

MAGNACHIP SEMICONDUCTOR Corp  
Form 10-Q  
May 03, 2011  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

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

For the quarterly period ended March 31, 2011

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: 001-34791

**MagnaChip Semiconductor Corporation**

(Exact name of registrant as specified in its charter)

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**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**83-0406195**  
(I.R.S. Employer  
Identification No.)

**c/o MagnaChip Semiconductor S.A.**

**74, rue de Merl, B.P. 709 L-2146**

**Luxembourg R.C.S.**

**Luxembourg B97483**

**(352) 45-62-62**

(Address, zip code, and telephone number, including area code, of registrant's principal executive offices)

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

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.  Yes  No

As of March 31, 2011, the registrant had 39,356,749 shares of common stock outstanding.

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**MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES**

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FORWARD LOOKING STATEMENTS

The following Management's Discussion and Analysis of Financial Condition and Results of Operations contain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended, that involve risks and uncertainties. Forward-looking statements give our current expectations and projections relating to our financial condition, results of operations, plans, objectives, future performance and business. You can identify these statements by the fact that they do not relate strictly to historical or current facts. These statements may include words such as anticipate, estimate, expect, project, intend, plan, and other words and terms of similar meaning in connection with any discussion of the timing or nature of future operating or financial performance or other events. All statements other than statements of historical facts included in this report that address activities, events or developments that we expect, believe or anticipate will or may occur in the future are forward-looking statements.

These forward-looking statements are largely based on our expectations and beliefs concerning future events, which reflect estimates and assumptions made by our management. These estimates and assumptions reflect our best judgment based on currently known market conditions and other factors relating to our operations and business environment, all of which are difficult to predict and many of which are beyond our control. Although we believe our estimates and assumptions to be reasonable, they are inherently uncertain and involve a number of risks and uncertainties that are beyond our control. In addition, management's assumptions about future events may prove to be inaccurate. Management cautions all readers that the forward-looking statements contained in this report are not guarantees of future performance, and we cannot assure any reader that those statements will be realized or the forward-looking events and circumstances will occur. Actual results may differ materially from those anticipated or implied in the forward-looking statements due to the factors listed in this section and in Part II: Item 1A. Risk Factors in this report.

All forward-looking statements speak only as of the date of this report. We do not intend to publicly update or revise any forward-looking statements as a result of new information or future events or otherwise, except as required by law. These cautionary statements qualify all forward-looking statements attributable to us or persons acting on our behalf.

Statements made in this Quarterly Report on Form 10-Q, unless the context otherwise requires, include the use of the terms we, us, our and MagnaChip refer to MagnaChip Semiconductor Corporation and its consolidated subsidiaries. The term Korea refers to the Republic of Korea or South Korea.

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Interim Consolidated Financial Statements (Unaudited)  
MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****(Unaudited; in thousands of US dollars, except share data)**

	<b>March 31, 2011</b>	<b>December 31, 2010</b>
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$ 194,179	\$ 172,172
Accounts receivable, net	131,020	119,054
Inventories, net	73,879	68,435
Other receivables	4,006	2,919
Prepaid expenses	11,082	8,207
Other current assets	9,937	18,920
<b>Total current assets</b>	<b>424,103</b>	<b>389,707</b>
Property, plant and equipment, net	179,240	179,012
Intangible assets, net	26,154	27,538
Long-term prepaid expenses	7,456	8,235
Other non-current assets	21,357	21,252
<b>Total assets</b>	<b>\$ 658,310</b>	<b>\$ 625,744</b>
<b>Liabilities and Stockholders Equity</b>		
Current liabilities		
Accounts payable	\$ 74,040	\$ 58,264
Other accounts payable	10,869	14,645
Accrued expenses	43,710	32,635
Current portion of capital lease obligations	5,850	5,557
Other current liabilities	3,932	5,048
<b>Total current liabilities</b>	<b>138,401</b>	<b>116,149</b>
Long-term borrowings, net	246,952	246,882
Long-term obligations under capital lease	1,665	3,105
Accrued severance benefits, net	91,503	87,778
Other non-current liabilities	7,902	8,979
<b>Total liabilities</b>	<b>486,423</b>	<b>462,893</b>
Commitments and contingencies (Note 14)		
Stockholders equity		
Common stock, \$0.01 par value, 150,000,000 shares authorized, 39,356,749 and 38,401,985 shares issued and outstanding at March 31, 2011 and December 31, 2010, respectively	394	384

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Additional paid-in capital	97,812	95,585
Retained earnings	94,625	72,157
Accumulated other comprehensive loss	(20,944)	(5,275)
Total stockholders' equity	171,887	162,851
Total liabilities and stockholders' equity	\$ 658,310	\$ 625,744

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

**Table of Contents****MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited; in thousands of US dollars, except share data)**

	<b>Three Months Ended</b>	
	<b>March 31,</b>	<b>March 31,</b>
	<b>2011</b>	<b>2010</b>
Net sales	\$ 187,921	\$ 179,485
Cost of sales	131,447	130,127
<b>Gross profit</b>	<b>56,474</b>	<b>49,358</b>
Selling, general and administrative expenses	15,401	17,908
Research and development expenses	18,498	20,531
Restructuring and impairment charges		336
IPO incentive	12,146	
Operating income	10,429	10,583
Other income (expenses)		
Interest expense, net	(7,111)	(2,049)
Foreign currency gain, net	21,359	21,616
Other	166	(52)
	14,414	19,515
Income before income taxes	24,843	30,098
Income tax expenses (benefits)	2,375	(1,003)
Net income	\$ 22,468	\$ 31,101
Earnings per common share		
Basic	\$ 0.59	\$ 0.82
Diluted	\$ 0.57	\$ 0.81
Weighted average number of shares		
Basic	38,332,750	37,805,445
Diluted	39,570,522	38,441,991

