

ALPHA & OMEGA SEMICONDUCTOR Ltd
Form 10-Q
February 09, 2017
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(MARK ONE)

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

For the quarterly period ended December 31, 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 001-34717

Alpha and Omega Semiconductor Limited
(Exact name of Registrant as Specified in its Charter)

Bermuda 77-0553536

(State or Other Jurisdiction of Incorporation or Organization) (I.R.S. Employer Identification Number)

Clarendon House, 2 Church Street

Hamilton HM 11, Bermuda

(Address of Principal Registered

Offices including Zip Code)

(408) 830-9742

(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 smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

(Do not check if a smaller reporting company)

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

Number of common shares outstanding as of January 31, 2017: 23,605,765

Alpha and Omega Semiconductor Limited
 Form 10-Q
 Fiscal First Quarter Ended December 31, 2016
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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ALPHA AND OMEGA SEMICONDUCTOR LIMITED
CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited, in thousands except par value per share)

| | December 31, 2016 | June 30, 2016 |
|--|----------------------|------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 122,793 | \$ 87,774 |
| Restricted cash | 324 | 188 |
| Accounts receivable, net | 24,482 | 26,594 |
| Inventories | 70,239 | 68,848 |
| Other current assets | 5,762 | 4,526 |
| Total current assets | 223,600 | 187,930 |
| Property, plant and equipment, net | 122,686 | 116,084 |
| Deferred income tax assets - long term | 5,502 | 12,132 |
| Other long-term assets | 10,240 | 2,359 |
| Total assets | \$ 362,028 | \$ 318,505 |
| LIABILITIES AND EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 38,010 | \$ 42,718 |
| Accrued liabilities | 25,099 | 22,590 |
| Income taxes payable | 2,583 | 2,356 |
| Deferred margin | 955 | 997 |
| Capital leases | 809 | 819 |
| Total current liabilities | 67,456 | 69,480 |
| Income taxes payable - long term | 1,608 | 1,577 |
| Deferred income tax liabilities | 2,924 | 2,973 |
| Capital leases - long term | 1,296 | 1,695 |
| Other long term liabilities | 623 | 741 |
| Total liabilities | 73,907 | 76,466 |
| Commitments and contingencies (Note 9) | | |
| Equity: | | |
| Preferred shares, par value \$0.002 per share: | | |
| Authorized: 10,000 shares, issued and outstanding: none at December 31, 2016 and June 30, 2016 | — | — |
| Common shares, par value \$0.002 per share: | | |
| Authorized: 50,000 shares, issued and outstanding: 29,214 shares and 23,594 shares, respectively at December 31, 2016 and 28,405 shares and 22,754 shares, respectively at June 30, 2016 | | 57 |
| Treasury shares at cost, 5,620 shares at December 31, 2016 and 5,651 shares at June 30, 2016 | (49,934 |) (50,199) |
| Additional paid-in capital | 202,370 | 191,444 |
| Accumulated other comprehensive income (loss) | (422 |) 769 |
| Retained earnings | 106,284 | 100,071 |

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| | | |
|--|------------|-----------|
| Total Alpha and Omega Semiconductor Limited shareholder's equity | 258,356 | 242,142 |
| Noncontrolling interest | 29,765 | (103) |
| Total equity | 288,121 | 242,039 |
| Total liabilities and equity | \$ 362,028 | \$318,505 |

See accompanying notes to these condensed consolidated financial statements.

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ALPHA AND OMEGA SEMICONDUCTOR LIMITED
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 (Unaudited, in thousands except per share data)

| | Three Months Ended December 31, | | Six Months Ended December 31, | |
|--|---------------------------------------|------------|----------------------------------|------------|
| | 2016 | 2015 | 2016 | 2015 |
| Revenue | \$94,687 | \$79,825 | \$192,049 | \$161,264 |
| Cost of goods sold | 72,593 | 64,853 | 148,011 | 131,231 |
| Gross profit | 22,094 | 14,972 | 44,038 | 30,033 |
| Operating expenses | | | | |
| Research and development | 7,284 | 5,941 | 14,303 | 12,105 |
| Selling, general and administrative | 11,974 | 8,872 | 23,157 | 18,369 |
| Impairment of long-lived assets | — | 432 | — | 432 |
| Total operating expenses | 19,258 | 15,245 | 37,460 | 30,906 |
| Operating income (loss) | 2,836 | (273) | 6,578 | (873) |
| Interest income and other income (loss), net | (70) | (316) | (119) | (467) |
| Interest expense | (24) | (7) | (50) | (17) |
| Net income (loss) before income taxes | 2,742 | (596) | 6,409 | (1,357) |
| Income tax expense | 1,085 | 1,015 | 2,322 | 2,229 |
| Net income (loss) including noncontrolling interest | 1,657 | (1,611) | 4,087 | (3,586) |
| Net loss attributable to noncontrolling interest | (1,190) | — | (2,067) | — |
| Net income (loss) attributable to Alpha and Omega Semiconductor Limited | \$2,847 | \$(1,611) | \$6,154 | \$(3,586) |
| Net income (loss) per common share attributable to Alpha and Omega Semiconductor Limited | | | | |
| Basic | \$0.12 | \$(0.07) | \$0.26 | \$(0.16) |
| Diluted | \$0.11 | \$(0.07) | \$0.25 | \$(0.16) |
| Weighted average number of common shares attributable to Alpha and Omega Semiconductor Limited used to compute net income (loss) per share | | | | |
| Basic | 23,481 | 22,269 | 23,256 | 22,483 |
| Diluted | 24,977 | 22,269 | 24,695 | 22,483 |

See accompanying notes to these condensed consolidated financial statements.

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ALPHA AND OMEGA SEMICONDUCTOR LIMITED
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
 (Unaudited, in thousands)

| | Three Months | | Six Months | |
|---|----------------|-----------|----------------|-----------|
| | Ended December | | Ended December | |
| | 31, | 31, | 31, | 31, |
| | 2016 | 2015 | 2016 | 2015 |
| Net income (loss) including noncontrolling interest | \$1,657 | \$(1,611) | \$4,087 | \$(3,586) |
| Other comprehensive income, net of tax | | | | |
| Foreign currency translation adjustment | (2,326) | 11 | (2,256) | (155) |
| Comprehensive income (loss) | (669) | (1,600) | 1,831 | (3,741) |
| Noncontrolling interest | (2,234) | — | (3,132) | — |
| Comprehensive income (loss) attributable to Alpha and Omega Semiconductor Limited | \$1,565 | \$(1,600) | \$4,963 | \$(3,741) |

See accompanying notes to these condensed consolidated financial statements.

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, in thousands)

| | Six Months Ended December 31, | |
|---|----------------------------------|------------|
| | 2016 | 2015 |
| Cash flows from operating activities | | |
| Net income (loss) | \$4,087 | \$(3,586) |
| Adjustments to reconcile net loss to net cash provided by operating activities: | | |
| Depreciation and amortization | 13,263 | 13,778 |
| Share-based compensation expense | 2,870 | 1,874 |
| Deferred income taxes, net | 6,581 | 506 |
| Gain on disposal of property and equipment | (370) |) |
| Impairment of long-lived assets | — | 432 |
| Changes in assets and liabilities: | | |
| Accounts receivable | 2,112 | 12,727 |
| Inventories | (1,391) |) 3,073 |
| Other current and long-term assets | (7,032) |) 831 |
| Accounts payable | (4,605) |) (6,454) |
| Income taxes payable | 257 | 364 |
| Accrued and other liabilities | 2,297 | 1,086 |
| Net cash provided by operating activities | 18,069 | 24,631 |
| Cash flows from investing activities | | |
| Purchases of property and equipment | (23,740) |) (10,770) |
| Proceeds from sale of property and equipment | 411 | — |
| (Increase) decrease in restricted cash | (135) |) 137 |
| Net cash used in investing activities | (23,464) |) (10,633) |
| Cash flows from financing activities | | |
| Proceeds from investment by noncontrolling interest | 33,000 | — |
| Withholding tax on restricted stock units | (348) |) (189) |
| Proceeds from exercise of stock options and ESPP | 8,729 | 2,772 |
| Payment for repurchases of common shares | — | (40,257) |
| Principal payments on capital leases | (408) |) (456) |
| Net cash provided by (used in) financing activities | 40,973 | (38,130) |
| Effect of exchange rate changes on cash and cash equivalents | (559) |) (95) |
| Net increase (decrease) in cash and cash equivalents | 35,019 | (24,227) |
| Cash and cash equivalents at beginning of period | 87,774 | 106,085 |
| Cash and cash equivalents at end of period | \$122,793 | \$81,858 |
| Supplemental disclosures of non-cash investing and financing information: | | |
| Property and equipment purchased but not yet paid | \$5,153 | \$1,645 |
| Re-issuance of treasury stock | \$59 | \$43 |

See accompanying notes to these condensed consolidated financial statements.

ALPHA AND OMEGA SEMICONDUCTOR LIMITED
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. The Company and Significant Accounting Policies

The Company

Alpha and Omega Semiconductor Limited and its subsidiaries (the "Company," "AOS," "we" or "us") design, develop and supply a broad range of power semiconductors. The Company's portfolio of products targets high-volume applications, including personal computers, flat panel TVs, LED lighting, smart phones, battery packs, consumer and industrial motor controls and power supplies for TVs, computers, servers and telecommunications equipment. The Company conducts its operations primarily in the United States of America ("USA"), Hong Kong, China, Taiwan, Korea and Japan.

Basis of Preparation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP") for interim financial information and with the instructions to Article 10 of Securities and Exchange Commission Regulation S-X, as amended. They do not include all information and footnotes necessary for a fair presentation of financial position, results of operations and cash flows in conformity with U.S. 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 the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2016. 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 results of operations for the periods presented have been included in the interim periods. Operating results for the six months ended December 31, 2016 are not necessarily indicative of the results that may be expected for the fiscal year ending June 30, 2017. The condensed consolidated balance sheet at June 30, 2016 is derived from the audited financial statements included in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2016.

Reclassification

The Company has reclassified certain amounts previously reported in its financial statements to conform to the current presentation. These reclassifications did not have a material impact on our consolidated financial statements.

Joint Venture

In March 2016, the Company executed an agreement with two strategic investment funds owned by the Municipality of Chongqing, China (the "Chongqing Funds") to form a joint venture for a new state-of-the-art power semiconductor packaging, testing and wafer fabrication facility in Liangjiang New Area of Chongqing (the "Joint Venture"). The initial capitalization of the Joint Venture under the agreement is \$330.0 million, which includes cash contributions from the Chongqing Funds and contributions of cash, equipment and intangible assets from the Company. The Company owns 51% and the Chongqing Funds owns 49% of the equity interest of the Joint Venture. The financial statements of the Joint Venture are consolidated in the financial statements of the company because the Company has a controlling financial interest.

Use of Estimates

The preparation of the condensed consolidated financial statements in conformity with U.S. GAAP requires the Company to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses. To the extent there are material differences between these estimates and actual results, the Company's condensed consolidated financial statements will be affected. On an ongoing basis, the Company evaluates the estimates, judgments and assumptions including those related to stock rotation returns, price adjustments, allowance for doubtful accounts, inventory reserves, warranty accrual, income taxes, share-based compensation, and useful lives for property, plant and equipment and intangible assets.

