

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

FORM 10-Q

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

For the quarterly period ended September 30, 2021

or

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

For the transition period from _____ to _____.

Commission File Number: 001-34791



Magnachip Semiconductor Corporation
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

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

c/o MagnaChip Semiconductor S.A.
1, Allée Scheffer, L-2520
Luxembourg, Grand Duchy of Luxembourg
(352) 45-62-62
(Address, zip code, and telephone number, including area code, of registrant's principal executive offices)

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, par value \$0.01 per share	MX	New York Stock Exchange

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 every Interactive Data File required to be submitted 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 such files). Yes No

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

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

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of October 29, 2021, the registrant had 46,464,889 shares of common stock outstanding.

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PART I—FINANCIAL INFORMATION

Item 1. Interim Consolidated Financial Statements (Unaudited)

**MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS (Unaudited)**

	<u>September 30,</u> <u>2021</u>	<u>December 31,</u> <u>2020</u>
<small>(In thousands of U.S. dollars, except share data)</small>		
Assets		
Current assets		
Cash and cash equivalents	\$ 276,301	\$ 279,940
Accounts receivable, net	52,523	64,390
Inventories, net	38,773	39,039
Other receivables	8,971	4,338
Prepaid expenses	9,666	7,332
Hedge collateral (Note 9)	3,720	5,250
Other current assets (Notes 10 and 19)	1,919	9,321
Total current assets	391,873	409,610
Property, plant and equipment, net	103,352	96,383
Operating lease right-of-use assets	3,727	4,632
Intangible assets, net	2,405	2,727
Long-term prepaid expenses	9,451	4,058
Deferred income taxes	41,255	44,541
Other non-current assets	10,626	9,739
Total assets	\$ 562,689	\$ 571,690
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	\$ 33,386	\$ 52,164
Other accounts payable	18,671	2,531
Accrued expenses (Note 8)	13,168	16,241
Accrued income taxes	1,955	12,398
Operating lease liabilities	1,757	2,210
Current portion of long-term borrowings, net	—	83,479
Other current liabilities (Note 10)	7,800	4,595
Total current liabilities	76,737	173,618
Accrued severance benefits, net	37,741	40,462
Non-current operating lease liabilities	1,970	2,422
Other non-current liabilities (Note 10)	12,944	9,588
Total liabilities	129,392	226,090
Commitments and contingencies (Note 19)		
Stockholders' equity		
Common stock, \$0.01 par value, 150,000,000 shares authorized, 55,676,851 shares issued and 46,464,889 outstanding at September 30, 2021 and 44,943,854 shares issued and 35,783,347 outstanding at December 31, 2020	557	450
Additional paid-in capital	256,619	163,010
Retained earnings	289,931	286,834
Treasury stock, 9,211,962 shares at September 30, 2021 and 9,160,507 shares at December 31, 2020, respectively	(109,407)	(108,397)
Accumulated other comprehensive income (loss)	(4,403)	3,703
Total stockholders' equity	433,297	345,600
Total liabilities and stockholders' equity	\$ 562,689	\$ 571,690

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

MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
	(In thousands of U.S. dollars, except share data)			
Revenues:				
Net sales – standard products business	\$ 117,415	\$ 116,262	\$ 333,589	\$ 335,953
Net sales – transitional Fab 3 foundry services	9,585	8,551	30,306	28,161
Total revenues	<u>127,000</u>	<u>124,813</u>	<u>363,895</u>	<u>364,114</u>
Cost of sales:				
Cost of sales – standard products business	71,641	87,494	221,297	245,917
Cost of sales – transitional Fab 3 foundry services	8,772	8,731	27,659	28,341
Total cost of sales	<u>80,413</u>	<u>96,225</u>	<u>248,956</u>	<u>274,258</u>
Gross profit	46,587	28,588	114,939	89,856
Operating expenses:				
Selling, general and administrative expenses	12,550	12,888	39,185	37,398
Research and development expenses	12,270	12,477	39,015	34,094
Other charges	1,766	—	17,202	554
Total operating expenses	<u>26,586</u>	<u>25,365</u>	<u>95,402</u>	<u>72,046</u>
Operating income	20,001	3,223	19,537	17,810
Interest expense	(113)	(5,485)	(1,239)	(16,522)
Foreign currency gain (loss), net	(7,579)	8,864	(12,000)	(13,638)
Other income, net	1,608	714	2,839	2,343
Income (loss) from continuing operations before income tax expense	13,917	7,316	9,137	(10,007)
Income tax expense (benefit)	3,149	(1,145)	6,040	836
Income (loss) from continuing operations	10,768	8,461	3,097	(10,843)
Income from discontinued operations, net of tax	—	264,501	—	289,227
Net income	<u>\$ 10,768</u>	<u>\$ 272,962</u>	<u>\$ 3,097</u>	<u>\$ 278,384</u>
Basic earnings (loss) per common share—				
Continuing operations	\$ 0.23	\$ 0.24	\$ 0.07	\$ (0.31)
Discontinued operations	—	7.50	—	8.24
Total	<u>\$ 0.23</u>	<u>\$ 7.74</u>	<u>\$ 0.07</u>	<u>\$ 7.93</u>
Diluted earnings (loss) per common share—				
Continuing operations	\$ 0.23	\$ 0.21	\$ 0.07	\$ (0.31)
Discontinued operations	—	5.68	—	8.24
Total	<u>\$ 0.23</u>	<u>\$ 5.89</u>	<u>\$ 0.07</u>	<u>\$ 7.93</u>
Weighted average number of shares—				
Basic	46,449,234	35,280,864	44,377,250	35,089,479
Diluted	47,808,457	46,581,788	45,811,792	35,089,479

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

MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (Unaudited)

	<u>Three Months Ended</u>		<u>Nine Months Ended</u>	
	<u>September 30,</u> <u>2021</u>	<u>September 30,</u> <u>2020</u>	<u>September 30,</u> <u>2021</u>	<u>September 30,</u> <u>2020</u>
	(In thousands of U.S. dollars)			
Net income	\$ 10,768	\$ 272,962	\$ 3,097	\$ 278,384
Other comprehensive income (loss)				
Foreign currency translation adjustments	(860)	(6,517)	(2,809)	9,191
Derivative adjustments				
Fair valuation of derivatives	(3,271)	1,390	(4,964)	(1,410)
Reclassification adjustment for loss (gain) on derivatives included in net income	653	41	(333)	292
Total other comprehensive income (loss)	(3,478)	(5,086)	(8,106)	8,073
Total comprehensive income (loss)	<u>\$ 7,290</u>	<u>\$ 267,876</u>	<u>\$ (5,009)</u>	<u>\$ 286,457</u>

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

MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (Unaudited)

(In thousands of U.S. dollars, except share data)	Common Stock		Additional Paid-In Capital	Retained Earnings (Deficit)	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total
	Shares	Amount					
Three Months Ended September 30, 2021:							
Balance at June 30, 2021	46,350,945	\$ 556	\$253,244	\$279,163	\$(109,407)	\$ (925)	\$422,631
Stock-based compensation	—	—	2,005	—	—	—	2,005
Exercise of stock options	112,944	1	1,370	—	—	—	1,371
Settlement of restricted stock units	1,000	0	(0)	—	—	—	—
Other comprehensive loss, net	—	—	—	—	—	(3,478)	(3,478)
Net income	—	—	—	10,768	—	—	10,768
Balance at September 30, 2021	<u>46,464,889</u>	<u>\$ 557</u>	<u>\$256,619</u>	<u>\$289,931</u>	<u>\$(109,407)</u>	<u>\$ (4,403)</u>	<u>\$433,297</u>
Three Months Ended September 30, 2020:							
Balance at June 30, 2020	35,143,033	\$ 443	\$155,591	\$ (52,709)	\$(107,649)	\$ 10,499	\$ 6,175
Stock-based compensation	—	—	2,226	—	—	—	2,226
Exercise of stock options	287,292	3	2,024	—	—	—	2,027
Settlement of restricted stock units	59,395	1	(1)	—	—	—	—
Other comprehensive loss, net	—	—	—	—	—	(5,086)	(5,086)
Net income	—	—	—	272,962	—	—	272,962
Balance at September 30, 2020	<u>35,489,720</u>	<u>\$ 447</u>	<u>\$159,840</u>	<u>\$220,253</u>	<u>\$(107,649)</u>	<u>\$ 5,413</u>	<u>\$278,304</u>
Nine Months Ended September 30, 2021:							
Balance at December 31, 2020	35,783,347	\$ 450	\$163,010	\$286,834	\$(108,397)	\$ 3,703	\$345,600
Stock-based compensation	—	—	6,056	—	—	—	6,056
Exchange of exchangeable senior note	10,144,131	101	83,639	—	—	—	83,740
Exercise of stock options	289,704	3	3,917	—	—	—	3,920
Settlement of restricted stock units	299,162	3	(3)	—	—	—	—
Acquisition of treasury stock	(51,455)	—	—	—	(1,010)	—	(1,010)
Other comprehensive loss, net	—	—	—	—	—	(8,106)	(8,106)
Net income	—	—	—	3,097	—	—	3,097
Balance at September 30, 2021	<u>46,464,889</u>	<u>\$ 557</u>	<u>\$256,619</u>	<u>\$289,931</u>	<u>\$(109,407)</u>	<u>\$ (4,403)</u>	<u>\$433,297</u>
Nine Months Ended September 30, 2020:							
Balance at December 31, 2019	34,800,312	\$ 439	\$152,404	\$ (58,131)	\$(107,033)	\$ (2,660)	\$ (14,981)
Stock-based compensation	—	—	4,754	—	—	—	4,754
Exercise of stock options	375,643	4	2,686	—	—	—	2,690
Settlement of restricted stock units	367,759	4	(4)	—	—	—	—
Acquisition of treasury stock	(53,994)	—	—	—	(616)	—	(616)
Other comprehensive income, net	—	—	—	—	—	8,073	8,073
Net income	—	—	—	278,384	—	—	278,384
Balance at September 30, 2020	<u>35,489,720</u>	<u>\$ 447</u>	<u>\$159,840</u>	<u>\$220,253</u>	<u>\$(107,649)</u>	<u>\$ 5,413</u>	<u>\$278,304</u>

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

MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	Nine Months Ended	
	September 30, 2021	September 30, 2020
(In thousands of U.S. dollars)		
Cash flows from operating activities		
Net income	\$ 3,097	\$ 278,384
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	10,576	13,333
Provision for severance benefits	5,514	14,150
Amortization of debt issuance costs and original issue discount	261	1,824
Loss on foreign currency, net	32,607	6,609
Restructuring and other charges	750	490
Provision for inventory reserves	1,484	4,079
Stock-based compensation	6,056	4,754
Gain on sale of discontinued operations	—	(287,117)
Other, net	442	85
Changes in operating assets and liabilities		
Accounts receivable, net	6,696	(16,583)
Unbilled accounts receivable, net	—	14,260
Inventories	(4,561)	1,390
Other receivables	(5,287)	6,111
Other current assets	7,933	9,143
Accounts payable	(16,192)	(5,156)
Other accounts payable	(3,729)	(8,034)
Accrued expenses	(2,391)	1,991
Accrued income taxes	(8,308)	12,546
Other current liabilities	555	2,243
Other non-current liabilities	(666)	2,868
Payment of severance benefits	(4,772)	(5,888)
Other, net	(49)	59
Net cash provided by operating activities	30,016	51,541
Cash flows from investing activities		
Proceeds from settlement of hedge collateral	3,995	8,029
Payment of hedge collateral	(2,744)	(7,841)
Purchase of property, plant and equipment	(13,368)	(16,353)
Payment for intellectual property registration	(455)	(664)
Collection of guarantee deposits	3,192	891
Payment of guarantee deposits	(4,960)	(611)
Proceeds from sale of discontinued operations	—	350,553
Other, net	(103)	26
Net cash provided by (used in) investing activities	(14,443)	334,030
Cash flows from financing activities		
Proceeds from exercise of stock options	3,920	2,690
Acquisition of treasury stock	(1,653)	(1,021)
Repayment of financing related to water treatment facility arrangement	(427)	(402)
Repayment of principal portion of finance lease liabilities	(49)	(165)
Net cash provided by financing activities	1,791	1,102
Effect of exchange rates on cash and cash equivalents	(21,003)	3,781
Net increase (decrease) in cash and cash equivalents	(3,639)	390,454
Cash and cash equivalents		
Beginning of the period	279,940	151,657
End of the period	<u>\$ 276,301</u>	<u>\$ 542,111</u>
Supplemental cash flow information		
Cash paid for interest	\$ 2,094	\$ 19,044
Cash paid for income taxes	\$ 12,609	\$ 2,573
Non-cash investing activities		
Property, plant and equipment additions in other accounts payable	\$ 11,513	\$ 3,865
Non-cash financing activities		
Exchange of exchangeable senior notes into common stock	\$ 83,740	\$ —

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

MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(TABULAR DOLLARS IN THOUSANDS, EXCEPT SHARE DATA)

1. Business, Basis of Presentation and Significant Accounting Policies

Business

Magnachip Semiconductor Corporation (together with its subsidiaries, the “Company”) is a designer and manufacturer of analog and mixed-signal semiconductor platform solutions for communications, Internet of Things (“IoT”) applications, consumer and industrial applications.

On September 1, 2020 (the “Closing Date”), the Company completed the sale of the Company’s Foundry Services Group business and its fabrication facility located in Cheongju, Korea, known as “Fab 4” to Key Foundry Co., Ltd. (the “Buyer”), a Korean corporation, in exchange for a purchase price equal to approximately \$350.6 million in cash, pursuant to the terms of a business transfer agreement (the “Business Transfer Agreement”) dated March 31, 2020 by and among the Company and Magnus Semiconductor, LLC, a Korean limited liability company (“Magnus”). The purchase price was paid in a combination of U.S. Dollars in the amount of \$46.5 million and Korean Won in the amount of approximately KRW 360.6 billion. In addition to the purchase price, the Buyer assumed all severance liabilities relating to the transferred employees, which had a value of approximately \$100 million. The Buyer is a wholly owned subsidiary of Magnus, which was established by Alchemist Capital Partners Korea Co., Ltd. and Credian Partners, Inc. On April 20, 2020, Magnus assigned, and the Buyer assumed, all rights and obligations of Magnus under the Business Transfer Agreement. This divestiture of the Foundry Services Group business and Fab 4 was made in connection with the Company’s strategic shift of its operational focus to its standard products business. The Foundry Services Group was historically a reportable segment. The Foundry Services Group business was classified as discontinued operations in the Company’s consolidated statements of operations and excluded from both continuing operations and segment results for the three and nine months ended September 30, 2020. Accordingly, the Company has one reportable segment, its standard products business, together with transitional foundry services associated with its fabrication facility located in Gumi, Korea, known as “Fab 3,” that it expects to perform for the Buyer for a period of up to three years from the Closing Date (the “Transitional Fab 3 Foundry Services”).

The Company’s standard products business includes its Display Solutions and Power Solutions business lines. The Company’s Display Solutions products provide panel display solutions to major suppliers of large and small rigid and flexible panel displays, and mobile, automotive applications and home appliances. The Company’s Power Solutions products include discrete and integrated circuit solutions for power management in communications, consumer and industrial applications.

Basis of Presentation

The accompanying unaudited interim consolidated financial statements of the Company have been prepared in accordance with generally accepted accounting principles in the United States of America (“U.S. GAAP”). These interim consolidated financial statements include normal recurring adjustments and the elimination of all intercompany accounts and transactions which are, in the opinion of management, necessary to provide a fair statement of the Company’s financial condition and results of operations for the periods presented. These interim consolidated financial statements are presented in accordance with Accounting Standards Codification (“ASC”) 270, “Interim Reporting” and, accordingly, do not include all of the information and note disclosures required by U.S. GAAP for complete financial statements, except for the changes below. The results of operations for the three and nine months ended September 30, 2021 are not necessarily indicative of the results to be expected for a full year or for any other periods. The consolidated statement of cash flow for the nine months ended September 30, 2020 has not been adjusted to separately disclose the cash flow related to discontinued operations, but the material items in the operating and investing activities of the cash flow relating to discontinued operations for the same period is disclosed in Note 3. Unless otherwise stated, information in these notes to consolidated financial statements relates to the Company’s continuing operations and excludes the discontinued operations.

The December 31, 2020 balance sheet data was derived from the Company’s audited financial statements, but does not include all disclosures required by U.S. GAAP. The interim consolidated financial statements should be read in conjunction with the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2020.

Recently Adopted Accounting Pronouncements

In December 2019, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2019-12, “Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes” (“ASU 2019-12”). ASU 2019-12 removes certain exceptions to the general principles in Topic 740 and improves consistent application of and simplifies GAAP for other areas of Topic 740 by clarifying and amending existing guidance. The Company adopted ASU 2019-12 as of January 1, 2021, and the adoption of ASU 2019-12 did not have a material impact on the Company’s consolidated financial statements.

2. Merger Agreement

On March 25, 2021, the Company, South Dearborn Limited, an exempted company incorporated in the Cayman Islands with limited liability (“Parent”), formed by an affiliate of Wise Road Capital LTD, and Michigan Merger Sub, Inc., a Delaware corporation and a wholly owned subsidiary of Parent (“Merger Sub”), entered into an Agreement and Plan of Merger (as it may be amended, supplemented or modified from time to time, the “Merger Agreement”). The Merger Agreement provides that, among other things, and subject to the terms and conditions thereof, Merger Sub will be merged with and into the Company (the “Merger”), with the Company continuing its corporate existence under the General Corporation Law of the State of Delaware (the “DGCL”) as the surviving corporation in the Merger and becoming a wholly owned subsidiary of Parent.

Pursuant to the Merger Agreement, each share of the Company’s common stock, par value \$0.01 per share (the “Common Stock”), issued and outstanding immediately before the effective time of the Merger (the “Effective Time”) (other than (a) shares of Common Stock owned by the Company or any of its wholly owned subsidiaries or by Parent or any of its subsidiaries immediately before the Effective Time (collectively, the “Excluded Shares”) and (b) any shares of Common Stock for which the holder thereof (i) has not voted in favor of the Merger or consented to it in writing and (ii) has properly and validly exercised their statutory rights of appraisal in respect of such shares of Common Stock in accordance with Section 262 of the DGCL (collectively, “Dissenting Shares”)) will be cancelled and will cease to exist and will be automatically converted into the right to receive \$29.00 in cash, without interest (the “Merger Consideration”), subject to applicable withholding taxes.