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

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**MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY**

(Unaudited; in thousands of US dollars, except share data)

	Common Stock		Additional Paid-In Capital	Retained Earnings (Accumulated deficit)	Accumulated Other Comprehensive Income (loss)	Total
	Shares	Amount				
<b>Three Months Ended March 31, 2011</b>						
<b>Balance at January 1, 2011</b>	38,401,985	\$ 384	\$ 95,585	\$ 72,157	\$ (5,275)	\$ 162,851
Stock-based compensation			431			431
Issuance of new stock	950,000	10	1,768			1,778
Exercise of stock options	4,764		28			28
Comprehensive income:						
Net Income				22,468		22,468
Fair valuation of derivatives					2,336	2,336
Reclassification to net income from accumulated other comprehensive loss related to hedge derivatives					(4,293)	(4,293)
Foreign currency translation adjustments					(14,267)	(14,267)
Unrealized gains on investments					555	555
Total comprehensive income						6,799
<b>Balance at March 31, 2011</b>	39,356,749	\$ 394	\$ 97,812	\$ 94,625	\$ (20,944)	\$ 171,887
<b>Three Months Ended March 31, 2010</b>						
<b>Balance at January 1, 2010</b>	38,385,544	\$ 384	\$ 223,451	\$ (1,963)	\$ (6,182)	\$ 215,690
Stock-based compensation	18,750		883			883
Comprehensive income:						
Net income				31,101		31,101
Fair valuation of derivatives					(2,054)	(2,054)
Reclassification to net income from accumulated other comprehensive loss related to hedge derivatives					620	620
Foreign currency translation adjustments					(14,907)	(14,907)
Unrealized gains on investments					112	112
Total comprehensive income						14,872
<b>Balance at March 31, 2010</b>	38,404,294	\$ 384	\$ 224,334	\$ 29,138	\$ (22,411)	\$ 231,445

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



**Table of Contents****MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited; in thousands of US dollars)**

	<b>Three Months Ended</b>	
	<b>March 31,</b>	<b>March</b>
	<b>2011</b>	<b>31,</b>
		<b>2010</b>
<b>Cash flows from operating activities</b>		
Net income	\$ 22,468	\$ 31,101
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	13,903	15,477
Provision for severance benefits	2,854	3,166
Amortization of debt issuance costs and original issue discount	246	25
Gain on foreign currency translation, net	(23,684)	(23,478)
Gain on disposal of property, plant and equipment, net		(9)
Loss on disposal of intangible assets, net	4	2
Restructuring and impairment charges		336
Stock-based compensation	641	1,473
Cash used for reorganization items		1,579
Other	549	393
Changes in operating assets and liabilities		
Accounts receivable	(9,250)	(29,684)
Inventories	(3,467)	7,206
Other receivables	(1,041)	(1,238)
Other current assets	(1,449)	(3,659)
Deferred tax assets	548	264
Accounts payable	14,289	18,088
Other accounts payable	(1,348)	(1,612)
Accrued expenses	7,153	3,196
Other current liabilities	(1,518)	(2,107)
Long term other payable	184	(2,136)
Payment of severance benefits	(1,610)	(1,092)
Other	(256)	(788)
Net cash provided by operating activities before reorganization items	19,216	16,503
Cash used for reorganization items		(1,579)
Net cash provided by operating activities	19,216	14,924
<b>Cash flows from investing activities</b>		
Proceeds from disposal of plant, property and equipment		4
Purchase of plant, property and equipment	(6,779)	(891)
Payment for intellectual property registration	(165)	(152)
Decrease in short-term financial instruments		329
Collection of guarantee deposits	979	972
Payment of guarantee deposits	(1,004)	(56)
Other	(44)	33
Net cash provided by (used in) investing activities	(7,013)	239

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<b>Cash flows from financing activities</b>		
Proceeds from issuance of common stock	11,425	
Repayment of current portion of long-term debt		(154)
Repayment of obligations under capital lease	(1,562)	
Net cash provided by (used in) financing activities	9,863	(154)
Effect of exchange rates on cash and cash equivalents	(59)	2,754
Net increase in cash and cash equivalents	22,007	17,763
<b>Cash and cash equivalents</b>		
Beginning of the period	172,172	64,925
End of the period	\$ 194,179	\$ 82,688
<b>Supplemental cash flow information</b>		
Cash paid for interest	\$ 5,625	\$ 2,035
Cash paid for income taxes	\$ 2,004	\$ 1,513
<b>Noncash transactions</b>		
Deferred offering costs reclassified as reduction of additional paid-in capital	\$ 9,619	\$

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

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**MagnaChip Semiconductor Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements**

**(Unaudited; tabular dollars in thousands, except share data)**

**1. General**

***The Company***

MagnaChip Semiconductor Corporation (together with its subsidiaries, the Company) is a Korea-based designer and manufacturer of analog and mixed-signal semiconductor products for high-volume consumer applications. The Company's business is comprised of three key segments: Display Solutions, Power Solutions and Semiconductor Manufacturing Services. The Company's Display Solutions products include display drivers for use in a wide range of flat panel displays and mobile multimedia devices. The Company's Power Solutions products include discrete and integrated circuit solutions for power management in high-volume consumer applications. The Company's Semiconductor Manufacturing Services segment provides specialty analog and mixed-signal foundry services for fabless semiconductor companies that serve the consumer, computing and wireless end markets.

