three and nine months ended September 30, 2016 are not necessarily indicative of the results that may be expected for other interim periods or the year ending December 31, 2016.

The preparation of financial statements in conformity with GAAP 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. As permitted under GAAP, interim accounting for certain expenses, including income

taxes, are based on full year forecasts. For interim financial reporting purposes, income taxes are recorded based upon estimated annual effective income tax rates taking into consideration discrete items occurring in a quarter. Dollar amounts and share amounts are presented in thousands, except per share amounts, unless otherwise noted. Certain prior year's balances have been reclassified to conform to the current financial statement presentation.

#### Recently Issued Accounting Pronouncements

The Financial Accounting Standards Board ("FASB") issued the following Accounting Standards Updates ("ASU") which could have potential impact to the Company's financial statements:

ASU No. 2015-03, Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Cost ("ASU 2015-03"). This standard requires that costs associated with the issuance of debt previously recorded as deferred assets on the balance sheet now are reported as a direct reduction of the related debt balance. This standard is effective for interim and annual periods beginning January 1, 2016, but early adoption is permitted. We adopted this standard in the first quarter of 2016 and applied the standard retrospectively to all prior periods presented. The adoption of ASU 2015-03 resulted in a \$2.2 million retrospective reduction of both our other assets and long-term notes payable, net of current portion, as of December 31, 2015. Adoption of this standard had no impact on the consolidated statements of operations.

ASU No. 2015-16, Simplifying the Accounting for Measurement-Period Adjustments (“ASU 2015-16”). This standard eliminates the requirement for an acquirer to retrospectively adjust the financial statements for measurement-period adjustments that occur in periods after a business combination is consummated. These changes became effective for fiscal years beginning after December 31, 2015. We adopted this standard in the first quarter of 2016 and had adjustments to the previously reported fair values recorded related to the Pericom transaction. See Note 11 for additional information related to these adjustments. Adoption of this standard had no impact on the consolidated statements of operations.

ASU No. 2016-16, Income Taxes (Topic 740) Intra-Entity Transfers of Assets Other Than Inventory. This standard requires that an entity should recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. Current GAAP prohibits the recognition of current and deferred income taxes for an intra-entity asset transfer until the asset has been sold to an outside party. The amendments in this standard are effective for annual reporting periods beginning after December 15, 2017, including interim reporting periods within those annual reporting periods. The Company is evaluating the effect this new standard will have on its financial statements.

#### NOTE 2 – Earnings per Share

Earnings per share (“EPS”) are calculated by dividing net income attributable to common stockholders by the weighted-average number of shares of Common Stock outstanding during the period. Diluted EPS are calculated similarly but includes potential dilution from the exercise of stock options and stock awards, except when the effect would be anti-dilutive. A total of 1.7 million and 2.0 million stock options and stock awards outstanding during the three months ended September 30, 2016 and 2015, respectively, and 1.9 million and 0.9 million stock options and stock awards during nine months ended September 30, 2016 and 2015, respectively, were excluded from the calculation because the effect was anti-dilutive.

The table below sets forth the reconciliation between net income and the weighted average shares outstanding used for calculating basic and diluted EPS for the three and nine months ended September 30, 2016 and 2015:

|   | Three Months<br>Ended<br>September 30,<br>2016 |         | Nine Months<br>Ended<br>September 30,<br>2015 |          |
|---|--|---------|---|----------|
| <b>Earnings (numerator)</b>                                   |  |         |   |          |
| Net income attributable to common stockholders                | \$10,648                                       | \$2,837 | \$14,667                                      | \$29,047 |
| <b>Shares (denominator)</b>                                   |  |         |   |          |
| Weighted average common shares outstanding (basic)            | 48,814   | 48,586  | 48,496  | 48,114   |
| Dilutive effect of stock options and stock awards outstanding | 1,108  | 978     | 1,069   | 1,237    |
| Adjusted weighted average common shares outstanding (diluted) | 49,922   | 49,564  | 49,565  | 49,351   |
| <b>Earnings per share attributable to common stockholders</b> |  |         |   |          |
| Basic   | \$0.22   | \$0.06  | \$0.30  | \$0.60   |
| Diluted   | \$0.21   | \$0.06  | \$0.30  | \$0.59   |

## NOTE 3 – Inventories

The table below sets forth inventories which are stated at the lower of cost or market value:

|                  | September  | December   |
|------------------|------------|------------|
|                  | 30, 2016   | 31, 2015   |
| Raw materials    | \$ 86,427  | \$ 86,103  |
| Work-in-progress | 45,323     | 46,061     |
| Finished goods   | 72,501     | 70,668     |
| Total            | \$ 204,251 | \$ 202,832 |

## NOTE 4 – Goodwill and Intangible Assets

The table below sets forth the changes in goodwill:

|  |            |
|--|------------|
| Balance at December 31, 2015                         | \$ 132,913 |
| Pericom measurement period adjustments (See Note 11) | 2,741      |
| Foreign currency translation adjustment              | (3,993 )   |
| Balance at September 30, 2016                        | \$ 131,661 |

The table below sets forth the value of intangible assets, other than goodwill:

|   | September<br>30,<br>2016 | December<br>31,<br>2015 |
|---|--------------------------|-------------------------|
| <b>Intangible assets subject to amortization:</b>             |                          |                         |
| Gross carrying amount   | \$ 232,047               | \$ 232,047              |
| Reclassification from intangible assets with indefinite lives | 700                      | -                       |
| Accumulated amortization                                      | (64,146 )                | (48,828 )               |
| Foreign currency translation adjustment                       | (8,289 )                 | (7,725 )                |
| Total   | 160,312                  | 175,494                 |
| <b>Intangible assets with indefinite lives:</b>               |                          |                         |
| Gross carrying amount   | 21,703                   | 21,703                  |
| Reclassification to intangible assets subject to amortization | (700 )                   | -                       |
| Foreign currency translation adjustment                       | (1,083 )                 | (788 )                  |
| Total   | 19,920                   | 20,915                  |
| Total intangible assets, net                                  | \$ 180,232               | \$ 196,409              |

Amortization expense related to intangible assets subject to amortization was approximately \$5.1 million and \$15.4 million for the three and nine months ended September 30, 2016, respectively. Amortization expense related to intangible assets subject to amortization was approximately \$1.8 million and \$5.6 million for the three and nine months ended September 30, 2015, respectively.

## NOTE 5 – Income Tax Provision

Income tax expense for the three and nine months ended September 30, 2016 was \$4.1 million and \$5.9 million, respectively. Income tax expense for the three and nine months ended September 30, 2015 was \$6.6 million and \$16.2 million, respectively, resulting in an effective income tax rate of 26.5% for the nine months ended September 30, 2016, compared to 34.1% for the same period last year. The decrease in the effective tax rate over these comparable nine month periods is primarily attributable to a significant change in the proportion of income generated in North America, Europe and Asia, and in both periods the effective tax rates were lower than the U.S. statutory rate of 35%, principally from the impact of income from lower-taxed jurisdictions.

For the nine months ended September 30, 2016, the Company reported domestic and foreign pre-tax (loss)/income of approximately \$(25.5) million and \$47.9 million, respectively. Funds repatriated from foreign subsidiaries to the U.S. may be subject to federal and state income taxes. The Company intends to permanently reinvest overseas all of its earnings from its foreign subsidiaries, except to the extent such undistributed earnings have previously been subject to US tax; accordingly, deferred U.S. taxes are not recorded on undistributed foreign earnings.

The impact of tax holidays decreased our tax expense by approximately \$5.1 million for the nine months ended September 30, 2016 and \$1.6 million for the nine months ended September 30, 2015. The benefit of the tax holidays on both basic and diluted earnings per share for both the nine months ended September 30, 2016 and 2015 was approximately \$0.10 and \$0.03, respectively. The increase in the impact of tax holidays over these comparable nine month periods is primarily attributable to an increase in income generated by Chinese subsidiaries that qualify for a reduced income tax rate.

The Company files income tax returns in the U.S. federal jurisdiction and in various state and foreign jurisdictions. The Company is no longer subject to U.S. federal income tax examinations by tax authorities for tax years before 2007, or for the 2010 tax year. The Company is no longer subject to China income tax examinations by tax authorities for tax years before 2005. With respect to state and local jurisdictions and countries outside of the U.S. (other than China), with limited exceptions, the Company is no longer subject to income tax audits for years before 2006. Although the outcome of tax audits is always uncertain, the Company believes that adequate amounts of tax, interest and penalties, if any, have been provided for in the Company's reserve for any adjustments that may

result from tax audits. The Company recognizes accrued interest and penalties related to unrecognized tax benefits in interest expense. As of September 30, 2016, the gross amount of unrecognized tax benefits was approximately \$28.5 million.