Fair Value of Financial Instruments

The fair values of cash equivalents are based on observable market prices and have been categorized in Level 1 in the fair value hierarchy. Cash equivalents consist primarily of short term bank deposits. The carrying values of financial instruments

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ALPHA AND OMEGA SEMICONDUCTOR LIMITED
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

such as cash and cash equivalents, accounts receivable and accounts payable approximate their carrying values due to their short-term maturities.

Impairment of Long-Lived Assets

Long-lived assets or asset groups are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset might not be recoverable. Factors that would necessitate an impairment assessment include a significant decline in the observable market value of an asset, a significant change in the extent or manner in which an asset is used, or any other significant adverse change that would indicate that the carrying amount of an asset or group of assets may not be recoverable. Where such factors indicate potential impairment, the recoverability of an asset or asset group is assessed by determining if the carrying value of the asset or asset group exceeds the sum of the projected undiscounted cash flows expected to result from the use and eventual disposition of the assets over the remaining economic life. The impairment loss is measured based on the difference between the carrying amount and the estimated fair value.

Comprehensive Income (Loss)

Comprehensive income (loss) is defined as the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. The Company's accumulated other comprehensive income (loss) consists of cumulative foreign currency translation adjustments. Total comprehensive income (loss) is presented in the condensed consolidated statements of comprehensive income (loss).

Recent Accounting Pronouncements

In November 2016, the Financial Accounting Standards Board ("FASB") issued ASU 2016-18, "Statement of Cash Flows: Restricted Cash ("ASU 2016-18"). ASU 2016-18 requires amounts generally described as restricted cash and restricted cash equivalents be included with cash and cash equivalents when reconciling the total beginning and ending amounts for the periods shown on the statement of cash flows. This ASU will be effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years, with early adoption permitted and requires retrospective adoption. The Company does not expect the adoption of this guidance will have a material impact on its consolidated financial position, results of operations or cash flows.

In October 2016, the FASB issued ASU No. 2016-16, "Income Taxes - Intra-Entity Transfers of Assets Other Than Inventory ("ASU 2016-16"). ASU 2016-16 requires entities to recognize income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. The amended guidance is effective for annual reporting periods beginning after December 15, 2018, and interim reporting periods within annual periods beginning after December 15, 2019. Early adoption is permitted. The Company is currently evaluating the impact the adoption of ASU 2016-16 will have on its consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments ("ASU 2016-15"). ASU 2016-15 identifies how certain cash receipts and cash payments are presented and classified in the Statement of Cash Flows under Topic 230. ASU 2016-15 is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years, with early adoption permitted. Upon adoption, entities must apply the guidance retrospectively to all periods presented. The Company is currently evaluating the impact the adoption of ASU 2016-15 will have on its consolidated financial statements.

In May 2016, the FASB issued Accounting Standards Update ("ASU") 2016-12, "Revenue from Contracts with Customers (Topic 606) - Narrow-Scope Improvements and Practical Expedients." ASU 2016-12 provides additional guidance established by the FASB-IASB Joint Transition Resource Group for Revenue Recognition regarding the

implementation of certain aspects of the new revenue recognition guidance. More specifically, the amendment provides additional guidance regarding assessing the collectibility criterion, the presentation of sales taxes and other similar taxes collected from customers, noncash consideration, contract modifications or completed contracts at transition of the new revenue recognition guidance and technical corrections. The effective date is consistent with the effective date of ASU 2014-09. The Company is currently evaluating the impact the adoption of ASU 2016-12 will have on its consolidated financial statements. The Company does not plan to early adopt this standard.

ALPHA AND OMEGA SEMICONDUCTOR LIMITED
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

In April 2016, the FASB issued ASU 2016-10, Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing ("ASU 2016-10"). ASU 2016-10 clarifies two aspects of Topic 606: (a) identifying performance obligations; and (b) the licensing implementation guidance. The update is effective for annual periods beginning after December 15, 2017 including interim reporting periods therein. The Company is currently evaluating the impact the adoption of ASU 2016-10 will have on its consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, Improvements to Employee Share-Based Payment Accounting ("ASU 2016-09"). ASU 2016-09 simplifies several aspects of the accounting for employee share-based payment transactions including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification of related amounts within the statement of cash flows. This guidance is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Early adoption is permitted. The Company does not expect the adoption of this guidance will have a material impact on its consolidated financial position, results of operations or cash flows.

In February 2016, the FASB issued No. 2016-02, Leases ("ASU 2016-02"). This guidance requires a dual approach for lessee accounting under which a lessee will account for leases as finance leases or operating leases. Both finance and operating leases will result in the lessee recognizing a right-of-use asset and a corresponding liability on its balance sheet, with differing methodology for income statement recognition. This guidance is effective for public business entities for fiscal years, and interim periods within those years, beginning after December 15, 2018, and early adoption is permitted. A modified retrospective approach is required for all leases existing or entered into after the beginning of the earliest comparative period in the consolidated financial statements. The Company is currently assessing the impact that adoption of this guidance will have on its consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers ("ASU 2014-09"). The standard provides companies with a single model for use in accounting for revenue arising from contracts with customers and supersedes current revenue recognition guidance, including industry-specific revenue guidance. The core principle of the model is to recognize revenue when control of the goods or services transfers to the customer, as opposed to recognizing revenue when the risks and rewards transfer to the customer under the existing revenue guidance. In August 2015, the FASB issued an accounting standard update for a one-year deferral of the effective date of ASU 2014-09 to annual and interim periods beginning after December 15, 2017 and permits entities to early adopt the standard of ASU 2014-09 for annual and interim reporting periods beginning after December 15, 2016. Companies are permitted to either apply the requirements retrospectively to all prior periods presented, or apply the requirements in the year of adoption, through a cumulative adjustment. The Company is in the process of evaluating the timing of its adoption and the impact of adoption on its consolidated financial statements.

ALPHA AND OMEGA SEMICONDUCTOR LIMITED
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

2. Net Income (Loss) Per Common Share Attributable to Alpha and Omega Semiconductor Limited

The following table presents the calculation of basic and diluted net income (loss) per share attributable to common shareholders:

| | Three Months Ended December 31, 2016 | | Six Months Ended December 31, 2015 | |
|--|---|-----------|---|-----------|
| | (in thousands, except per share data) | | | |
| Numerator: | | | | |
| Net income (loss) attributable to Alpha and Omega Semiconductor Limited | \$2,847 | \$(1,611) | \$6,154 | \$(3,586) |
| Denominator: | | | | |
| Basic: | | | | |
| Weighted average number of common shares used to compute basic net income (loss) per share | 23,481 | 22,269 | 23,256 | 22,483 |
| Diluted: | | | | |
| Weighted average number of common shares used to compute basic net income (loss) per share | 23,481 | 22,269 | 23,256 | 22,483 |
| Effect of potentially dilutive securities: | | | | |
| Stock options, RSUs and ESPP shares | 1,496 | — | 1,439 | — |
| Weighted average number of common shares used to compute diluted net income (loss) per share | 24,977 | 22,269 | 24,695 | 22,483 |
| Net income (loss) per share attributable to Alpha and Omega Semiconductor Limited: | | | | |
| Basic | \$0.12 | \$(0.07) | \$0.26 | \$(0.16) |
| Diluted | \$0.11 | \$(0.07) | \$0.25 | \$(0.16) |

The following potential dilutive securities were excluded from the computation of diluted net income (loss) per share as their effect would have been anti-dilutive:

| | Three Months Ended December 31, 2016 | | Six Months Ended December 31, 2015 | |
|-------------------------------------|---|-------|--|-------|
| | (in thousands) | | (in thousands) | |
| Employee stock options and RSUs | — | 3,299 | 123 | 3,458 |
| ESPP | 16 | 551 | 8 | 369 |
| Total potential dilutive securities | 16 | 3,850 | 131 | 3,827 |

ALPHA AND OMEGA SEMICONDUCTOR LIMITED
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
 (Unaudited)

3. Concentration of Credit Risk and Significant Customers

The Company manages its credit risk associated with exposure to distributors and direct customers on outstanding accounts receivable through the application and review of credit approvals, credit ratings and other monitoring procedures. In some instances, the Company also obtains letters of credit from certain customers.

Credit sales, which are mainly on credit terms of 30 to 60 days, are only made to customers who meet the Company's credit requirements, while sales to new customers or customers with low credit ratings are usually made on an advance payment basis. The Company considers its trade accounts receivable to be of good credit quality because its key distributors and direct customers have long-standing business relationships with the Company and the Company has not experienced any significant write-offs of accounts receivable in the past. The Company closely monitors the aging of accounts receivable from its distributors and direct customers, and regularly reviews their financial positions, when available.

Summarized below are individual customers whose revenue or accounts receivable balances were more than 10% of the respective total consolidated amounts:

| | Three Months Ended December 31, | | Six Months Ended December 31, | |
|-----------------------|------------------------------------|-------|----------------------------------|-------|
| Percentage of revenue | 2016 | 2015 | 2016 | 2015 |
| Customer A | 27.0% | 24.0% | 25.6% | 23.6% |
| Customer B | 35.8% | 39.6% | 36.2% | 37.8% |
| Customer C | 10.7% | 10.8% | 12.3% | 12.6% |

| | December 31, 2016 | | June 30, 2016 | |
|-----------------------------------|-------------------|---|---------------|---|
| Percentage of accounts receivable | | % | | % |
| Customer A | 35.8 | % | 21.3 | % |
| Customer B | 9.6 | % | 16.7 | % |
| Customer C | 24.7 | % | 27.2 | % |

4. Balance Sheet Components

Accounts receivable:

| | December 31, 2016 | | June 30, 2016 | |
|---------------------------------------|-------------------|--|---------------|--|
| | (in thousands) | | | |
| Accounts receivable | \$42,109 | | \$43,324 | |
| Less: Allowance for price adjustments | (17,597) | | (16,700) | |
| Less: Allowance for doubtful accounts | (30) | | (30) | |
| Accounts receivable, net | \$24,482 | | \$26,594 | |

Inventories:

| | December 31, 2016 | | June 30, 2016 | |
|-----------------|-------------------|--|---------------|--|
| | (in thousands) | | | |
| Raw materials | \$25,622 | | \$23,982 | |
| Work in-process | 34,369 | | 32,446 | |
| Finished goods | 10,248 | | 12,420 | |
| | \$70,239 | | \$68,848 | |

ALPHA AND OMEGA SEMICONDUCTOR LIMITED
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
 (Unaudited)

Property, plant and equipment, net:

| | December 31, 2016 | June 30, 2016 |
|--|----------------------|------------------|
| | (in thousands) | |
| Land | \$4,877 | \$4,877 |
| Building | 4,325 | 4,323 |
| Manufacturing machinery and equipment | 201,425 | 193,164 |
| Equipment and tooling | 13,185 | 12,289 |
| Computer equipment and software | 23,921 | 23,448 |
| Office furniture and equipment | 1,943 | 1,822 |
| Leasehold improvements | 28,896 | 28,660 |
| | 278,572 | 268,583 |
| Less: Accumulated depreciation | (179,760) | (168,687) |
| | 98,812 | 99,896 |
| Equipment and construction in progress | 23,874 | 16,188 |
| Property, plant and equipment, net | \$122,686 | \$116,084 |