**2. Significant Accounting Policies**

***Basis of Presentation***

The accompanying unaudited interim consolidated financial statements of the Company have been prepared in accordance with generally accepted accounting principles in the United States of America (US GAAP). These interim consolidated financial statements include all adjustments consisting only of normal recurring adjustments and the elimination of all intercompany accounts and transactions which are, in the opinion of management, necessary to provide a fair presentation of financial condition and results of operations for the periods presented. These interim consolidated financial statements are presented in accordance with ASC 270, *Interim Reporting*, (ASC 270) and, accordingly, do not include all of the information and note disclosures required by US GAAP for complete financial statements. The results of operations for the three months ended March 31, 2011 are not necessarily indicative of the results to be expected for a full year or for any other periods.

The December 31, 2010 balance sheet data was derived from audited financial statements, but does not include all disclosures required by US GAAP.

***Recent Accounting Pronouncements***

In January 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update 2010-06 (ASU 2010-06), which amends the disclosure requirements of ASC 820, *Fair Value Measurements and Disclosures*, (ASC 820) as of January 1, 2010. ASU 2010-06 requires new disclosures for any transfers of fair value into and out of Level 1 and 2 fair value measurements and separate presentation of purchases, sales, issuances and settlements within the reconciliation of Level 3 unobservable inputs. The Company previously adopted ASC 820 on January 1, 2008 and January 1, 2009 for financial assets and liabilities and for nonfinancial assets and liabilities, respectively. ASU 2010-06 is effective for annual and interim periods beginning after December 15, 2009, except for the Level 3 reconciliation which is effective for annual and interim periods beginning after December 15, 2010. The adoption of ASU 2010-06 as of January 1, 2010 did not have a material effect on the Company's financial condition or results of operations. The adoption of ASU 2010-06 in relation to the Level 3 reconciliation as of January 1, 2011 also did not have a material impact on the Company's financial condition or results of operations.

**3. Completion of Initial Public Offering**

Prior to the Company's initial public offering (IPO), the Company's board of directors and the holders of a majority of its outstanding common units elected to convert the Company from a Delaware limited liability company to a Delaware corporation (the Corporation) and to change the Company's name from MagnaChip Semiconductor LLC to MagnaChip Semiconductor Corporation. The corporate conversion was completed on March 10, 2011. In connection with the corporate conversion, outstanding common units of the Company were automatically converted into shares of common stock of the Corporation, outstanding options to purchase common units of the Company were automatically converted into options to purchase shares of common stock of the Corporation and outstanding warrants to purchase common units of the Company were automatically converted into warrants to purchase shares of common stock of the Corporation, all at a ratio of one share of common stock for eight common units.



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**MagnaChip Semiconductor Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements - (Continued)**

**(Unaudited; tabular dollars in thousands, except share data)**

On March 16, 2011, the Company also completed an IPO of 9,500,000 shares of common stock at an offering price of \$14.00 per share and on March 11, 2011 listed on the NYSE. All shares were sold in the form of depositary shares and each depositary share represented an ownership interest in one share of common stock. Of the 9,500,000 shares, 950,000 shares were newly issued by the Company and 8,550,000 shares were sold by selling stockholders. The Company received \$12,369 thousand of net proceeds from the issuance of the new shares of common stock after deducting underwriters' discounts and commissions, and the Company did not receive any proceeds from the sale of shares of common stock offered by the selling stockholders. The Company incurred \$10,591 thousand of IPO expenses that were initially recorded as other current assets and, upon completion of IPO, reclassified as reduction of additional paid-in capital in the consolidated balance sheets.

The Company previously stated an intention to use a part of the net proceeds from the IPO to make incentive payments to all employees, excluding management. The payment of such employee incentives was contingent upon the consummation of the IPO. The Company paid \$12,146 thousand of the incentives in March 2011.

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements - (Continued)****(Unaudited; tabular dollars in thousands, except share data)****4. Inventories**

Inventories as of March 31, 2011 and December 31, 2010 consist of the following:

	<b>March 31, 2011</b>	<b>December 31, 2010</b>
Finished goods	\$ 10,851	\$ 13,529
Semi-finished goods and work-in-process	52,920	50,542
Raw materials	14,740	9,762
Materials in-transit	1,108	1,643
Less: inventory reserve	(5,740)	(7,041)
Inventories, net	\$ 73,879	\$ 68,435

**5. Property, Plant and Equipment**

Property, plant and equipment as of March 31, 2011 and December 31, 2010 comprise the following:

	<b>March 31, 2011</b>	<b>December 31, 2010</b>
Buildings and related structures	\$ 76,061	\$ 73,945
Machinery and equipment	122,220	112,398
Vehicles and others	8,513	8,007
Equipment under capital lease	11,748	11,457
	218,542	205,807
Less: accumulated depreciation	(53,726)	(41,440)
accumulated depreciation on equipment under capital lease	(1,500)	(836)
Land	15,924	15,481
Property, plant and equipment, net	\$ 179,240	\$ 179,012

**6. Intangible Assets**

Intangible assets as of March 31, 2011 and December 31, 2010 are as follows:

	<b>March 31, 2011</b>	<b>December 31, 2010</b>
Technology	\$ 20,762	\$ 19,969
Customer relationships	27,892	27,115

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Intellectual property assets	5,737	5,444
In-process research and development	3,295	3,418
Less: accumulated amortization	(31,532)	(28,408)
Intangible assets, net	\$ 26,154	\$ 27,538

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements - (Continued)****(Unaudited; tabular dollars in thousands, except share data)****7. Derivative Financial Instruments**

The Company's Korean subsidiary entered into option, forward and zero cost collar contracts to hedge the risk of changes in the functional-currency-equivalent cash flows attributable to currency rate changes on U.S. dollar denominated revenues.