It is reasonably possible that the amount of the unrecognized benefit with respect to certain of the Company's unrecognized tax positions will significantly increase or decrease within the next 12 months. At this time, an estimate of the range of the reasonably possible outcomes cannot be made.

#### NOTE 6 – Share-Based Compensation

The table below sets forth the line items where share-based compensation expense was recorded for the three and nine months ended September 30, 2016 and 2015:

|  | Three Months<br>Ended<br>September 30, |         | Nine Months<br>Ended<br>September 30, |          |
|--|--|---------|---------------------------------------|----------|
|  | 2016                                   | 2015    | 2016                                  | 2015     |
| Cost of goods sold                     | \$172                                  | \$99    | \$609                                 | \$345    |
| Selling, general and administrative    | 2,901                                  | 3,713   | 10,237                                | 10,307   |
| Research and development               | 684                                    | 287     | 1,991                                 | 1,003    |
| Total share-based compensation expense | \$3,757                                | \$4,099 | \$12,837                              | \$11,655 |

The table below sets forth share-based compensation expense by type for the three and nine months ended September 30, 2016 and 2015:

|  | Three Months<br>Ended<br>September 30, |         | Nine Months<br>Ended<br>September 30, |          |
|--|--|---------|---------------------------------------|----------|
|  | 2016                                   | 2015    | 2016                                  | 2015     |
| Stock options                          | \$304                                  | \$517   | \$1,212                               | \$1,999  |
| Share grants                           | 3,453                                  | 3,582   | 11,625                                | 9,656    |
| Total share-based compensation expense | \$3,757                                | \$4,099 | \$12,837                              | \$11,655 |

Stock Options. Stock options generally vest in equal annual installments over a four-year period and expire eight years after the grant date. Stock option expense was estimated on the date of grant using the Black-Scholes-Merton option pricing model.

There were no cash proceeds received from stock option exercises during the nine months ended September 30, 2016.

The table below sets forth a summary of stock option activity for the nine months ended September 30, 2016:

| Stock Options | Shares | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual | Aggregate<br>Intrinsic<br>Value |
|---------------|--------|--|---|---------------------------------|
|---------------|--------|--|---|---------------------------------|

|                                   |        |          | Term<br>(years) |          |
|-----------------------------------|--------|----------|-----------------|----------|
| Outstanding at January 1, 2016    | 2,063  | \$ 23.03 | 3.9             | \$ 4,111 |
| Granted                           | -      | -        | -               | -        |
| Exercised                         | -      | -        | -               | -        |
| Forfeited or expired              | (210 ) | 22.39    | -               | -        |
| Outstanding at September 30, 2016 | 1,853  | \$ 23.10 | 3.6             | \$ 2,712 |
| Exercisable at September 30, 2016 | 1,726  | \$ 22.86 | 3.5             | \$ 2,712 |

The aggregate intrinsic value in the table above is before applicable income taxes and represents the amount option holders would have received if all options had been exercised on the last business day of the period indicated, based on our closing stock price.

As of September 30, 2016, total unrecognized share-based compensation expense related to unvested stock options, net of estimated forfeitures, was approximately \$1.5 million, before income taxes, and is expected to be recognized over a weighted average period of approximately one year.

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

-10-

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The table below sets forth a summary of restricted stock awards and restricted stock units for the nine months ended September 30, 2016:

| Share Grants                     | Shares | Weighted<br>Average<br>Grant-Date<br>Fair Value | Aggregate<br>Intrinsic<br>Value |
|----------------------------------|--------|---|---------------------------------|
| Non-vested at January 1, 2016    | 2,679  | \$ 23.51  | \$ 61,247                       |
| Granted                          | 873    | 18.60   | -                               |
| Vested                           | (789 ) | 19.54   | 15,227                          |
| Forfeited                        | (57 )  | 20.59   | -                               |
| Non-vested at September 30, 2016 | 2,706  | \$ 21.05  | \$ 57,742                       |

As of September 30, 2016, total unrecognized share-based compensation expense related to non-vested restricted stock awards and restricted stock units, net of estimated forfeitures, was approximately \$49.2 million, before income taxes, and is expected to be recognized over a weighted average period of approximately three years.

#### NOTE 7 – Segment Information and Enterprise-Wide Disclosure

For financial reporting purposes, we operate in a single segment, standard semiconductor products, through our various manufacturing and distribution facilities. We aggregate our products because the products are similar and have similar economic characteristics, use similar production processes and share the same customer type. Our primary operations include operations in Asia, North America and Europe.

The tables below set forth net sales based on the location of subsidiaries producing the net sales:

| Three Months Ended       |           |          |          |              |
|--------------------------|-----------|----------|----------|--------------|
|                          |           | North    |          |              |
| September 30, 2016       | Asia      | America  | Europe   | Consolidated |
| Total sales              | \$239,447 | \$30,067 | \$38,451 | \$ 307,965   |
| Intercompany elimination | (37,228 ) | (5,726 ) | (14,317) | (57,271 )    |
| Net sales                | \$202,219 | \$24,341 | \$24,134 | \$ 250,694   |

| Three Months Ended       |           |          |          |              |
|--------------------------|-----------|----------|----------|--------------|
|                          |           | North    |          |              |
| September 30, 2015       | Asia      | America  | Europe   | Consolidated |
| Total sales              | \$194,642 | \$33,880 | \$40,380 | \$ 268,902   |
| Intercompany elimination | (27,874 ) | (15,015) | (17,125) | (60,014 )    |

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Net sales \$166,768 \$18,865 \$23,255 \$208,888

As of and for the Nine Months Ended

|                                    |           | North     |           |              |   |
|------------------------------------|-----------|-----------|-----------|--------------|---|
| September 30, 2016                 | Asia      | America   | Europe    | Consolidated |   |
| Total sales                        | \$671,252 | \$91,176  | \$121,501 | \$883,929    |   |
| Intercompany elimination           | (107,268) | (21,390)  | (45,194)  | (173,852)    | ) |
| Net sales                          | \$563,984 | \$69,786  | \$76,307  | \$710,077    |   |
| Property, plant and equipment, net | \$341,320 | \$58,408  | \$15,890  | \$415,618    |   |
| Total assets                       | \$956,647 | \$422,041 | \$173,752 | \$1,552,440  |   |

As of and for the Nine Months Ended

|                                    |           | North     |           |              |   |
|------------------------------------|-----------|-----------|-----------|--------------|---|
| September 30, 2015                 | Asia      | America   | Europe    | Consolidated |   |
| Total sales                        | \$588,662 | \$113,042 | \$128,616 | \$830,320    |   |
| Intercompany elimination           | (89,432)  | (49,057)  | (57,309)  | (195,798)    | ) |
| Net sales                          | \$499,230 | \$63,985  | \$71,307  | \$634,522    |   |
| Property, plant and equipment, net | \$325,942 | \$25,039  | \$20,055  | \$371,036    |   |
| Total assets                       | \$903,317 | \$133,019 | \$176,857 | \$1,213,193  |   |

## Geographic Information

The tables below set forth the amount of net sales that were derived from (shipped to) customers located in the following countries:

|                           | Net Sales for the  |           | Percentage |       |
|---------------------------|--------------------|-----------|------------|-------|
|                           | Three Months Ended |           | of         |       |
|                           | September 30,      |           | Net Sales  |       |
|                           | 2016               | 2015      | 2016       | 2015  |
| China                     | \$148,567          | \$126,268 | 59 %       | 60 %  |
| United States             | 21,802             | 17,905    | 9 %        | 9 %   |
| Korea                     | 15,993             | 16,210    | 6 %        | 8 %   |
| Germany                   | 14,737             | 13,467    | 6 %        | 6 %   |
| Singapore                 | 12,497             | 11,009    | 5 %        | 5 %   |
| Taiwan                    | 12,424             | 7,013     | 5 %        | 3 %   |
| All others <sup>(1)</sup> | 24,674             | 17,016    | 10 %       | 9 %   |
| Total                     | \$250,694          | \$208,888 | 100 %      | 100 % |

|                           | Net Sales for the |           | Percentage |       |
|---------------------------|-------------------|-----------|------------|-------|
|                           | Nine Months Ended |           | of         |       |
|                           | September 30,     |           | Net Sales  |       |
|                           | 2016              | 2015      | 2016       | 2015  |
| China                     | \$411,512         | \$378,251 | 58 %       | 60 %  |
| United States             | 62,460            | 59,531    | 9 %        | 9 %   |
| Korea                     | 43,452            | 51,457    | 6 %        | 8 %   |
| Germany                   | 47,963            | 45,003    | 7 %        | 7 %   |
| Singapore                 | 35,657            | 38,699    | 5 %        | 6 %   |
| Taiwan                    | 44,413            | 18,424    | 6 %        | 3 %   |
| All others <sup>(1)</sup> | 64,620            | 43,157    | 9 %        | 7 %   |
| Total                     | \$710,077         | \$634,522 | 100 %      | 100 % |

(1) Represents countries with less than 3% of the total net sales each.