Consummation of the Merger is subject to certain customary closing conditions, including (i) approval of the Merger Agreement by our stockholders, (ii) the receipt of certain required or requested governmental approvals or authorizations (including from the Committee on Foreign Investment in the United States (“CFIUS”) and the Korean Ministry of Trade, Industry and Energy (“MOTIE”)), (iii) the absence of any order or law issued, enacted or deemed applicable by certain governmental authorities specified in the Merger Agreement that makes consummation of the Merger illegal and that remains in effect (a “Prohibitive Order”), (iv) the absence of a Company Material Adverse Effect (as defined in the Merger Agreement) and (v) other customary closing conditions, including the accuracy of each party’s representations and warranties, and each party’s compliance with its obligations under the Merger Agreement (subject in the case of this clause (v) to certain materiality qualifiers).

The Merger Agreement contains termination rights for each of the Company and Parent, including if (i) the consummation of the Merger does not occur by 11:59 p.m. (New York time) on December 25, 2021 (subject to extension to March 25, 2022 at the option of either party if certain regulatory approvals or authorizations have not been obtained by such date or certain governmental authorities specified in the Merger Agreement have issued, enacted or deemed applicable a Prohibitive Order), (ii) the Requisite Company Vote is not obtained, (iii) any of certain governmental authorities specified in the Merger Agreement issues, enacts or deems applicable after the date of the Merger Agreement a Prohibitive Order that has become final and non-appealable, or (iv) the other party has breached the Merger Agreement, which breach would give rise to a failure, or has materially contributed to the failure, of certain conditions to the non-breaching party’s obligations to close (subject to a cure period). Additionally, each of the Company and Parent may terminate the Merger Agreement in certain other circumstances.

For the three and nine months ended September 30, 2021, the Company incurred \$1,552 thousand and \$13,842 thousand, respectively, of professional fees and certain transaction related-expenses incurred in connection with the Merger, which were recognized in other charges in the consolidated statements of operations.

The foregoing description of the Merger Agreement is not complete and is qualified in its entirety by reference to the Merger Agreement, which is filed as Exhibit 2.1 to the Company’s Current Report on Form 8-K filed on March 29, 2021 and as amended by the Letter Agreement attached as Exhibit 2.1 to the Company’s Form 8-K filed on August 23, 2021.

3. Discontinued Operations

On September 1, 2020, the Company completed the sale of the Company's Foundry Services Group business and Fab 4. As a result of the sale of the Foundry Services Group business and Fab 4, the Company recorded a gain of \$287,117 thousand and all operations from the Foundry Services Group business and Fab 4 were classified as discontinued operations for the three and nine months ended September 30, 2020. Following the consummation of the sale, and for up to three years, the Company is expected to provide the Transitional Fab 3 Foundry Services at an agreed upon cost plus mark-up. For the periods prior to the Closing Date, revenue from providing the Transitional Fab 3 Foundry Services to the Foundry Services Group is recorded at cost on both of the continuing and discontinued businesses for comparative purposes. Cash inflows to the Company from the Buyer related to providing the Transitional Fab 3 Foundry Services were \$11,428 thousand and \$36,218 thousand for the three and nine months ended September 30, 2021, respectively.

The following table summarizes the results from discontinued operations, net of tax, for the three and nine months ended September 30, 2020.

	<u>Three Months Ended</u>	<u>Nine Months Ended</u>
	<u>September 30, 2020</u>	
	<u>(In thousands of U.S. dollars)</u>	
Revenues:		
Net sales – Foundry Services Group	\$ 72,674	\$ 254,732
Net sales – transitional Fab 3 foundry services	(6,277)	(25,887)
Total revenues	66,397	228,845
Cost of sales:		
Cost of sales – Foundry Services Group	52,420	182,872
Cost of sales – transitional Fab 3 foundry services	(6,277)	(25,887)
Total cost of sales	46,143	156,985
Gross profit	20,254	71,860
Operating expenses:		
Selling, general and administrative expenses	4,068	14,704
Research and development expenses	5,166	19,484
Restructuring and other charges	7,870	10,574
Total operating expenses	17,104	44,762
Operating income from discontinued operations	3,150	27,098
Foreign currency gain (loss), net	(797)	1,277
Others, net	18	66
Income from discontinued operations before income tax expense	2,371	28,441
Income tax expense	14,173	15,517
Gain on sale of discontinued operations	287,117	287,117
Transaction costs	(10,814)	(10,814)
Income from discontinued operations, net of tax	<u>264,501</u>	<u>289,227</u>

For the three and nine months ended September 30, 2020, the Company recorded \$7,870 thousand and \$10,574 thousand, respectively, in professional fees incurred in connection with the sale of the Foundry Services Group business and Fab 4, and recorded such costs as restructuring and other charges in the above.

The following table provides supplemental cash flows information related to discontinued operations:

	<u>Nine Months Ended</u>	
	<u>September 30,</u>	
	<u>2020</u>	
	<u>(In thousands of U.S. dollars)</u>	
Significant non-cash operating activities:		
Depreciation and amortization	\$	5,365
Provision for severance benefits		8,209
Stock-based compensation		388
Investing activities:		
Capital expenditures	\$	(5,838)

4. Inventories

Inventories as of September 30, 2021 and December 31, 2020 consist of the following (in thousands):

	September 30, 2021	December 31, 2020
Finished goods	\$ 6,529	\$ 6,425
Semi-finished goods and work-in-process	29,895	30,968
Raw materials	7,801	6,526
Materials in-transit	284	1,021
Less: inventory reserve	(5,736)	(5,901)
Inventories, net	<u>\$ 38,773</u>	<u>\$ 39,039</u>

Changes in inventory reserve for the three and nine months ended September 30, 2021 and 2020 are as follows (in thousands):

	Three Months Ended September 30, 2021	Nine Months Ended September 30, 2021	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2020
Beginning balance	\$ (8,101)	\$ (5,901)	\$ (5,307)	\$ (5,947)
Change in reserve				
Inventory reserve charged to costs of sales	(242)	(5,592)	(3,472)	(6,541)
Sale of previously reserved inventory	2,099	4,076	1,578	3,231
	1,857	(1,516)	(1,894)	(3,310)
Write off	180	1,110	835	1,976
Translation adjustments	328	571	(139)	82
Reclassified to assets held for sale	—	—	—	694
Ending balance	<u>\$ (5,736)</u>	<u>\$ (5,736)</u>	<u>\$ (6,505)</u>	<u>\$ (6,505)</u>

Inventory reserve represents the Company's best estimate in value lost due to excessive inventory level, physical deterioration, obsolescence, changes in price levels, or other causes based on individual facts and circumstances. Inventory reserve relates to inventory items including finished goods, semi-finished goods, work-in-process and raw materials. Write off of this reserve is recognized only when the related inventory has been disposed or scrapped.

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5. Property, Plant and Equipment

Property, plant and equipment as of September 30, 2021 and December 31, 2020 are comprised of the following (in thousands):

	September 30, 2021	December 31, 2020
Buildings and related structures	\$ 24,159	\$ 24,882
Machinery and equipment	102,280	106,244
Finance lease right-of-use assets	316	344
Others	29,591	31,208
	<u>156,346</u>	<u>162,678</u>
Less: accumulated depreciation	(92,363)	(90,370)
Land	13,905	15,167
Construction in progress	25,464	8,908
Property, plant and equipment, net	<u>\$ 103,352</u>	<u>\$ 96,383</u>

Aggregate depreciation expenses totaled \$10,018 thousand and \$7,473 thousand for the nine months ended September 30, 2021 and 2020, respectively.

6. Intangible Assets

Intangible assets as of September 30, 2021 and December 31, 2020 are comprised of the following (in thousands):

	September 30, 2021		
	Gross amount	Accumulated amortization	Net amount
Intellectual property assets	\$9,176	\$ (6,771)	\$2,405
Intangible assets	<u>\$9,176</u>	<u>\$ (6,771)</u>	<u>\$2,405</u>
	December 31, 2020		
	Gross amount	Accumulated amortization	Net amount
Intellectual property assets	\$9,486	\$ (6,759)	\$2,727
Intangible assets	<u>\$9,486</u>	<u>\$ (6,759)</u>	<u>\$2,727</u>

Aggregate amortization expenses for intangible assets totaled \$558 thousand and \$495 thousand for the nine months ended September 30, 2021 and 2020, respectively.

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7. Leases

The Company has operating and finance leases for buildings and other assets such as vehicles and office equipment. The Company's leases have remaining lease terms ranging from 1 year to 4 years.

The tables below present financial information related to the Company's leases.

Supplemental balance sheets information related to leases as of September 30, 2021 and December 31, 2020 are as follows (in thousands):

Leases	Classification	September 30, 2021	December 31, 2020
Assets			
Operating lease	Operating lease right-of-use assets	\$ 3,727	\$ 4,632
Finance lease	Property, plant and equipment, net	142	206
Total lease assets		<u>\$ 3,869</u>	<u>\$ 4,838</u>
Liabilities			
Current			
Operating	Operating lease liabilities	\$ 1,757	\$ 2,210
Finance	Other current liabilities	67	68
Non-current			
Operating	Non-current operating lease liabilities	1,970	2,422
Finance	Other non-current liabilities	90	153
Total lease liabilities		<u>\$ 3,884</u>	<u>\$ 4,853</u>

The following table presents the weighted average remaining lease term and discount rate:

	September 30, 2021	December 31, 2020
Weighted average remaining lease term		
Operating leases	2.7 years	3.0 years
Finance leases	2.3 years	3.0 years
Weighted average discount rate		
Operating leases	4.61%	5.55%
Finance leases	7.75%	7.75%

The components of lease cost included in the Company's consolidated statements of operations, are as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Operating lease cost	\$ 691	\$ 480	\$ 2,098	\$ 1,409
Finance lease cost				
Amortization of right-of-use assets	17	16	50	47
Interest on lease liabilities	4	4	11	13
Total lease cost	<u>\$ 712</u>	<u>\$ 500</u>	<u>\$ 2,159</u>	<u>\$ 1,469</u>

The above table does not include an immaterial cost of short-term leases for the three and nine months ended September 30, 2021 and 2020.

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Other lease information is as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Cash paid for amounts included in the measurement of lease liabilities				
Operating cash flows from operating leases	\$ 691	\$ 480	\$ 2,098	\$ 1,409
Operating cash flows from finance leases	4	4	11	13
Financing cash flows from finance leases	16	15	49	43

The aggregate future lease payments for operating and finance leases as of September 30, 2021 are as follows (in thousands):

	Operating Leases	Finance Leases
Remainder of 2021	\$ 674	\$ 19
2022	1,518	76
2023	812	76
2024	581	—
2025	396	—
Total future lease payments	3,981	171
Less: Imputed interest	(254)	(14)
Present value of future payments	<u>\$ 3,727</u>	<u>\$ 157</u>

8. Accrued Expenses

Accrued expenses as of September 30, 2021 and December 31, 2020 are comprised of the following (in thousands):

	September 30, 2021	December 31, 2020
Payroll, benefits and related taxes, excluding severance benefits	\$ 9,095	\$ 10,296
Withholding tax attributable to intercompany interest income	1,789	28
Interest on senior notes	—	1,396
Outside service fees	1,014	755
Restructuring and others	750	2,658
Others	520	1,108
Accrued expenses	<u>\$ 13,168</u>	<u>\$ 16,241</u>

9. Derivative Financial Instruments

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

Details of the zero cost collar contracts as of September 30, 2021 are as follows (in thousands):

<u>Date of transaction</u>	<u>Total notional amount</u>	<u>Month of settlement</u>
December 15, 2020	\$ 15,000	October 2021 to December 2021
February 26, 2021	\$ 9,000	October 2021 to December 2021
May 13, 2021	\$ 39,000	January 2022 to September 2022
August 13, 2021	\$ 48,000	January 2022 to December 2022

Details of the zero cost collar contracts as of December 31, 2020 are as follows (in thousands):

<u>Date of transaction</u>	<u>Total notional amount</u>	<u>Month of settlement</u>
July 13, 2020	\$ 30,000	January 2021 to June 2021
December 15, 2020	\$ 30,000	July 2021 to December 2021
December 18, 2020	\$ 18,000	March 2021 to June 2021

The zero cost collar contracts qualify as cash flow hedges under ASC 815, "Derivatives and Hedging," since at both the inception of the contracts and on an ongoing basis, the hedging relationship was and is expected to be highly effective in achieving offsetting cash flows attributable to the hedged risk during the term of the contracts.

The fair values of the Company's outstanding zero cost collar contracts recorded as assets and liabilities as of September 30, 2021 and December 31, 2020 are as follows (in thousands):

<u>Derivatives designated as hedging instruments:</u>		<u>September 30, 2021</u>	<u>December 31, 2020</u>
Asset Derivatives:			
Zero cost collars	Other current assets	\$ —	\$ 2,036
Liability Derivatives:			
Zero cost collars	Other current liabilities	\$ 3,196	\$ 195
Zero cost collars	Other non-current liabilities	\$ 257	\$ —

Offsetting of derivative liabilities as of September 30, 2021 is as follows (in thousands):

<u>As of September 30, 2021</u>	<u>Gross amounts of recognized liabilities</u>	<u>Gross amounts offset in the balance sheets</u>	<u>Net amounts of liabilities presented in the balance sheets</u>	<u>Gross amounts not offset in the balance sheets</u>		<u>Net amount</u>
				<u>Financial instruments</u>	<u>Cash collateral pledged</u>	
Liability Derivatives:						
Zero cost collars	\$ 3,453	\$ —	\$ 3,453	\$ —	\$ (2,720)	\$ 733

Offsetting of derivative assets and liabilities as of December 31, 2020 is as follows (in thousands):

<u>As of December 31, 2020</u>	<u>Gross amounts of recognized assets/liabilities</u>	<u>Gross amounts offset in the balance sheets</u>	<u>Net amounts of assets/liabilities presented in the balance sheets</u>	<u>Gross amounts not offset in the balance sheets</u>		<u>Net amount</u>
				<u>Financial instruments</u>	<u>Cash collateral pledged</u>	
Asset Derivatives:						
Zero cost collars	\$ 2,036	\$ —	\$ 2,036	\$ —	\$ —	\$ 2,036
Liability Derivatives:						
Zero cost collars	\$ 195	\$ —	\$ 195	\$ —	\$ —	\$ 195

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

The following table summarizes the impact of derivative instruments on the consolidated statements of operations for the three months ended September 30, 2021 and 2020. Net sales of discontinued operations for the three months ended September 30, 2020 are included in the below table (in thousands):

Derivatives in ASC 815 Cash Flow Hedging Relationships	Amount of Gain (Loss) Recognized in AOCI on Derivatives		Location/Amount of Gain (Loss) Reclassified from AOCI Into Statement of Operations	Location/Amount of Gain (Loss) Recognized in Statement of Operations on Derivatives				
	Three Months Ended September 30,			Three Months Ended September 30,				
	2021	2020		2021	2020			
Zero cost collars	\$ (3,271)	\$ 1,390	Net sales	\$ (653)	\$ (41)	Other income, net	\$ 237	\$ 50

The following table summarizes the impact of derivative instruments on the consolidated statements of operations for the nine months ended September 30, 2021 and 2020. Net sales of discontinued operations for the nine months ended September 30, 2020 are included in the below table (in thousands):

Derivatives in ASC 815 Cash Flow Hedging Relationships	Amount of Gain (Loss) Recognized in AOCI on Derivatives		Location/Amount of Gain (Loss) Reclassified from AOCI Into Statement of Operations	Location/Amount of Gain (Loss) Recognized in Statement of Operations on Derivatives				
	Nine Months Ended September 30,			Nine Months Ended September 30,				
	2021	2020		2021	2020			
Zero cost collars	\$(4,964)	\$(1,410)	Net sales	\$ 333	\$(292)	Other income, net	\$ 94	\$ 222

As of September 30, 2021, the amount expected to be reclassified from accumulated other comprehensive loss into loss within the next 12 months is \$3,406 thousand.

The Company set aside cash deposits to the counterparties, Nomura Financial Investment (Korea) Co., Ltd. (“NFIK”), Deutsche Bank AG, Seoul Branch (“DB”) and Standard Chartered Bank Korea Limited (“SC”), as required for the zero cost collar contracts. These cash deposits are recorded as hedge collateral on the consolidated balance sheets. Cash deposits as of September 30, 2021 and December 31, 2020 are as follows (in thousands):

Counterparties	September 30, 2021	December 31, 2020
NFIK	\$ —	\$ 3,250
DB	—	1,000
SC	1,000	1,000
Total	\$ 1,000	\$ 5,250

The Company is required to deposit additional cash collateral with NFIK, DB and SC for any exposure in excess of \$500 thousand, and \$2,720 thousand of additional cash collateral was required and recorded as hedge collateral on the consolidated balance sheet as of September 30, 2021. There was no such cash collateral required as of December 31, 2020.

These zero cost collar contracts may be terminated by the counterparties in a number of circumstances, including if the Company’s credit rating falls below B-/B3 or if the Company’s total cash and cash equivalents is less than \$30,000 thousand at the end of a fiscal quarter, unless a waiver is obtained.

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10. Fair Value Measurements

Fair Value of Financial Instruments

As of September 30, 2021, the following table represents the Company's liabilities measured at fair value on a recurring basis and the basis for that measurement (in thousands):

	Carrying Value September 30, 2021	Fair Value Measurement September 30, 2021	Quoted Prices in Active Markets for Identical Liability (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Liabilities:					
Derivative liabilities (other current liabilities)	\$ 3,196	\$ 3,196	—	\$ 3,196	—
Derivative liabilities (other non-current liabilities)	\$ 257	\$ 257	—	\$ 257	—

As of December 31, 2020, the following table represents the Company's assets and liabilities measured at fair value on a recurring basis and the basis for that measurement (in thousands):

	Carrying Value December 31, 2020	Fair Value Measurement December 31, 2020	Quoted Prices in Active Markets for Identical Asset / Liability (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:					
Derivative assets (other current assets)	\$ 2,036	\$ 2,036	—	\$ 2,036	—
Liabilities:					
Derivative liabilities (other current liabilities)	\$ 195	\$ 195	—	\$ 195	—

Items not reflected in the table above include cash equivalents, accounts receivable, other receivables, accounts payable, and other accounts payable, fair value of which approximate carrying values due to the short-term nature of these instruments. The fair value of assets and liabilities whose carrying value approximates fair value is determined using Level 2 inputs.