Other long-term assets:

| | December 31, 2016 | June 30, 2016 |
|--|----------------------|------------------|
| | (in thousands) | |
| Prepayments for property and equipment | \$2,087 | \$ 506 |
| Prepayment for others | 226 | 42 |
| Prepaid income tax | 4,998 | — |
| Investment in a privately held company | 100 | 100 |
| Office leases deposits | 2,546 | 1,427 |
| Intangible assets | 14 | 15 |
| Goodwill | 269 | 269 |
| | \$10,240 | \$ 2,359 |

Accrued liabilities:

| | December 31, 2016 | June 30, 2016 |
|-------------------------------------|----------------------|------------------|
| | (in thousands) | |
| Accrued compensation and benefit | \$13,457 | \$10,211 |
| Warranty accrual | 2,382 | 1,495 |
| Stock rotation accrual | 1,707 | 1,988 |
| Accrued professional fees | 1,741 | 1,867 |
| Accrued inventory | 448 | 918 |
| Accrued facilities related expenses | 1,269 | 1,544 |
| Other accrued expenses | 4,095 | 4,567 |
| | \$25,099 | \$22,590 |

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The activities in the warranty accrual, included in accrued liabilities, are as follows:

| | Six Months Ended December 31, | |
|-------------------|-------------------------------------|----------|
| | 2016 | 2015 |
| | (in thousands) | |
| Beginning balance | \$1,495 | \$1,957 |
| Additions | 1,040 | 747 |
| Utilization | (153) | (1,108) |
| Ending balance | \$2,382 | \$1,596 |

The activities in the stock rotation accrual, included in accrued liabilities, are as follows:

| | Six Months Ended December 31, | |
|-------------------|-------------------------------------|----------|
| | 2016 | 2015 |
| | (in thousands) | |
| Beginning balance | \$1,988 | \$1,894 |
| Additions | 3,008 | 3,120 |
| Utilization | (3,289) | (3,142) |
| Ending balance | \$1,707 | \$1,872 |

Other Long-term liabilities:

| | December 31, | |
|---------------|----------------|--------|
| | 2016 | 2016 |
| | (in thousands) | |
| Deferred rent | \$ 623 | \$ 741 |

5. Joint Venture

On March 29, 2016, the Company entered into a joint venture contract (the “JV Agreement”) with two investment funds owned by the Municipality of Chongqing (the “Chongqing Funds”), pursuant to which the Company and the Chongqing Funds formed a joint venture, (the “JV Company”), for the purpose of constructing a power semiconductor packaging, testing and 12-inch wafer fabrication facility in the Liangjiang New Area of Chongqing, China (the “JV Transaction”). The total initial capitalization of the JV Company is \$330.0 million (the “Initial Capitalization”), which includes cash contribution from the Chongqing Funds and contributions of cash, equipments and intangible assets from the Company. The Initial Capitalization will be completed in stages commencing on the incorporation of the JV Company. The Company owns 51%, and the Chongqing Funds owns 49%, of the equity interest in the JV Company. If both parties agree that the termination of the JV Company is the best interest of each party or the JV Company is bankrupt or insolvent where either party may terminate early, after paying the debts of the JV Company, the remaining assets of the JV Company shall be paid to the Chongqing Funds to cover the principal of its total paid-in contributions plus interest at 10% simple annual rate prior to distributing the balance of the JV Company's assets to the Company. The Company expects the JV Company to commence its initial production in the first half of fiscal 2018.

As part of the JV Transaction, the JV Company entered into an Engineering, Procurement and Construction Contract (the "EPC Contract") with The IT Electronics Eleventh Design & Research Institute Scientific and Technological Engineering Corporation Limited (the "Contractor"), effective as of January 10, 2017 (the "Effective Date"), pursuant which the Contractor

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was engaged to construct the manufacturing facility contemplated under the JV Agreement. Under the EPC Contract, the Contractor's obligations include, but are not limited to: (i) the development of conceptual design, initial design, construction drawing design and optimization, and submission of such designs to the JV Company for examination and confirmation; and (ii) the construction of the assembly and wafer fabrication facilities and related procurement services, including the selection and engagement of subcontractors, in accordance with a construction schedule agreed upon by the parties. The total price payable under the EPC Contract is Chinese Renminbi (RMB) 540,000,000, or approximately \$77,996,360 based on the currency exchange rate between RMB and U.S. Dollars on the Effective Date, which consists of \$2,820,154 (RMB 19,525,052) of design fees ("Design Fees") and \$75,176,206 (RMB 520,474,948) of construction and procurement fees (including compliance with safety and aesthetic requirements) ("Construction Fees"). The Design Fees and Construction Fees will be paid by the JV Company pursuant to a payment schedule based on the progress of the construction and the achievements of specified milestones, approximately \$58.3 million and \$19.7 million in calendar year 2017 and 2018, respectively. The payment may be subject to volatility as a result of exposure to fluctuations in RMB foreign exchange rates.

The Company began consolidating the financial statements of the JV Company in the quarter ended June 30, 2016. During the quarter ended September 30, 2016, the Chongqing Funds contributed \$33.0 million of initial capital in cash and the Company fulfilled its obligation to contribute certain packaging equipments as required by the JV Agreement by transferring the legal titles of such equipment to the JV Company. Within one year from June 30, 2016, the Company expects to contribute certain intangible assets and cash of \$10.0 million pursuant to the terms of the JV Agreement.

The changes in total stockholders' equity and noncontrolling interest were as follows (in thousands):

| | Total AOS Stockholders' Equity | Noncontrolling Interest | Total Equity |
|--|--------------------------------------|----------------------------|-----------------|
| Balance, June 30, 2016 | \$ 242,142 | \$ (103) | \$ 242,039 |
| Contributions from noncontrolling interest | — | 33,000 | 33,000 |
| Exercise of common stock options and release of RSUs | 7,239 | — | 7,239 |
| Issuance of shares under ESPP | 1,166 | — | 1,166 |
| Reissuance of treasury stock upon exercise of common stock options and release of RSUs | 324 | — | 324 |
| Withholding tax on restricted stock units | (348) | — | (348) |
| Stock-based compensation expense | 2,870 | — | 2,870 |
| Net income (loss) | 6,154 | (2,067) | 4,087 |
| Cumulative translation adjustment | (1,191) | (1,065) | (2,256) |
| Balance, December 31, 2016 | \$ 258,356 | \$ 29,765 | \$ 288,121 |

6. Shareholders' Equity and Share-based Compensation

Share Repurchase

In April 2015, the Board of Directors approved an increase in the remaining available amount under the Company's then effective share repurchase program from approximately \$17.8 million to \$50.0 million. The repurchases may be made from the open market pursuant to a pre-established Rule 10b5-1 trading plan (as amended, the "Repurchase Trading Plan") or through privately negotiated transactions.

In July 2015, the Company completed a Dutch tender offer (the "Tender Offer") in which it purchased 3,296,703 shares of its common shares, at a purchase price of \$9.10 per share, for an aggregate purchase price of \$30.0 million, excluding fees and expenses relating to the Tender Offer. The Tender Offer was part of the \$50.0 million share repurchase program approved by the Board on April 15, 2015. Shares repurchased are accounted for as treasury shares and the total cost of shares repurchased is recorded as a reduction of shareholders' equity.

During the six months ended December 31, 2016, the Company did not repurchase any shares pursuant to the repurchase program. Since the inception of the program in 2010, the Company repurchased an aggregate of 5,723,093 shares from the open

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market for a total cost of \$50.8 million, at an average price of \$8.87 per share, excluding fees and related expenses. No repurchased shares have been retired. Of the 5,723,093 repurchased shares, 103,003 shares with a weighted average repurchase price of \$11.17 per share, were reissued at an average price of \$6.13 per share pursuant to option exercises and vested restricted share units. As of December 31, 2016, \$6.4 million remained available under the share repurchase program.

Shelf Registration

In January 2017, the Company filed a shelf registration statement on Form S-3/A with the U.S. Securities and Exchange Commission through which it may offer and sell from time to time shares of common shares, shares of preferred shares, debt securities or warrants to purchase shares of common shares or shares of preferred shares, or units. Under this shelf registration statement, it may sell any combination of the above described securities, in one or more offerings in amounts, at prices and on terms to be determined at the time of the offering for an aggregate offering price of up to \$250.0 million.

Stock Options

The Company did not grant any stock options during the six months ended December 31, 2016. Options expected to vest are the result of applying the pre-vesting forfeiture rate assumption to total outstanding options.

The following table summarizes the Company's stock option activities for the six months ended December 31, 2016:

| | Number of Shares | Weighted Average Exercise Price Per Share | Weighted Average Remaining Contractual Term (in years) | Aggregate Intrinsic Value |
|-------------------------------------|---------------------|---|--|---------------------------------|
| Outstanding at June 30, 2016 | 1,859,260 | \$ 11.37 | 4.71 | \$5,959,720 |
| Granted | — | \$ — | | |
| Exercised | (637,406) | \$ 11.87 | | \$5,189,023 |
| Canceled or forfeited | (90,000) | \$ 12.63 | | |
| Outstanding at December 31, 2016 | 1,131,854 | \$ 11.00 | 4.93 | \$11,625,154 |
| Options vested and expected to vest | 1,121,561 | \$ 11.03 | 4.91 | \$11,484,305 |
| Exercisable at December 31, 2016 | 951,973 | \$ 11.65 | 4.50 | \$9,162,612 |

Restricted Stock Units ("RSU")

The following table summarizes the Company's RSU activities for the six months ended December 31, 2016:

| | Number of Restricted Stock Units | Weighted Average Grant Date Fair Value Per Share | Weighted Average Remaining Recognition Period (Years) | Aggregate Intrinsic Value |
|----------------------------------|--|--|--|---------------------------------|
| Nonvested at June 30, 2016 | 933,063 | \$ 9.18 | 1.73 | \$12,997,568 |
| Granted | 109,617 | \$ 20.18 | | |
| Vested | (78,235) | \$ 9.40 | | |
| Forfeited | (18,725) | \$ 10.94 | | |
| Nonvested at December 31, 2016 | 945,720 | \$ 10.40 | 1.40 | \$20,115,464 |
| RSUs vested and expected to vest | 829,631 | | 1.30 | \$17,646,257 |

The fair value of RSU is estimated based on the market price of the Company's share on the date of grant.
 Employee Share Purchase Plan ("ESPP")

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The assumptions used to estimate the fair values of common shares issued under the ESPP were as follows:

| | Six Months Ended December 31, 2016 |
|-------------------------|---------------------------------------|
| Volatility rate | 39.09% |
| Risk-free interest rate | 0.6% - 1.0% |
| Expected term | 1.3 years |
| Dividend yield | 0% |

Share-based Compensation Expense

The total share-based compensation expense related to stock options, RSUs and ESPP described above, recognized in the condensed consolidated statements of operations for the periods presented was as follows:

| | Three Months Ended December 31, 2016 | | Six Months Ended December 31, 2015 | |
|-------------------------------------|---|---------|---|---------|
| | 2016 | 2015 | 2016 | 2015 |
| | (in thousands) | | (in thousands) | |
| Cost of goods sold | \$205 | \$157 | \$400 | \$288 |
| Research and development | 383 | 264 | 743 | 457 |
| Selling, general and administrative | 966 | 664 | 1,727 | 1,129 |
| | \$1,554 | \$1,085 | \$2,870 | \$1,874 |

As of December 31, 2016, total unrecognized compensation cost under the Company's equity plans was \$5.4 million, which is expected to be recognized over a weighted-average period of 1.3 years.