## NOTE 8 – Commitments and Contingencies

Purchase commitments – As of September 30, 2016, we had approximately \$14.5 million in non-cancelable purchase contracts related to capital expenditures, primarily related to Asia manufacturing facilities.

Contingencies – From time to time, we are involved in various legal proceedings that arise in the normal course of business. While we intend to defend any lawsuit vigorously, we presently believe that the ultimate outcome of any

current pending legal proceeding will not have any material adverse effect on our financial position, cash flows or operating results. However, litigation is subject to inherent uncertainties, and unfavorable rulings could occur. An unfavorable ruling could include monetary damages, which could impact on our business and operating results for the period in which the ruling occurs or future periods. Based on information available, we evaluate the likelihood of potential outcomes. We record the appropriate liability when the amount is deemed probable and reasonably estimable. In addition, we do not accrue for estimated legal fees and other directly related costs as they are expensed as incurred. The Company is not currently a party to any pending litigation that the Company considers material.

#### NOTE 9 – Employee Benefit Plans

##### Defined Benefit Plan

We have a contributory defined benefit plan that covers certain employees in the United Kingdom (“U.K.”). The net pension and supplemental retirement benefit obligations and the related periodic costs are based on, among other things, assumptions regarding the discount rate, estimated return on plan assets and mortality rates. These obligations and related periodic costs are

measured using actuarial techniques and assumptions. The projected unit credit method is the actuarial cost method used to compute the pension liabilities and related expenses.

For the three months ended September 30, 2016 and 2015 net periodic benefit costs associated with the defined benefit plan were \$0.1 million and \$0.3 million, respectively. For the nine months ended September 30, 2016 and 2015, net periodic benefit costs associated with the defined benefit plan were \$0.2 million and \$1.0 million, respectively.

The tables below set forth the benefit obligation, the fair value of plan assets, and the funded status of our plan:

|   | Defined<br>Benefit<br>Plan |
|---|----------------------------|
| Change in benefit obligation:                   |                            |
| Balance at December 31, 2015                    | \$ 145,019                 |
| Service cost                                    | 209                        |
| Interest cost                                   | 3,965                      |
| Actuarial gain                                  | 45,103                     |
| Benefits paid                                   | (6,543 )                   |
| Currency changes                                | (20,819 )                  |
| Benefit obligation at September 30, 2016        | \$ 166,934                 |
| Change in plan assets:                          |                            |
| Fair value of plan assets at December 31, 2015  | \$ 116,385                 |
| Actual return on plan assets                    | 33,922                     |
| Employer contribution                           | 278                        |
| Benefits paid                                   | (6,543 )                   |
| Currency changes                                | (16,271 )                  |
| Fair value of plan assets at September 30, 2016 | \$ 127,771                 |
| Underfunded status at September 30, 2016        | \$ 39,163                  |

Based on an actuarial study performed as of September 30, 2016, the plan is underfunded and a liability is reflected in our consolidated financial statements as a long-term liability. The weighted-average discount rate assumption used to determine benefit obligations as of September 30, 2016 was 2.45%.

The following weighted-average assumptions were used to determine net periodic benefit costs for the three months ended September 30, 2016:

|  |      |
|--|------|
| Discount rate                            | 4.0% |
| Expected long-term return on plan assets | 6.0% |

In the first quarter of 2015, based on the pension deficit, we adopted (as required every three years) an amended payment plan with the trustee of the defined benefit plan in which we will pay approximately GBP 2 million (approximately \$2.4 million based on a GBP:USD exchange rate of 1.2) annually through 2030.)

We also have pension plans in Germany and Asia for which the benefit obligation, fair value of the plan assets and the funded status amounts are deemed immaterial and therefore, are not included in the figures or assumptions above.

#### Deferred Compensation

We maintain a Non-Qualified Deferred Compensation Plan (the “Deferred Compensation Plan”) for executive officers, key employees and members of the Board of Directors. The Deferred Compensation Plan allows eligible participants to defer the receipt of eligible compensation, including equity awards, until designated future dates. We offset our obligations under the Deferred Compensation Plan by investing in the actual underlying investments. These investments are classified as trading securities and are carried at fair value. At September 30, 2016, these investments totaled approximately \$6.2 million. All gains and losses in these investments are materially offset by corresponding gains and losses in the Deferred Compensation Plan liabilities.

## NOTE 10 – Related Parties

We conduct business with two related party companies, Lite-On Semiconductor Corporation and its subsidiaries and affiliates (collectively, “LSC”), and Nuvoton Technology Corporation and its subsidiaries and affiliates (collectively, “Nuvoton”). LSC is our largest stockholder, owning approximately 17% of our outstanding Common Stock as of September 30, 2016, and is a member of the Lite-On Group of companies. Raymond Soong, the Chairman of the Board of Directors, is the Chairman of LSC, and is the Chairman of Lite-On Technology Corporation (“LTC”), a significant shareholder of LSC. C.H. Chen, our former President and Chief Executive Officer and currently the Vice Chairman of the Board of Directors, is also Vice Chairman of LSC and a board member of LTC. Dr. Keh-Shew Lu, our President and Chief Executive Officer and a member of our Board of Directors, is a board member of LTC, and a board member of Nuvoton. L.P. Hsu, a member of our Board of Directors serves as a consultant to LTC, and is a supervisor of the board of Nuvoton. We consider our relationships with LSC and Nuvoton to be mutually beneficial, and we plan to continue our strategic alliance with LSC and Nuvoton. We sell semiconductor products to LSC and purchase semiconductor products from LSC for subsequent sale, making LSC one of our largest suppliers. We purchase wafers from Nuvoton that we use in the production of finished goods.

We also conduct business with two significant companies, Keylink International (B.V.I.) Inc. and its subsidiaries and affiliates (collectively, “Keylink”), and Chengdu Ya Guang Electronic Company Limited (“Ya Guang”). Keylink is our 5% joint venture partner in our Shanghai assembly and test facilities. In addition, Ya Guang is our 5% joint venture partner in our two Chengdu assembly and test facilities; however, we have no material transactions with Ya Guang. We sell semiconductor products to Keylink and purchase semiconductor products from Keylink for subsequent sale. In addition, our subsidiaries in China lease their manufacturing facilities in Shanghai from, and subcontract a portion of our manufacturing process (metal plating and environmental services) to, Keylink. We also pay a fee to Keylink for consulting services. The aggregate amounts for these services for the three months ended September 30, 2016 and 2015 were approximately \$4.1 million and \$4.7 million, respectively. The aggregate amounts for these services for the nine months ended September 30, 2016 and 2015 were approximately \$12.5 million and \$14.0 million, respectively.

The Audit Committee of the Board reviews 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.

The table below sets forth sales to, and purchases from, LSC, Nuvoton and Keylink:

|                | Three Months Ended September 30, |         | Nine Months Ended September 30, |          |
|----------------|----------------------------------|---------|---------------------------------|----------|
|                | 2016                             | 2015    | 2016                            | 2015     |
| <b>LSC</b>     |                                  |         |                                 |          |
| Net sales      | \$275                            | \$36    | \$552                           | \$423    |
| Purchases      | \$4,867                          | \$5,274 | \$16,794                        | \$18,941 |
| <b>Nuvoton</b> |                                  |         |                                 |          |
| Purchases      | \$2,827                          | \$3,208 | \$8,449                         | \$9,953  |
| <b>Keylink</b> |                                  |         |                                 |          |
| Net sales      | \$2,712                          | \$2,931 | \$6,689                         | \$7,608  |
| Purchases      | \$1,254                          | \$1,382 | \$4,089                         | \$5,063  |

The table below sets forth accounts receivable from, and accounts payable to, LSC, Nuvoton and Keylink:

|                            | September<br>30,<br>2016 | December<br>31,<br>2015 |
|----------------------------|--------------------------|-------------------------|
| <b>Accounts receivable</b> |                          |                         |
| LSC                        | \$ 225                   | \$ 55                   |
| Keylink                    | 4,675                    | 4,112                   |
|                            | \$ 4,900                 | \$ 4,167                |
| <b>Accounts payable</b>    |                          |                         |
| LSC                        | \$ 3,731                 | \$ 2,845                |
| Nuvoton                    | 1,092                    | 1,477                   |
| Keylink                    | 4,844                    | 5,147                   |
|                            | \$ 9,667                 | \$ 9,469                |

## NOTE 11 – Pericom Semiconductor Corporation Acquisition

During the fourth quarter of 2015, we completed the acquisition of Pericom Semiconductor Corporation (“Pericom”). The effect of the Pericom acquisition is reflected in our audited consolidated financial statements included in our Form 10-K filed with the SEC on March 11, 2016.