Details of derivative contracts as of March 31, 2011 are as follows:

Date of transaction	Type of derivative	Total notional amount	Month of settlement
May 25, 2010	Option	\$ 30,000	January to June 2011
May 25, 2010	Forward	78,000	January to June 2011
August 12, 2010	Zero cost collar	108,000	July to December 2011
January 17, 2011	Zero cost collar	60,000	January to June 2012
March 16, 2011	Zero cost collar	24,000	January to March 2012

The option, forward and zero cost collar contracts qualify as cash flow hedges under ASC 815, *Derivatives and Hedging*, (ASC 815), since at both the inception of the contracts and on an ongoing basis, the hedging relationship was and is expected to be highly effective in achieving offsetting cash flows attributable to the hedged risk during the term of the contracts. The Company is utilizing the hypothetical derivative method to measure the effectiveness by comparing the changes in value of the actual derivative versus the change in fair value of the hypothetical derivative.

The fair values of the Company's outstanding option, forward and zero cost collar contracts recorded as assets and liabilities as of March 31, 2011 and December 31, 2010 are as follows:

		March 31, 2011	December 31, 2010
<b>Derivatives designated as hedging instruments:</b>			
Asset Derivatives:			
Options	Other current assets	\$ 23	\$ 104
Forward	Other current assets	\$ 4,605	\$ 6,674
Zero cost collars	Other current assets	\$ 2,309	\$ 1,544
Liability Derivatives:			
Zero cost collars	Other non current liabilities	\$ 149	\$

For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of accumulated other comprehensive income (AOCI) and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative, representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness, are recognized in current earnings.



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**MagnaChip Semiconductor Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements - (Continued)**

**(Unaudited; tabular dollars in thousands, except share data)**

The following table summarizes the impact of derivative instruments on the consolidated statement of operations for the three months ended March 31, 2011:

Derivatives in Cash Flow	Amount of Gain (Loss) Recognized in AOCI on Derivatives (Effective Portion)	Location of Gain (Loss) Reclassified from AOCI into Statement of Operations (Effective Portion)	Amount of Gain (Loss) Reclassified from AOCI into Statement of Operations (Effective Portion)	Location of Gain (Loss) Recognized in Statement of Operations on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)		Amount of Gain (Loss) Recognized in Statement of Operations on Derivatives (Ineffective Portion and Amount Excluded from Effectiveness Testing)
				Other income (expenses)	Others	
Options	\$ (71)	Net sales	\$ (333)	Other income (expenses)	Others	\$ (11)
Forward	1,810	Net sales	4,626	Other income (expenses)	Others	178
Zero cost collars	597	Net sales		Other income (expenses)	Others	(9)
Total	\$ 2,336		\$ 4,293			\$ 158

The following table summarizes the impact of derivative instruments on the consolidated statement of operations for the three months ended March 31, 2010:

Derivatives in Cash Flow Hedging Relationships	Amount of Loss Recognized in AOCI on	Location of Loss Reclassified from AOCI into	Amount of Loss Reclassified from AOCI into	Location of Loss Recognized in Statement of	Amount of Loss Recognized in Statement of Operations on Derivatives
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	Derivatives (Effective Portion)	Statement of Operations (Effective Portion)	Statement of Operations (Effective Portion)	Operations on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)	(Ineffective Portion and Amount Excluded from Effectiveness Testing)
Options	\$ (533)	Net sales	\$ (17)	Other income (expenses) Others	\$ (33)
Forward	(1,521)	Net sales	(603)	Other income (expenses) Others	(24)
Total	\$ (2,054)		\$ (620)		\$ (57)

The estimated net gain as of March 31, 2011 that is expected to be reclassified from accumulated other comprehensive income (loss) into earnings within the next twelve months is \$6,835 thousand.

The Company's option, forward and zero cost collar contracts are subject to termination upon the occurrence of the following events:

- (i) On the last day of a fiscal quarter, the sum of qualified and unrestricted cash and cash equivalents held by the Company is less than \$30 million.
- (ii) The rating of the Company's debt is B- or lower by Standard & Poor's Ratings Group or any successor rating agency thereof ( S&P ) or B3 or lower by Moody's Investor Services, Inc. or any successor rating agency thereof ( Moody's ) or the Company's debt ceases to be assigned a rating by either S&P or Moody's.

In addition, the Company is required to deposit cash collateral with Goldman Sachs International Bank, the counterparty to the option, forward and zero cost collar contracts, for any exposure in excess of \$5 million.