7. Income Taxes

The Company recognized income tax expense of approximately \$1.1 million and \$1.0 million for the three months ended December 31, 2016 and 2015, respectively. The Company recognized income tax expense of approximately \$2.3 million and \$2.2 million for the six months ended December 31, 2016 and 2015, respectively. The estimated effective tax rate for the three months ended December 31, 2016 was 39.6% compared to (170.3)% for the three months ended December 31, 2015. The estimated effective tax rate for the six months ended December 31, 2016 was 36.2% compared to (164.3)% for the six months ended December 31, 2015. The changes in the effective tax rate and tax expense between the periods resulted primarily from changes in the mix of earnings in various geographic jurisdictions between the current quarter and the same period of last year.

During the quarter ended September 30, 2016, the Company fulfilled its obligations to contribute certain packaging equipment as required by the JV Agreement by transferring the legal titles of such equipment to the JV Company. The Company recorded \$6.6 million on both deferred tax assets and prepaid tax asset, which is amortized to tax expense over the useful life of the assets. As of December 31, 2016, the prepaid tax asset was amortized down to \$6.1 million, of which \$1.1 million and \$5.0 million were included in prepaid and other current assets and other long-term assets on the Company's balance sheet, respectively.

The Company files its income tax returns in the United States and in various foreign jurisdictions. The tax years 2001 to 2016 remain open to examination by U.S. federal and state tax authorities. The tax years 2009 to 2016 remain open to examination by foreign tax authorities.

The Company's income tax returns are subject to examinations by the Internal Revenue Service and other tax authorities in various jurisdictions. In accordance with the guidance on the accounting for uncertainty in income taxes, the Company regularly assesses the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of its provision for income taxes. These assessments can require considerable estimates and judgments. As of December 31, 2016, the gross amount of unrecognized tax benefits was approximately \$6.9 million, of which

\$4.5 million, if recognized, would reduce the effective income tax rate in future periods. If the Company's estimate of income tax liabilities proves to be less than the ultimate assessment, then a further charge to expense would be required. If events occur and the payment of these amounts ultimately proves to be unnecessary, the reversal of the liabilities would result in tax benefits being recognized in the period

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when the Company determines the liabilities are no longer necessary. The Company does not anticipate any material changes to its uncertain tax positions during the next twelve months.

On July 27, 2015, in *Altera Corp. v. Commissioner*, the U.S. Tax Court issued an opinion related to the treatment of share-based compensation expense in an intercompany cost-sharing arrangement. A final decision has yet to be issued by the Tax Court due to other outstanding issues related to the case. At this time, the U.S. Department of the Treasury has not withdrawn the requirement to include share-based compensation from its regulations. Due to the uncertainty surrounding the status of the current regulations, questions related to the scope of potential benefits, and the risk of the Tax Court's decision being overturned upon appeal, the Company has not recorded any benefit as of December 31, 2016. The Company will continue to monitor ongoing developments and potential impacts to its financial statements.

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8. Segment and Geographic Information

The Company is organized as, and operates in, one operating segment: the design, development and supply of power semiconductor products for computing, consumer electronics, communication and industrial applications. The chief operating decision-maker is the Chief Executive Officer. The financial information presented to the Company's Chief Executive Officer is on a consolidated basis, accompanied by information about revenue by customer and geographic region, for purposes of evaluating financial performance and allocating resources. The Company has one business segment, and there are no segment managers who are held accountable for operations, operating results and plans for products or components below the consolidated unit level. Accordingly, the Company reports as a single operating segment.

The Company sells its products primarily to distributors in the Asia Pacific region, who in turn sell these products to end customers. Because the Company's distributors sell their products to end customers which may have a global presence, revenue by geographical location is not necessarily representative of the geographical distribution of sales to end user markets.

The revenue by geographical location in the following tables is based on the country or region to which the products were shipped to:

| | Three Months Ended December 31, | | Six Months Ended December 31, | |
|-----------------|---------------------------------------|----------|----------------------------------|-----------|
| | 2016 | 2015 | 2016 | 2015 |
| | (in thousands) | | (in thousands) | |
| Hong Kong | \$78,253 | \$69,904 | \$161,088 | \$140,357 |
| China | 14,383 | 7,922 | 26,825 | 16,938 |
| South Korea | 393 | 442 | 759 | 1,100 |
| United States | 798 | 784 | 1,692 | 1,501 |
| Other Countries | 860 | 773 | 1,685 | 1,368 |
| | \$94,687 | \$79,825 | \$192,049 | \$161,264 |

The following is a summary of revenue by product type:

| | Three Months Ended December 31, | | Six Months Ended December 31, | |
|--------------------------------|---------------------------------------|----------|----------------------------------|-----------|
| | 2016 | 2015 | 2016 | 2015 |
| | (in thousands) | | (in thousands) | |
| Power discrete | \$69,822 | \$59,392 | \$141,250 | \$119,305 |
| Power IC | 21,859 | 16,400 | 44,857 | 33,913 |
| Packaging and testing services | 3,006 | 4,033 | 5,942 | 8,046 |
| | \$94,687 | \$79,825 | \$192,049 | \$161,264 |

Long-lived assets, net consisting of property, plant and equipment, by geographical area are as follows:

| | December 31, | |
|-----------------|----------------|-----------|
| | 2016 | 2016 |
| | (in thousands) | |
| China | \$68,639 | \$64,272 |
| United States | 53,432 | 51,214 |
| Other Countries | 615 | 598 |
| | \$122,686 | \$116,084 |

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9. Commitments and Contingencies

Purchase Commitments

As of December 31, 2016 and June 30, 2016, the Company had approximately \$25.9 million and \$39.6 million, respectively, of outstanding purchase commitments primarily for purchases of semiconductor raw materials, wafers, spare parts and packaging and testing services, and approximately \$10.3 million and \$6.6 million, respectively, of capital commitments for the purchase of property and equipment.

Contingencies and Indemnities

The Company is currently not a party to any pending material legal proceedings. The Company has in the past, and may from time to time in the future, become involved in legal proceedings arising from the normal course of business activities. The semiconductor industry is characterized by frequent claims and litigation, including claims regarding patent and other intellectual property rights as well as improper hiring practices. Irrespective of the validity of such claims, the Company could incur significant costs in the defense of such claims and suffer adverse effects on its operations.

The Company is a party to a variety of agreements that it has contracted with various third parties. Pursuant to these agreements, the Company may be obligated to indemnify another party to such an agreement with respect to certain matters. Typically, these obligations arise in the context of contracts entered into by the Company, under which the Company customarily agrees to hold the other party harmless against losses arising from a breach of representations and covenants related to such matters as title to assets sold, certain intellectual property rights, specified environmental matters and certain income taxes. In these circumstances, payment by the Company is customarily conditioned on the other party making a claim pursuant to the procedures specified in the particular contract, which procedures typically allow the Company to challenge the other party's claim. Further, the Company's obligations under these agreements may be limited in time and/or amount, and in some instances, the Company may have recourse against third parties for certain payments made by it under these agreements. The Company has not historically paid or recorded any material indemnifications and no accrual has been made at December 31, 2016 and June 30, 2016.

The Company has agreed to indemnify its directors and certain employees as permitted by law and pursuant to its bye-laws, and has entered into indemnification agreements with its directors and executive officers. The Company has not recorded a liability associated with these indemnification arrangements, as it historically has not incurred any material costs associated with such indemnification obligations. Costs associated with such indemnification obligations may be mitigated by insurance coverage that the Company maintains. However, such insurance may not cover any, or may cover only a portion of, the amounts the Company may be required to pay. In addition, the Company may not be able to maintain such insurance coverage in the future.

Joint Venture

In March 2016, the Company executed an agreement with two strategic investment funds owned by the Municipality of Chongqing, China to form a joint venture for a new state-of-the-art power semiconductor packaging, testing and wafer fabrication facility in Liangjiang New Area of Chongqing (the "Joint Venture"). The initial capitalization of the Joint Venture under the agreement is \$330.0 million, which includes cash contribution from the Chongqing Funds and contributions of cash, equipment and intangible assets from the Company. The Company owns 51% and the Chongqing Funds owns 49% of the equity interest of the Joint Venture. The Joint Venture is accounted under the provisions of the consolidation guidance since the Company has controlling financial interest.

The Joint Venture is expected to commence its initial packaging production in the first half of fiscal 2018. Within one year from June 30, 2016, the Company is expected to contribute cash of \$10.0 million and certain intangible assets. Over the long term, the Joint Venture plans to construct a 12-inch wafer fabrication facility for the production of power semiconductors.

In January 2017, the JV Company entered into an Engineering, Procurement and Construction Contract with The IT Electronics Eleventh Design & Research Institute Scientific and Technological Engineering Corporation Limited. The total price payable by the JV Company under the EPC Contract is RMB 540,000,000, or \$77,996,360 based on the currency exchange rate between RMB and U.S. Dollars on the Effective Date, which consists of \$2,820,154 (RMB 19,525,052) of design fees and \$75,176,206 (RMB 520,474,948) of construction and procurement fees, including compliance with safety and aesthetic requirements.

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. 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 the Company’s 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. The Company undertakes 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 “AOS,” the “Company,” “we,” “us” and “our” refer to Alpha and Omega Semiconductor Limited and its subsidiaries.

This management’s discussion should be read in conjunction with the management’s discussion included in the Company’s Annual Report on Form 10-K for the fiscal year ended June 30, 2016, filed with the Securities and Exchange Commission on August 26, 2016.

Overview

We are a designer, developer and global supplier of a broad portfolio of power semiconductors. Our portfolio of power semiconductors includes approximately 1,600 products, and has grown with the introduction of over 90 new products during each of the fiscal years ended June 30, 2016, 2015 and 2014. During the six months ended December 31, 2016, we introduced an additional 45 new products. Our teams of scientists and engineers have developed extensive intellectual properties and technical knowledge that encompass major aspects of power semiconductors, which we believe enables us to introduce and develop innovative products to address the increasingly complex power requirements of advanced electronics. We have an extensive patent portfolio that consists of 644 patents and 140 patent applications in the United States as of December 31, 2016. We differentiate ourselves by integrating our expertise in technology, design and advanced packaging to optimize product performance and cost. Our portfolio of products targets high-volume applications, including personal computers, flat panel TVs, LED lighting, smart phones, battery packs, consumer and industrial motor controls and power supplies for TVs, computers, servers and telecommunications equipment.