During 2016 we have continued to finalize our purchase price allocation during the measurement period and obtained additional information related to the assets acquired and liabilities assumed of Pericom. As we have updated our purchase accounting, we have become aware of facts and circumstances that existed at the date of acquisition and, if known, would have affected the measurement of the amounts originally recognized at that date. In accordance with ASC 805, Business Combinations, measurement period adjustments are not included in current earnings, but recognized as of the date of the acquisition with a corresponding adjustment to goodwill resulting from the change in preliminary amounts. As a result, we adjusted the preliminary estimated fair value estimates initially recorded at the acquisition date to reflect these measurement period adjustments. While significant progress was made during the first nine months of 2016, the estimated fair values are preliminary and subject to change. The size and breadth of the Pericom acquisition may necessitate the use of the one year measurement period to adequately analyze and assess a number of the factors used in establishing the asset and liability fair values as of the acquisition date including the estimated fair values of (i) fixed assets and inventories, (ii) intangible assets such as trademarks and in process research and development and developed technology and (iii) other assets and liabilities. The final estimates of fair value and related valuation work may also result in changes to amortization periods assigned to the assets. Any potential adjustments made could be material in relation to the preliminary values. A final determination of the estimated fair values of the assets acquired and liabilities assumed has not been completed and the following table is considered preliminary. These measurement period adjustments recorded in the first nine months of 2016 had no impact on our condensed consolidated statement of operations.

The table below sets forth the original preliminary fair values determined under the acquisition method as of November 24, 2015, the measurement period adjustments for the nine months ended September 30, 2016 and the revised preliminary fair values as of November 24, 2015.

|   | Preliminary<br>November<br>24, 2015 | Measurement<br>Period<br>Adjustments | Adjusted<br>November<br>24, 2015 |
|---|-------------------------------------|--------------------------------------|----------------------------------|
| <b>Assets acquired:</b>                   |                                     |                                      |                                  |
| Cash and cash equivalents                 | \$ 48,806                           | \$ -                                 | \$48,806                         |
| Short-term investments                    | 72,537                              | -                                    | 72,537                           |
| Accounts receivable                       | 22,740                              | -                                    | 22,740                           |
| Inventory                                 | 22,488                              | -                                    | 22,488                           |
| Prepaid expenses and other current assets | 5,793                               | (1,622 )                             | 4,171                            |
| Fixed assets                              | 72,210                              | -                                    | 72,210                           |
| Intangible assets                         | 156,700                             | -                                    | 156,700                          |
| Goodwill                                  | 54,304                              | 2,741                                | 57,045                           |
| Other long-term assets                    | 16,069                              | -                                    | 16,069                           |
| <b>Total assets acquired</b>              | <b>\$ 471,647</b>                   | <b>\$ 1,119</b>                      | <b>\$472,766</b>                 |

|   |            |       |            |
|---|------------|-------|------------|
|   |            |       | -          |
| Liabilities assumed:                            |            |       | -          |
| Accounts payable                                | 16,925     | -     | 16,925     |
| Accrued liabilities and other                   | 8,818      | 695   | 9,513      |
| Income tax payable                              | 1,498      | 333   | 1,831      |
| Deferred tax liability                          | 29,077     | 91    | 29,168     |
| Other liabilities                               | 12,155     | -     | 12,155     |
| Total liabilities assumed                       | 68,473     | 1,119 | 69,592     |
| Total net assets acquired                       | \$ 403,174 | \$ -  | \$ 403,174 |
| Total net assets acquired, net of cash acquired | \$ 354,368 | \$ -  | \$ 354,368 |

The following unaudited pro forma consolidated results of operations for the three and nine months ended September 30, 2015 has been prepared as if the acquisition of Pericom had occurred at January 1, 2015.

|  | Three<br>Months<br>Ended<br>September<br>30, 2015 | Nine<br>Months<br>Ended<br>September<br>30, 2015 |
|--|---|--|
| Net revenues                                   | \$ 240,458  | \$ 728,413                                       |
| Net income attributable to common stockholders | \$ 3,392  | \$ 23,855  |
| Earnings per share - Basic                     | \$ 0.07   | \$ 0.49  |
| Earnings per share - Diluted                   | \$ 0.07   | \$ 0.48  |

The unaudited pro forma consolidated results of operations do not purport to be indicative of the results that would have been obtained if the above acquisition had actually occurred as of the dates indicated or of those results that may be obtained in the future. The unaudited pro forma consolidated results for the three and nine months September 30, 2015, exclude \$13.9 million of acquisition related costs and \$8.0 million of costs from Diodes restricted stock grants and change-in-control agreements for Pericom employees, and include additional \$6.1 million of inventory fair value adjustments, additional amortization and depreciation of \$3.3 million and \$9.9 million, respectively, additional interest expense of \$3.3 million and \$8.5 million, respectively, and income tax benefit of \$3.8 million and \$7.8 million, respectively. These unaudited pro forma consolidated results of operations were derived, in part, from the historical consolidated financial statements of Pericom and other available information and assumptions believed to be reasonable under the circumstances.

#### NOTE 12 – Subsequent Events

##### Debt refinancing

On October 26, 2016, the Company and Diodes International B.V. (the “Foreign Borrower” and, collectively with the Company, the “Borrowers”), and certain subsidiaries of the Company as guarantors, entered into an Amended and Restated Credit Agreement (the “Credit Agreement”) that amends and restates that certain Credit Agreement dated as of January 8, 2013, as previously amended (the “Existing Credit Agreement”). Certain capitalized terms used in this description of the Credit Agreement have the meanings given to them in the Credit Agreement.

The following summary does not purport to be a complete summary of the Credit Agreement and is qualified in its entirety by reference to the Credit Agreement, a copy of which was filed on Form 8-K as Exhibit 10.1 on November 1, 2016.

The Credit Agreement rebalances the Company’s existing senior credit facilities under the Existing Credit Agreement from a \$400,000,000 revolving senior credit facility and a \$100,000,000 term loan to a \$250,000,000 revolving senior credit facility (the “Revolver”), which includes a \$10,000,000 swing line sublimit, a \$10,000,000 letter of credit sublimit, and a \$20,000,000 alternative currency sublimit, and a \$250,000,000 term loan (the “Term Loan”). The Borrowers may from time to time request additional increases in the aggregate commitments under the Credit Agreement of up to \$200,000,000, subject to the Lenders electing to increase their commitments or by means of the addition of new Lenders, and subject to at least half of each increase in aggregate commitments being in the form of term loans, with the remaining amount of each increase being an increase in the amount of the Revolver.

The Revolver and the Term Loan mature on October 26, 2021 (the “Maturity Date”). The Company plans to use a portion of the proceeds available under the Revolver and the Term Loan (i) to refinance certain existing indebtedness of the Borrowers and their subsidiaries under the Existing Credit Agreement and (ii) for working capital, capital expenditures, and other lawful corporate purposes, including, without limitation, financing permitted acquisitions.

The Credit Agreement contains certain financial and non-financial covenants, including, but not limited to, a maximum Consolidated Leverage Ratio, a minimum Consolidated Fixed Charge Coverage Ratio, and restrictions on liens, indebtedness, investments, fundamental changes, dispositions, and restricted payments (including dividends and share repurchases). These covenants are generally similar to the corresponding covenants in the Existing Credit Agreement, except that certain amounts permitted as exceptions to negative covenants restricting liens, indebtedness, investments, dispositions and restricted payments have been increased, and the maximum Consolidated Leverage Ratio set forth in the Credit Agreement has been increased. Under the Credit Agreement, restricted payments, including dividends and share repurchases, are permitted in certain circumstances, including while the Consolidated Leverage Ratio is at least 0.25 to 1.00 less than the maximum permitted under the Credit Agreement.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Except for the historical information contained herein, the matters addressed in this Item 2 constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended and as identified under the heading "Cautionary Statement for Purposes of the "Safe Harbor" Provision of the Private Securities Litigation Reform Act of 1995" herein. Such forward-looking statements are subject to a variety of risks and uncertainties, including those discussed below under the heading "Risk Factors" and elsewhere in this Quarterly Report on Form 10-Q, that could cause actual results to differ materially from those anticipated by our management. 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 Quarterly Report on Form 10-Q are made pursuant to the Act. We undertake no obligation to publicly release the results of any revisions to its forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unexpected events. Unless the context otherwise requires, the words "Diodes," the "Company," "we," "us" and "our" refer to Diodes Incorporated and its subsidiaries.