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements - (Continued)****(Unaudited; tabular dollars in thousands, except share data)****8. Fair Value Measurements**

The Company's assets and liabilities measured at fair value on a recurring basis as of March 31, 2011, and the basis for that measurement is as follows:

	Carrying Value	Fair Value Measurement	Quoted Prices in Active Markets for Identical Asset (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets:</b>					
Current derivative assets	\$ 6,937	\$ 6,937	\$	\$ 6,937	\$
Available-for-sale securities	1,249	1,249	1,249		
<b>Liabilities:</b>					
Non current derivative liabilities	149	149		149	

**9. Capital leases**

The Company entered into several lease agreements for the use of equipment for manufacturing and research and development. These leases are accounted for as capital leases as the ownership of the equipment will be transferred to the Company upon expiration of the lease terms or the Company has bargain purchase options at the end of the lease terms.

<b>Payable during</b>	<b>Capital Lease</b>
Remainder of 2011	\$ 4,753
2012	3,266
2013	24
Total future minimum lease payments	8,043
Less: Amount representing interest (a)	(528)
Present value of net minimum lease payments	7,515
Less: Current portion of capital lease obligations	(5,850)
Long-term obligations under capital lease	\$ 1,665

(a) The lessor's implicit rate at lease inception was applied.

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements - (Continued)****(Unaudited; tabular dollars in thousands, except share data)****10. Accrued Severance Benefits**

The majority of accrued severance benefits is for employees in the Company's Korean subsidiary, MagnaChip Semiconductor Ltd. (Korea). Pursuant to the Employee Retirement Benefit Security Act of Korea, most employees and executive officers with one or more years of service are entitled to severance benefits upon the termination of their employment based on their length of service and rate of pay. As of March 31, 2011, 98.5% of employees of the Company were eligible for severance benefits.

Changes in accrued severance benefits for each period are as follows:

	<b>Three Months Ended</b>	
	<b>March 31, 2011</b>	<b>March 31, 2010</b>
Beginning balance	\$ 88,973	\$ 73,646
Provisions	2,854	3,166
Severance payments	(1,610)	(1,092)
Translation adjustments	2,498	2,386
	92,715	78,106
Less: Cumulative contributions to the National Pension Fund	(463)	(540)
Group Severance insurance plan	(749)	(723)
Accrued severance benefits, net	\$ 91,503	\$ 76,843

The severance benefits are funded approximately 1.31% and 1.62% as of March 31, 2011 and 2010, respectively, through the Company's National Pension Fund and group severance insurance plan which will be used exclusively for payment of severance benefits to eligible employees. These amounts have been deducted from the accrued severance benefit balance.

The Company is liable to pay the following future benefits to its non-executive employees upon their normal retirement age:

	<b>Severance benefit</b>
Remainder of 2011	\$
2012	155
2013	
2014	314
2015	356
2016	1,240
2017 - 2021	13,732

The above amounts were determined based on the non-executive employees' current salary rates and the number of service years that will be accumulated upon their retirement dates. These amounts do not include amounts that might be paid to non-executive employees that will cease working with the Company before their normal retirement ages.



**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements - (Continued)****(Unaudited; tabular dollars in thousands, except share data)****11. Restructuring and Impairment Charges**

The Company recognized \$336 thousand of impairment charges for the three months ended March 31, 2010 from two abandoned in-process research and development projects.

**12. Income Taxes**

The Company files income tax returns in the U.S., Korea, Japan, Taiwan and various other jurisdictions.

The predecessor entity to MagnaChip Semiconductor Corporation (the Parent) was a non-taxable partnership entity until its conversion to a Delaware corporation on March 10, 2011.

MagnaChip Semiconductor Ltd. (Korea) is the principal operating entity within the consolidated Company. For the three months ended March 31, 2011 and 2010, no income tax expense for MagnaChip Semiconductor, Ltd. (Korea) was recorded due to net operating loss carry-forwards available to offset taxable income and full allowance for deferred tax assets.

**13. Geographic and Segment Information**

The following sets forth information relating to the reportable segments:

	<b>Three Months Ended</b>	
	<b>March 31,</b>	<b>March 31,</b>
	<b>2011</b>	<b>2010</b>
<b>Net Sales</b>		
Display Solutions	\$ 74,464	\$ 76,730
Semiconductor Manufacturing Services	92,266	93,201
Power Solutions	20,412	9,034
All other	779	520
Total segment net sales	\$ 187,921	\$ 179,485
<b>Gross Profit</b>		
Display Solutions	\$ 19,843	\$ 14,431
Semiconductor Manufacturing Services	33,287	32,844
Power Solutions	2,565	1,563
All other	779	520
Total segment gross profit	\$ 56,474	\$ 49,358

The following is a summary of net sales by region, based on the location of the customer:

**Three Months Ended**

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	March 31, 2011	March 31, 2010
Korea	\$ 87,513	\$ 97,660
Asia Pacific	57,295	48,474
Japan	13,339	10,195
North America	25,922	20,380
Europe	2,967	2,776
Africa	885	
<b>Total</b>	<b>\$ 187,921</b>	<b>\$ 179,485</b>

Net sales from the Company's top ten largest customers accounted for 61.1% and 64.1% for the three months ended March 31, 2011 and 2010, respectively.

The Company recorded \$26,681 thousand and \$35,578 thousand of sales to one customer within its Display Solutions segment, which represents greater than 10% of net sales, for the three months ended March 31, 2011 and 2010, respectively.

Over 99% of the Company's property, plant and equipment are located in Korea as of March 31, 2011.