Fair Value of Borrowings

	December 31, 2020	
	Carrying Value	Fair Value
(In thousands of U.S. dollars)		
Borrowings:		
5.0% Exchangeable Senior Notes due March 2021 (Level 2)	\$ 83,479	\$ 145,466

On January 17, 2017, the Company's wholly owned subsidiary, MagnaChip Semiconductor S.A., closed an offering (the "Exchangeable Notes Offering") of 5.0% Exchangeable Senior Notes due March 1, 2021 (the "Exchangeable Notes"), of \$86,250 thousand, which represents the principal amount, excluding \$5,902 thousand of debt issuance costs. In December 2018 and February 2019, MagnaChip Semiconductor S.A. repurchased a principal amount equal to \$1,590 thousand and \$920 thousand, respectively, of the Exchangeable Notes in the open market. The Exchangeable Notes matured on March 1, 2021, unless they were earlier repurchased or converted. The Company estimated the fair value of the Exchangeable Notes using the market approach, which utilizes quoted market prices that fall under Level 2. For further description of the Exchangeable Notes, see Note 11, "Borrowings."

Fair Values Measured on a Non-recurring Basis

The Company's non-financial assets, such as property, plant and equipment, and intangible assets are recorded at fair value upon acquisition and are remeasured at fair value only if an impairment charge is recognized. As of September 30, 2021 and 2020 the Company did not have any assets or liabilities measured at fair value on a non-recurring basis.

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11. Borrowings

There were no borrowings outstanding as of September 30, 2021. As of December 31, 2020, the following table represents the Company's borrowings (in thousands):

	<u>December 31,</u> <u>2020</u>
5.0% Exchangeable Senior Notes due March 2021	\$ 83,740
Less: unamortized discount and debt issuance costs	(261)
Total borrowings, net	83,479
Less: current portion of long-term borrowings, net	83,479
Long-term borrowings, net	<u>\$ —</u>

5.0% Exchangeable Senior Notes

On January 17, 2017, MagnaChip Semiconductor S.A. closed the Exchangeable Notes Offering of \$86,250 thousand aggregate principal amount of 5.0% Exchangeable Notes. Interest on the Exchangeable Notes accrued at a rate of 5.0% per annum, payable semi-annually on March 1 and September 1 of each year, beginning on March 1, 2017. The Exchangeable Notes matured on March 1, 2021, unless they were earlier repurchased or converted. Holders had the right to convert their notes at their option at any time prior to the close of business on the business day immediately preceding the stated maturity date.

The Company incurred debt issuance costs of \$5,902 thousand related to the issuance of the Exchangeable Notes. The debt issuance costs are recorded as a direct deduction from the long-term borrowings in the consolidated balance sheets and amortized to interest expense using the effective interest method over the term of the Exchangeable Notes. Interest expense related to the Exchangeable Notes for the nine months ended September 30, 2021 was \$958 thousand. Interest expense related to the Exchangeable Notes for the three and nine months ended September 30, 2020 were \$1,429 thousand and \$4,720 thousand, respectively.

In February 2019, the Company repurchased a principal amount equal to \$920 thousand of the Exchangeable Notes in the open market, resulting in a loss of \$63 thousand, which was recorded as loss on early extinguishment of borrowings, net in the consolidated statements of operations for the year ended December 31, 2019. In December 2018, the Company repurchased a principal amount equal to \$1,590 thousand of the Exchangeable Notes in the open market, resulting in a loss of \$234 thousand, which was recorded as loss on early extinguishment of borrowings, net in the consolidated statements of operations for the year ended December 31, 2018.

Prior to the March 1, 2021 maturity of the Exchangeable Notes, holders elected to exchange all outstanding Exchangeable Notes for an aggregate of 10,144,131 shares of the Company's common stock in satisfaction in full of the outstanding obligations under the Exchangeable Notes. Upon exchange, the Company delivered for each \$1,000 principal amount of exchanged Exchangeable Notes a number of shares equal to the exchange rate of 121.1387 shares of common stock per \$1,000 principal amount of Exchangeable Notes, which was equivalent to an exchange price of approximately \$8.26 per share of common stock. In connection with the exchanges, the fractional shares were paid in cash. Following March 1, 2021, the Company does not have any Exchangeable Notes outstanding.

12. Accrued Severance Benefits

The majority of accrued severance benefits are for employees in the Company's Korean subsidiary. Pursuant to the Employee Retirement Benefit Security Act of Korea, eligible employees and executive officers with one or more years of service are entitled to severance benefits upon the termination of their employment based on their length of service and rate of pay. As of September 30, 2021, 98% of all employees of the Company were eligible for severance benefits.

Changes in accrued severance benefits are as follows (in thousands):

	<u>Three Months Ended</u>		<u>Three Months Ended</u>	
	<u>September 30, 2021</u>		<u>September 30, 2020</u>	
Beginning balance	\$ 53,105	\$ 54,452	\$ 51,785	\$ 53,344
Provisions	2,007	5,514	2,167	5,941
Severance payments	(1,936)	(4,772)	(1,295)	(4,749)
Translation adjustments	(2,441)	(4,459)	1,204	(675)
	<u>50,735</u>	<u>50,735</u>	<u>53,861</u>	<u>53,861</u>
Less: Cumulative contributions to severance insurance deposit accounts				
The National Pension Fund	(12,739)	(12,739)	(1,616)	(1,616)
Group severance insurance plan	(55)	(55)	(73)	(73)
	(200)	(200)	(219)	(219)
Accrued severance benefits, net	<u>\$ 37,741</u>	<u>\$ 37,741</u>	<u>\$ 51,953</u>	<u>\$ 51,953</u>

The severance benefits funded through the Company's National Pension Fund and group severance insurance plan will be used exclusively for payment of severance benefits to eligible employees. These amounts have been deducted from the accrued severance benefit balance.

Beginning in July 2018, the Company contributes to certain severance insurance deposit accounts a certain percentage of severance benefits that are accrued for eligible employees for their services from January 1, 2018. These accounts consist of time deposits and other guaranteed principal and interest, and are maintained at insurance companies, banks or security companies for the benefit of employees. The Company deducts the contributions made to these severance insurance deposit accounts from its accrued severance benefits.

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

	<u>Severance benefits</u>
Remainder of 2021	\$ —
2022	254
2023	631
2024	903
2025	1,840
2026	2,281
2027 – 2031	18,701

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

Korea's mandatory retirement age is 60 under the Employment Promotion for the Aged Act.

13. Foreign Currency Gain (Loss), Net

Net foreign currency gain or loss includes non-cash translation gain or loss associated with intercompany balances. A substantial portion of the Company's net foreign currency gain or loss is non-cash translation gain or loss associated with intercompany long-term loans to the Company's Korean subsidiary. The loans are denominated in U.S. dollars and are affected by changes in the exchange rate between the Korean won and the U.S. dollar. As of September 30, 2021 and December 31, 2020, the outstanding intercompany loan balances including accrued interest between the Korean subsidiary and the Dutch subsidiary were \$393,235 thousand and \$378,852 thousand, respectively. The Korean won to U.S. dollar exchange rates were 1,184.9:1 and 1,088.0:1 using the first base rate as of September 30, 2021 and December 31, 2020, respectively, as quoted by the KEB Hana Bank.

14. Income Taxes

The Company and its subsidiaries file income tax returns in Korea, Japan, Taiwan, the U.S. and in various other jurisdictions. The Company is subject to income or non-income tax examinations by tax authorities of these jurisdictions for all open tax years.

For the three and nine months ended September 30, 2021, the Company recorded an income tax expense from continuing operations of \$3,149 thousand and \$6,040 thousand, respectively, primarily attributable to the Company's Korean subsidiary based on its estimated taxable income for the respective period, combined with its ability to utilize net operating loss carryforwards up to 60%, and interest on intercompany loan balances. During the second quarter of 2021, income tax expense of \$624 thousand was also recorded for certain income-based tax assessments as a result of a regular tax examination completed for the Company's Korean subsidiary for multiple tax years.

For the three months ended September 30, 2020, the Company recorded an income tax benefit from continuing operations of \$1,145 thousand, primarily attributable to the foreign translation loss realized by the Company's Korean subsidiary upon the repayment of a part of its intercompany loan by the Dutch subsidiary to fund the redemption of the 2021 Notes and interest. For the nine months ended September 30, 2020, the Company recorded income tax expense from continuing operations of \$836 thousand, primarily attributable to interest on intercompany loan balances. Income tax expense was recorded for the Company's Korean subsidiary based on the estimated taxable income for the respective period, combined with its ability to utilize net operating loss carryforwards up to 60% in 2020.

15. Geographic and Other Information

The following sets forth information relating to the single continuing operating segment (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Revenues				
Standard products business				
Display Solutions	\$ 58,528	\$ 69,583	\$ 164,024	\$ 216,352
Power Solutions	58,887	46,679	169,565	119,601
Total standard products business	117,415	116,262	333,589	335,953
Transitional Fab 3 foundry services	9,585	8,551	30,306	28,161
Total revenues	\$ 127,000	\$ 124,813	\$ 363,895	\$ 364,114
Gross Profit				
Standard products business	\$ 45,773	\$ 28,768	\$ 112,291	\$ 90,036
Transitional Fab 3 foundry services	814	(180)	2,648	(180)
Total gross profit	\$ 46,587	\$ 28,588	\$ 114,939	\$ 89,856

The following is a summary of net sales—standard products business (which does not include the Transitional Fab 3 Foundry Services) by geographic region, based on the location to which the products are billed (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Korea	\$ 29,664	\$ 28,370	\$ 86,966	\$ 81,144
Asia Pacific (other than Korea)	84,220	84,188	237,312	245,940
United States	1,756	1,789	4,393	3,959
Europe	1,398	1,451	3,847	3,278
Others	377	464	1,071	1,632
Total	\$ 117,415	\$ 116,262	\$ 333,589	\$ 335,953

For the three months ended September 30, 2021 and 2020, of the Company's net sales – standard products business in Asia Pacific (other than Korea), net sales – standard products business in China and Hong Kong represented 72.0% and 87.7%, respectively, and net sales—standard products business in Vietnam represented 19.6% and 8.9%, respectively. For the nine months ended September 30, 2021 and 2020, of the Company's net sales – standard products business in Asia Pacific (other than Korea), net sales – standard products business in China and Hong Kong represented 63.4% and 88.4%, respectively, and net sales—standard products business in Vietnam represented 29.5% and 8.1%, respectively.

Net sales from the Company's top ten largest customers in the standard products business (which does not include the Transitional Fab 3 Foundry Services) accounted for 81% and 87% for the three months ended September 30, 2021 and 2020, respectively, and 81% and 88% for the nine months ended September 30, 2021 and 2020, respectively.

For the three months ended September 30, 2021, the Company had two customers that represented 44.7% and 10.1% of its net sales – standard products business. For the nine months ended September 30, 2021, the Company had two customers that represented 44.6% and 10.6% of its net sales – standard products business. For the three months ended September 30, 2020, the Company had one customer that represented 52.9% of its net sales – standard products business, and for the nine months ended September 30, 2020, the Company had one customer that represented 54.0% of its net sales – standard products business.

As of September 30, 2021 and December 31, 2020, one customer accounted for 24.8% and 45.1% of accounts receivable, respectively.

16. Accumulated Other Comprehensive Income (Loss)

Accumulated other comprehensive income (loss) consists of the following as of September 30, 2021 and December 31, 2020, respectively (in thousands):

	September 30, 2021	December 31, 2020
Foreign currency translation adjustments	\$ (740)	\$ 2,069
Derivative adjustments	(3,663)	1,634
Total	<u>\$ (4,403)</u>	<u>\$ 3,703</u>

Changes in accumulated other comprehensive income (loss) for the three months ended September 30, 2021 and 2020 are as follows (in thousands):

	Foreign currency translation adjustments	Derivative adjustments	Total
Three Months Ended September 30, 2021			
Beginning balance	\$ 120	\$ (1,045)	\$ (925)
Other comprehensive loss before reclassifications	(860)	(3,271)	(4,131)
Amounts reclassified from accumulated other comprehensive loss	—	653	653
Net current-period other comprehensive loss	(860)	(2,618)	(3,478)
Ending balance	<u>\$ (740)</u>	<u>\$ (3,663)</u>	<u>\$ (4,403)</u>

	Foreign currency translation adjustments	Derivative adjustments	Total
Three Months Ended September 30, 2020			
Beginning balance	\$ 11,503	\$ (1,004)	\$ 10,499
Other comprehensive income (loss) before reclassifications	(6,517)	1,390	(5,127)
Amounts reclassified from accumulated other comprehensive loss	—	41	41
Net current-period other comprehensive income (loss)	(6,517)	1,431	(5,086)
Ending balance	<u>\$ 4,986</u>	<u>\$ 427</u>	<u>\$ 5,413</u>

Changes in accumulated other comprehensive income (loss) for the nine months ended September 30, 2021 and 2020 are as follows (in thousands):

	Foreign currency translation adjustments	Derivative adjustments	Total
Nine Months Ended September 30, 2021			
Beginning balance	\$ 2,069	\$ 1,634	\$ 3,703
Other comprehensive loss before reclassifications	(2,809)	(4,964)	(7,773)
Amounts reclassified from accumulated other comprehensive income	—	(333)	(333)
Net current-period other comprehensive loss	(2,809)	(5,297)	(8,106)
Ending balance	<u>\$ (740)</u>	<u>\$ (3,663)</u>	<u>\$ (4,403)</u>

	Foreign currency translation adjustments	Derivative adjustments	Total
Nine Months Ended September 30, 2020			
Beginning balance	\$ (4,205)	\$ 1,545	\$ (2,660)
Other comprehensive income (loss) before reclassifications	9,191	(1,410)	7,781
Amounts reclassified from accumulated other comprehensive loss	—	292	292
Net current-period other comprehensive income (loss)	9,191	(1,118)	8,073
Ending balance	<u>\$ 4,986</u>	<u>\$ 427</u>	<u>\$ 5,413</u>

17. Earnings (Loss) Per Share

The following table illustrates the computation of basic and diluted earnings (loss) per common share for the three and nine months ended September 30, 2021 and 2020:

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
	(In thousands of U.S. dollars, except share data)			
Basic earnings (loss) per share				
Income (loss) from continuing operations	\$ 10,768	\$ 8,461	\$ 3,097	\$ (10,843)
Income from discontinued operations, net of tax	—	264,501	—	289,227
Net income	<u>\$ 10,768</u>	<u>\$ 272,962</u>	<u>\$ 3,097</u>	<u>\$ 278,384</u>
Basic weighted average common stock outstanding	46,449,234	35,280,864	44,377,250	35,089,479
Basic earnings (loss) per common share				
Continuing operations	\$ 0.23	\$ 0.24	\$ 0.07	\$ (0.31)
Discontinued operations	—	7.50	—	8.24
Total	<u>\$ 0.23</u>	<u>\$ 7.74</u>	<u>\$ 0.07</u>	<u>\$ 7.93</u>
Diluted earnings (loss) per share				
Income (loss) from continuing operations	\$ 10,768	\$ 8,461	\$ 3,097	\$ (10,843)
Add back: Interest expense on Exchangeable Notes	—	1,429	—	—
Income (loss) from continuing operations allocated to common stockholders	\$ 10,768	\$ 9,890	\$ 3,097	\$ (10,843)
Income from discontinued operations, net of tax	—	264,501	—	289,227
Net income allocated to common stockholders	<u>\$ 10,768</u>	<u>\$ 274,391</u>	<u>\$ 3,097</u>	<u>\$ 278,384</u>
Basic weighted average common stock outstanding	46,449,234	35,280,864	44,377,250	35,089,479
Net effect of dilutive equity awards	1,359,223	1,156,769	1,434,542	—
Net effect of assumed conversion of 5.0% Exchangeable Notes to common stock	—	10,144,155	—	—
Diluted weighted average common stock outstanding	47,808,457	46,581,788	45,811,792	35,089,479
Diluted earnings (loss) per common share				
Continuing operations	\$ 0.23	\$ 0.21	\$ 0.07	\$ (0.31)
Discontinued operations	—	5.68	—	8.24
Total	<u>\$ 0.23</u>	<u>\$ 5.89</u>	<u>\$ 0.07</u>	<u>\$ 7.93</u>

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

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Options	50,000	697,667	50,000	1,788,202
Restricted Stock Units	—	—	—	1,248,113

For the nine months ended September 30, 2021 and 2020, 1,906,786 shares and 10,144,155 shares, respectively, of potential common stock from the assumed conversion of Exchangeable Notes were also excluded from the computation of diluted earnings (loss) per share as the effect were anti-dilutive for the period.

18. Other Charges

For the three months ended September 30, 2021, other charges totaled \$1,766 thousand, of which \$1,552 thousand related to professional fees and certain transaction related expenses incurred in connection with the Merger and \$214 thousand related to certain non-recurring professional fees and expenses in connection with regulatory requests.

For the nine months ended September 30, 2021, other charges totaled \$17,202 thousand, of which \$13,842 thousand related to professional fees and certain transaction related expenses incurred in connection with the Merger and \$3,360 thousand related to certain non-recurring professional fees and expenses in connection with regulatory requests. For the nine months ended September 30, 2020, other charges were \$554 thousand, which pertained to non-recurring professional service fees and expenses incurred in connection with certain treasury and finance initiatives.

19. Commitments and Contingencies

COVID-19 Pandemic

In December 2019, a strain of coronavirus causing a disease known as COVID-19 surfaced in Wuhan, China, resulting in significant disruptions among Chinese manufacturing and other facilities and travel throughout China. In March 2020, the World Health Organization declared the COVID-19 outbreak a pandemic. Governmental authorities throughout the world have implemented numerous containment measures, including travel bans and restrictions, quarantines, shelter-in-place orders, and business restrictions and shutdowns, resulting in rapidly changing market and economic conditions. Although some of these restrictions and other containment measures have since been lifted or scaled back, ongoing surges of COVID-19 have in some cases resulted in the re-imposition of certain restrictions and containment measures, and may continue to lead to other restrictions being re-implemented in the foreseeable future in response to efforts to reduce the rapid spread of COVID-19.

The Company experienced some minor disruption in its Power Solutions business from assembly and test subcontractors located in China in the first quarter of 2020 as a result of the COVID-19 pandemic. To date, its external Display Solutions business contractors and sub-contractors have not been materially impacted by the COVID-19 pandemic. The Company is, however, unable to accurately predict the full impact that the COVID-19 pandemic will have on its future results of operations due to numerous uncertainties, including the severity and duration of the outbreak, the efficacy of ongoing global vaccination efforts, potential future recurrences of the outbreak, the spread of disease variants that may be resistant to the existing vaccines, further containment actions that may be taken by governmental authorities, the impact to the businesses of its customers and suppliers, and other factors.