This management's discussion should be read in conjunction with the management's discussion included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2015 ("Form 10-K"), previously filed with Securities and Exchange Commission ("SEC") on March 11, 2016.

Factors Relevant to Our Results of Operations for the Three Months Ended September 30, 2016

- We continue to experience pressure from customers to reduce the selling price for our products;
- During the third quarter of 2016, we experienced a sequential increase in gross profit margin due to increased capacity utilization;
- The third quarter of 2016 included a full quarter of Pericom Semiconductor Corporation ("Pericom");
- We completed the sales integration of Pericom in China and the rest of Asia after successfully completing these efforts in North America and Europe during the first half of the year;
- In terms of our end markets, our automotive business reached a record, increasing to 7 percent of revenue;
- We have higher borrowing levels in 2016 compared to 2015, leading to higher interest expense, than in previous periods reflecting the debt incurred to acquire Pericom in the fourth quarter of 2015;

We expect future improvements in net income to result primarily from increases in sales volume and improvements in product mix, as well as manufacturing cost reduction in order to offset any reduction in the average selling prices of our products. We have released new products for the consumer market and we are beginning to see growth in the virtual reality market.

-17-

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## Overview

We are a leading global manufacturer and supplier of high-quality, application-specific standard products within the broad discrete, logic, analog and mixed-signal semiconductor markets. For detailed information, see Note 1 – Nature of Operations, Basis of Presentation and Recently Issued Accounting Pronouncements, included in the condensed consolidated financial statements in Item 1 above. Our products are sold primarily throughout Asia, North America and Europe. We believe that our focus on application-specific standard products utilizing innovative, highly efficient packaging and cost-effective process technologies, coupled with our collaborative, customer-focused product development, provides us with a meaningful competitive advantage relative to other semiconductor companies.

## Results of Operations for the Three Months Ended September 30, 2016 and 2015

The following table sets forth the percentage that certain items in the statements of operations bear to net sales.

|  | Percent<br>of Net Sales<br>Three<br>Months<br>Ended<br>September<br>30,<br>2016 2015 |       |
|--|--|-------|
| Net sales  | 100%   | 100%  |
| Cost of goods sold                                     | (68 )  | (70 ) |
| Gross profit   | 32   | 30    |
| Total operating expenses                               | 24   | 25    |
| Income from operations                                 | 8  | 5     |
| Total other expense                                    | (2 )   | -     |
| Income before income taxes and noncontrolling interest | 6  | 5     |
| Income tax provision                                   | (2 )   | (3 )  |
| Net income   | 4  | 2     |
| Net income attributable to common stockholders         | 4  | 2     |

The following table and discussion explains in greater detail our consolidated operating results and financial condition for the three months ended September 30, 2016, compared to the three months ended September 30, 2015. This discussion should be read in conjunction with the condensed consolidated financial statements and notes thereto appearing elsewhere in this quarterly report (in thousands).

| Three Months Ended<br>September 30, |      |                     | %      |
|-------------------------------------|------|---------------------|--------|
| 2016                                | 2015 | Increase/(Decrease) | Change |

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|  |           |           |           |         |   |
|--|-----------|-----------|-----------|---------|---|
| Net sales                                | \$250,694 | \$208,888 | \$ 41,806 | 20.0    | % |
| Cost of goods sold                       | 170,071   | 147,252   | 22,819    | 15.5    | % |
| Gross profit                             | 80,623    | 61,636    | 18,987    | 30.8    | % |
| Total operating expenses                 | 60,670    | 51,663    | 9,007     | 17.4    | % |
| Interest income                          | 321       | 153       | 168       | 109.8   | % |
| Interest expense                         | (3,684 )  | (781 )    | 2,903     | 371.7   | % |
| Loss on securities carried at fair value | -         | (91 )     | (91 )     | (100.0) | % |
| Other income (expense)                   | (959 )    | 974       | (1,933 )  | (198.5) | % |
| Income tax provision                     | 4,097     | 6,593     | (2,496 )  | (37.9)  | % |

Net sales increased approximately \$41.8 million for the three months ended September 30, 2016, compared to the same period last year. The 20.0% increase in net sales includes approximately \$31.0 million from Pericom in the third quarter of 2016 and increased revenue from the discrete market.

Cost of goods sold increased approximately \$22.8 million for the three months ended September 30, 2016, compared to the same period last year. As a percent of sales, cost of goods sold was 68% for the three months ended September 30, 2016 compared to 70% for the same period last year. Cost of goods sold related to Pericom for the third quarter of 2016 was approximately \$17.0 million. Cost of goods sold also increased due to increased sales in the discrete market, but were positively impacted by lower underutilization costs at our wafer fabrication plants during the third quarter of 2016, when compared to the same period of 2015. Excluding Pericom, average unit cost decreased 12.6% for the three months ended September 30, 2016, compared to the same period last year. Including Pericom, average unit cost decreased 4.5% for the three months ended September 30, 2016, compared to the same period last year. For the three months ended September 30, 2016, gross profit increased approximately 30.8% when compared to the same period last year. Gross profit margin for the three month periods ended September 30, 2016 and 2015 was 32.2% and 29.5%, respectively.

Operating expenses for the three months ended September 30, 2016 increased approximately \$9.0 million, or 17.4%, compared to the same period last year. The increase in operating expense reflects approximately \$16.1 million of operating expenses from Pericom. Selling, general and administrative expenses (“SG&A”) increased approximately \$3.7 million due primarily to \$7.7 million of Pericom SG&A recognized in the third quarter of 2016. Research and development expenses (“R&D”) increased approximately \$3.3 million due to Pericom R&D expense of \$5.1 million recognized in the third quarter of 2016. Amortization of acquisition related intangibles increased approximately \$3.3 million reflecting the amortization of the intangible assets acquired in the Pericom acquisition. SG&A, as a percentage of sales, was 15.3% and 16.6% for the three months ended September 30, 2016 and 2015, respectively. R&D, as a percentage of sales, was 6.8% and 6.6% for the three months ended September 30, 2016 and 2015, respectively.

Interest income increased for the three months ended September 30, 2016 due to a higher amount of invested funds. The increase in interest expense for the three months ended September 30, 2016 is due to higher levels of borrowing to effect the Pericom acquisition. During the third quarter of 2015, we recognized a loss on the sale of marketable securities that was not repeated in 2016. Other expense for the three months ended September 30, 2016 reflects approximately \$1.4 million of foreign currency losses.

We recognized an income tax expense of approximately \$4.1 million for the three months ended September 30, 2016 and income tax expense of approximately \$6.6 million for the three months ended September 30, 2015. The decrease in income taxes for 2016 compared to 2015 is primarily attributable to changes in the proportion of income generated in North America, Europe and Asia, respectively.

#### Results of Operations for the Nine months Ended September 30, 2016 and 2015

The following table sets forth the percentage that certain items in the statements of operations bear to net sales.

|  | Percent<br>of Net Sales<br>Nine Months<br>Ended<br>September<br>30,<br>2016 2015 |      |
|--|--|------|
| Net sales  | 100%   | 100% |
| Cost of goods sold                                     | (69)   | (69) |
| Gross profit   | 31   | 31   |
| Total operating expenses                               | (26)   | (23) |
| Income from operations                                 | 5  | 8    |
| Total other income (expense)                           | (2)  | -    |
| Income before income taxes and noncontrolling interest | 3  | 8    |

|  |   |      |
|--|---|------|
| Income tax provision                           | 1 | (3 ) |
| Net income                                     | 2 | 5    |
| Net income attributable to common stockholders | 2 | 5    |

The following table and discussion explains in greater detail our consolidated operating results and financial condition for the nine months ended September 30, 2016, compared to the nine months ended September 30, 2015. This discussion should be read in conjunction with the condensed consolidated financial statements and notes thereto appearing elsewhere in this quarterly report (in thousands).

|  | Nine Months Ended<br>September 30, |           |                     | %<br>Change |
|--|------------------------------------|-----------|---------------------|-------------|
|  | 2016                               | 2015      | Increase/(Decrease) |             |
| Net sales                                | \$710,077                          | \$634,522 | \$ 75,555           | 11.9 %      |
| Cost of goods sold                       | 490,417                            | 439,536   | 50,881              | 11.6 %      |
| Gross profit                             | 219,660                            | 194,986   | 24,674              | 12.7 %      |
| Total operating expenses                 | 186,975                            | 146,112   | 40,863              | 28.0 %      |
| Interest income                          | 1,075                              | 695       | 380                 | 54.7 %      |
| Interest expense                         | (9,880 )                           | (2,602 )  | 7,278               | 279.7 %     |
| Loss on securities carried at fair value | -                                  | (145 )    | (145 )              | 100.0 %     |
| Other income (expense)                   | (1,494 )                           | 626       | 2,120               | (338.7 %)   |
| Income tax provision                     | 5,941                              | 16,179    | (10,238 )           | (63.3 %)    |

Net sales increased approximately \$75.6 million for the nine months ended September 30, 2016, compared to the same period last year. The 11.9% increase in net sales includes approximately \$94.8 million from Pericom recognized in 2016. The decrease in sales excluding Pericom reflects weaker demand in the consumer market along with weak domestic demand in China.