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements - (Continued)****(Unaudited; tabular dollars in thousands, except share data)****14. Commitments and Contingencies**

The California Institute of Technology has made a claim against Samsung Fiber Optics for the infringement of certain patent rights in relation to image sensor products provided by Samsung Fiber Optics. Samsung Fiber Optics has made a claim against the Company as a provider of embedded components. The Company believes it is probable that the pending claim will have an unfavorable outcome and further believes the associated loss can be reasonably estimated according to ASC 450 Contingencies (ASC 450). The Company charged the best estimate of loss, \$718 thousand, to operating expenses for the ten month period ended October 25, 2009, and the Company presents the estimated liabilities as accrued expenses as of March 31, 2011 and December 31, 2010 in the accompanying consolidated balance sheets. The estimate was based on the most recent communications with Samsung Fiber Optics. Accordingly, the Company cannot provide assurance that the estimated liabilities will be realized. The actual results could vary materially.

**15. Earnings per Share**

The following table illustrates the computation of basic and diluted earnings per common share:

	Three Months Ended	
	March 31, 2011	March 31, 2010
Net income	\$ 22,468	\$ 31,101
Weighted average common stock outstanding		
Basic	38,332,750	37,805,445
Diluted	39,570,522	38,441,991
Earnings per share		
Basic	\$ 0.59	\$ 0.82
Diluted	\$ 0.57	\$ 0.81

The following outstanding instruments were excluded from the computation of diluted earnings per share, as they have an anti-dilutive effect on the calculation:

	Three Months Ended	
	March 31, 2011	March 31, 2010
Options		114,250
Warrants	1,875,017	1,875,017



**Table of Contents**

**MagnaChip Semiconductor Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements - (Continued)**

**(Unaudited; tabular dollars in thousands, except share data)**

**16. Condensed Consolidating Financial Information**

The \$250 million senior notes are fully and unconditionally, jointly and severally, guaranteed by the Company and all of its subsidiaries, except for MagnaChip Semiconductor, Ltd. (Korea) and MagnaChip Semiconductor (Shanghai) Company Limited.

The senior notes are structurally subordinated to the creditors of the Company's principal manufacturing and selling subsidiary, MagnaChip Semiconductor, Ltd. (Korea), which accounts for substantially all of the Company's net sales and assets.

Below are condensed consolidating balance sheets as of March 31, 2011 and December 31, 2010, condensed consolidating statements of operations for the three months ended March 31, 2011 and 2010 and condensed consolidating statements of cash flows for the three months ended March 31, 2011 and 2010 of those entities that guarantee the senior notes, those that do not, MagnaChip Semiconductor Corporation, and the co-issuers.

For the purpose of the guarantor financial information, the investments in subsidiaries are accounted for under the equity method.

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements - (Continued)****(Unaudited; tabular dollars in thousands, except share data)****Condensed Consolidating Balance Sheets****March 31, 2011**

	<b>MagnaChip Semiconductor Corporation (Parent)</b>	<b>Co-Issuers</b>	<b>Non-Guarantors</b>	<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
<b>Assets</b>						
Current assets						
Cash and cash equivalents	\$ 4,180	\$ 38,205	\$ 144,847	\$ 6,947	\$	\$ 194,179
Accounts receivable, net			132,491	22,460	(23,931)	131,020
Inventories, net			73,879	158	(158)	73,879
Other receivables			5,504	247	(1,745)	4,006
Prepaid expenses	45		13,596	338	(2,897)	11,082
Short-term intercompany loan		95,000		95,000	(190,000)	
Other current assets	34,305	141,236	7,876	125,030	(298,510)	9,937
Total current assets	38,530	274,441	378,193	250,180	(517,241)	424,103
Property, plant and equipment, net						
			178,874	366		179,240
Intangible assets, net						
			25,673	481		26,154
Long-term prepaid expenses						
			15,631	247	(8,422)	7,456
Investment in subsidiaries						
	(560,148)	(654,620)		(474,010)	1,688,778	
Long-term intercompany loan						
	697,125	803,547		637,518	(2,138,190)	
Other non-current assets						
		7,645	7,377	6,335		21,357
Total Assets	\$ 175,507	\$ 431,013	\$ 605,748	\$ 421,117	\$ (975,075)	\$ 658,310
<b>Liabilities and Stockholders Equity</b>						
Current liabilities						
Accounts payable	\$	\$	\$ 96,176	\$ 1,681	\$ (23,817)	\$ 74,040
Other accounts payable	1,766	145	10,027	676	(1,745)	10,869
Accrued expenses	1,855	46,418	151,164	142,898	(298,625)	43,710
Short-term intercompany borrowings						
			95,000	95,000	(190,000)	
Current portion of capital lease obligations						
			5,667	183		5,850
Other current liabilities	(1)		3,517	3,313	(2,897)	3,932
Total current liabilities	3,620	46,563	361,551	243,751	(517,084)	138,401
Long-term borrowings, net						
		944,077	621,000	820,065	(2,138,190)	246,952
Long-term obligations under capital lease						
			1,498	167		1,665
Accrued severance benefits, net						
			90,203	1,300		91,503
Other non-current liabilities						
			5,445	10,879	(8,422)	7,902