Our business model leverages global resources, including research and development and manufacturing in the United States and Asia. Our sales and technical support teams are localized in several growing markets. We operate a 200mm wafer fabrication facility in Hillsboro, Oregon, or the Oregon fab, which is critical for us to accelerate proprietary technology development and new product introduction as well as to improve our financial performance in the long run. To meet the market demand for more mature high volume products, we also utilize the wafer manufacturing capacity of selected third party foundries. For assembly and test, we primarily rely upon our in-house facilities in China. In addition, we utilize subcontracting partners for industry standard packages. We believe our in-house packaging and testing capability provides us with a competitive advantage in proprietary packaging technology, product quality, cost and sales cycle time.

On March 29, 2016, we entered into a joint venture contract (the “JV Agreement”) with two investment funds owned by the Municipality of Chongqing (the “Chongqing Funds”), pursuant to which we and the Chongqing Funds formed a joint venture, (the “JV Company”), for the purpose of constructing a power semiconductor packaging, testing and wafer fabrication facility in the Liangjiang New Area of Chongqing, China (the “JV Transaction”). The total initial capitalization of the JV Company is \$330.0 million (the “Initial Capitalization”). The Initial Capitalization will be completed in stages commencing on the incorporation of the JV Company. During the quarter ended September 30, 2016, the Chongqing Funds contributed \$33.0 million of initial capital in cash and we fulfilled our obligations to contribute certain packaging equipment as required by the JV Agreement by transferring the legal titles of such equipment to the JV Company. We own 51%, and the Chongqing Funds owns 49%, of the equity interest in the JV Company. If both parties agree that the termination of the JV Company is the best interest of each party or the JV

Company is bankrupt or insolvent where either party may terminate early, after paying the debts of the JV Company, the remaining assets of the JV Company shall be paid to the Chongqing Funds to cover the principal of its total paid-in contributions plus the interest at 10% simple annual rate prior to distributing the balance of the JV Company's assets to us. During the three months and six months ended December 31, 2016, we recorded \$1.2 million and \$2.1 million in net loss attributable to noncontrolling interest, representing 49% of the net loss incurred in the JV Company, which was attributable to operating expenses and depreciation expenses offset by equipment lease income and interest income. We expect the JV Company to commence its initial production in the first half of fiscal 2018. Over the long term, the JV Company plans to construct a 12-

inch wafer fabrication facility for the production of power semiconductors. We expect the joint venture to deliver significant cost savings, enhance our market positions in China, and drive meaningful improvements in working capital and capital expenditures.

As part of the JV Transaction, the JV Company entered into an Engineering, Procurement and Construction Contract (the "EPC Contract") with The IT Electronics Eleventh Design & Research Institute Scientific and Technological Engineering Corporation Limited (the "Contractor"), effective as of January 10, 2017 (the "Effective Date"), pursuant to which the Contractor was engaged to construct the manufacturing facility contemplated under the JV Agreement. Under the EPC Contract, the Contractor's obligations include, but are not limited to: (i) the development of conceptual design, initial design, construction drawing design and optimization, and submission of such designs to the JV Company for examination and confirmation; and (ii) the construction of the assembly and wafer fabrication facilities and related procurement services, including the selection and engagement of subcontractors, in accordance with a construction schedule agreed upon by the parties. The total price payable under the EPC Contract is Chinese Renminbi (RMB) 540,000,000, or approximately \$77,996,360 based on the currency exchange rate between RMB and U.S. Dollars on the Effective Date, which consists of \$2,820,154 (RMB 19,525,052) of design fees ("Design Fees") and \$75,176,206 (RMB 520,474,948) of construction and procurement fees (including compliance with safety and aesthetic requirements) ("Construction Fees"). The Design Fees and Construction Fees will be paid by JV Company pursuant to a payment schedule based on the progress of the construction and the achievements of specified milestones, approximately \$58.3 million and \$19.7 million in calendar year 2017 and 2018, respectively. The payment may be subject to volatility as a result of exposure to fluctuations in RMB foreign exchange rates.

During the second quarter of fiscal year of 2017, we released AOC3860, a common-drain 12V dual n-channel MOSFET with the lowest on-resistance in the product family of 2.15mOhm typical at 4.5V gate drive. This new device provides further improved source-to-source resistance, which is a critical factor for smart phone makers to achieve faster battery charge with a higher charging current. We also released AOK40B65H2AL, the introductory device in the new 650V H2-series IGBT family. The AOK40B65H2AL has been optimized to deliver high-speed switching performance by improving fast turn-off switching in applications such as welding machines, power factor correction and high switching converters. In addition, we released two new products in the 100V MOSFET family, AO4290A and AON6220. These products are designed for synchronous rectification for flyback converters, used in high-speed charger and PD adapters. Both parts are designed to be fully driven with 4.5V gate drive voltage. During the three months ended September 30, 2016, we released AOZ5166QI-01, the high efficiency power modules which are fully compliant with Intel's DrMOS specifications. This new device enables high power density voltage regulator solutions ideal for servers, work stations, graphic cards and high-end desktop PC applications. We also announced the addition of AOK30B135W1 to its 1350V AlphaIGBT™ family. The new AOK30B135W1 has been optimized to deliver high performance by reducing switching loss in soft-switching home appliance applications such as induction cooking, rice cookers, and inverter-based microwave ovens. In addition, we introduced two new products based on its high efficiency XS-PairFET package and latest low voltage technology. The AOE6932 and AOE6936 are the newest extensions to the flagship device, AOE6930, that was released in 2015. Both products are newly optimized for enhanced driving and switching performance.

Factors affecting our performance

Our performance is affected by several key factors, including the following:

The global, regional economic and PC market conditions: Because our products primarily serve consumer electronic applications, a deterioration of the global and regional economic conditions could materially affect our revenue and results of operations. In particular, because a significant amount of our revenue is derived from sales of products in the personal computing ("PC") markets, such as notebooks, motherboards and notebook battery packs, a significant decline or downturn in the PC market can have a material adverse effect on our revenue and results of operations. Our revenue from the PC market accounted for approximately 38.4% and 36.5% of our total revenue for the three months

ended December 31, 2016 and 2015, respectively, and 37.2% and 41.3% for the six months ended December 31, 2016 and 2015, respectively. In the past, we have experienced a significant decline in the global PC market due to continued growth of demand in tablets and smart phones, worldwide economic conditions and the industry inventory correction which had and may continue to have a material negative impact on the demand for our products, revenue, factory utilization, gross margin, our ability to resell excess inventory, and other performance measures.

In response to this trend, we executed and continue to execute strategies to diversify our portfolio of products and expand into other market segments, including the consumer, communications and industrial market segments, and to improve gross margin and profit by implementing cost control measures. While making progress in reducing our reliance on the PC market, we continue to support our computing business and capitalize on opportunities with a more focused and competitive PC product strategy. As we develop and sell new products that serve more diversified markets, we expect sales based on the PC market, as a percentage of the total revenue to decline. If the rate of decline in the PC market is faster than our expectation, or if we cannot

successfully diversify or introduce new products to offset the decline in the PC market, we may not be able to alleviate its negative impact on our operating results.

Manufacturing costs: Our gross margin may be affected by our manufacturing costs, including utilization of our manufacturing facilities, pricing of wafers from third party foundries and semiconductor raw materials, which may fluctuate from time to time largely due to the market demand and supply. Capacity utilization affects our gross margin because we have certain fixed costs associated with our packaging and testing facilities and our Oregon fab. If we are unable to utilize our manufacturing facilities at a desired level, our gross margin may be adversely affected. In addition, we expect that in the long term our joint venture agreement with the Chongqing Funds will reduce our costs of manufacturing. However, our manufacturing costs may increase in the short term prior to the commencement of operation of the JV Company, because we may be required to incur additional costs to acquire packaging and testing capacity in order make up for the reduced capacity during the period in which we transfer and relocate our equipment from Shanghai to Chongqing.

Erosion of average selling price: Erosion of average selling prices of established products is typical in our industry. Consistent with this historical trend, we expect our average selling prices of existing products to decline in the future. However, in the normal course of business, we seek to offset the effect of declining average selling price by introducing new and higher value products, expanding existing products for new applications and new customers and reducing the manufacturing cost of existing products.

Product introductions and customers' product requirements: Our success depends on our ability to introduce products on a timely basis that meet or are compatible with our customers' specifications and performance requirements. Both factors, timeliness of product introductions and conformance to customers' requirements, are equally important in securing design wins with our customers. As we accelerate the development of new technology platforms, we expect to increase the pace at which we introduce new products and obtain design wins. Our failure to introduce new products on a timely basis that meet customers' specifications and performance requirements, particularly those products with major OEM customers, and our inability to continue to expand our serviceable markets, could adversely affect our financial performance, including loss of market share. We expect our joint venture with the Chongqing Funds to commence operation in the first half of fiscal 2018, and we believe that the joint venture will increase and diversify our customer base, particularly in China, in the long term. However, there is no guarantee that the joint venture will commence timely or at all. Even if we are able to commence operation, we may not be successful in acquiring a sufficient number of new customers to offset the additional costs due to various factors, including but are not limited to, competition from other semiconductor companies in the region, our lack of history and prior relationships with customers as a new entrant, difficulties in executing our joint venture strategies, lack of control over our operations and the general economic conditions in Chongqing and China.

Distributor ordering patterns, customer demand and seasonality: Our distributors place purchase orders with us based on their forecasts of end customer demand, and this demand may vary significantly depending on the sales outlook and market and economic conditions of end customers. Because these forecasts may not be accurate, channel inventory held at our distributors may fluctuate significantly, which in turn may prompt distributors to make significant adjustments to their purchase orders placed with us. As a result, our revenue and operating results may fluctuate significantly from quarter to quarter. In addition, because our products are used in consumer electronics products, our revenue is subject to seasonality. Our sales seasonality is affected by numerous factors, including global and regional economic conditions as well as the PC market conditions, revenue generated from new products, changes in distributor ordering patterns in response to channel inventory adjustments and end customer demand for our products and fluctuations in consumer purchase patterns prior to major holiday seasons. In recent periods, broad fluctuations in the semiconductor markets and the global and regional economic conditions, in particular the decline of the PC market conditions, have had a more significant impact on our results of operations than seasonality. Furthermore, our revenue may be impacted by the level of demand from our major customers due to factors outside of

our control. If these major customers experience significant decline in the demand of their products, encounter difficulties or defects in their products, or otherwise fail to execute their sales and marketing strategies successfully, it may adversely affect our revenue and results of operations.

Principal line items of statements of operations

The following describes the principal line items set forth in our condensed consolidated statements of operations:

Revenue

We generate revenue primarily from the sale of power semiconductors, consisting of power discretes and power ICs. Historically, a majority of our revenue was derived from power discrete products and a smaller amount was derived from power IC products. Because our products typically have three to five year life cycles, the rate of new product introduction is an important driver of revenue growth over time. We believe that expanding the breadth of our product portfolio is important to our

business prospects, because it provides us with an opportunity to increase our total bill-of-materials within an electronic system and to address the power requirements of additional electronic systems. In addition, a small percentage of our total revenue is generated by providing packaging and testing services to third-parties through one of our subsidiaries.