The Company continues to closely monitor and evaluate the nature and scope of the impact of the COVID-19 pandemic to its business, consolidated results of operations, and financial condition, and may take further actions altering its business operations and managing its costs and liquidity that the Company deems necessary or appropriate to respond to this fast moving and uncertain global health crisis and the resulting global economic consequences.

Merger-related Complaints

Since April 22, 2021, eleven complaints (each, a “Shareholder Complaint,” and together, the “Shareholder Complaints”) have been filed seeking to enjoin the Merger, or, if the Merger is consummated, rescind the Merger or recover damages, as well as an award of each plaintiff’s fees and litigation expenses. The Shareholder Complaints, each filed as an individual action by a purported stockholder of the Company, are captioned as *Schulthess v. Magnachip Semiconductor Corporation, et al.*, Case No. 1:21-cv-03587 (S.D.N.Y.) (the “Schulthess Complaint”), *Pittman v. Magnachip Semiconductor Corporation, et al.*, Case No. 1:21-cv-02306 (E.D.N.Y.) (the “Pittman Complaint”), *Flanagan v. Magnachip Semiconductor Corporation, et al.*, Case No. 1:21-cv-03743 (S.D.N.Y.) (the “Flanagan Complaint”), *Castelli v. Magnachip Semiconductor Corporation, et al.*, Case No. 1:21-cv-03769 (S.D.N.Y.) (the “Castelli Complaint”), *Doolittle v. Magnachip Semiconductor Corporation, et al.*, Case No. 1:21-cv-03801 (S.D.N.Y.) (the “Doolittle Complaint”), *Thomas v. Magnachip Semiconductor Corporation, et al.*, Case No. 1:21-cv-03860 (S.D.N.Y.) (the “Thomas Complaint”), *Finger v. Magnachip Semiconductor Corporation, et al.*, Case No. 1:21-cv-03927 (S.D.N.Y.), *Kent v. Magnachip Semiconductor Corporation, et al.*, Case No. 1:21-cv-00657 (D. Del.) (the “Kent Complaint”), *Kennedy v. Magnachip Semiconductor Corporation, et al.*, Case No. 2:21-cv-02110 (E.D. Pa.) (the “Kennedy Complaint”), *Monroy v. Magnachip Semiconductor Corporation, et al.*, Case No. 1:21-cv-04921 (S.D.N.Y.) (the “Monroy Complaint”), and *Jones v. Magnachip Semiconductor Corporation, et al.*, Case No. 1:21-cv-04966 (S.D.N.Y.). Each Shareholder Complaint alleges either that the preliminary proxy statement filed by the Company with the Securities and Exchange Commission (“SEC”) on April 19, 2021 or the definitive proxy statement filed by the Company with the SEC on May 7, 2021, is false and/or misleading and asserts claims for violations of Section 14(a) and 20(a) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and SEC Rule 14a-9 against the Company and certain current or former members of the Company’s board of directors (the “Board”). The Schulthess Complaint, Castelli Complaint and Monroy Complaint also allege breaches of fiduciary duties by certain current or former members of the Board. The Schulthess Complaint further alleges that the Company aided and abetted purported breaches of fiduciary duties by certain current or former members of the Board.

On June 8, 2021, the Company voluntarily made supplemental disclosures related to the Merger on Form 8-K in response to certain allegations raised in the Shareholder Complaints described above in order to avoid the risk that the Shareholder Complaints may delay or otherwise adversely affect the consummation of the Merger and to minimize the expense of defending such actions. Since June 8, 2021, the plaintiffs who filed the Pittman Complaint, the Doolittle Complaint, the Flanagan Complaint, the Kennedy Complaint, the Kent Complaint, and the Thomas Complaint voluntarily dismissed their respective complaints.

On August 11, 2021, certain of the complaints filed in the U.S. District Court for the Southern District of New York were consolidated and interim co-lead plaintiffs’ counsel were appointed. On August 26, 2021, the court entered the parties’ stipulated proposed scheduling order. Among other things, the order provides that the plaintiffs will file a consolidated amended complaint after the consummation of the Merger, followed by deadlines for the Company to respond to any such complaint.

Merger-related Events

CFIUS

On May 26, 2021, outside legal counsel of each of the Company and Parent received an e-mail from the U.S. Department of Treasury on behalf of the Staff Chairperson of the CFIUS. In the e-mail, the CFIUS Staff Chairperson, acting on the recommendation of CFIUS, requested that the parties file a notice concerning the Merger and thereby undergo formal CFIUS review of the Merger. Under the terms of the Merger Agreement, the parties' receipt of the request from CFIUS to file a notice concerning the Merger results in the closing of the Merger now being conditioned on the receipt of CFIUS approval without the imposition of a "Burdensome Condition" (as defined in the Merger Agreement), other than a Burdensome Condition to which Parent had previously agreed. The Company and Parent filed such notice with CFIUS on June 11, 2021.

On June 15, 2021, outside legal counsel of each of the Company and Parent received a letter attaching an "Order Establishing Interim Mitigation Measures" (the "Interim Order") from the U.S. Department of Treasury on behalf of CFIUS. The Interim Order imposes the following interim measures, effective as of June 15, 2021, on the Company and Parent: (i) neither of the Company or Parent shall take any action, directly or indirectly, to close, consummate, complete, or effectuate the purpose of the Merger, including: (a) the transfer, lease, license, or sale of any asset or subsidiary of the Company to Parent or any affiliate thereof, (b) the merger of Parent or any affiliate thereof with or into the Company or any affiliate thereof, or (c) the acquisition of any equity or other ownership interest in the Company or any affiliate thereof by Parent or any subsidiary thereof; (ii) Parent shall not take, and shall ensure that none of its subsidiaries take, any security interest in the Company or any affiliate thereof; and (iii) the Company shall not take any action to: (a) change its state of incorporation from Delaware to any other jurisdiction or (b) delist from, or modify the existing listing of the Company on, the New York Stock Exchange. The Interim Order is to remain in effect until (1) CFIUS concludes action under Section 721 of the Defense Production Act of 1950, as amended (the "DPA") with respect to the Merger, (2) the President takes action or declines to take action under Section 721 of the DPA with respect to the Merger or (3) CFIUS or the President revokes or terminates the Interim Order.

On June 17, 2021, in light of the Interim Order, the Company announced the postponement of its special meeting of stockholders, which was scheduled to be held at 8:00 p.m. Eastern time on June 17, 2021, pending further developments with respect to the Interim Order.

On July 26, 2021, outside legal counsel of each of the Company and Parent received a letter from the Acting CFIUS Staff Chairperson notifying the parties that CFIUS will undertake an investigation of the Merger pursuant to Section 721(b)(2) of the DPA, which will be completed no later than September 13, 2021.

On August 27, 2021, outside legal counsel for each of the Company and Parent received a letter from the Department of Treasury on behalf of CFIUS indicating that (i) CFIUS has identified risks to the national security of the United States arising as a result of the Merger, (ii) CFIUS has not identified any mitigation measures, including those proposed jointly by the Company and Parent, that CFIUS believes would adequately mitigate the identified risks, (iii) absent new information arising during the investigation period that alters CFIUS's assessment of the national security risks or the feasibility of mitigation measures to resolve those risks, CFIUS anticipates that it will refer the matter to the President for decision, and (iv) the Company and Parent could provide additional information to CFIUS for consideration, including proposals to permanently mitigate the identified national security risks.

By letter dated September 10, 2021, the Company and Parent, through outside legal counsel, asked CFIUS to permit them to withdraw and re-file their June 11, 2021 notice concerning the Merger, in order to permit further discussion with CFIUS concerning potential options for permanently mitigating risks to the national security that have been identified by CFIUS. By letter dated September 13, 2021, the Acting CFIUS Staff Chairperson notified the parties that CFIUS had granted this request and that a new CFIUS review period for the Merger would commence on September 14, 2021 and conclude no later than October 28, 2021. By letter dated October 28, 2021, the Acting CFIUS Staff Chairperson notified the parties that CFIUS is undertaking an investigation of the Merger pursuant to Section 721(b)(2) of the DPA, which will be completed no later than December 13, 2021.

MOTIE

On June 16, 2021, the Company's Korean subsidiary received a letter from the MOTIE requesting it to either apply for an approval or file a report, as may be applicable, under Article 11-2 of the Act on Prevention of Divulgence and Protection of Industrial Technology (the "ITA") concerning the Merger.

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Under the terms of the Merger Agreement, the Company's Korean subsidiary's receipt of the request from MOTIE to apply for approval or file a report pursuant to the ITA concerning the Merger may be deemed to have resulted in the closing of the Merger now being conditioned on the receipt of MOTIE's authorization without the imposition of a "Burdensome Condition" (as defined in the Merger Agreement), other than a Burdensome Condition to which Parent had previously agreed. The Company's Korean subsidiary filed such report with MOTIE on July 20, 2021.

SAMR

On June 30, 2021, based on an application filed by the Company and Parent on May 7, 2021, the State Administration for Market Regulation ("SAMR") announced that the Merger was cleared pursuant to the Anti-monopoly Law (China) on June 21, 2021. Under the terms of the Merger Agreement, the parties' receipt of the clearance from SAMR satisfies one of the conditions to the closing of the Merger.

Advances to Suppliers

The Company, from time to time, may make advances in form of prepayments or deposits to suppliers to procure materials to meet its planned production. The Company recorded advances of \$1,150 thousand and \$5,500 thousand as other current assets as of September 30, 2021 and December 31, 2020, respectively.

FORWARD LOOKING STATEMENTS

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

These forward-looking statements are largely based on our expectations and beliefs concerning future events, which reflect estimates and assumptions made by our management. These estimates and assumptions reflect our best judgment based on currently known market conditions and other factors relating to our operations and business environment, all of which are difficult to predict and many of which are beyond our control. Although we believe our estimates and assumptions to be reasonable, they are inherently uncertain and involve a number of risks and uncertainties that are beyond our control. In addition, management’s assumptions about future events may prove to be inaccurate. Management cautions all readers that the forward-looking statements contained in this report are not guarantees of future performance, and we cannot assure any reader that those statements will be realized or the forward-looking events and circumstances will occur. Actual results may differ materially from those anticipated or implied in the forward-looking statements due to the factors listed in this section, in “Part II: Item 1A. Risk Factors” herein and in “Part I: Item 1A. Risk Factors” in our Annual Report on Form 10-K filed on March 9, 2021 (“2020 Form 10-K”) (including that the impact of the COVID-19 pandemic may also exacerbate the risks discussed therein).

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

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

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

The following discussion and analysis should be read in conjunction with the interim unaudited consolidated financial statements and the related notes included elsewhere in this Report.

Overview

We are a designer and manufacturer of analog and mixed-signal semiconductor platform solutions for communications, IoT applications, consumer, computing, industrial and automotive applications. We have a proven record with more than 40 years of operating history, a portfolio of approximately 1,200 registered patents and pending applications and extensive engineering and manufacturing process expertise.

Our standard products business includes our Display Solutions and Power Solutions business lines.

Our Display Solutions products provides flat panel display solutions to major suppliers of large and small flat panel displays. These products include source and gate drivers and timing controllers that cover a wide range of flat panel displays used in mobile communications, automobiles, entertainment devices, notebook PCs, monitors and liquid crystal display (LCD) and organic light emitting diodes (OLED). Our Display Solutions products support some of the industry's most advanced display technologies, such as OLEDs, low temperature polysilicon thin film transistors (LTFS TFTs) and amorphous silicon thin film transistors (a-Si TFTs). Since 2007, we have designed and manufactured OLED display driver integrated circuit (IC) products. Our current portfolio of OLED solutions address a wide range of resolutions ranging from HD to Wide Quad High Definition (WQHD) for applications including smartphones, TVs, and other mobile devices.

Our Power Solutions business line produces power management semiconductor products including discrete and integrated circuit solutions for power management in consumer, communications, computing and industrial applications. These products include metal oxide semiconductor field effect transistors (MOSFETs), insulated-gate bipolar transistors (IGBTs), AC-DC converters, DC-DC converters, LED drivers, switching regulators, linear regulators, interface ICs and power management ICs (PMICs) for a range of devices, including televisions, smartphones, desktop PCs, notebooks, tablets, servers, telecommunication power, home appliances, industrial applications such as uninterruptible power supplies (UPSs), LED lighting, personal mobility, motor drives and battery management systems (BMS).

Our wide variety of analog and mixed-signal semiconductor products combined with our mature technology platform allow us to address multiple high-growth end markets and rapidly develop and introduce new products and services in response to market demands. Our design center and substantial manufacturing operations in Korea place us at the core of the global electronics device supply chain. We believe this enables us to quickly and efficiently respond to our customers' needs, and allows us to better serve and capture additional demand from existing and new customers.

To maintain and increase our profitability, we must accurately forecast trends in demand for electronics devices that incorporate semiconductor products we produce. We must understand our customers' needs as well as the likely end market trends and demand in the markets they serve. We must also invest in relevant research and development activities and purchase necessary materials on a timely basis to meet our customers' demand while maintaining our target margins and cash flow.

The semiconductor markets in which we participate are highly competitive. The prices of our products tend to decrease regularly over their useful lives, and such price decreases can be significant as new generations of products are introduced by us or our competitors. We strive to offset the impact of declining selling prices for existing products through cost reductions and the introduction of new products that command selling prices above the average selling price of our existing products. In addition, we seek to manage our inventories and manufacturing capacity so as to mitigate the risk of losses from product obsolescence.

Demand for our products and services is driven by overall demand for communications, IoT, consumer and industrial products and can be adversely affected by periods of weak consumer and enterprise spending or by market share losses by our customers. In order to mitigate the impact of market volatility on our business, we continually strive to diversify our portfolio of products, customers, and target applications. We also expect that new competitors will emerge in these markets that may place increased pressure on the pricing for our products and services. While we believe we are well positioned competitively to compete in these markets and against these new competitors as a result of our long operating history, existing manufacturing capacity and our worldwide customer base, if we are not effective in competing in these markets, our operating results may be adversely affected.

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Net sales for our standard products business are driven by design wins in which we are selected by an electronics original equipment manufacturer (OEM) or other potential customer to supply its demand for a particular product. A customer will often have more than one supplier designed into multi-source components for a particular product line. Once we have design wins and the products enter into mass production, we often specify the pricing of a particular product for a set period of time, with periodic discussions and renegotiations of pricing with our customers. In any given period, our net sales depend heavily upon the end-market demand for the goods in which our products are used, the inventory levels maintained by our customers and, in some cases, allocation of demand for components for a particular product among selected qualified suppliers.

In contrast to completely fabless semiconductor companies, our internal manufacturing capacity provides us with greater control over manufacturing costs and the ability to implement process and production improvements for our internally manufactured products, which can favorably impact gross profit margins. Our internal manufacturing capacity also allows for better control over delivery schedules, improved consistency over product quality and reliability and improved ability to protect intellectual property from misappropriation on these products. However, having internal manufacturing capacity exposes us to the risk of under-utilization of manufacturing capacity that results in lower gross profit margins, particularly during downturns in the semiconductor industry.

Our standard products business requires investments in capital equipment. Analog and mixed-signal manufacturing facilities and processes are typically distinguished by the design and process implementation expertise rather than the use of the most advanced equipment. Many of these processes also tend to migrate more slowly to smaller geometries due to technological barriers and increased costs. For example, some of our products use high-voltage technology that requires larger geometries and that may not migrate to smaller geometries for several years, if at all. As a result, our manufacturing base and strategy do not require substantial investment in leading edge process equipment for those products, allowing us to utilize our facilities and equipment over an extended period of time with moderate required capital investments. In addition, we are less likely to experience significant industry overcapacity, which can cause product prices to decline significantly. In general, we seek to invest in manufacturing capacity that can be used for multiple high-value applications over an extended period of time. In addition, we outsource manufacturing of those products which do require advanced technology and 12-inch wafer capacity, such as organic light emitting diodes (OLED). We believe this balanced capital investment strategy enables us to optimize our capital investments and facilitates more diversified product and service offerings.

Since 2007, we had designed and manufactured OLED display driver ICs in our internal manufacturing facilities. As we expanded our design capabilities to products that require lower geometries unavailable at our existing manufacturing facilities, we began outsourcing manufacturing of certain OLED display driver ICs to an external 12-inch foundry starting in the second half of 2015. This additional source of manufacturing is an increasingly important part of our supply chain management. By outsourcing manufacturing of OLED products to external 12-inch foundries, we are able to adapt dynamically to changing customer requirements and address growing markets without substantial capital investments by us. However, relying on external foundries exposes us to the risk of being unable to secure manufacturing capacity, particularly under the current global shortage of foundry services. Although we are working strategically with external foundries to secure long-term wafer capacity, if we are unsuccessful, our ability to deliver products to our customers may be negatively impacted, which would adversely affect our relationship with customers and opportunities to secure new design-wins.

Our success going forward will depend upon our ability to adapt to future challenges such as the emergence of new competitors for our products and services or the consolidation of current competitors. Additionally, we must innovate to remain ahead of, or at least rapidly adapt to, technological breakthroughs that may lead to a significant change in the technology necessary to deliver our products and services. We believe that our established relationships and close collaboration with leading customers enhance our awareness of new product opportunities, market and technology trends and improve our ability to adapt and grow successfully.

Recent Developments

The Merger

On March 25, 2021, we entered into the Merger Agreement with Parent and Merger Sub, pursuant to which, among other things, and subject to the terms and conditions thereof, Merger Sub will be merged with and into the Company, with the Company continuing its corporate existence as the surviving corporation in the Merger and becoming a wholly owned subsidiary of Parent.

Under the terms of the Merger Agreement, each share of our common stock issued and outstanding immediately before the Effective Time (other than Excluded Shares and Dissenting Shares) will be cancelled and will cease to exist and will be automatically converted into the right to receive \$29.00 in cash, without interest, and subject to applicable withholding taxes. The all-cash transaction has an equity value of approximately \$1.4 billion. The Merger is fully backed by equity commitments and not contingent on any financing conditions.

We have incurred, and will continue to incur, significant costs, expenses and fees for professional services and other transaction costs in connection with the Merger.

For more information on the Merger Agreement and the Merger, see “Item 1. Interim Consolidated Financial Statements—Notes to Consolidated Financial Statements—Note 2. Merger Agreement” in this Report.