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Total liabilities	3,620	990,640	1,079,697	1,076,162	(2,663,696)	486,423
Commitments and contingencies						
Stockholders' equity						
Common stock	394	136,229	39,005	51,976	(227,210)	394
Additional paid-in capital	97,812	(733,795)	(537,359)	(731,907)	2,003,061	97,812
Retained earnings	94,625	58,884	47,870	45,857	(152,611)	94,625
Accumulated other comprehensive loss	(20,944)	(20,945)	(23,465)	(20,971)	65,381	(20,944)
Total stockholders' equity	171,887	(559,627)	(473,949)	(655,045)	1,688,621	171,887
Total liabilities and stockholders' equity	\$ 175,507	\$ 431,013	\$ 605,748	\$ 421,117	\$ (975,075)	\$ 658,310

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements - (Continued)****(Unaudited; tabular dollars in thousands, except share data)****Condensed Consolidating Balance Sheets****December 31, 2010**

	<b>MagnaChip Semiconductor Corporation (Parent)</b>	<b>Co-Issuers</b>	<b>Non- Guarantors</b>	<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
<b>Assets</b>						
Current assets						
Cash and cash equivalents	\$ 79	\$ 46,595	\$ 112,370	\$ 13,128	\$	\$ 172,172
Accounts receivable, net			160,317	60,533	(101,796)	119,054
Inventories, net			68,435	158	(158)	68,435
Other receivables	718	718	23,111	2,969	(24,597)	2,919
Prepaid expenses	52	2	10,957	93	(2,897)	8,207
Short-term intercompany loan		95,000		95,000	(190,000)	
Other current assets	41,363	124,376	9,606	111,628	(268,053)	18,920
Total current assets	42,212	266,691	384,796	283,509	(587,501)	389,707
Property, plant and equipment, net			178,623	389		179,012
Intangible assets, net			27,009	529		27,538
Long-term prepaid expenses			17,371		(9,136)	8,235
Investment in subsidiaries	(567,941)	(641,799)		(475,696)	1,685,436	
Long-term intercompany loan	697,125	792,846		621,000	(2,110,971)	
Other non-current assets		7,819	6,611	6,821	1	21,252
Total Assets	\$ 171,396	\$ 425,557	\$ 614,410	\$ 436,552	\$ (1,022,171)	\$ 625,744
<b>Liabilities and Stockholders Equity</b>						
Current liabilities						
Accounts payable	\$	\$	\$ 118,353	\$ 41,634	\$ (101,723)	\$ 58,264
Other accounts payable	8,334	8,987	15,994	5,927	(24,597)	14,645
Accrued expenses	211	39,887	134,460	126,204	(268,127)	32,635
Short-term intercompany borrowings			95,000	95,000	(190,000)	
Current portion of capital lease obligations			5,373	184		5,557
Other current liabilities			3,815	4,130	(2,897)	5,048
Total current liabilities	8,545	48,874	372,995	273,079	(587,344)	116,149
Long-term borrowings, net		944,007	621,000	792,846	(2,110,971)	246,882
Long-term obligations under capital lease			2,888	217		3,105
Accrued severance benefits, net			86,511	1,267		87,778
Other non-current liabilities			6,653	11,462	(9,136)	8,979

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Total liabilities	8,545	992,881	1,090,047	1,078,871	(2,707,451)	462,893
Commitments and contingencies						
Stockholders' equity						
Common stock	384	136,229	39,005	51,976	(227,210)	384
Additional paid-in capital	95,585	(734,101)	(537,608)	(732,266)	2,003,975	95,585
Retained earnings	72,157	35,823	31,799	43,269	(110,891)	72,157
Accumulated other comprehensive loss	(5,275)	(5,275)	(8,833)	(5,298)	19,406	(5,275)
Total stockholders' equity	162,851	(567,324)	(475,637)	(642,319)	1,685,280	162,851
Total liabilities and stockholders' equity	\$ 171,396	\$ 425,557	\$ 614,410	\$ 436,552	\$ (1,022,171)	\$ 625,744

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements - (Continued)****(Unaudited; tabular dollars in thousands, except share data)****Condensed Consolidating Statements of Operations****For the three months ended March 31, 2011**

	<b>MagnaChip Semiconductor Corporation (Parent)</b>	<b>Co-Issuers</b>	<b>Non-Guarantors</b>	<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
Net sales	\$	\$	\$ 187,750	\$ 6,616	\$ (6,445)	\$ 187,921
Cost of sales			131,445	74	(72)	131,447
Gross profit			56,305	6,542	(6,373)	56,474
Selling, general and administrative expenses	637	235	15,614	3,103	(4,188)	15,401
Research and development expenses			19,301	1,382	(2,185)	18,498
IPO incentive			11,355	791		12,146
Operating income (loss)	(637)	(235)	10,035	1,266		10,429
Other income (expense)		20,752	6,190	(12,528)		14,414
Income (loss) before income taxes, equity in earnings of related equity investment	(637)	20,517	16,225	(11,262)		24,843
Income tax expenses			154	2,221		2,375
Income (loss) before equity in earnings of related investment	(637)	20,517	16,071	(13,483)		22,468
Equity in earnings of related investment	23,105	2,544		16,071	(41,720)	
Net Income	\$ 22,468	\$ 23,061	\$ 16,071	\$ 2,588	\$ (41,720)	\$ 22,468

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements - (Continued)****(Unaudited; tabular dollars in thousands, except share data)****Condensed Consolidating Statements of Operations****For the three months ended March 31, 2010**