Our product revenue includes the effect of the estimated stock rotation returns and price adjustments that we expect to provide to our distributors. Stock rotation returns are governed by contract and are limited to a specified percentage of the monetary value of products purchased by the distributor during a specified period. At our discretion or upon our direct negotiations with the original design manufacturers ("ODMs") or original equipment manufacturers ("OEMs"), we may elect to grant special pricing that is below the prices at which we sold our products to the distributors. In these situations, we will grant price adjustments to the distributors reflecting such special pricing. We estimate the price adjustments for inventory at the distributors based on factors such as distributor inventory levels, pre-approved future distributor selling prices, distributor margins and demand for our products.

Cost of goods sold

Our cost of goods sold primarily consists of costs associated with semiconductor wafers, packaging and testing, personnel, including share-based compensation expense, overhead attributable to manufacturing, operations and procurement, and cost associated with yield improvements, capacity utilization, warranty and inventory reserves. As the volume of sales increases, we expect cost of goods sold to increase. We implemented a process to improve our factory capacity utilization rates by transferring more wafer production to our Oregon fab and reducing our reliance on outside foundries. While our utilization rates cannot be immune to market conditions, our goal is to make such rates less vulnerable to market fluctuations. We believe our market diversification strategy and product growth will drive higher volumes of manufacturing which will improve our factory utilization rates and gross margin in the long run.

Operating expenses

Our operating expenses consist of research and development, selling, general and administrative expenses. We expect our operating expenses as a percentage of revenue to fluctuate from period to period as we continue to exercise cost control measures in response to the declining PC market as well as align our operating expenses to the revenue level. Research and development expenses. Our research and development expenses consist primarily of salaries, bonuses, benefits, share-based compensation expense, expenses associated with new product prototypes, travel expenses, fees for engineering services provided by outside contractors and consultants, amortization of software and design tools, depreciation of equipment and overhead costs. We continue to invest in developing new technologies and products utilizing our own fabrication and packaging facilities as it is critical to our long-term success. We also evaluate appropriate investment levels and stay focused on new product introductions to improve our competitiveness. We expect that our research and development expenses will fluctuate from time to time.

Selling, general and administrative expenses. Our selling, general and administrative expenses consist primarily of salaries, bonuses, benefits, share-based compensation expense, product promotion costs, occupancy costs, travel expenses, expenses related to sales and marketing activities, amortization of software, depreciation of equipment, maintenance costs and other expenses for general and administrative functions as well as costs for outside professional services, including legal, audit and accounting services. We expect our selling, general and administrative expenses to fluctuate in the near future as we continue to exercise cost control measures in response to the declining PC market.

Impairment of Long-Lived Assets: Long-lived assets or asset groups are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset might not be recoverable. The recoverability of an asset or asset group is assessed by determining if the carrying value of the asset or asset group exceeds the sum of the projected undiscounted cash flows expected to result from the use and eventual disposition of the assets over the remaining economic life. The impairment loss is measured based on the difference between the carrying amount and estimated fair value.

Income tax expense

We are subject to income taxes in various jurisdictions. Significant judgment and estimates are required in determining our worldwide income tax expense. The calculation of tax liabilities involves dealing with uncertainties in the application of complex tax regulations of different jurisdictions globally. We establish accruals for potential liabilities and contingencies based on a more likely than not threshold to the recognition and de-recognition of uncertain tax positions. If the recognition threshold is met, the applicable accounting guidance permits us to recognize a tax benefit measured at the largest amount of tax benefit that is more likely than not to be realized upon settlement with a taxing authority. If the actual tax outcome of such exposures is different

from the amounts that were initially recorded, the differences will impact the income tax and deferred tax provisions in the period in which such determination is made. Changes in the location of taxable income (loss) could result in significant changes in our income tax expense.

We record a valuation allowance against deferred tax assets if it is more likely than not that a portion of the deferred tax assets will not be realized, based on historical profitability and our estimate of future taxable income in a particular jurisdiction. Our judgments regarding future taxable income may change due to changes in market conditions, changes in tax laws, tax planning strategies or other factors. If our assumptions and consequently our estimates change in the future, the deferred tax assets may increase or decrease, resulting in corresponding changes in income tax expense. Our effective tax rate is highly dependent upon the geographic distribution of our worldwide profits or losses, the tax laws and regulations in each geographical region where we have operations, the availability of tax credits and carry-forwards and the effectiveness of our tax planning strategies.

Results of Operations

The following tables set forth statements of operations, also expressed as a percentage of revenue, for the three and six months ended December 31, 2016 and 2015. Our historical results of operations are not necessarily indicative of the results for any future period.

| | Three Months Ended December 31, | | | | Six Months Ended December 31, | | | |
|---|---------------------------------|------------------------|------------------------|------------------------|-------------------------------|------------------------|------------------------|------------------------|
| | 2016 (in thousands) | 2015 (in thousands) | 2016 (% of revenue) | 2015 (% of revenue) | 2016 (in thousands) | 2015 (in thousands) | 2016 (% of revenue) | 2015 (% of revenue) |
| Revenue | \$94,687 | \$79,825 | 100.0 % | 100.0 % | \$192,049 | \$161,264 | 100.0 % | 100.0 % |
| Cost of goods sold | 72,593 | 64,853 | 76.7 % | 81.2 % | 148,011 | 131,231 | 77.1 % | 81.4 % |
| Gross profit | 22,094 | 14,972 | 23.3 % | 18.8 % | 44,038 | 30,033 | 22.9 % | 18.6 % |
| Operating expenses | | | | | | | | |
| Research and development | 7,284 | 5,941 | 7.7 % | 7.4 % | 14,303 | 12,105 | 7.4 % | 7.5 % |
| Selling, general and administrative | 11,974 | 8,872 | 12.6 % | 11.1 % | 23,157 | 18,369 | 12.1 % | 11.4 % |
| Impairment of long-lived assets | — | 432 | — % | 0.5 % | — | 432 | — % | 0.3 % |
| Total operating expenses | 19,258 | 15,245 | 20.3 % | 19.0 % | 37,460 | 30,906 | 19.5 % | 19.2 % |
| Operating income (loss) | 2,836 | (273) | 3.0 % | (0.2)% | 6,578 | (873) | 3.4 % | (0.6)% |
| Interest income and other income (loss), net | (70) | (316) | (0.1)% | (0.4)% | (119) | (467) | (0.1)% | (0.3)% |
| Interest expense | (24) | (7) | — % | — % | (50) | (17) | — % | — % |
| Net Income (loss) before income taxes | 2,742 | (596) | 2.9 % | (0.6)% | 6,409 | (1,357) | 3.3 % | (0.9)% |
| Income tax expense | 1,085 | 1,015 | 1.1 % | 1.3 % | 2,322 | 2,229 | 1.2 % | 1.4 % |
| Net income (loss) including noncontrolling interest | 1,657 | (1,611) | 1.8 % | (1.9)% | 4,087 | (3,586) | 2.1 % | (2.3)% |
| Net loss attributable to noncontrolling interest | (1,190) | — | (1.3)% | — % | (2,067) | — | (1.1)% | — % |
| Net income (loss) attributable to Alpha and Omega Semiconductor Limited | \$2,847 | \$(1,611) | 3.1 % | (1.9)% | \$6,154 | \$(3,586) | 3.2 % | (2.3)% |

Share-based compensation expense was allocated as follow:

| | Three Months Ended | | | | Six Months Ended | | | |
|-------------------------------------|--------------------|---------|----------------|------|------------------|---------|----------------|------|
| | December 31, | | | | December 31, | | | |
| | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 |
| | (in thousands) | | (% of revenue) | | (in thousands) | | (% of revenue) | |
| Cost of goods sold | \$205 | \$157 | 0.2% | 0.2% | \$400 | \$288 | 0.2% | 0.2% |
| Research and development | 383 | 264 | 0.4% | 0.3% | 743 | 457 | 0.4% | 0.3% |
| Selling, general and administrative | 966 | 664 | 1.0% | 0.8% | 1,727 | 1,129 | 0.9% | 0.7% |
| Total | \$1,554 | \$1,085 | 1.6% | 1.3% | \$2,870 | \$1,874 | 1.5% | 1.2% |

Three And Six Months Ended December 31, 2016 and 2015

Revenue

The following is a summary of revenue by product type:

| | Three Months Ended December 31, | | | | Six Months Ended December 31, | | | |
|--------------------------------|---------------------------------|----------|----------------|-----------------|-------------------------------|-----------|----------------|-----------------|
| | 2016 | 2015 | Change | | 2016 | 2015 | Change | |
| | (in thousands) | | (in thousands) | (in percentage) | (in thousands) | | (in thousands) | (in percentage) |
| Power discrete | \$69,822 | \$59,392 | \$10,430 | 17.6 % | \$141,250 | \$119,305 | \$21,945 | 18.4 % |
| Power IC | 21,859 | 16,400 | 5,459 | 33.3 % | 44,857 | 33,913 | 10,944 | 32.3 % |
| Packaging and testing services | 3,006 | 4,033 | (1,027) | (25.5)% | 5,942 | 8,046 | (2,104) | (26.1)% |
| | \$94,687 | \$79,825 | \$14,862 | 18.6 % | \$192,049 | \$161,264 | \$30,785 | 19.1 % |

Total revenue was \$94.7 million for the three months ended December 31, 2016, an increase of \$14.9 million, or 18.6%, as compared to \$79.8 million for the same quarter last year. The increase consisted of \$10.4 million and \$5.5 million in sales of power discrete products and power IC products, respectively, partially offset by a \$1.0 million decrease in sales of packaging and testing services. The increase in power discrete and power IC product sales was primarily due to 30.3% increase in unit shipments, partially offset by a 7.1% decrease in average selling price as compared to the same quarter last year due to selling price erosion in the computing and consumer markets and to a lesser extent, a shift in product mix. The decrease in packaging and testing services revenue for the three months ended December 31, 2016 compared to the same quarter last year was primarily due to softened demand.

Total revenue was \$192.0 million for the six months ended December 31, 2016, an increase of \$30.8 million, or 19.1%, as compared to \$161.3 million for the same period last year. The increase primarily consisted of \$21.9 million and 10.9 million in sales of power discrete products and power IC products, respectively. The increase in power discrete and power IC product sales was primarily due to a 24.1% increase in unit shipments, partially offset by a 2.4% decrease in average selling price as compared to the same period of last year mainly due to selling price erosion in the computing and consumer markets, partially offset by a shift in product mix. The decrease in revenue of packaging and testing services for the six months ended December 31, 2016 as compared to the same period last year was primarily due to reduced demand as a result of the declining PC markets.