Conversion of 5.0% Exchangeable Senior Notes due 2021 (the “Exchangeable Notes”)

Prior to the March 1, 2021 maturity of our Exchangeable Notes, holders thereof elected to exchange the Exchangeable Notes for an aggregate of 10,144,131 shares of our common stock in satisfaction in full of the outstanding obligations under the Exchangeable Notes. On March 1, 2021, we paid the final interest payment on the Exchangeable Notes of \$2.1 million and no longer have any Exchangeable Notes obligations outstanding as of such date.

COVID-19 Pandemic

In December 2019, a strain of coronavirus causing a disease known as COVID-19 surfaced in Wuhan, China, resulting in significant disruptions among Chinese manufacturing and other facilities and travel throughout China. In March 2020, the World Health Organization declared the COVID-19 outbreak a pandemic. Governmental authorities throughout the world have implemented numerous containment measures, including travel bans and restrictions, quarantines, shelter-in-place orders, and business restrictions and shutdowns, resulting in rapidly changing market and economic conditions. Although some of these restrictions and other containment measures have since been lifted or scaled back, ongoing surges of COVID-19 have, in some cases, resulted in the re-imposition of certain restrictions and containment measures, and may continue to lead to other restrictions being re-implemented in the foreseeable future in response to efforts to reduce the rapid spread of COVID-19.

We experienced some minor disruption in our Power Solutions business from assembly and test subcontractors located in China in the first quarter of 2020 as a result of the COVID-19 pandemic. To date, our external Display Solutions business contractors and sub-contractors have not been materially impacted by the COVID-19 pandemic. We are, however, unable to accurately predict the full impact that the COVID-19 pandemic will have on future results of operations due to numerous uncertainties, including the severity and the duration of the outbreak, the efficacy of ongoing global vaccination efforts, potential future recurrences of the outbreak, the spread of disease variants that may be resistant to the existing vaccines, further containment actions that may be taken by governmental authorities, the impact to the businesses of our customers and suppliers, and other factors.

We continue to closely monitor and evaluate the nature and scope of the impact of the COVID-19 pandemic to our business, consolidated results of operations, and financial condition, and may take further actions altering our business operations and managing our costs and liquidity that we deem necessary or appropriate to respond to this fast moving and uncertain global health crisis and the resulting global economic consequences.

Global Semiconductor Chip Shortage

Recent sharp increases in demand for semiconductor products have resulted in a global shortage of manufacturing capacity. As a result, we may experience increased costs to manufacture our products and may not be able to manufacture and deliver all of the orders placed by our customers. Specifically, if we are unable to secure manufacturing capacity from the external foundries we rely on, our ability to deliver products to our customers may be negatively impacted. Also, this shortage of manufacturing capacity may lead to an increase in our manufacturing costs which we may not be fully able to pass on to our customers.

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In an effort to minimize the potential adverse impact of the supply shortage, we are working strategically with external foundries to secure long-term wafer capacity. If we are unsuccessful, however, such shortage could limit our ability to meet demand for our products in the future, which would adversely affect our reputation and competitive position, resulting in a negative impact on results of operations.

We are not able to foresee when the current shortage of manufacturing capacity will subside. A prolonged global supply shortage could negatively impact our financial condition, potentially resulting in a need for additional capital to fund strategic initiatives or operating activities.

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Explanation and Reconciliation of Non-U.S. GAAP Measures

Adjusted EBITDA, Adjusted Operating Income and Adjusted Net Income

We use the terms Adjusted EBITDA, Adjusted Operating Income and Adjusted Net Income (including on a per share basis) in this Report. Adjusted EBITDA, as we define it, is a non-U.S. GAAP measure. We define Adjusted EBITDA for the periods indicated as EBITDA (as defined below), adjusted to exclude (i) equity-based compensation expense, (ii) foreign currency loss (gain), net, (iii) derivative valuation gain, net, (iv) inventory reserve related to Huawei impact of downstream trade restrictions, (v) expenses related to Fab 3 power outage and (vi) other charges, net. EBITDA for the periods indicated is defined as income (loss) from continuing operations before interest expense (income), net, income tax expense (benefit), and depreciation and amortization.

See the footnotes to the table below for further information regarding these items. We present Adjusted EBITDA as a supplemental measure of our performance because:

- we believe that Adjusted EBITDA, by eliminating the impact of a number of items that we do not consider to be indicative of our core ongoing operating performance, provides a more comparable measure of our operating performance from period-to-period and may be a better indicator of future performance;
- we believe that Adjusted EBITDA is commonly requested and used by securities analysts, investors and other interested parties in the evaluation of the Company as an enterprise level performance measure that eliminates the effects of financing, income taxes and the accounting effects of capital spending, as well as other one time or recurring items described above; and
- we believe that Adjusted EBITDA is useful for investors, among other reasons, to assess the Company's period-to-period core operating performance and to understand and assess the manner in which management analyzes operating performance.

We use Adjusted EBITDA in a number of ways, including:

- for planning purposes, including the preparation of our annual operating budget;
- to evaluate the effectiveness of our enterprise level business strategies;
- in communications with our Board of Directors concerning our consolidated financial performance; and
- in certain of our compensation plans as a performance measure for determining incentive compensation payments.

We encourage you to evaluate each adjustment and the reasons we consider them appropriate. In evaluating Adjusted EBITDA, you should be aware that in the future we may incur expenses similar to the adjustments in this presentation. Adjusted EBITDA is not a measure defined in accordance with U.S. GAAP and should not be construed as an alternative to income from continuing operations, cash flows from operating activities or net income, as determined in accordance with U.S. GAAP. A reconciliation of loss from continuing operations to Adjusted EBITDA from continuing operations is as follows:

	Three Months Ended September 30, 2021	Nine Months Ended September 30, 2021	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2020
	(Dollars in millions)			
Income (loss) from continuing operations	\$ 10.8	\$ 3.1	\$ 8.5	\$ (10.8)
Interest expense (income), net	(0.4)	(0.5)	4.9	14.5
Income tax expense (benefit)	3.1	6.0	(1.1)	0.8
Depreciation and amortization	3.6	10.6	2.9	8.0
EBITDA	\$ 17.1	\$ 19.2	\$ 15.0	\$ 12.5
Adjustments:				
Equity-based compensation expense(a)	2.0	6.1	2.1	4.4
Foreign currency loss (gain), net(b)	7.6	12.0	(8.9)	13.6
Derivative valuation gain, net(c)	(0.2)	(0.1)	(0.1)	(0.2)
Inventory reserve related to Huawei impact of downstream trade restrictions(d)	(1.1)	(1.1)	2.3	2.3
Expenses related to Fab 3 power outage(e)	—	—	1.2	1.2
Other charges, net(f)	1.0	16.5	—	0.6
Adjusted EBITDA	\$ 26.4	\$ 52.6	\$ 11.7	\$ 34.3

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- (a) This adjustment eliminates the impact of non-cash equity-based compensation expenses. Although we expect to incur non-cash equity-based compensation expenses in the future, these expenses do not generally require cash settlement, and, therefore, are not used by us to assess the profitability of our operations. We believe that analysts and investors will find it helpful to review our operating performance without the effects of these non-cash expenses as supplemental information.
- (b) This adjustment mainly eliminates the impact of non-cash foreign currency translation associated with intercompany debt obligations and foreign currency denominated receivables and payables, as well as the cash impact of foreign currency transaction gains or losses on collection of such receivables and payment of such payables. Although we expect to incur foreign currency translation gains or losses in the future, we believe that analysts and investors will find it helpful to review our operating performance without the effects of these primarily non-cash gains or losses, which we cannot control. Additionally, we believe the isolation of this adjustment provides investors with enhanced comparability to prior and future periods of our operating performance results.
- (c) This adjustment eliminates the impact of gain or loss recognized in income on derivatives, which represents derivatives value changes excluded from the risk being hedged. We enter into derivative transactions to mitigate foreign exchange risks. As our derivative transactions are limited to a certain portion of our expected cash flows denominated in U.S. dollars, and we do not enter into derivative transactions for trading or speculative purposes, we do not believe that these charges or gains are indicative of our core operating performance.
- (d) For the three and nine months ended September 30, 2020, this adjustment eliminates the impact of excess and obsolete inventory charge that we recorded in relation to the U.S. Government's export restrictions on Huawei, which is a downstream customer of some of our direct customers. For the three and nine months ended September 31, 2021, this adjustment eliminates a partial reversal of such inventory charge as a portion of such reserved inventory was subsequently sold to certain other customers. As this charge and the timing of its partial reversal meaningfully impacted our operational results and are not expected to represent an ongoing operating expense subject to our ability to foresee and control, we believe our operating performance results are more meaningfully compared if this charge and related reversal are excluded.
- (e) This adjustment eliminates \$1.2 million in expenses related to the write-off of the damaged work in process wafers and charges for facility recovery. These charges are inconsistent in amount and frequency, and we do not believe that these charges are indicative of our core operation performance and have been excluded for comparative purposes.
- (f) For the three and nine months ended September 30, 2021, this adjustment eliminates non-recurring professional service fees and expenses of \$1.8 million and \$17.2 million, respectively, incurred in connection with the Merger and regulatory requests, both of which were offset in part by a \$0.7 million legal settlement gain related to certain expenses incurred in prior periods in connection with our legacy Fab 4 (which was sold during the year ended December 31, 2020) and awarded in the current quarter. For the nine months ended September 30, 2020, this adjustment eliminates non-recurring professional service fees and expenses incurred in connection with certain treasury and finance initiatives. As these expenses meaningfully impacted our operating results and are not expected to represent an ongoing operating expense to us, we believe our operating performance results are more usefully compared if these expenses are excluded.

Adjusted EBITDA has limitations as an analytical tool, and you should not consider it in isolation, or as a substitute for analysis of our results as reported under U.S. GAAP. Some of these limitations are:

- Adjusted EBITDA does not reflect our cash expenditures, or future requirements, for capital expenditures or contractual commitments;
- Adjusted EBITDA does not reflect changes in, or cash requirements for, our working capital needs;
- Adjusted EBITDA does not reflect the interest expense, or the cash requirements necessary to service interest or principal payments, on our debt;
- although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often need to be replaced in the future, and Adjusted EBITDA does not reflect any cash requirements for such replacements;
- Adjusted EBITDA does not consider the potentially dilutive impact of issuing equity-based compensation to our management team and employees;
- Adjusted EBITDA does not reflect the costs of holding certain assets and liabilities in foreign currencies; and
- other companies in our industry may calculate Adjusted EBITDA differently than we do, limiting its usefulness as a comparative measure.

Because of these limitations, Adjusted EBITDA should not be considered as a measure of discretionary cash available to us to invest in the growth of our business. We compensate for these limitations by relying primarily on our U.S. GAAP results and using Adjusted EBITDA only supplementally.

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We present Adjusted Operating Income as supplemental measures of our performance. We prepare Adjusted Operating Income by adjusting operating income to eliminate the impact of equity-based compensation expenses and other items that may be either one time or recurring that we do not consider to be indicative of our core ongoing operating performance. We believe that Adjusted Operating Income is useful to investors to provide a supplemental way to understand our underlying operating performance and allows investors to monitor and understand changes in our ability to generate income from ongoing business operations.

Adjusted Operating Income is not a measure defined in accordance with U.S. GAAP and should not be construed as an alternative to operating income, income from continuing operations, cash flows from operating activities or net income, as determined in accordance with U.S. GAAP. We encourage you to evaluate each adjustment and the reasons we consider them appropriate. Other companies in our industry may calculate Adjusted Operating Income differently than we do, limiting its usefulness as a comparative measure. In addition, in evaluating Adjusted Operating Income, you should be aware that in the future we may incur expenses similar to the adjustments in this presentation. We define Adjusted Operating Income for the periods indicated as operating income adjusted to exclude (i) equity-based compensation expense, (ii) inventory reserve related to Huawei impact of downstream trade restrictions, (iii) expenses related to Fab 3 power outage and (iv) other charges.

The following table summarizes the adjustments to operating income that we make in order to calculate Adjusted Operating Income from continuing operations for the periods indicated:

	Three Months Ended September 30, 2021	Nine Months Ended September 30, 2021	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2020
	(In millions)			
Operating income	\$ 20.0	\$ 19.5	\$ 3.2	\$ 17.8
Adjustments:				
Equity-based compensation expense(a)	2.0	6.1	2.1	4.4
Inventory reserve related to Huawei impact of downstream trade restrictions(b)	(1.1)	(1.1)	2.3	2.3
Expenses related to Fab 3 power outage(c)	—	—	1.2	1.2
Other charges(d)	1.8	17.2	—	0.6
Adjusted Operating Income	<u>\$ 22.7</u>	<u>\$ 41.7</u>	<u>\$ 8.8</u>	<u>\$ 26.2</u>

- (a) This adjustment eliminates the impact of non-cash equity-based compensation expenses. Although we expect to incur non-cash equity-based compensation expenses in the future, these expenses do not generally require cash settlement, and, therefore, are not used by us to assess the profitability of our operations. We believe that analysts and investors will find it helpful to review our operating performance without the effects of these non-cash expenses as supplemental information.
- (b) For the three and nine months ended September 30, 2020, this adjustment eliminates the impact of excess and obsolete inventory charge that we recorded in relation to the U.S. Government's export restrictions on Huawei, which is a downstream customer of some of our direct customers. For the three and nine months ended September 31, 2021, this adjustment eliminates a partial reversal of such inventory charge as a portion of such reserved inventory was subsequently sold to certain other customers. As this charge and the timing of its partial reversal meaningfully impacted our operational results and are not expected to represent an ongoing operating expense subject to our ability to foresee and control, we believe our operating performance results are more meaningfully compared if this charge and related reversal are excluded.
- (c) This adjustment eliminates \$1.2 million in expenses related to the write-off of the damaged work in process wafers and charges for facility recovery. These charges are inconsistent in amount and frequency, and we do not believe that these charges are indicative of our core operation performance and have been excluded for comparative purposes.
- (d) For the three and nine months ended September 30, 2021, this adjustment eliminates non-recurring professional service fees and expenses incurred in connection with the Merger and regulatory requests. For the nine months ended September 30, 2020, this adjustment eliminates non-recurring professional service fees and expenses incurred in connection with certain treasury and finance initiatives. As these expenses meaningfully impacted our operating results and are not expected to represent an ongoing operating expense to us, we believe our operating performance results are more usefully compared if these expenses are excluded.

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We present Adjusted Net Income (including on a per share basis) as a further supplemental measure of our performance. We prepare Adjusted Net Income (including on a per share basis) by adjusting income (loss) from continuing operations to eliminate the impact of a number of non-cash expenses and other items that may be either one time or recurring that we do not consider to be indicative of our core ongoing operating performance. We believe that Adjusted Net Income (including on a per share basis) is particularly useful because it reflects the impact of our asset base and capital structure on our operating performance. We present Adjusted Net Income (including on a per share basis) for a number of reasons, including:

- we use Adjusted Net Income (including on a per share basis) in communications with our Board of Directors concerning our consolidated financial performance without the impact of non-cash expenses and the other items as we discussed below since we believe that it is a more consistent measure of our core operating results from period to period; and
- we believe that reporting Adjusted Net Income (including on a per share basis) is useful to readers in evaluating our core operating results because it eliminates the effects of non-cash expenses as well as the other items we discuss below, such as foreign currency gains and losses, which are out of our control and can vary significantly from period to period.

Adjusted Net Income (including on a per share basis) is not a measure defined in accordance with U.S. GAAP and should not be construed as an alternative to income from continuing operations, cash flows from operating activities or net income, as determined in accordance with U.S. GAAP. We encourage you to evaluate each adjustment and the reasons we consider them appropriate. Other companies in our industry may calculate Adjusted Net Income (including on a per share basis) differently than we do, limiting its usefulness as a comparative measure. In addition, in evaluating Adjusted Net Income (including on a per share basis), you should be aware that in the future we may incur expenses similar to the adjustments in this presentation. We define Adjusted Net Income (including on a per share basis); for the periods indicated as income (loss) from continuing operations, adjusted to exclude (i) equity-based compensation expense, (ii) foreign currency loss (gain), net, (iii) derivative valuation gain, net, (iv) inventory reserve related to Huawei impact of downstream trade restrictions, (v) expenses related to Fab 3 power outage, (vi) other charges, net and (vii) income tax effect on non-GAAP adjustments.

The following table summarizes the adjustments to income (loss) from continuing operations that we make in order to calculate Adjusted Net Income (including on a per share basis) from continuing operations for the periods indicated:

	Three Months Ended September 30, 2021	Nine Months Ended September 30, 2021	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2020
	(In millions, except per share data)			
Income (loss) from continuing operations	\$ 10.8	\$ 3.1	\$ 8.5	\$ (10.8)
Adjustments:				
Equity-based compensation expense(a)	2.0	6.1	2.1	4.4
Foreign currency loss (gain), net(b)	7.6	12.0	(8.9)	13.6
Derivative valuation gain, net(c)	(0.2)	(0.1)	(0.1)	(0.2)
Inventory reserve related to Huawei impact of downstream trade restrictions(d)	(1.1)	(1.1)	2.3	2.3
Expenses related to Fab 3 power outage(e)	—	—	1.2	1.2
Other charges, net(f)	1.0	16.5	—	0.6
Income tax effect on non-GAAP adjustments(g)	—	—	—	—
Adjusted Net Income	<u>\$ 20.1</u>	<u>\$ 36.5</u>	<u>\$ 5.1</u>	<u>\$ 11.0</u>
Reported earnings (loss) per share – basic	\$ 0.23	\$ 0.07	\$ 0.24	\$ (0.31)
Reported earnings (loss) per share – diluted	\$ 0.23	\$ 0.07	\$ 0.21	\$ (0.31)
Weighted average number of shares – basic	46,449,234	44,377,250	35,280,864	35,089,479
Weighted average number of shares – diluted	47,808,457	45,811,792	46,581,788	35,089,479
Adjusted earnings per share – basic	\$ 0.43	\$ 0.82	\$ 0.15	\$ 0.31
Adjusted earnings per share – diluted	\$ 0.42	\$ 0.78	\$ 0.14	\$ 0.30
Weighted average number of shares – basic	46,449,234	44,377,250	35,280,864	35,089,479
Weighted average number of shares – diluted	47,808,457	47,718,578	46,581,788	36,151,622

- (a) This adjustment eliminates the impact of non-cash equity-based compensation expenses. Although we expect to incur non-cash equity-based compensation expenses in the future, these expenses do not generally require cash settlement, and, therefore, are not used by us to assess the profitability of our operations. We believe that analysts and investors will find it helpful to review our operating performance without the effects of these non-cash expenses as supplemental information.
- (b) This adjustment mainly eliminates the impact of non-cash foreign currency translation associated with intercompany debt obligations and foreign currency denominated receivables and payables, as well as the cash impact of foreign currency transaction gains or losses on collection of such receivables and payment of such payables. Although we expect to incur foreign

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currency translation gains or losses in the future, we believe that analysts and investors will find it helpful to review our operating performance without the effects of these primarily non-cash gains or losses, which we cannot control. Additionally, we believe the isolation of this adjustment provides investors with enhanced comparability to prior and future periods of our operating performance results.