	<b>MagnaChip Semiconductor Corporation (Parent)</b>	<b>Co-Issuers</b>	<b>Non-Guarantors</b>	<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
Net sales	\$	\$	\$ 174,814	\$ 11,682	\$ (7,011)	\$ 179,485
Cost of sales			126,504	5,693	(2,070)	130,127
Gross profit			48,310	5,989	(4,941)	49,358
Selling, general and administrative expenses	563	136	17,264	2,587	(2,642)	17,908
Research and development expenses			21,400	2,170	(3,039)	20,531
Restructuring and impairment charges			336			336
Operating income (loss)	(563)	(136)	9,310	1,232	740	10,583
Other income		1,423	7,377	10,715		19,515
Income before income taxes, equity in earnings of related equity investment	(563)	1,287	16,687	11,947	740	30,098
Income tax expenses (benefits)			(1,959)	956		(1,003)
Income before equity in earnings of related investment	(563)	1,287	18,646	10,991	740	31,101
Equity in earnings of related investment	31,664	30,507		18,940	(81,111)	
Net income	\$ 31,101	\$ 31,794	\$ 18,646	\$ 29,931	\$ (80,371)	\$ 31,101

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements - (Continued)****(Unaudited; tabular dollars in thousands, except share data)****Condensed Consolidating Statements of Cash Flows****For the three months ended March 31, 2011**

	<b>MagnaChip Semiconductor Corporation (Parent)</b>	<b>Co-Issuers</b>	<b>Non-Guarantors</b>	<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
<b>Cash flow from operating activities</b>						
Net income	\$ 22,468	\$ 23,061	\$ 16,071	\$ 2,588	\$ (41,720)	\$ 22,468
Adjustments to reconcile net income to net cash provided by (used in) operating activities						
Depreciation and amortization			13,826	77		13,903
Provision for severance benefits			2,796	58		2,854
Amortization of debt issuance costs and original issue discount.		246				246
Loss (gain) on foreign currency translation, net		(10,701)	(24,128)	11,145		(23,684)
Loss on disposal of intangible assets, net			4			4
Stock-based compensation	73		590	335	(357)	641
Equity in earnings of related investment	(23,105)	(2,544)		(16,071)	41,720	
Other	(1)		290	232	28	549
Changes in operating assets and liabilities						
Accounts receivable, net			30,499	38,116	(77,865)	(9,250)
Inventories, net			(3,467)			(3,467)
Other receivables	718	718	17,656	2,719	(22,852)	(1,041)
Other current assets	(713)	(16,858)	(531)	(14,432)	31,085	(1,449)
Deferred tax assets				548		548
Accounts payable			(22,873)	(40,744)	77,906	14,289
Other accounts payable	(6,613)	(8,842)	(3,455)	(5,290)	22,852	(1,348)
Accrued expenses	(151)	6,530	14,904	16,996	(31,126)	7,153
Other current liabilities			(415)	(1,103)		(1,518)
Long term other payable				184		184
Payment of severance benefits			(1,610)			(1,610)
Other			972	(1,228)		(256)
Net cash provided by (used in) operating activities	(7,324)	(8,390)	41,129	(5,870)	(329)	19,216
<b>Cash flows from investing activities</b>						
Purchases of plant, property and equipment			(6,765)	(14)		(6,779)
Payment for intellectual property registration			(165)			(165)
Collection of guarantee deposits			979			979
Payment of guarantee deposits			(1,004)			(1,004)
Other			(23)	(21)		(44)



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Net cash used in investing activities			(6,978)	(35)		(7,013)
<b>Cash flow from financing activities</b>						
Proceeds from issuance of common stock	11,425					11,425
Repayment of obligations under capital lease			(1,515)	(47)		(1,562)
Net cash provided by (used in) financing activities	11,425		(1,515)	(47)		9,863
Effect of exchanges rate on cash and cash equivalents			(159)	(229)	329	(59)
Net increase (decrease) in cash and cash equivalents	4,101	(8,390)	32,477	(6,181)		22,007
<b>Cash and cash equivalents</b>						
Beginning of the period	79	46,595	112,370	13,128		172,172
End of the period	\$ 4,180	\$ 38,205	\$ 144,847	\$ 6,947	\$	\$ 194,179

**Table of Contents****MagnaChip Semiconductor Corporation and Subsidiaries****Notes to Consolidated Financial Statements - (Continued)****(Unaudited; tabular dollars in thousands, except share data)****Condensed Consolidating Statements of Cash Flows****For the three months ended March 31, 2010**

	<b>MagnaChip Semiconductor Corporation (Parent)</b>	<b>Co-Issuers</b>	<b>Non-Guarantors</b>	<b>Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
<b>Cash flow from operating activities</b>						
Net income	\$ 31,101	\$ 31,794	\$ 18,646	\$ 29,931	\$ (80,371)	\$ 31,101
Adjustments to reconcile net income to net cash provided by (used in) operating activities						
Depreciation and amortization			15,405	72		15,477
Provision for severance benefits			3,081	85		3,166
Amortization of debt issuance costs		25				25
Loss (gain) on foreign currency translation, net		11,757	(23,734)	(11,501)		(23,478)
Loss (gain) on disposal of property, plant and equipment			(9)			(9)
Loss on disposal of intangible assets, net			2			2
Restructuring and impairment charges			336			336
Stock-based compensation	334		1,040	99		1,473
Cash used for reorganization items			51	1,528		1,579
Equity in earnings of related investment	(31,664)	(30,507)		(18,940)	81,111	
Other		1	480	(88)		393
<b>Changes in operating assets and liabilities</b>						
Accounts receivable, net			(18,065)	15,150	(26,769)	(29,684)
Inventories			3,661	4,312		