Cost of goods sold and gross profit

| | Three Months Ended December 31, | | | | Six Months Ended December 31, | | | |
|--------------------|---------------------------------|----------|----------------|-----------------|-------------------------------|-----------|----------------|-----------------|
| | 2016 | 2015 | Change | | 2016 | 2015 | Change | |
| | (in thousands) | | (in thousands) | (in percentage) | (in thousands) | | (in thousands) | (in percentage) |
| Cost of goods sold | \$72,593 | \$64,853 | \$7,740 | 11.9 % | \$148,011 | \$131,231 | \$16,780 | 12.8 % |

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| | | | | | | | | | | | | | | |
|-----------------------|----------|---|----------|---|---------|------|---|----------|---|----------|--|----------|------|---|
| Percentage of revenue | 76.7 | % | 81.2 | % | | 77.1 | % | 81.4 | % | | | | | |
| Gross profit | \$22,094 | | \$14,972 | | \$7,122 | 47.6 | % | \$44,038 | | \$30,033 | | \$14,005 | 46.6 | % |
| Percentage of revenue | 23.3 | % | 18.8 | % | | 22.9 | % | 18.6 | % | | | | | |

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Cost of goods sold was \$72.6 million for the three months ended December 31, 2016, an increase of \$7.7 million, or 11.9%, as compared to \$64.9 million for the same quarter last year. The increase was primarily due to increased unit shipments. The increase was partially offset by the overall manufacturing cost reduction due to improved factory utilization as compared to the same quarter last year. Gross margin increased by 4.5% point to 23.3% for the three months ended December 31, 2016 as compared to 18.8% for the same quarter last year. The increase in gross margin was primarily due to higher factory utilization partially offset by lower average selling prices during the three months ended December 31, 2016.

Cost of goods sold was \$148.0 million for the six months ended December 31, 2016, an increase of \$16.8 million, or 12.8%, as compared to \$131.2 million for the same period last year, primarily due to increased unit shipments partially offset by overall manufacturing cost reduction due to higher factory utilization as compared to the same period last year. Gross margin increased by 4.3 percentage point to 22.9% for the six months ended December 31, 2016 as compared to 18.6% for the same period last year. The increase in gross margin was primarily due to higher factory utilization partially offset by lower average selling prices during the current period.

Research and development expenses

| | Three Months Ended December 31, | | | Six Months Ended December 31, | | |
|--------------------------|---------------------------------|----------------|-----------------|-------------------------------|----------------|-----------------|
| | 2016 | 2015 | Change | 2016 | 2015 | Change |
| | (in thousands) | (in thousands) | (in percentage) | (in thousands) | (in thousands) | (in percentage) |
| Research and development | \$7,284 | \$5,941 | \$1,343 22.6 % | \$14,303 | \$12,105 | \$2,198 18.2 % |

Research and development expenses were \$7.3 million for the three months ended December 31, 2016, an increase of \$1.3 million, or 22.6%, as compared to \$5.9 million for the same quarter last year. The increase was primarily attributable to a \$0.9 million increase in employee compensation and benefit expense mainly due to increased headcount and higher bonus expenses, a \$0.3 million increase in product prototyping engineering expenses as a result of increased engineering activities, as well as a \$0.1 million increase in share-based compensation expense as a result of an increase of stock awards granted in the current quarter.

Research and development expenses were \$14.3 million for the six months ended December 31, 2016, an increase of \$2.2 million, or 18.2%, as compared to \$12.1 million for the same period last year. The increase was primarily attributable to a \$1.3 million increase in employee compensation expenses mainly due to increased headcount and higher bonus expenses, a \$0.7 million increase in product prototyping engineering expense as a result of increased engineering activities, as well as a \$0.3 million increase in share-based compensation expense as a result of a decrease in cancellation of stock award during the current period as compared to the same period last year.

Selling, general and administrative expenses

| | Three Months Ended December 31, | | | Six Months Ended December 31, | | |
|-------------------------------------|---------------------------------|----------------|-----------------|-------------------------------|----------------|-----------------|
| | 2016 | 2015 | Change | 2016 | 2015 | Change |
| | (in thousands) | (in thousands) | (in percentage) | (in thousands) | (in thousands) | (in percentage) |
| Selling, general and administrative | \$11,974 | \$8,872 | \$3,102 35.0 % | \$23,157 | \$18,369 | \$4,788 26.1 % |

Selling, general and administrative expenses were \$12.0 million for the three months ended December 31, 2016, an increase of \$3.1 million, or 35.0%, as compared to \$8.9 million for the same quarter last year. The increase was primarily attributable to a \$2.1 million increase in employee compensation and benefits expenses mainly due to increased headcount and higher bonus expenses, a \$0.3 million increase in share-based compensation expense as a result of an increase of stock award granted, a \$0.2 million increase in consulting fees primarily due to increased professional services costs and recruiting costs, a \$0.2 million increase in audit and tax consulting fees due to increased related consulting activities, as well as a \$0.2 million increase in employee business expenses due to increased travel expenses during the current quarter.

During the three and six months ended December 31, 2016, we recognized \$0.2 million and \$0.6 million of expenses, respectively, related to our joint venture, including noncontrolling interest, in our general and administrative expenses in connection with personnel and benefit related costs, outside professional services, travel expenses and office supplies expenses.

Selling, general and administrative expenses were \$23.2 million for the six months ended December 31, 2016, an increase of \$4.8 million, or 26.1%, as compared to \$18.4 million for the same quarter last year. The increase was primarily attributable to a \$3.1 million increase in employee compensation and benefits expenses primarily due to increased headcount and higher bonus

expenses, a \$0.6 million increase in share-based compensation expense as a result of a decrease of cancellation in stock award, a \$0.4 million increase in employee business expenses due to increased travel expenses, a \$0.3 million increase in consulting fees primarily due to increased professional services costs and recruiting costs, as well as a \$0.1 million increase in audit and tax consulting expenses due to increased related consulting activities during the current period as compared to the same period last year.

Impairment of long-lived assets

| | Three Months Ended December 31, 2016 | | | Six Months Ended December 31, 2016 | | |
|---------------------------------|--|----------------|-----------------|--|----------------|-----------------|
| | 2015 | Change | | 2015 | Change | |
| | (in thousands) | (in thousands) | (in percentage) | (in thousands) | (in thousands) | (in percentage) |
| Impairment of long-lived assets | \$-432 | \$(432) | (100.0)% | \$-432 | \$(432) | (100.0)% |

During the quarter ended December 31, 2015, we identified certain manufacturing equipment purchased for projects that were subsequently canceled. Because the equipment did not have values for other purposes, we recorded an asset impairment charge of approximately \$0.4 million related to these equipment during the quarter ended December 31, 2015.

Interest income and expenses

| | Three Months Ended December 31, 2016 | | | Six Months Ended December 31, 2016 | | |
|--|--|----------------|-----------------|---------------------------------------|----------------|-----------------|
| | 2015 | Change | | 2015 | Change | |
| | (in thousands) | (in thousands) | (in percentage) | (in thousands) | (in thousands) | (in percentage) |
| Interest income and other income (loss), net | \$(70) | \$(316) | \$246 (77.8)% | \$(119) | \$(467) | \$348 (74.5)% |

Interest income and other, net was primarily related to interest earned from cash and cash equivalents, as well as foreign exchange gains (losses). The decrease in interest income and other during the three and six months ended December 31, 2016 as compared to the same period last year was primarily due to lower foreign exchange losses as a result of recent appreciation of USD against RMB, offset by higher interest income due to increase in average cash balances.

Income tax expense

| | Three Months Ended December 31, 2016 | | | Six Months Ended December 31, 2016 | | |
|--------------------|--|----------------|-----------------|---------------------------------------|----------------|-----------------|
| | 2015 | Change | | 2015 | Change | |
| | (in thousands) | (in thousands) | (in percentage) | (in thousands) | (in thousands) | (in percentage) |
| Income tax expense | \$1,085 | \$1,015 | \$70 6.9% | \$2,322 | \$2,229 | \$93 4.2% |

We recognized income tax expense of approximately \$1.1 million and \$1.0 million for the three months ended December 31, 2016 and 2015, respectively. The income tax expense for the three months ended December 31, 2016 was slightly higher than the tax expense for the same quarter last year primarily due to changes in the mix of earnings in various geographic jurisdictions between the current and same quarter of last year.

We recognized income tax expense of approximately \$2.3 million and \$2.2 million for the six months ended December 31, 2016 and 2015, respectively. The income tax expense for the six months ended December 31, 2016 was slightly higher than that for the same period last year primarily due to changes in the mix of earnings in various geographic jurisdictions between the current and same period of last year.

Liquidity and Capital Resources

Our principal need for liquidity and capital resources is to maintain sufficient working capital to support our operations and to invest adequate capital expenditures to grow of our business. Currently, we financed our operations and capital expenditures primarily through funds generated from operations.

In March 2016, we entered into the JV Agreement with an initial capitalization of \$330.0 million. During the quarter ended September 30, 2016, the Chongqing Funds contributed \$33.0 million of initial capital in cash and we fulfilled our obligation to contribute of certain packaging equipment as required by the JV Agreement by transferring the legal titles of such equipment to the JV Company. Pursuant to terms of the JV Agreement, within one year from June 30, 2016, we expect to contribute certain intangible assets and \$10.0 million of cash pursuant to the terms of the JV Agreement. Over the long term, the JV Company plans to construct a 12-inch wafer fabrication facility for the manufacturing or semiconductor products.

In January 2017, the JV Company entered into the EPC Contract. The total price payable by the JV Company under the EPC Contract is approximately \$78.0 million, which consists of \$2.8 million of design fees and \$75.2 million of construction and procurement fees. These fees will be paid by the JV Company pursuant to a payment schedule based on the progress of the construction and the achievements of specified milestones. Assuming all of the specified milestones are achieved in accordance with the construction schedule, the JV Company expects to pay approximately \$58.3 million and \$19.7 million in calendar year 2017 and 2018, respectively. The actual payments may be subject to volatility as a result of exposure to fluctuations in RMB foreign exchange rates.

In April 2015, our Board of Directors of the Company approved an increase in the remaining available amount under the Company's then effective share repurchase program from approximately \$17.8 million to \$50.0 million. The repurchases may be made from the open market pursuant to a pre-established Rule 10b5-1 trading plan (as amended, the "Repurchase Trading Plan") or through privately negotiated transactions. The amount and timing of any repurchases depend on a number of factors, including but not limited to, the trading price, volume and availability of our common shares, applicable legal requirements, our business and financial conditions and general market environment. There is no guarantee that such repurchases under the Program will enhance the value of our shares.

In June 2015, we commenced a modified Dutch auction tender offer (the "Tender Offer") to repurchase an aggregate of \$30.0 million of our outstanding common shares with a price range between \$8.50 and \$9.20 per share. In July 2015, we completed the Tender Offer in which we purchased 3,296,703 shares of its common shares, at a purchase price of \$9.10 per share, for an aggregate purchase price of \$30.0 million, excluding fees and expenses relating to the Tender Offer. These shares represented approximately 12.53% of the total number of the Company's common shares issued and outstanding as of June 30, 2015. The Tender Offer was part of the \$50.0 million share repurchase program approved by the Board on April 15, 2015.

During the six months ended December 31, 2016, we did not repurchase any shares pursuant to the share repurchase program. Since the inception of the program in 2010, the Company repurchased an aggregate of 5,723,093 shares from the open market for a total cost of \$50.8 million, at an average price of \$8.87 per share, excluding fees and related expenses. As of December 31, 2016, approximately \$6.4 million remained available under the share repurchase program. Shares repurchased are accounted for as treasury shares and the total cost of shares repurchased is recorded as a reduction of shareholders' equity.

In January 2017, we filed a "universal" shelf registration statement on Form S-3/A with the U.S. Securities and Exchange Commission, through which we may offer and sell, from time to time, our securities up to an aggregate offering price of up to \$250.0 million. We currently do not have any specific plan to utilize the shelf registration statement.