- (c) This adjustment eliminates the impact of gain or loss recognized in income on derivatives, which represents derivatives value changes excluded from the risk being hedged. We enter into derivative transactions to mitigate foreign exchange risks. As our derivative transactions are limited to a certain portion of our expected cash flows denominated in U.S. dollars, and we do not enter into derivative transactions for trading or speculative purposes, we do not believe that these charges or gains are indicative of our core operating performance.
- (d) For the three and nine months ended September 30, 2020, this adjustment eliminates the impact of excess and obsolete inventory charge that we recorded in relation to the U.S. Government's export restrictions on Huawei, which is a downstream customer of some of our direct customers. For the three and nine months ended September 31, 2021, this adjustment eliminates a partial reversal of such inventory charge as a portion of such reserved inventory was subsequently sold to certain other customers. As this charge and the timing of its partial reversal meaningfully impacted our operational results and are not expected to represent an ongoing operating expense subject to our ability to foresee and control, we believe our operating performance results are more meaningfully compared if this charge and related reversal are excluded.
- (e) This adjustment eliminates \$1.2 million in expenses related to the write-off of the damaged work in process wafers and charges for facility recovery. These charges are inconsistent in amount and frequency, and we do not believe that these charges are indicative of our core operation performance and have been excluded for comparative purposes.
- (f) For the three and nine months ended September 30, 2021, this adjustment eliminates non-recurring professional service fees and expenses of \$1.8 million and \$17.2 million, respectively, incurred in connection with the Merger and regulatory requests, both of which were offset in part by a \$0.7 million legal settlement gain related to certain expenses incurred in prior periods in connection with our legacy Fab 4 (which was sold during the year ended December 31, 2020) and awarded in the current quarter. For the nine months ended September 30, 2020, this adjustment eliminates non-recurring professional service fees and expenses incurred in connection with certain treasury and finance initiatives. As these expenses meaningfully impacted our operating results and are not expected to represent an ongoing operating expense to us, we believe our operating performance results are more usefully compared if these expenses are excluded.
- (g) For the three and nine months ended September 30, 2021 and 2020, there was no tax impact from the adjustments to net income to calculate our Adjusted Net Income due to net operating loss carry-forwards available at our parent entity in the U.S., based on the nature and origination of the adjustments, to offset related taxable income.

We believe that all adjustments to income (loss) from continuing operations used to calculate Adjusted Net Income was applied consistently to the periods presented.

Adjusted Net Income has limitations as an analytical tool, and you should not consider it in isolation, or as a substitute for analysis of our results as reported under U.S. GAAP. Some of these limitations are:

- Adjusted Net Income does not reflect changes in, or cash requirements for, our working capital needs;
- Adjusted Net Income does not consider the potentially dilutive impact of issuing equity-based compensation to our management team and employees;
- Adjusted Net Income does not reflect the costs of holding certain assets and liabilities in foreign currencies; and
- other companies in our industry may calculate Adjusted Net Income differently than we do, limiting its usefulness as a comparative measure.

Because of these limitations, Adjusted Net Income should not be considered as a measure of profitability of our business. We compensate for these limitations by relying primarily on our U.S. GAAP results and using Adjusted Net Income only as a supplement.

Factors Affecting Our Results of Operations

Net Sales. We derive substantially all of our sales (net of sales returns and allowances) from our standard products business. We outsource manufacturing of OLED products to external 12-inch foundries. Our product inventory is primarily located in Korea and is available for drop shipment globally. Outside of Korea, we maintain limited product inventory, and our sales representatives generally relay orders to our factories in Korea for fulfillment. We have strategically located our sales offices near concentrations of major customers. Our sales offices are located in Korea, Japan and Greater China. Our network of authorized agents and distributors is in the United States, Europe and the Asia Pacific region.

We recognize revenue when a customer obtains control of the product, which is generally upon product shipment, delivery at the customer's location or upon customer acceptance, depending on the terms of the arrangement. For the nine months ended September 30, 2021 and 2020, we sold products to 175 and 170 customers, respectively, and our net sales to our ten largest customers represented 81% and 88% of our net sales—standard products business, respectively.

We will provide the Transitional Fab 3 Foundry Services up to September 1, 2023 at an agreed upon cost plus a mark-up. For the periods prior to the closing of the sale of the Foundry Services Group business and Fab 4 as of September 1, 2020 (which are accounted for as discontinued operations beginning in the first quarter of 2020), revenue derived from the Transitional Fab 3 Foundry Services is recorded at cost in both our continuing and discontinued operations.

Gross Profit. Our overall gross profit generally fluctuates as a result of changes in overall sales volumes and in the average selling prices of our products and services. Other factors that influence our gross profit include changes in product mix, the introduction of new products and services and subsequent generations of existing products and services, shifts in the utilization of our manufacturing facility and the yields achieved by our manufacturing operations, changes in material, labor and other manufacturing costs including outsourced manufacturing expenses, and variation in depreciation expense.

Average Selling Prices. Average selling prices for our products tend to be highest at the time of introduction of new products which utilize the latest technology and tend to decrease over time as such products mature in the market and are replaced by next generation products. We strive to offset the impact of declining selling prices for existing products through our product development activities and by introducing new products that command selling prices above the average selling price of our existing products. In addition, we seek to manage our inventories and manufacturing capacity so as to preclude losses from product and productive capacity obsolescence.

Material Costs. Our material costs consist of costs of raw materials, such as silicon wafers, chemicals, gases and tape and packaging supplies. We use processes that require specialized raw materials, such as silicon wafers, that are generally available from a limited number of suppliers. If demand increases or supplies decrease, the costs of our raw materials could increase significantly.

Labor Costs. A significant portion of our employees are located in Korea. Under Korean labor laws, most employees and certain executive officers with one or more years of service are entitled to severance benefits upon the termination of their employment based on their length of service and rate of pay. As of September 30, 2021, approximately 98% of our employees were eligible for severance benefits.

Depreciation Expense. We periodically evaluate the carrying values of long-lived assets, including property, plant and equipment and intangible assets, as well as the related depreciation periods. We depreciated our property, plant and equipment using the straight-line method over the estimated useful lives of our assets. Depreciation rates vary from 30-40 years on buildings to 5 to 12 years for certain equipment and assets. Our evaluation of carrying values is based on various analyses including cash flow and profitability projections. If our projections indicate that future undiscounted cash flows are not sufficient to recover the carrying values of the related long-lived assets, the carrying value of the assets is impaired and will be reduced, with the reduction charged to expense so that the carrying value is equal to fair value.

Selling Expenses. We sell our products worldwide through a direct sales force as well as a network of sales agents and representatives to OEMs, including major branded customers and contract manufacturers, and indirectly through distributors. Selling expenses consist primarily of the personnel costs for the members of our direct sales force, a network of sales representatives and other costs of distribution. Personnel costs include base salary, benefits and incentive compensation.

General and Administrative Expenses. General and administrative expenses consist of the costs of various corporate operations, including finance, legal, human resources and other administrative functions. These expenses primarily consist of payroll-related expenses, consulting and other professional fees and office facility-related expenses.

Research and Development. The rapid technological change and product obsolescence that characterize our industry require us to make continuous investments in research and development. Product development time frames vary but, in general, we incur research and development costs one to two years before generating sales from the associated new products. These expenses include personnel costs for members of our engineering workforce, cost of photomasks, silicon wafers and other non-recurring engineering charges related to product design. Additionally, we develop base line process technology through experimentation and through the design and use of characterization wafers that help achieve commercially feasible yields for new products. The majority of research and development expenses of our display business are material and design-related costs for OLED display driver IC product development involving 28-nanometer or finer processes. The majority of research and development expenses of our power business are certain equipment, material and design-related costs for power discrete products and material and design-related costs for power IC products. Power IC uses standard BCD process technologies which can be sourced from multiple foundries, including Fab 4.

Interest Expense. Our interest expense was incurred primarily under our 6.625% Senior Notes due July 15, 2021 (the “2021 Notes”) and the Exchangeable Notes. We redeemed all outstanding 2021 Notes on October 2, 2020. Our Exchangeable Notes were exchanged for common stock prior to their maturity date of March 1, 2021. From and after October 2, 2020 and March 1, 2021, we have not incurred interest expense associated with the 2021 Notes and Exchangeable Notes, respectively.

Impact of Foreign Currency Exchange Rates on Reported Results of Operations. Historically, a portion of our revenues and greater than the majority of our operating expenses and costs of sales have been denominated in non-U.S. currencies, principally the Korean won, and we expect that this will remain true in the future. Because we report our results of operations in U.S. dollars converted from our non-U.S. revenues and expenses based on monthly average exchange rates, changes in the exchange rate between the Korean won and the U.S. dollar could materially impact our reported results of operations and distort period to period comparisons. In particular, because of the difference in the amount of our consolidated revenues and expenses that are in U.S. dollars relative to Korean won, depreciation in the U.S. dollar relative to the Korean won could result in a material increase in reported costs relative to revenues, and therefore could cause our profit margins and operating income to appear to decline materially, particularly relative to prior periods. The converse is true if the U.S. dollar were to appreciate relative to the Korean won. Moreover, our foreign currency gain or loss would be affected by changes in the exchange rate between the Korean won and the U.S. dollar as a substantial portion of non-cash translation gain or loss is associated with the intercompany long-term loans to our Korean subsidiary, which is denominated in U.S. dollars. As of September 30, 2021, the outstanding intercompany loan balance including accrued interest between our Korean subsidiary and our Dutch subsidiary was \$393.2 million. As a result of such foreign currency fluctuations, it could be more difficult to detect underlying trends in our business and results of operations. In addition, to the extent that fluctuations in currency exchange rates cause our results of operations to differ from our expectations or the expectations of our investors, the trading price of our stock could be adversely affected.

From time to time, we may engage in exchange rate hedging activities in an effort to mitigate the impact of exchange rate fluctuations. Our Korean subsidiary enters into foreign currency zero cost collar contracts in order to mitigate a portion of the impact of U.S. dollar-Korean won exchange rate fluctuations on our operating results. Obligations under these foreign currency zero cost collar contracts must be cash collateralized if our exposure exceeds certain specified thresholds. These zero cost collar contracts may be terminated by a counterparty in a number of circumstances, including if our credit rating falls below B-/B3 or if our total cash and cash equivalents is less than \$30.0 million at the end of a fiscal quarter unless a waiver is obtained from the counterparty. We cannot assure that any hedging technique we implement will be effective. If our hedging activities are not effective, changes in currency exchange rates may have a more significant impact on our results of operations.

Foreign Currency Gain or Loss. Foreign currency translation gains or losses on transactions by us or our subsidiaries in a currency other than our or our subsidiaries’ functional currency are included in foreign currency gain (loss), net in our statements of operations. A substantial portion of this net foreign currency gain or loss relates to non-cash translation gain or loss related to the principal balance of intercompany balances at our Korean subsidiary that are denominated in U.S. dollars. This gain or loss results from fluctuations in the exchange rate between the Korean won and U.S. dollar.

Income Taxes. We record our income taxes in each of the tax jurisdictions in which we operate. This process involves using an asset and liability approach whereby deferred tax assets and liabilities are recorded for differences in the financial reporting bases and tax basis of our assets and liabilities. We exercise significant management judgment in determining our provision for income taxes, deferred tax assets and liabilities. We assess whether it is more likely than not that the deferred tax assets existing at the period-end will be realized in future periods. In such assessment, we consider all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent results of operations. In the event we were to determine that we would be able to realize the deferred income tax assets in the future in excess of their net recorded amount, we would adjust the valuation allowance, which would reduce the provision for income taxes.

We are subject to income- or non-income-based tax examinations by tax authorities of the U.S., Korea and multiple other foreign jurisdictions for all open tax years. Significant estimates and judgments are required in determining our worldwide provision for income- or non-income based taxes. Some of these estimates are based on interpretations of existing tax laws or regulations. The ultimate amount of tax liability may be uncertain as a result.

Discontinued Operations. On March 30, 2020, we entered into the Business Transfer Agreement for the sale of our Foundry Services Group business and Fab 4 to the Buyer. As a result, the results of the Foundry Services Group business were classified as discontinued operations in our consolidated statements of operations and excluded from both continuing operations and segment results for all periods presented. On September 1, 2020, we completed the sale for a purchase price of approximately \$350.6 million in cash.

Capital Expenditures. We primarily invest in manufacturing equipment, software design tools and other tangible assets mainly for fabrication facility maintenance, capacity expansion and technology improvement. Capacity expansions and technology improvements typically occur in anticipation of increases in demand. We typically pay for capital expenditures in partial installments with portions due on order, delivery and final acceptance. Our capital expenditures mainly include our payments for the purchase of property, plant and equipment.

Inventories. We monitor our inventory levels in light of product development changes and market expectations. We may be required to take additional charges for quantities in excess of demand, cost in excess of market value and product age. Our analysis may take into consideration historical usage, expected demand, anticipated sales price, new product development schedules, the effect new products might have on the sales of existing products, product age, customer design activity, customer concentration and other factors. These forecasts require us to estimate our ability to predict demand for current and future products and compare those estimates with our current inventory levels and inventory purchase commitments. Our forecasts for our inventory may differ from actual inventory use.

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Results of Operations – Comparison of Three Months Ended September 30, 2021 and 2020

The following table sets forth consolidated results of operations for the three months ended September 30, 2021 and 2020:

	Three Months Ended September 30, 2021		Three Months Ended September 30, 2020		Change Amount
	Amount	% of Total revenues	Amount	% of Total revenues	
(Dollars in millions)					
Revenues					
Net sales – standard products business	\$ 117.4	92.5%	\$ 116.3	93.1%	\$ 1.2
Net sales – transitional Fab 3 foundry services	9.6	7.5	8.6	6.9	1.0
Total revenues	127.0	100.0	124.8	100.0	2.2
Cost of sales					
Cost of sales – standard products business	71.6	56.4	87.5	70.1	(15.9)
Cost of sales – transitional Fab 3 foundry services	8.8	6.9	8.7	7.0	0.0
Total cost of sales	80.4	63.3	96.2	77.1	(15.8)
Gross profit	46.6	36.7	28.6	22.9	18.0
Selling, general and administrative expenses	12.6	9.9	12.9	10.3	(0.3)
Research and development expenses	12.3	9.7	12.5	10.0	(0.2)
Other charges	1.8	1.4	—	—	1.8
Operating income	20.0	15.7	3.2	2.6	16.8
Interest expense	(0.1)	(0.1)	(5.5)	(4.4)	5.4
Foreign currency gain (loss), net	(7.6)	(6.0)	8.9	7.1	(16.4)
Others, net	1.6	1.3	0.7	0.6	0.9
	(6.1)	(4.8)	4.1	3.3	(10.2)
Income from continuing operations before income tax expense	13.9	11.0	7.3	5.9	6.6
Income tax expense (benefit)	3.1	2.5	(1.1)	(0.9)	4.3
Income from continuing operations	10.8	8.5	8.5	6.8	2.3
Income from discontinued operations, net of tax	—	—	264.5	211.9	(264.5)
Net income	<u>\$ 10.8</u>	8.5	<u>\$273.0</u>	218.7	<u>\$(262.2)</u>

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The following sets forth information relating to our continuing operations:

	Three Months Ended September 30, 2021		Three Months Ended September 30, 2020		Change Amount
	Amount	% of Total revenues	Amount	% of Total revenues	
(Dollars in millions)					
Revenues					
Net sales – standard products business					
Display Solutions	\$ 58.5	46.1%	\$ 69.6	55.7%	\$ (11.1)
Power Solutions	58.9	46.4	46.7	37.4	12.2
Total standard products business	117.4	92.5	116.3	93.1	1.2
Net sales – transitional Fab 3 foundry services	9.6	7.5	8.6	6.9	1.0
Total revenues	<u>\$127.0</u>	<u>100.0%</u>	<u>\$124.8</u>	<u>100.0%</u>	<u>\$ 2.2</u>

	Three Months Ended September 30, 2021		Three Months Ended September 30, 2020		Change Amount
	Amount	% of Net sales	Amount	% of Net sales	
(Dollars in millions)					
Gross Profit					
Gross profit – standard products business	\$ 45.8	39.0%	\$ 28.8	24.7%	\$ 17.0
Gross profit – transitional Fab 3 foundry services	0.8	8.5	(0.2)	(2.1)	1.0
Total gross profit	<u>\$ 46.6</u>	<u>36.7%</u>	<u>\$ 28.6</u>	<u>22.9%</u>	<u>\$ 18.0</u>

Revenues

Total revenues were \$127.0 million for the three months ended September 30, 2021, a \$2.2 million, or 1.8%, increase compared to \$124.8 million for the three months ended September 30, 2020.

The standard products business. Net sales from our standard products business were \$117.4 million for the three months ended September 30, 2021, a \$1.2 million, or 1.0%, increase compared to \$116.3 million for the three months ended September 30, 2020. This increase was primarily attributable to a higher demand for power products such as MOSFETs, including high-end MOSFETs, primarily for TVs and e-bikes, whereas the revenue for power products in 2020 was impacted by COVID-19-related supply chain issues and market softness in China. This increase was offset in part by a decrease in revenue from our mobile OLED display driver ICs stemming from a continuing global shortage in manufacturing capacity, as we outsource manufacturing of these products to external 12-inch foundries.

The transitional Fab 3 foundry services. Net sales from the transitional Fab 3 foundry services were \$9.6 million and \$8.6 million for the three months ended September 30, 2021 and 2020, respectively.

Gross Profit

Total gross profit was \$46.6 million for the three months ended September 30, 2021 compared to \$28.6 million for the three months ended September 30, 2020, an \$18.0 million, or 63.0%, increase. Gross profit as a percentage of net sales for the three months ended September 30, 2021 increased to 36.7% compared to 22.9% for the three months ended September 30, 2020.