Cost of goods sold increased approximately \$50.9 million for the nine months ended September 30, 2016, compared to the same period last year. As a percent of sales, cost of goods sold was 69.1% and 69.3% for the nine months ended September 30, 2016 and 2015, respectively. Cost of goods sold related to Pericom for the nine months ended September 30, 2016 was approximately \$53.4 million. Excluding Pericom, average unit cost increased 0.4% for the nine months ended September 30, 2016, compared to the same period last year. Including Pericom, average unit cost increased 10.6% for the nine months ended September 30, 2016, compared to the same period last year. For the nine months ended September 30, 2016, gross profit increased approximately 12.7% when compared to the same period last year. Gross profit margin for the nine month periods ended September 30, 2016 and 2015 was 30.9% and 30.7%, respectively.

Operating expenses for the nine months ended September 30, 2016 increased approximately \$40.9 million, or 28.0%, compared to the same period last year. The increase in operating expense reflects approximately \$46.1 million of operating expenses from Pericom. SG&A increased approximately \$20.9 million due primarily to \$21.6 million of Pericom SG&A recognized in 2016. R&D increased approximately \$11.6 million due to Pericom R&D expense of \$14.6 million recognized in 2016. Amortization of acquisition-related intangibles increased approximately \$9.7 million reflecting the amortization of the intangible assets acquired in the Pericom acquisition. SG&A, as a percentage of sales, was 16.8% and 15.5% for the nine months ended September 30, 2016 and 2015, respectively. R&D, as a percentage of sales, was 7.4% and 6.4% for the nine months ended September 30, 2016 and 2015, respectively.

Interest income increased for the nine months ended September 30, 2016 due to a higher amount of invested funds, reflecting the investments acquired in the Pericom acquisition. The increase in interest expense for the nine months ended September 30, 2016 is due to higher levels of borrowing to effect the Pericom acquisition. During 2015, we recognized losses on the sale of marketable securities that was not repeated in 2016.

We recognized an income tax expense of approximately \$5.9 million for the nine months ended September 30, 2016 and income tax expense of approximately \$16.2 million for the nine months ended September 30, 2015. The decrease in income taxes for 2016 compared to 2015 is primarily attributable to changes in the proportion of income generated in North America, Europe and Asia, respectively.

## Financial Condition

### Liquidity and Capital Resources

Our primary sources of liquidity are cash and cash equivalents, funds from operations and, if necessary, borrowings under our credit facilities. We currently have a U.S. banking credit facility under which we may draw up to \$250 million (in addition to a \$250 million term loan included in the U.S. banking credit facility). The Borrowers may from time to time request increases in the aggregate commitments under the Credit Agreement of up to \$200 million, subject to the Lenders electing to increase their commitments or by means of the addition of new Lenders, and subject to at least half of each increase in aggregate commitments being in the form of term loans, with the remaining amount of each increase being an increase in the amount of the Revolver. The Credit Agreement contains certain financial and non-financial covenants, including, but not limited to, a maximum Consolidated Leverage Ratio, a minimum Consolidated Fixed Charge Coverage Ratio, and restrictions on liens, indebtedness, investments, fundamental changes, dispositions, and restricted payments (including dividends and share repurchases). At September 30, 2016, we had \$417.5 million drawn under the U.S. banking credit facility as it was in effect on that date (including the balance on the term loan then included in the U.S. banking credit facility). In addition, we have short-term foreign credit facilities with borrowing capacities of approximately \$73.4 million with \$1.1 million used for import and export guarantees. At September 30, 2016, we also have foreign long-term debt of approximately \$1.6 million. Our primary liquidity requirements have been to meet our inventory and capital expenditure needs and to fund on-going operations. At September 30, 2016 and December 31, 2015, our working capital was \$566.9 million and \$570.9 million, respectively. We expect cash generated by our operations together with existing cash, cash equivalents, short-term investments and available credit facilities to be sufficient to cover cash needs for working capital and capital expenditures for at least the next 12 months.

During October 2016, we refinanced our U.S. banking credit facility. For additional information related to this refinancing see Note 12 – “Subsequent Events”, in the Notes to Condensed Consolidated Financial Statements.

Capital expenditures for the nine months ended September 30, 2016 and 2015 were \$39.6 million and \$119.9 million, respectively. For the first nine months of 2016 capital expenditures were approximately 5.6% of our net sales, which is in line with our capital spending target range of 5% to 9% of net sales.

We intend to permanently reinvest overseas all of our earnings from our foreign subsidiaries, except to the extent such undistributed earnings have previously been subject to U.S. tax; accordingly, deferred U.S. taxes are not recorded on undistributed foreign earnings. As of September 30, 2016, our foreign subsidiaries held approximately \$247.6 million of cash, cash equivalents and investments of which approximately \$172.5 million would be subject to a potential tax if repatriated to the U.S. as dividends.

As of September 30, 2016, we had short-term investments totaling \$34.8 million. These investments are highly liquid with maturity dates greater than three months at the date of purchase. We generally can access these investments in a relatively short amount of time but in doing so we generally forfeit all earned and future interest income.

## Share Repurchase Program

During 2015, our Board of Directors (“Board”) approved a stock repurchase program. The Board authorized the repurchase of up to an aggregate of \$100.0 million of our outstanding common stock, \$0.66 2/3 par value per share. The share repurchase program is expected to continue through the end of 2019 unless extended or shortened by the Board. Currently there is approximately \$89.0 million available for repurchase of outstanding common stock under this publically announced repurchase program. No shares were repurchased during the nine months ended September 30, 2016. During the fourth quarter of 2015, the Company repurchased 466,010 shares at a cost of approximately \$11.0 million.

## Discussion of Cash Flow

Our primary source of liquidity is cash flow from operations. Additional sources of liquidity are cash and cash equivalents, short-term investments and our credit facility. Our primary cash and cash equivalents increased from \$218.4 million at December 31, 2015 to \$220.5 million at September 30, 2016.

-21-

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The table below sets forth a summary of the condensed consolidated statements of cash flows:

|  | Nine Months Ended September 30, |             |            |
|--|---------------------------------|-------------|------------|
|  | 2016                            | 2015        | Change     |
| Cash flows from operating activities                         | \$74,935                        | \$98,453    | \$(23,518) |
| Net cash and cash equivalents used in investing activities   | (19,811)                        | (109,280)   | 89,469     |
| Net cash and cash equivalents used in financing activities   | (54,288)                        | (39,445 )   | (14,843)   |
| Effect of exchange rate changes on cash and cash equivalents | 1,255                           | (3,973 )    | 5,228      |
| Net increase (decrease) in cash and cash equivalents         | \$2,091                         | \$(54,245 ) | \$56,336   |

### Operating Activities

Net cash provided by operating activities for the nine months ended September 30, 2016 was \$74.9 million. Net cash flow provided by operating activities resulted from net income of \$16.4 million, depreciation and amortization of \$74.4 million and share-based compensation of \$12.8 million. These cash and cash equivalents provided by operations were partially offset by a decrease in working capital. Net cash provided by operating activities was \$98.5 million for the same period last year, resulting primarily from \$31.3 million in net income, \$62.2 million in depreciation and amortization, \$11.7 million of non-cash share-based compensation expense and increases in accounts payable and accrued liabilities, partially offset by an increase in inventories, prepaid expenses, and other assets.

### Investing Activities

Net cash used in investing activities was \$19.8 million for the nine months ended September 30, 2016, compared to net cash used in investing activities of \$109.3 million for the same period last year. Net cash used in investing activities was primarily due to the purchase of property, plant and equipment of \$47.1 million, and purchases of short-term investments of \$17.5 million, partially offset by net funds received from the sale and purchase of short-term investments of \$46.4 million.

### Financing Activities

Net cash used in financing activities was \$54.3 million for the nine months ended September 30, 2016, compared to net cash used in financing activities of \$39.4 million in the same period last year. Net cash used in 2016 consisted primarily of repayments of long-term debt. Net cash used in 2015 consisted primarily of repayments on lines of credit and long-term debt, partially offset by advances on lines of credit and proceeds from issuance of common stock.

#### 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 provide off-balance sheet financing, liquidity or market or credit risk support, nor do we engage in leasing, swap agreements, or outsourcing of research and development services, that could expose us to liability that is not reflected on the face of our financial statements.