We believe that our current cash and cash equivalents and cash flows from operations will be sufficient to meet our anticipated cash needs, including working capital and capital expenditures, for at least the next twelve months. We may require additional capital due to changing business conditions or other future developments, including any investments or acquisitions we may decide to pursue. If our cash is insufficient to meet our needs, we may seek to raise capital through equity or debt financing. The sale of additional equity securities could result in dilution to our shareholders. The incurrence of indebtedness would result in increased debt service obligations and may include operating and financial covenants that would restrict our operations. We cannot be certain that any financing will be available in the amounts we need or on terms acceptable to us, if at all.

Cash and cash equivalents

As of December 31, 2016 and June 30, 2016, we had \$122.8 million and \$87.8 million of cash and cash equivalents, including \$112.4 million and \$66.1 million were held by foreign subsidiaries, respectively. Our cash and cash equivalents primarily consisted of cash on hand and short-term bank deposits with original maturities of three months or less.

The following table shows our cash flows from operating, investing and financing activities for the periods indicated:

| | Six Months Ended December 31, | |
|--|----------------------------------|-------------|
| | 2016 | 2015 |
| | (in thousands) | |
| Net cash provided by operating activities | \$ 18,069 | \$ 24,631 |
| Net cash used in investing activities | (23,464) | (10,633) |
| Net cash provided by (used in) financing activities | 40,973 | (38,130) |
| Effect of exchange rate changes on cash and cash equivalents | (559) | (95) |
| Net increase (decrease) in cash and cash equivalents | \$ 35,019 | \$ (24,227) |

Cash flows from operating activities

Net cash provided by operating activities of \$18.1 million for the six months ended December 31, 2016 resulted primarily from net income of \$4.1 million and non-cash expenses of \$22.3 million, offset by net changes in assets and liabilities of \$8.4 million. The non-cash expenses of \$22.3 million include a \$13.3 million of depreciation and amortization expenses, a \$2.9 million of share-based compensation expense, a \$0.4 million of gain on disposal of property and equipment, and a \$6.6 million of deferred income taxes. The net changes in assets and liabilities of \$8.4 million were primarily due to a \$7.0 million increase in other current and long term assets due to increase in advance payments to vendors, a \$4.6 million decrease in accounts payable due to timing of payment, a \$1.4 million increase in inventories, partially offset by \$2.1 million decrease in accounts receivable from timing of billings and collection of payments, a \$2.3 million increase in accrued and other liabilities and \$0.3 million increase in income taxes payable. Net cash provided by operating activities of \$24.6 million for the six months ended December 31, 2015 resulted primarily from net loss of \$3.6 million, non-cash charges of \$16.6 million, and net change in assets and liabilities providing net cash of \$11.6 million. The non-cash charges of \$16.6 million included a \$13.8 million of depreciation and amortization expenses, a \$1.9 million of share-based compensation expense, a \$0.4 million of impairment of long-lived assets, and a \$0.5 million of deferred income taxes. The net change in assets and liabilities providing net cash of \$11.6 million was primarily due to a \$12.7 million decrease in accounts receivable due to the timing of billings and collection of payments, a \$3.1 million decrease in inventories as we reduced our inventories, a \$1.1 million increase in accrued and other liabilities, a \$0.8 million decrease in other current and long term assets primarily due to decrease in advance payments to vendors, and a \$0.4 million increase in income taxes payable, partially offset by a \$6.5 million decrease in accounts payable primarily due to timing of payment.

Cash flows from investing activities

Net cash used in investing activities of \$23.5 million for the six months ended December 31, 2016 was primarily attributable to \$23.7 million purchases of property and equipment and land to increase our in-house production capacity and to support the Joint Venture Company, as well as \$0.1 million increase in restricted cash, partially offset by \$0.4 million proceeds from sale of certain equipment.

Net cash used in investing activities of \$10.6 million for the six months ended December 31, 2015 was primarily attributable to purchase of property and equipment of \$10.8 million to increase our in-house production capacity, partially offset by \$0.1 million decrease in restricted cash during the period.

Cash flows from financing activities

Net cash used in financing activities of \$41.0 million for the six months ended December 31, 2016 was primarily attributable to \$33.0 million proceeds from investment by noncontrolling interest and \$8.7 million of proceeds from exercise of stock options and issuance of shares under the ESPP, partially offset by \$0.4 million in payment of capital lease obligations and \$0.3 million in common shares acquired to settle withholding tax related to vesting of restricted stock units.

Net cash used in financing activities of \$38.1 million for the six months ended December 31, 2015 was primarily attributable to \$40.3 million for repurchase of common shares, including repurchases in the Dutch tender offer, \$0.5 million in payment of capital lease obligations and \$0.2 million in common shares acquired to settle withholding tax related to vesting of restricted stock units, partially offset by \$2.8 million of proceeds from exercise of stock options and issuance of shares under the ESPP.

Capital expenditures

Capital expenditures were \$23.7 million and \$10.8 million for the six months ended December 31, 2016 and 2015, respectively. Our capital expenditures primarily consisted of purchases of equipment for our packaging and testing services and for our Oregon fab, and purchase of equipment and land in Chongqing for the Joint Venture Company, as well as for upgrading our operational and financial systems. The increase in capital expenditure was primarily due to the additional purchases of equipment and assets and land in connection with the JV Transaction and to improve our technology and support our new product introductions to fuel business growth.

Commitments

As of December 31, 2016 and June 30, 2016, we had approximately \$25.9 million and \$39.6 million, respectively, of outstanding purchase commitments consisted primarily of purchases of semiconductor raw materials, wafers, spare parts and packaging and testing services.

As of December 31, 2016 and June 30, 2016, we had approximately \$10.3 million and \$6.6 million, respectively, of capital commitments for the purchase of property and equipment.

Joint Venture Commitments

In March 2016, we executed the JV Agreement with the Chongqing Funds to form a joint venture for the construction of a new state-of -the-art power semiconductor packaging, testing and wafer fabrication facility in Liangjiang New Area of Chongqing. The Joint Venture is expected to commence its initial packaging production in the first half of fiscal 2018. Under the JV Agreement, we are required to contribute \$10.0 million in cash and certain intangible assets within one year from June 30, 2016.

In January 2017, the JV company entered into an Engineering, Procurement and Construction Contract with The IT Electronics Eleventh Design & Research Institute Scientific and Technological Engineering Corporation Limited. The total price payable by the JV Company under the EPC Contract is approximately \$78.0 million, which consists of \$2.8 million of design fees and \$75.2 million of construction and procurement fees. These fees will be paid by the JV Company pursuant to a payment schedule based on the progress of the construction and the achievements of specified milestones, approximately \$58.3 million and \$19.7 million in calendar year 2017 and 2018, respectively.

Off-Balance Sheet Arrangements

As of December 31, 2016, we had no material off-balance sheet arrangements as defined in Regulation S-K 303(a)(4)(ii) arrangements.

Contractual Obligations

Except EPC contract discussed above, there were no material changes in our contractual obligations, as disclosed in our Annual Report on Form 10-K for the fiscal year ended June 30, 2016.

Recent Accounting Pronouncements

See Note 1 of the Notes to the Condensed Consolidated Financial Statements contained in this Quarterly Report on Form 10-Q for a description of recent accounting pronouncements, including the expected dates of adoption and estimated effects on results of operations and financial condition, which is incorporated herein by reference.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes in the market risks previously disclosed in Part II, Item 7A, "Quantitative and Qualitative Disclosures About Market Risk," of our Annual Report on Form 10-K for the year ended June 30, 2016, filed with the SEC on August 26, 2016.

ITEM 4. CONTROLS AND PROCEDURES

Management's Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, (the "Exchange Act")), as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures as of December 31, 2016 have been designed and are functioning effectively to provide reasonable assurance that the information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the three months ended December 31, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Limitation on Effectiveness of Controls

While our disclosure controls and procedures and internal control over financial reporting are designed to provide reasonable assurance that their respective objectives will be met, we do not expect that our disclosure controls and procedures or our internal control over financial reporting are or will be capable of preventing or detecting all errors and all fraud. Any control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are currently not a party to any material legal proceedings. We have in the past, and may from time to time in the future, become involved in legal proceedings arising from the normal course of business activities. The semiconductor industry is characterized by frequent claims and litigation, including claims regarding patent and other intellectual property rights as well as improper hiring practices. Irrespective of the validity of such claims, we could incur significant costs in the defense thereof or could suffer adverse effects on its operations.

ITEM 1A. RISK FACTORS

Item 1A of Part I of our Annual Report on Form 10-K for the year ended June 30, 2016, filed with the SEC on August 26, 2016, contains risk factors identified by the Company. There have been no material changes to the risk factors we previously disclosed. Our operations could also be affected by additional factors that are not presently known to us or by factors that we currently consider immaterial to our business.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

During the six months ended December 31, 2016, we did not repurchase any shares under the share repurchase program. As of December 31, 2016, approximately \$6.4 million remained available under the share repurchase program.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

On February 6, 2017, the Board of Directors of the Company approved a new form of indemnification agreement (the “Indemnification Agreement”), to be entered into with the Company’s directors and certain officers to be designated by the Board (each, an “Indemnitee”). The Indemnification Agreement clarifies and enhances the rights and obligations of the Company and the Indemnitee with respect to indemnification and advancement of expenses provided in the prior form of indemnification agreement and the Company’s bye-laws.

The Indemnification Agreement requires the Company, among other things, to indemnify the Indemnitee to the fullest extent authorized by the Companies Act of Bermuda, on the terms set forth in the agreement, against all expenses, liabilities and losses incurred or paid by the Indemnitee or on the Indemnitee’s behalf in connection with certain legal proceedings, including shareholder derivative law suits, by reason of the fact that the Indemnitee was a director, officer, employee of the Company or its subsidiaries, and to advance expenses incurred by the Indemnitee in defending any proceeding against the Indemnitee with respect to which the Indemnitee may be entitled to indemnification by the Company. The Indemnification Agreement also clarifies the standards of care that is applicable for indemnification, and provides certain exceptions to the Company’s obligations of indemnification. The Indemnification Agreement also specifies the substantive and procedural requirements for determining the indemnifiable amount payable by the Company. The foregoing description of the form of Indemnification Agreement is only a summary and is qualified in its entirety by reference to the full text of the form of Indemnification Agreement, which is filed as Exhibit 10.1 to this Quarterly Report on Form 10-Q and is incorporated herein by reference.

ITEM 6. EXHIBITS

- 10.1 Form of Indemnification Agreement
- 31.1 Certification of Chief Executive Officer pursuant to Securities Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Chief Financial Officer pursuant to Securities Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INS XBRL Instance
- 101.SCH XBRL Taxonomy Extension Schema
- 101.CAL XBRL Taxonomy Extension Calculation
- 101.DEF XBRL Taxonomy Extension Definition
- 101.LAB XBRL Taxonomy Extension Labels
- 101.PRE XBRL Taxonomy Extension Presentation

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.

February 9, 2017

ALPHA AND OMEGA SEMICONDUCTOR
LIMITED

By: /s/ YIFAN LIANG

Yifan Liang

Chief Financial Officer and Corporate Secretary

(Principal Financial Officer)