The standard products business. Gross profit from our standard products business was \$45.8 million for the three months ended September 30, 2021, which represented a \$17.0 million, or 59.1%, increase from gross profit of \$28.8 million for the three months ended September 30, 2020. Gross profit as a percentage of net sales for the three months ended September 30, 2021 increased to 39.0% compared to 24.7% for the three months ended September 30, 2020. The increase in both gross profit and gross profit margin was primarily attributable to an improved product mix, an increase in average selling price and a higher utilization rate of our internal fabrication facility in Gumi, whereas unexpected excess and obsolete inventory charge of \$2.3 million in relation to the U.S. Government's export restrictions on Huawei, which is a downstream customer of some of our direct customers, negatively affected both gross profit and gross profit as a percentage of net sales in the third quarter of 2020. This excess and obsolete inventory charge was reversed by \$1.1 million during the three months ended September 30, 2021 as a portion of such reserved inventory was subsequently sold to certain other customers, which also positively affected both gross profit and gross profit as a percentage of net sales for the three months ended September 30, 2021.

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Net Sales – Standard Products Business by Geographic Region

We report net sales – standard products business by geographic region based on the location to which the products are billed. The following table sets forth our net sales—standard products business by geographic region and the percentage of total net sales—standard products business represented by each geographic region for the three months ended September 30, 2021 and 2020:

	Three Months Ended September 30, 2021		Three Months Ended September 30, 2020		Change Amount
	Amount	% of Net sales – standard products business	Amount	% of Net sales – standard products business	
	(Dollars in millions)				
Korea	\$ 29.7	25.3%	\$ 28.4	24.4%	\$ 1.3
Asia Pacific (other than Korea)	84.2	71.7	84.2	72.4	0.0
United States	1.8	1.5	1.8	1.5	(0.0)
Europe	1.4	1.2	1.5	1.2	(0.1)
Others	0.4	0.3	0.5	0.4	(0.1)
	<u>\$ 117.4</u>	<u>100.0%</u>	<u>\$ 116.3</u>	<u>100.0%</u>	<u>\$ 1.2</u>

Net sales – standard products business in Korea for the three months ended September 30, 2021 increased from \$28.4 million to \$29.7 million compared to the three months ended September 30, 2020, or by \$1.3 million, or 4.6%, primarily due to a higher demand for power products such as MOSFETs, including high-end MOSFETs, primarily for TV and smartphone applications. This increase was offset in part by a decrease in revenue related to our mobile OLED display driver ICs stemming from a continuing global shortage in manufacturing capacity, as we outsource manufacturing of these products to external 12-inch foundries.

Net sales – standard products business in Asia Pacific (other than Korea) for the three months ended September 30, 2021 was \$84.2 million, which remained flat, compared to \$84.2 million in the three months ended September 30, 2020. The increase in revenue was primarily attributable to a higher demand for power products such as MOSFETs, including high-end MOSFETs, primarily for TVs and e-bikes, and a higher demand for auto-LCD DDIC business, which was entirely offset by a decrease in revenue from our mobile OLED display driver ICs stemming from a continuing global shortage in manufacturing capacity, as we outsource manufacturing of these products to external 12-inch foundries.

Operating Expenses

Selling, General and Administrative Expenses. Selling, general and administrative expenses were \$12.6 million, or 9.9% of total revenues, for the three months ended September 30, 2021, compared to \$12.9 million, or 10.3% of total revenues, for the three months ended September 30, 2020. The decrease of \$0.3 million, or 2.6%, was primarily attributable to a decrease in professional fees mainly comprised of legal and consulting fees.

Research and Development Expenses. Research and development expenses were \$12.3 million, or 9.7% of total revenues, for the three months ended September 30, 2021, which remained almost flat, compared to \$12.5 million, or 10.0% of total revenues, for the three months ended September 30, 2020.

Other Charges. Other charges were \$1.8 million for the three months ended September 30, 2021, which consisted of non-recurring professional service fees and expenses incurred in connection with the Merger and regulatory requests.

Operating Income

As a result of the foregoing, operating income was \$20.0 million for the three months ended September 30, 2021 compared to operating income of \$3.2 million the three months ended September 30, 2020. As discussed above, the increase in operating income of \$16.8 million resulted primarily from an \$18.0 million increase in gross profit, a \$0.3 million decrease in selling, general and administrative expenses, and a \$0.2 million increase in research and development expenses. This increase was offset in part by a \$1.8 million increase in other charges.

Other Income (Expense)

Interest Expense. Interest expense was \$0.1 million and \$5.5 million for the three months ended September 30, 2021 and September 30, 2020, respectively. Interest expense was incurred primarily under our 2021 Notes and Exchangeable Notes. We redeemed all outstanding 2021 Notes on October 2, 2020. Our Exchangeable Notes were exchanged for common stock prior to their maturity date of March 1, 2021. From and after October 2, 2020 and March 1, 2021, we have not incurred interest expense associated with the 2021 Notes and Exchangeable Notes, respectively.

Foreign Currency Loss (Gain), Net. Net foreign currency loss for the three months ended September 30, 2021 was \$7.6 million compared to net foreign currency gain of \$8.9 million for the three months ended September 30, 2020. The net foreign currency loss for the three months ended September 30, 2021 was due to the depreciation in value of the Korean won relative to the U.S. dollar during the period. The net foreign currency gain for the three months ended September 30, 2020 was due to the appreciation in value of the Korean won relative to the U.S. dollar during the period.

A substantial portion of our net foreign currency gain or loss is non-cash translation gain or loss associated with intercompany long-term loans to our Korean subsidiary, which are denominated in U.S. dollars, and are affected by changes in the exchange rate between the Korean won and the U.S. dollar. As of September 30, 2021 and September 30, 2020, the outstanding intercompany loan balances, including accrued interest between our Korean subsidiary and our Dutch subsidiary, were \$393 million and \$446 million, respectively. Foreign currency translation gain or loss from intercompany balances were included in determining our consolidated net income since the intercompany balances were not considered long-term investments in nature because management intended to settle these intercompany balances at their respective maturity dates.

Others, Net. Others were comprised of interest income, rental income, and gains and losses from valuation of derivatives which were designated as hedging instruments. Others, net for the three months ended September 30, 2021 and September 30, 2020 was \$1.6 million and \$0.7 million, respectively. During the three months ended September 30, 2021, others, net included a \$0.7 million legal settlement gain related to certain expenses incurred in prior periods in connection with our legacy Fab 4 (which was sold during the year ended December 31, 2020) and awarded in the current quarter.

Income Tax Expense (Benefit)

Income tax expense was \$3.1 million for the three months ended September 30, 2021, which was primarily attributable to interest on intercompany loan balances and the estimated taxable income for the respective period in our Korean subsidiary, combined with its ability to utilize net operating loss carryforwards up to 60%. Income tax benefit was \$1.1 million for the three months ended September 30, 2020, which was primarily attributable to the foreign translation loss realized by our Korean subsidiary upon the repayment of a part of its intercompany loans by the Dutch subsidiary to fund the redemption of the 2021 Notes.

Income from Continuing Operations

As a result of the foregoing, income from continuing operations increased by \$2.3 million for the three months ended September 30, 2021 compared to the three months ended September 30, 2020. As discussed above, the increase in income from continuing operations primarily resulted from a \$16.8 million increase in operating income and a \$5.4 million decrease in interest expense, which were offset in part by a \$16.4 million increase in net foreign currency loss and a \$4.3 million increase in income tax expense.

Income from Discontinued Operations, Net of Tax

On March 30, 2020, we entered into the Business Transfer Agreement for the sale of our Foundry Services Group business and Fab 4. As a result, the results of the Foundry Services Group business were classified as discontinued operations in our consolidated statements of operations and excluded from our continuing operations for all periods presented. Income from discontinued operations, net of tax was \$264.5 million for the three months ended September 30, 2020. On September 1, 2020, we completed the sale of our Foundry Services Group business and Fab 4 for a purchase price equal to approximately \$350.6 million in cash. We have not incurred a gain or loss from discontinued operations in 2021 as the sale of the Foundry Service Group business and Fab 4 was completed in 2020.

Net Income

As a result of the foregoing, a net income of \$10.8 million was recorded for the three months ended September 30, 2021 compared to a net income of \$273.0 million for the three months ended September 30, 2020. As discussed above, the decrease in net income of \$262.2 million primarily resulted from a \$264.5 million decrease in income from discontinued operations, net of tax, which was offset by a \$2.3 million increase in income from continuing operations.

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Results of Operations – Comparison of Nine Months Ended September 30, 2021 and 2020

The following table sets forth consolidated results of operations for the nine months ended September 30, 2021 and 2020:

	Nine Months Ended September 30, 2021		Nine Months Ended September 30, 2020		Change Amount
	Amount	% of Total revenues	Amount	% of Total revenues	
(Dollars in millions)					
Revenues					
Net sales – standard products business	\$333.6	91.7%	\$336.0	92.3%	\$ (2.4)
Net sales – transitional Fab 3 foundry services	30.3	8.3	28.2	7.7	2.1
Total revenues	363.9	100.0	364.1	100.0	(0.2)
Cost of sales					
Cost of sales – standard products business	221.3	60.8	245.9	67.5	(24.6)
Cost of sales – transitional Fab 3 foundry services	27.7	7.6	28.3	7.8	(0.7)
Total cost of sales	249.0	68.4	274.3	75.3	(25.3)
Gross profit	114.9	31.6	89.9	24.7	25.1
Selling, general and administrative expenses	39.2	10.8	37.4	10.3	1.8
Research and development expenses	39.0	10.7	34.1	9.4	4.9
Other charges	17.2	4.7	0.6	0.2	16.6
Operating income	19.5	5.4	17.8	4.9	1.7
Interest expense	(1.2)	(0.3)	(16.5)	(4.5)	15.3
Foreign currency loss, net	(12.0)	(3.3)	(13.6)	(3.7)	1.6
Others, net	2.8	0.8	2.3	0.6	0.5
	(10.4)	(2.9)	(27.8)	(7.6)	17.4
Income (loss) from continuing operations before income tax expense	9.1	2.5	(10.0)	(2.7)	19.1
Income tax expense	6.0	1.7	0.8	0.2	5.2
Income (loss) from continuing operations	3.1	0.9	(10.8)	(3.0)	13.9
Income from discontinued operations, net of tax	—	—	289.2	79.4	(289.2)
Net income	\$ 3.1	0.9	\$278.4	76.5	\$(275.3)

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The following sets forth information relating to our continuing operations:

	Nine Months Ended September 30, 2021		Nine Months Ended September 30, 2020		Change Amount
	Amount	% of Total revenues	Amount	% of Total revenues	
(Dollars in millions)					
Revenues					
Net sales – standard products business					
Display Solutions	\$ 164.0	45.1%	\$ 216.4	59.4%	\$ (52.3)
Power Solutions	169.6	46.6	119.6	32.8	50.0
Total standard products business	333.6	91.7	336.0	92.3	(2.4)
Net sales – transitional Fab 3 foundry services	30.3	8.3	28.2	7.7	2.1
Total revenues	<u>\$ 363.9</u>	<u>100.0%</u>	<u>\$ 364.1</u>	<u>100.0%</u>	<u>\$ (0.2)</u>

	Nine Months Ended September 30, 2021		Nine Months Ended September 30, 2020		Change Amount
	Amount	% of Net sales	Amount	% of Net sales	
(Dollars in millions)					
Gross Profit					
Gross profit – standard products business	\$ 112.3	33.7%	\$ 90.0	26.8%	\$ 22.3
Gross profit – transitional Fab 3 foundry services	2.6	8.7	(0.2)	(0.6)	2.8
Total gross profit	<u>\$ 114.9</u>	<u>31.6%</u>	<u>\$ 89.9</u>	<u>24.7%</u>	<u>\$ 25.1</u>

Revenues

Total revenues were \$363.9 million for the nine months ended September 30, 2021, a \$0.2 million, or 0.1%, decrease compared to \$364.1 million for the nine months ended September 30, 2020.

The standard products business. Net sales from our standard products business were \$333.6 million for the nine months ended September 30, 2021, a \$2.4 million, or 0.7%, decrease compared to \$336.0 million for the nine months ended September 30, 2020. This decrease was primarily attributable to a decrease in revenue from our mobile OLED display driver ICs stemming from a continuing global shortage in manufacturing capacity, as we outsource manufacturing of these products to external 12-inch foundries, and a strategic reduction of our lower margin non-auto LCD business. This decrease was offset in part by a higher demand for power products such as MOSFETs, including high-end MOSFETs, primarily for TVs and e-bikes, whereas the revenue for power products in 2020 was impacted by COVID-19-related supply chain issues and market softness in China.

The transitional Fab 3 foundry services. Net sales from the transitional Fab 3 foundry services were \$30.3 million and \$28.2 million for the nine months ended September 30, 2021 and 2020, respectively.

Gross Profit

Total gross profit was \$114.9 million for the nine months ended September 30, 2021 compared to \$89.9 million for the nine months ended September 30, 2020, a \$25.1 million, or 27.9%, increase. Gross profit as a percentage of net sales for the nine months ended September 30, 2021 increased to 31.6% compared to 24.7% for the nine months ended September 30, 2020. The increase in gross profit and gross profit as a percentage of net sales was primarily due to our standard products business as further described below.

The standard products business. Gross profit from our standard products business was \$112.3 million for the nine months ended September 30, 2021, which represented a \$22.3 million, or 24.7%, increase from gross profit of \$90.0 million for the nine months ended September 30, 2020. Gross profit as a percentage of net sales for the nine months ended September 30, 2021 increased to 33.7% compared to 26.8% for the nine months ended September 30, 2020. The increase in both gross profit and gross profit margin was primarily attributable to an improved product mix, an increase in average selling price and a higher utilization rate of our internal fabrication facility in Gumi, whereas unexpected excess and obsolete inventory charge of \$2.3 million in relation to the U.S. Government's export restrictions on Huawei, which is a downstream customer of some of our direct customers, negatively affected both gross profit and gross profit as a percentage of net sales in the third quarter of 2020. This excess and obsolete inventory charge was reversed by \$1.1 million in the third quarter of 2021 as a portion of such reserved inventory was subsequently sold to certain other customers, which also positively affected both gross profit and gross profit as a percentage of net sales for the nine months ended September 30, 2021.

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Net Sales – Standard Products Business by Geographic Region

We report net sales – standard products business by geographic region based on the location to which the products are billed. The following table sets forth our net sales—standard products business by geographic region and the percentage of total net sales—standard products business represented by each geographic region for the nine months ended September 30, 2021 and 2020:

	<u>Nine Months Ended September 30, 2021</u>		<u>Nine Months Ended September 30, 2020</u>		<u>Change Amount</u>
	<u>Amount</u>	<u>% of Net sales – standard products business</u>	<u>Amount</u>	<u>% of Net sales – standard products business</u>	
	(Dollars in millions)				
Korea	\$ 87.0	26.1%	\$ 81.1	24.2%	\$ 5.8
Asia Pacific (other than Korea)	237.3	71.1	245.9	73.2	(8.6)
United States	4.4	1.3	4.0	1.2	0.4
Europe	3.8	1.2	3.3	1.0	0.6
Others	1.1	0.3	1.6	0.5	(0.6)
	<u>\$333.6</u>	<u>100.0%</u>	<u>\$336.0</u>	<u>100.0%</u>	<u>\$ (2.4)</u>

Net sales – standard products business in Korea for the nine months ended September 30, 2021 increased from \$81.1 million to \$87.0 million compared to the nine months ended September 30, 2020, or by \$5.8 million, or 7.2%, primarily due to a higher demand for power products such as MOSFETs, including high-end MOSFETs, primarily for TV and smartphone applications. This increase was offset in part by a decrease in revenue related to our mobile OLED display driver ICs stemming from a continuing global shortage in manufacturing capacity, as we outsource manufacturing of these products to external 12-inch foundries, and a strategic reduction of our lower margin non-auto LCD business.

Net sales – standard products business in Asia Pacific (other than Korea) for the nine months ended September 30, 2021 decreased to \$237.3 million from \$245.9 million in the nine months ended September 30, 2020, or by \$8.6 million, or 3.5%, primarily due to a decrease in revenue from our mobile OLED display driver ICs stemming from a continuing global shortage in manufacturing capacity, as we outsource manufacturing of these products to external 12-inch foundries, which was offset in part by a higher demand for power products such as MOSFETs, including high-end MOSFETs, primarily for TVs and e-bikes.

Operating Expenses

Selling, General and Administrative Expenses. Selling, general and administrative expenses were \$39.2 million, or 10.8% of total revenues, for the nine months ended September 30, 2021, compared to \$37.4 million, or 10.3% of total revenues, for the nine months ended September 30, 2020. The increase of \$1.8 million, or 4.8%, was primarily attributable to certain non-income-based tax assessments of \$0.6 million as a result of a regular tax examination completed for our primary operating entity in Korea for multiple tax years, and the grant timing of equity-based compensation. This increase was offset in part by a decrease in professional fees mainly comprised of legal and consulting fees.

Research and Development Expenses. Research and development expenses were \$39.0 million, or 10.7% of total revenues, for the nine months ended September 30, 2021, compared to \$34.1 million, or 9.4% of total revenues, for the nine months ended September 30, 2020. The increase of \$4.9 million, or 14.4%, was primarily attributable to an increase in outside service fees and variable overhead expenses, and an increase in material costs for new product development.

Other Charges. Other charges were \$17.2 million for the nine months ended September 30, 2021, which were consisted of non-recurring professional service fees and expenses incurred in connection with the Merger and regulatory requests. Other charges were \$0.6 million for the nine months ended September 30, 2020, which pertained to non-recurring professional service fees and expenses incurred in connection with certain treasury and finance initiatives.

Operating Income

As a result of the foregoing, operating income was \$19.5 million for the nine months ended September 30, 2021 compared to operating income of \$17.8 million the nine months ended September 30, 2020. As discussed above, the increase in operating income of \$1.7 million resulted primarily from a \$25.1 million increase in gross profit, which was offset in part by a \$16.6 million increase in other charges, a \$4.9 million increase in research and development expenses, and a \$1.8 million increase in selling, general and administrative expenses.

Other Income (Expense)

Interest Expense. Interest expenses was \$1.2 million and \$16.5 million for the nine months ended September 30, 2021 and September 30, 2020, respectively. Interest expenses was incurred primarily under our 2021 Notes and Exchangeable Notes. We redeemed all outstanding 2021 Notes on October 2, 2020. Our Exchangeable Notes were exchanged for common stock prior to their maturity date of March 1, 2021. From and after October 2, 2020 and March 1, 2021, we have not incurred interest expense associated with the 2021 Notes and Exchangeable Notes, respectively.