#### Contractual Obligations

There have been no material changes in any of our contractual obligations as disclosed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2015, filed on March 11, 2016.

#### Critical Accounting Policies

No material changes were made to the Company's critical accounting policies as set forth in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations," included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2015, filed with the SEC on March 11, 2016.

#### Recently Issued Accounting Pronouncements

See Note 1 - Nature of Operations, Basis of Presentation and Recently Issued Accounting Pronouncements of the Notes to Condensed Consolidated Financial Statements, for detailed information regarding the status of recently issued accounting pronouncements.

## Available Information

Our Internet address is <http://www.diodes.com>. We make available, free of charge through our Internet website, our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, proxy statements, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (“Exchange Act”) as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission (the “SEC”). Our website also provides access to investor financial information, including SEC filings and press releases, as well as stock quotes and information on corporate governance compliance.

## Cautionary Statement for Purposes of the “Safe Harbor” Provision of the Private Securities Litigation Reform Act of 1995

Except for the historical information contained herein, the matters addressed in this Quarterly Report on Form 10-Q constitute “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. 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,” or similar phrases or the negatives of such terms. Such forward-looking statements are subject to a variety of risks and uncertainties, including those discussed under “Risks Factors” and elsewhere in this Quarterly Report on Form 10-Q that could cause actual results to differ materially from those anticipated by our management. 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 Quarterly Report on Form 10-Q are made pursuant to the Act.

All forward-looking statements contained in this Quarterly Report on Form 10-Q are subject to, in addition to the other matters described in this Quarterly Report on Form 10-Q, a variety of significant risks and uncertainties. The following discussion highlights some of these risks and uncertainties. Further, from time to time, information provided by us or statements made by our employees may contain forward-looking information. There can be no assurance that actual results or business conditions will not differ materially from those set forth or suggested in such forward-looking statements as a result of various factors, including those discussed below.

For more detailed discussion of these factors, see the “Risk Factors” discussion in Item 1A of our most recent Annual Report on Form 10-K as filed with the SEC and in Part II, Item 1A of this report. The forward-looking statements included in this Quarterly Report on Form 10-Q are made only as of the date of this report, and we undertake no obligation to update the forward-looking statements to reflect subsequent events or circumstances.

## Risk Factors

### Risk Relating to the Referendum of the United Kingdom’s Membership of the European Union

The announcement of the Referendum of the United Kingdom's (the "U.K.") Membership of the European Union (the "E.U.") ("Brexit"), advising for the exit of the U.K. from the E.U., could cause disruptions to and create uncertainty surrounding our business, including affecting our relationships with our existing and future customers, suppliers and employees, which could have an adverse effect on our business, financial results and operations.

## RISKS RELATED TO OUR BUSINESS

The success of our business depends on the strength of the global economy and the stability of the financial markets, and any weaknesses in these areas may have a material adverse effect on our net sales, operating results and financial condition.

During times of difficult market conditions, our fixed costs combined with lower net sales and lower profit margins may have a negative impact on our business, operating results and financial condition.

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

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

One of our external suppliers is also a related party. The loss of this supplier could harm our business, operating results and financial condition.

Delays in initiation of production at facilities due to implementing new production techniques or resolving problems associated with technical equipment malfunctions could adversely affect our manufacturing efficiencies, operating results and financial condition.

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.

Our customers require our products to undergo a lengthy and expensive qualification process without any assurance of product sales and may demand to audit our operations from time to time. A failure to qualify a product or a negative audit finding could adversely affect our net sales, operating results and financial condition.

Our customer orders are subject to cancellation or modification usually with no penalty. High volumes of order cancellation or reduction in quantities ordered could adversely affect our net sales, operating results and financial condition.

Production at our manufacturing facilities could be disrupted for a variety of reasons, including natural disasters and other extraordinary events, which could prevent us from producing enough of our products to maintain our sales and satisfy our customers' demands and could adversely affect our operating results and financial condition.

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 would adversely affect our net sales, market share, operating results and financial condition.

We may be adversely affected by any disruption in our information technology systems, which could adversely affect our cash flows, operating results and financial condition.

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, reduction in our intellectual property rights and a negative impact on our business, operating results and financial condition.

We depend on third-party suppliers for timely deliveries of raw materials, manufacturing services, product and process development, parts and equipment, as well as finished products from other manufacturers, and our reputation with customers, operating results and financial condition could be adversely affected if we are unable to obtain

adequate supplies in a timely manner.

If we do not succeed in continuing to vertically integrate our business, we will not realize the cost and other efficiencies we anticipate, which could adversely affect our ability to compete, our operating results and financial condition.

Part of our growth strategy involves identifying and acquiring companies. 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, which could adversely affect our business, operating results and financial condition.

We are subject to litigation risks, including securities class action litigation, which may be costly to defend and the outcome of which is uncertain and could adversely affect our business and financial condition.

We are subject to many environmental laws and regulations that could result in significant expenses and could adversely affect our business, operating results and financial condition.

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

We may fail to attract or retain the qualified technical, sales, marketing, finance and management/executive personnel required to operate our business successfully, which could adversely affect our business, operating results and financial condition.

We may not be able to achieve future growth, and any such growth may place a strain on our management and on our systems and resources, which could adversely affect our business, operating results and financial condition.

Obsolete inventories as a result of changes in demand for our products and change in life cycles of our products could adversely affect our business, operating results and financial condition.

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



We are subject to interest rate risk that could have an adverse effect on our cost of working capital and interest expenses, which could adversely affect our business, operating results and financial condition.

We may have a significant amount of debt with various financial institutions worldwide. Any indebtedness could adversely affect our business, operating results, financial condition and our ability to meet payment obligations under such debt.

Restrictions in our credit facilities may limit our business and financial activities, including our ability to obtain additional capital in the future.

Our business benefits from certain Chinese government incentives. Expiration of, or changes to, these incentives could adversely affect our operating results and financial condition.

We operate a global business through numerous foreign subsidiaries, and there is a risk that tax authorities will challenge our transfer pricing methodologies or legal entity structures, which could adversely affect our operating results and financial condition.

The value of our benefit plan assets and liabilities is based on estimates and assumptions, which may prove inaccurate and the actual amount of expenses recorded in the consolidated financial statements could differ materially from the assumptions used.

Changes in actuarial assumptions for our defined benefit plan could increase the volatility of the plan's asset value, require us to increase cash contributions to the plan and have a negative impact on our cash flows, operating results and financial condition.

Certain of our customers and suppliers require us to comply with their codes of conduct, which may include certain restrictions that may substantially increase our cost of doing business as well as have an adverse effect on our operating efficiencies, operating results and financial condition.

Compliance with government regulations and customer demands regarding the use of "conflict minerals" may result in increased costs and may have a negative impact on our business, operating results and financial condition.

There are risks associated with previous and future acquisitions. We may ultimately not be successful in overcoming these risks or any other problems encountered in connection with acquisitions.

If we fail to maintain an effective system of internal controls or discover material weaknesses in our internal control 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.

Our management certification and auditor attestation regarding the effectiveness of our internal control over financial reporting as of December 31, 2015 excluded the operations of Pericom. If we are not able to integrate Pericom operations into our internal control over financial reporting, our internal control over financial reporting may not be effective.

Terrorist attacks, or threats or occurrences of other terrorist activities, whether in the U.S. or internationally, may affect the markets in which our Common Stock trades, the markets in which we operate and our operating results and financial condition.

System security risks, data protection breaches, cyber-attacks and other related cybersecurity issues could disrupt our internal operations, and any such disruption could reduce our expected net sales, increase our expenses, damage our reputation and adversely affect our stock price.

## RISKS RELATED TO OUR INTERNATIONAL OPERATIONS

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

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

A slowdown in the Chinese economy could limit the growth in demand for electronic devices containing our products, which would have a material adverse effect on our business, operating results and prospects.

Economic regulation in China could materially and adversely affect our business, operating results and prospects.

We could be adversely affected by violations of the United States' Foreign Corrupt Practices Act, the U.K.'s Bribery Act 2010 and similar worldwide anti-bribery laws.

-25-

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

China is experiencing rapid social, political and economic change, which has increased labor costs and other related costs that could make doing business in China less advantageous than in prior years. Increased labor costs in China could adversely affect our business, operating results and financial condition.

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

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

#### RISKS RELATED TO OUR COMMON STOCK

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

We may enter into future acquisitions and take certain actions in connection with such acquisitions that could 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.

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.

Non-cash tender offers, debt equity swaps or equity exchanges to consummate our business activities are likely to have the effect of diluting the ownership interest of existing stockholders, including qualified stockholders who receive shares of our Common Stock in such business activities.

Anti-takeover effects of certain provisions of Delaware law and our Certificate of Incorporation and Bylaws, may hinder a take-over attempt.

Section 203 of Delaware General Corporation Law may deter a take-over attempt.

Certificate of Incorporation and Bylaw Provisions may deter a take-over attempt.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk.

There have been no material changes to our market risks as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2015, filed on March 11, 2016.

### Item 4. Controls and Procedures.

Our Chief Executive Officer, Keh-Shew Lu, and Chief Financial Officer, Richard D. White, with the participation of our management, carried out an evaluation, as of September 30, 2016, of the effectiveness of our 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 Quarterly Report on Form 10-Q, our disclosure controls and procedures are effective at the reasonable assurance level to ensure that information required to be included in this report is:

- recorded, processed, summarized and reported within the time period specified in the Commission's rules and forms; and

- accumulated and communicated to our management, including the Chief Executive Officer and the Chief Financial Officer, to allow timely decisions on required disclosure.

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.

#### Previously Reported Material Weakness; Remediation

Our management previously concluded that our internal control over financial reporting was ineffective as of December 31, 2015 as a result of certain errors in accounting for equity awards and change-in-control agreements related to the Pericom acquisition.

We have taken the following steps to improve our internal control over financial reporting related to equity awards and change-in-control agreements in a business combination:

• prepared a work flow document detailing the policies and procedures (and related controls) for future acquisitions;

• committed to hiring external resources at an early stage to prepare and analyze non-routine or complex transactions;

- planned for close oversight and supervision of, and communication with, those external resources; and

• committed to complete and substantive documentation around the review processes in acquisitions for equity awards and change-in-control agreements.

The above changes to remediate the previously reported material weakness over our internal control over financial reporting were implemented during the first quarter of 2016.

#### Changes in Controls over Financial Reporting

There was no change in our internal control over financial reporting, known to our Chief Executive Officer or Chief Financial Officer, that occurred in the three months ended September 30, 2016, which has materially affected, or is reasonably likely to materially affect our internal control over financial reporting.

## PART II—OTHER INFORMATION

### Item 1. Legal Proceedings.

See Note 8 - Commitments and Contingencies, of the Notes to Condensed Consolidated Financial Statements for detailed information regarding the status of our lawsuits.

From time to time, we are involved in various legal proceedings that arise in the normal course of business. While we intend to defend any lawsuit vigorously, we presently believe that the ultimate outcome of any current pending legal proceeding will not have any material adverse effect on our financial position, cash flows or operating results. However, litigation is subject to inherent uncertainties, and unfavorable rulings could occur. An unfavorable ruling could include monetary damages, which could impact our business and operating results for the period in which the ruling occurs or future periods.

### Item 1A. Risk Factors.

#### Risk Relating to the Referendum of the United Kingdom's Membership of the European Union

The announcement of the Referendum of the United Kingdom's (the "U.K.") Membership of the European Union (the "E.U.") ("Brexit"), advising for the exit of the U.K. from the E.U., could cause disruptions to and create uncertainty surrounding our business, including affecting our relationships with our existing and future customers, suppliers and employees, which could have an adverse effect on our business, financial results and operations.

The announcement of Brexit could cause disruptions to and create uncertainty surrounding our business, including affecting our relationships with our existing and future customers, suppliers and employees, which could have an adverse effect on our business, financial results and operations. The Brexit vote is non-binding; however if passed into law, negotiations would commence to determine the future terms of the U.K.'s relationship with the E.U., including the terms of trade between the U.K. and the E.U. The effects of Brexit will depend on any agreements the U.K. makes to retain access to E.U. markets either during a transitional period or more permanently. The measures could potentially disrupt the markets we serve and the tax jurisdictions in which we operate and adversely change tax benefits or liabilities in these or other jurisdictions, and may cause us to lose customers, suppliers, and employees. In addition, Brexit could lead to legal uncertainty and potentially divergent national laws and regulations as the U.K. determines which E.U. laws to replace or replicate.

The announcement of Brexit caused significant volatility in global stock markets and currency exchange rate fluctuations that resulted in the strengthening of the U.S. dollar against foreign currencies in which we conduct business. The strengthening of the U.S. dollar relative to other currencies may adversely affect our results of

operations, in a number of ways, including:

- Our international sales are denominated in both the U.S. dollar and currencies other than U.S. dollars. A fluctuation of currency exchanges rates may expose us to gains and losses on non U.S. currency transactions and a potential devaluation of the local currencies of our customers relative to the U.S. dollar may impair the purchasing power of our customer and could cause customers to decrease or cancel orders or default on payment; and
- We translate sales and other results denominated in foreign currency into U.S. dollars for our financial statements. During periods of a strengthening dollar, our reported international sales and earnings could be reduced because foreign currencies may translate into fewer U.S. dollars.

The announcement of Brexit may also create global economic uncertainty, which may cause our customers to closely monitor their costs and reduce their spending budget on our products and services.

Any of these effects of Brexit, among others, could materially adversely affect our business, business opportunities, results of operations, financial condition and cash flows.

Except as otherwise described here, there have been no material changes from the risk factors disclosed in the “Risk Factors” section of our Annual Report on Form 10-K for the fiscal year ended December 31, 2015, filed on March 11, 2016.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

None.

## Item 6. Exhibits.

| Number  | Description  | Form | Date of First Filing | Exhibit Number | Filed Herewith |
|---------|--|------|----------------------|----------------|----------------|
| 3.1     | Certificate of Incorporation, as amended   | 10-Q | May 10, 2013         | 3.1            |                |
| 3.2     | Amended By-laws of the Company as of January 6, 2016   | 8-K  | January 11, 2016     | 3.1            |                |
| 4.1     | Form of Certificate for Common Stock, par value \$0.66<br>2/3 per share  | S-3  | August 25, 2005      | 4.1            |                |
| 10.1    | Amended and Restated Credit Agreement, dated October 26, 2016, by and among Diodes Incorporated, Diodes International B.V., Diodes Holding B.V., Diodes Investment Company, Diodes FabTech Inc., Diodes Holdings UK Limited, Diodes Zetex Limited, Pericom Semiconductor Corporation, Bank of America, N.A., as Administrative Agent, Swing Line Lender and L/C Issuer, and the other Lenders party thereto. | 8-K  | November 1, 2016     | 10.1           |                |
| 31.1    | Certification Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002   |      |                      |                | X              |
| 31.2    | Certification Pursuant to Rule 13a-14(a) /15d-14(a) of the Securities Exchange Act of 1934, adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.   |      |                      |                | X              |
| 32.1*   | Certification Pursuant to 18 U.S.C. 1350 adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002   |      |                      |                | X              |
| 32.2*   | Certification Pursuant to 18 U.S.C. 1350 adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002   |      |                      |                | X              |
| 101.INS | XBRL Instance Document   |      |                      |                | X              |

|  |   |
|--|---|
| 101.SCH XBRL Taxonomy Extension Schema                       | X |
| 101.CAL XBRL Taxonomy Extension Calculation Linkbase         | X |
| 101.DEF XBRL Taxonomy Extension Definition Linkbase Document | X |
| 101.LAB XBRL Taxonomy Extension Labels Linkbase              | X |
| 101.PRE XBRL Taxonomy Extension Presentation Linkbase        | X |

\* A certification furnished pursuant to Item 601 of the Regulation S-K will not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), or otherwise subject to the liability of that section. Such certification will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Exchange Act, except to the extent that the registrant specifically incorporates it by reference.

PLEASE NOTE: It is inappropriate for investors to assume the accuracy of any covenants, representations or warranties that may be contained in agreements or other documents filed as exhibits to this Quarterly Report on Form 10-Q. In certain instances the disclosure schedules to such agreements or documents contain information that modifies, qualifies and creates exceptions to the representations, warranties and covenants. Moreover, some of the representations and warranties may not be complete or accurate as of a particular date because they are subject to a contractual standard of materiality that is different from those generally applicable to stockholders and/or were used for the purpose of allocating risk among the parties rather than establishing certain matters as facts. Accordingly, you should not rely on the representations and warranties as characterizations of the actual state of facts at the time they were made or otherwise.

SIGNATURES

Pursuant to the requirements 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.

DIODES INCORPORATED  
(Registrant)

November 9, 2016 By: /s/ Keh-Shew Lu  
Date KEH SHEW LU  
President and Chief Executive Officer  
(Principal Executive Officer)

November 9, 2016 By: /s/ Richard D. White  
Date RICHARD D. WHITE  
Chief Financial Officer and Secretary  
(Principal Financial Officer)

November 9, 2016 By: /s/ Brett R. Whitmire  
Date BRETT R. WHITMIRE  
  
Corporate Controller  
(Principal Accounting Officer)