Foreign Currency Loss, Net. Net foreign currency loss for the nine months ended September 30, 2021 was \$12.0 million compared to net foreign currency loss of \$13.6 million for the nine months ended September 30, 2020. The net foreign currency loss for the nine months ended September 30, 2021 and September 30, 2020 was due to the depreciation in value of the Korean won relative to the U.S. dollar during the period.

A substantial portion of our net foreign currency gain or loss is non-cash translation gain or loss associated with intercompany long-term loans to our Korean subsidiary, which are denominated in U.S. dollars, and are affected by changes in the exchange rate between the Korean won and the U.S. dollar. As of September 30, 2021 and September 30, 2020, the outstanding intercompany loan balances, including accrued interest between our Korean subsidiary and our Dutch subsidiary, were \$393 million and \$446 million, respectively. Foreign currency translation gain or loss from intercompany balances were included in determining our consolidated net income since the intercompany balances were not considered long-term investments in nature because management intended to settle these intercompany balances at their respective maturity dates.

Others, Net. Others were comprised of interest income, rental income, and gains and losses from valuation of derivatives which were designated as hedging instruments. Others, net for the nine months ended September 30, 2021 and September 30, 2020 was \$2.8 million and \$2.3 million, respectively. In the third quarter of 2021, others, net included a \$0.7 million legal settlement gain related to certain expenses incurred in prior periods in connection with our legacy Fab 4 (which was sold during the year ended December 31, 2020) and awarded in the current quarter.

Income Tax Expense

Income tax expense was \$6.0 million for the nine months ended September 30, 2021, which was primarily attributable to interest on intercompany loan balances and the estimated taxable income for the respective period in our Korean subsidiary, combined with its ability to utilize net operating loss carryforwards up to 60%. Income tax expense was \$0.8 million for the nine months ended September 30, 2020, which was primarily attributable to interest on intercompany loan balances, which was offset in part by the income tax benefit due mainly to the foreign translation loss realized by our Korean subsidiary upon the repayment of a part of its intercompany loans by the Dutch subsidiary to fund the redemption of the 2021 Notes.

Income (Loss) from Continuing Operations

Income from continuing operations for the nine months ended September 30, 2021 was \$3.1 million compared to loss from continuing operations of \$10.8 million for the nine months ended September 30, 2020. The \$14.0 million improvement in results from continuing operations was primarily attributable to a \$15.3 million decrease in interest expense, a \$1.7 million increase in operating income and a \$1.6 million improvement in net foreign currency loss, which were offset in part by a \$5.2 million increase in income tax expense.

Income from Discontinued Operations, Net of Tax

On March 30, 2020, we entered into the Business Transfer Agreement for the sale of our Foundry Services Group business and Fab 4. As a result, the results of the Foundry Services Group business were classified as discontinued operations in our consolidated statements of operations and excluded from our continuing operations for all periods presented. Income from discontinued operations, net of tax was \$289.2 million for the nine months ended September 30, 2020. On September 1, 2020, we completed the sale of our Foundry Services Group business and Fab 4 for a purchase price equal to approximately \$350.6 million in cash. We have not incurred a gain or loss from discontinued operations in 2021 as the sale of the Foundry Service Group business and Fab 4 was completed in 2020.

Net Income

As a result of the foregoing, a net income of \$3.1 million was recorded for the nine months ended September 30, 2021 compared to a net income of \$278.4 million for the nine months ended September 30, 2020. As discussed above, the decrease in net income of \$275.2 million primarily resulted from a \$289.2 million decrease in income from discontinued operations, net of tax, which was offset by a \$14.0 million improvement in loss from continuing operations.

Liquidity and Capital Resources

Our principal capital requirements are to fund sales and marketing, invest in research and development and capital equipment and to fund working capital needs. We calculate working capital as current assets less current liabilities.

Our principal sources of liquidity are our cash, cash equivalents, cash flows from operations and financing activities. Our ability to manage cash and cash equivalents may be limited, as our primary cash flows are dictated from time to time by the terms of our sales and supply agreements, contractual obligations, debt instruments and legal and regulatory requirements. From time to time, we may sell accounts receivable to third parties under factoring agreements or engage in accounts receivable discounting to facilitate the collection of cash. In addition, from time to time, we may make payments to our vendors on extended terms with their consent. As of September 30, 2021, we do not have any accounts payable on extended terms or payment deferment with our vendors.

On September 1, 2020, we completed the sale of our Foundry Services Group business and Fab 4 to Key Foundry Co., Ltd. in exchange for a purchase price equal to approximately \$350.6 million in cash. The purchase price was paid in a combination of U.S. Dollars in the amount of \$46.5 million and Korean Won in the amount of approximately KRW 360.6 billion.

On October 2, 2020, we redeemed of all of our outstanding 2021 Notes. We paid approximately \$227.4 million to fully redeem all of the outstanding \$224.25 million aggregate principal amount of the 2021 Notes at a redemption price equal to the sum of 100% of the principal amount plus accrued and unpaid interest thereon.

On January 17, 2017, we issued an aggregate of \$86.3 million in principal amount of our Exchangeable Notes. Prior to the March 1, 2021 maturity of our Exchangeable Notes, holders elected to exchange for an aggregate of 10,144,131 shares of our common stock in satisfaction in full of the remaining outstanding obligations under the Exchangeable Notes.

We currently believe that we will have sufficient cash reserves from cash on hand and expected cash from operations to fund our operations as well as capital expenditures for the next 12 months and the foreseeable future.

Working Capital

Our working capital balance as of September 30, 2021 was \$315.1 million compared to \$236.0 million as of December 31, 2020. The \$79.1 million increase was primarily attributable to the exchange of our Exchangeable Notes for common stock prior to their maturity date of March 1, 2021.

Cash Flows

The consolidated statements of cash flows have not been adjusted to separately disclose cash flows related to discontinued operations for the nine months ended September 30, 2020, but the material items in the operating and investing activities of cash flows relating to discontinued operations in the referred period are disclosed in “Item 1. Financial Statements and Supplementary Data – Notes to Consolidated Financial Statements – Note 3 – Discontinued Operations” included elsewhere in this Report.

Cash Flows from Operating Activities

Cash inflow provided by operating activities totaled \$30.0 million for the nine months ended September 30, 2021, compared to \$51.5 million of cash inflow provided by operating activities for the nine months ended September 30, 2020. The net operating cash inflow for the nine months ended September 30, 2021 reflects our net income of \$3.1 million, as adjusted favorably by \$57.7 million, which mainly consisted of depreciation and amortization, provision for severance benefits, stock-based compensation and net foreign currency loss, and net unfavorable impact of \$30.8 million from changes of operating assets and liabilities.

Cash Flows from Investing Activities

Cash outflow used in investing activities totaled \$14.4 million for the nine months ended September 30, 2021, compared to \$334.0 million of cash inflow provided by investing activities for the nine months ended September 30, 2020. The \$348.5 million decrease in cash inflow was primarily attributable to \$350.6 million of proceeds received from the sale of the Foundry Services Group business and Fab 4 in the third quarter of 2020, and a \$2.0 million net increase in guarantee deposits, which were offset in part by a \$3.0 million decrease in purchase of property, plant and equipment and a \$1.1 million net decrease in hedge collateral.

Cash Flows from Financing Activities

Cash inflow provided by financing activities totaled \$1.8 million for the nine months ended September 30, 2021, compared to \$1.1 million of cash inflow provided by financing activities for the nine months ended September 30, 2020. The financing cash inflow for the nine months ended September 30, 2021 was primarily attributable to \$3.9 million of proceeds received from the issuance of common stock in connection with the exercise of stock options, which was offset in part by a payment of \$1.7 million for the repurchase of our common stock to satisfy tax withholding obligations in connection with the vesting of restricted stock units. The financing cash inflow for the nine months ended September 30, 2020 was primarily attributable to \$2.7 million of proceeds received from the issuance of common stock in connection with the exercise of stock options, which was offset in part by a payment of \$1.0 million for the repurchase of our common stock to satisfy tax withholding obligations in connection with the vesting of restricted stock units.

Capital Expenditures

We routinely make capital expenditures for fabrication facility maintenance, enhancement of our existing facilities and reinforcement of our global research and development capability. For the nine months ended September 30, 2021, capital expenditures for property, plant and equipment were \$13.4 million, a \$3.0 million, or 18.3%, decrease from \$16.4 million, including \$5.8 million capital expenditures for discontinued operations, for the nine months ended September 30, 2020. The capital expenditures for the nine months ended September 30, 2021 and 2020 were related to meeting our customer demand and supporting technology and facility improvement at our fabrication facilities.

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Contractual Obligations

The following summarizes our contractual obligations as of September 30, 2021:

	Payments Due by Period						
	Total	Remainder of 2021	2022	2023	2024	2025	Thereafter
Operating leases(1)	\$ 4.0	\$ 0.7	\$ 1.5	\$ 0.8	\$ 0.6	\$ 0.4	\$ —
Finance leases(1)	0.2	0.0	0.1	0.1	—	—	—
Water Treatment Services(1)(2)	25.0	1.0	3.9	3.8	3.7	3.7	8.9
Others(3)	16.5	3.4	7.0	5.9	0.1	0.1	—

- (1) Assumes constant currency exchange rate for Korean won to U.S. dollars of 1,184.9:1, the exchange rate as of September 30, 2021.
(2) Includes future payments for water treatment services for our fabrication facility in Gumi, Korea based on the contractual terms.
(3) Includes license agreements and other contractual obligations.

We lease land, office space and equipment under various operating lease agreements that expire through 2025.

We are a party to an arrangement for the water treatment facility in Gumi, Korea, which includes a 10-year service agreement beginning July 1, 2018.

Beginning in July 2018, we have contributed a certain percentage of severance benefits, accrued for eligible employees for their services beginning January 1, 2018, to certain severance insurance deposit accounts. These accounts consist of time deposits and other guaranteed principal and interest, and are maintained at insurance companies, banks or security companies for the benefit of employees. We deduct the contributions made to these severance insurance deposit accounts from our accrued severance benefits. As of September 30, 2021, our accrued severance benefits, net, totaled \$37.7 million and cumulative contributions to these severance insurance deposit accounts amounted to \$12.7 million.

We follow U.S. GAAP guidance on uncertain tax positions. Our unrecognized tax benefits totaled \$0.4 million as of September 30, 2021. These unrecognized tax benefits have been excluded from the above table because we cannot estimate the period of cash settlement with the respective taxing authorities.

Off-Balance Sheet Arrangements

As of September 30, 2021, we did not have any off-balance sheet arrangements, as defined in Item 303(a)(4)(ii) of Regulation S-K.

Critical Accounting Policies and Estimates

Preparing financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements, the reported amounts of revenues and expenses during the reporting periods and the related disclosures in our consolidated financial statements and accompanying notes.

We believe that our significant accounting policies, which are described further in Note 1 to our consolidated financial statements in our Annual Report on Form 10-K for our fiscal year ended December 31, 2020, or our 2020 Form 10-K, are critical due to the fact that they involve a high degree of judgment and estimates about the effects of matters that are inherently uncertain. We base these estimates and judgments on historical experience, knowledge of current conditions and other assumptions and information that we believe to be reasonable. Estimates and assumptions about future events and their effects cannot be determined with certainty. Accordingly, these estimates may change as new events occur, as more experience is acquired, as additional information is obtained and as the business environment in which we operate changes.

A description of our critical accounting policies that involve significant management judgement appears in our 2020 Form 10-K, under “Management’s Discussion and Analysis of Financial Conditions and Reports of Operations—Critical Accounting Policies and Estimates.” There have been no other material changes to our critical accounting policies and estimates as compared to our critical accounting policies and estimates included in our 2020 Form 10-K.

Recent Accounting Pronouncements

For a full description of new accounting pronouncements and recently adopted accounting pronouncements, please see “Item 1. Interim Consolidated Financial Statements—Notes to Consolidated Financial Statements—Note 1. Business, Basis of Presentation and Significant Accounting Policies” in this Report.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to the market risk that the value of a financial instrument will fluctuate due to changes in market conditions, primarily from changes in foreign currency exchange rates. In the normal course of our business, we are subject to market risks associated with currency movements on our assets and liabilities.

Foreign Currency Exposures

We have exposure to foreign currency exchange rate fluctuations on net income from our subsidiaries denominated in currencies other than U.S. dollars, as our foreign subsidiaries in Korea, Taiwan, China, Japan and Hong Kong use local currency as their functional currency. From time to time these subsidiaries have cash and financial instruments in local currency. The amounts held in Japan, Taiwan, Hong Kong and China are not material in regards to foreign currency movements. However, based on the cash and financial instruments balance at September 30, 2021 for our Korean subsidiary, a 10% devaluation of the Korean won against the U.S. dollar would have resulted in a decrease of \$2.2 million in our U.S. dollar financial instruments and cash balances.

See “Note 9. Derivative Financial Instruments” to our consolidated financial statements under “Item 1. Interim Consolidated Financial Statements” and “Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations—Factors Affecting Our Results of Operations—Impact of Foreign Currency Exchange Rates on Reported Results of Operations” for additional information regarding our foreign exchange hedging activities.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our periodic reports filed or submitted 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, as appropriate, to allow timely decisions regarding required disclosure.

In connection with the preparation of this Report, we carried out an evaluation under the supervision of and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, as of September 30, 2021, of the effectiveness of the design and operation of our disclosure controls and procedures, as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act. Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of September 30, 2021.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended September 30, 2021 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

For a discussion of legal proceedings, see “Item 1. Interim Consolidated Financial Statements—Notes to Consolidated Financial Statements—Note 19. Commitments and Contingencies” in this Report and “Part I: Item 3. Legal Proceedings” of our 2020 Form 10-K.

See also “Item 1A. Risk Factors” in this Report and “Part I: Item 1A. Risk Factors” of our 2020 Form 10-K for additional information.

Item 1A. Risk Factors

The Company is subject to risks and uncertainties, any of which could have a significant or material adverse effect on our business, financial condition, liquidity or consolidated financial statements. You should carefully consider the risk factors disclosed in Part I, Item 1A of our 2020 Form 10-K (including that the impact of the COVID-19 pandemic may also exacerbate the risks discussed therein), herein and other reports we have filed with the SEC. The risks described herein and therein are not the only ones we face. This information should be considered carefully together with the other information contained in this Report and the other reports and materials the Company files with the SEC.

Risks Related to the Merger

There are risks and uncertainties associated with the Merger.

On March 25, 2021, we entered into the Merger Agreement with Parent and Merger Sub, pursuant to which, among other things, and subject to the terms and conditions thereof, Merger Sub will be merged with and into the Company, with the Company continuing its corporate existence as the surviving corporation in the Merger and becoming a wholly owned subsidiary of Parent. The consummation of the Merger is conditioned on the receipt of the approval of our stockholders, as well as the satisfaction of other customary closing conditions, including (i) the receipt of certain required or requested governmental approvals or authorizations (including from CFIUS and MOTIE), (ii) the absence of any order or law issued, enacted or deemed applicable by certain governmental authorities specified in the Merger Agreement that makes consummation of the Merger illegal and that remains in effect, (iii) the absence of a Company Material Adverse Effect (as defined in the Merger Agreement) and (iv) other customary closing conditions, including the accuracy of each party’s representations and warranties, and each party’s compliance with its obligations under the Merger Agreement (subject in the case of this clause (iv) to certain materiality qualifiers). There is no assurance that the conditions to the Merger will be satisfied in a timely manner or at all. Additionally, if the Merger is not completed, we may suffer a number of consequences that could adversely affect our business, results of operations, and stock price. There are numerous other risks related to the Merger as well, including the following:

- the possibility that any or all of the conditions precedent to the consummation of the proposed Merger, including the receipt of stockholder and regulatory approvals or authorizations, may not be satisfied or waived;
- unanticipated difficulties or expenditures relating to the proposed Merger;
- the failure to consummate the proposed Merger may result in negative publicity and a negative impression of us in the investment community;

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- required or requested regulatory approvals or authorizations from governmental entities may delay the proposed Merger or result in the imposition of conditions that could cause Parent to abandon the Merger;
- the occurrence of any event, change or circumstance that could give rise to the termination of the Merger Agreement;
- the effects that any termination of the Merger Agreement may have on the Company or our business, including the risks that (a) the price of our common stock may decline significantly if the Merger is not completed, (b) the Merger Agreement may be terminated in circumstances requiring the Company to pay Parent a termination fee, or (c) the circumstances of the termination, including the possible imposition of a 12-month tail period during which the termination fee could be payable upon certain subsequent transactions, may have a chilling effect on alternatives to the Merger;
- the diversion of and attention of management of Magnachip on transaction-related issues;
- legal proceedings, judgments or settlements, including those that have been and may in the future be instituted against Magnachip, our Board of Directors and executive officers and others following the announcement of the proposed Merger;
- disruptions of current plans and operations caused by the announcement and pendency of the proposed Merger;
- potential difficulties in employee retention (including executive and other key officers) due to the announcement and pendency of the proposed Merger;
- the response of customers, suppliers, business partners and regulators to the announcement of the proposed Merger;
- the effect of limitations that the Merger Agreement places on our ability to operate our business or engage in alternative transactions;
- the Merger may be completed even though certain events occur prior to consummation of the Merger that materially and adversely affect us; and
- other risks and uncertainties and the factors identified under “Forward-Looking Information” in our Proxy Statement on Schedule 14A filed on May 7, 2021 and under “Risk Factors” in Part I, Item 1A of Magnachip’s Annual Report on Form 10-K for the year ended December 31, 2020, and updated in subsequent reports filed by Magnachip with the SEC.

In addition, we have incurred, and will continue to incur, significant costs, expenses and fees for professional services and other transaction costs in connection with the Merger, and these fees and costs are payable by us regardless of whether the Merger is consummated.

Lawsuits have been filed, and other lawsuits may be filed, against the Company and current or former members of our Board of Directors in connection with the Merger, and an adverse ruling in any such lawsuit may delay or prevent the completion of the Merger or result in an award of damages against the Company.

See “Item 1. Interim Consolidated Financial Statements—Notes to Consolidated Financial Statements—19. Commitments and Contingencies” in this Report for a description of the Merger-related lawsuits.

Additional lawsuits arising out of or relating to the Merger Agreement or the Merger may be filed in the future. The results of complex legal proceedings are difficult to predict and could delay or prevent the completion of the Merger. The existence of litigation relating to the Merger could impact the likelihood of obtaining stockholder approval of the Merger. Moreover, the pending litigation is, and any future additional litigation could be, time consuming and expensive and could divert management’s attention away from its regular business.

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Item 6. Exhibits.

<u>Exhibit Number</u>	<u>Description</u>
2.1	<u>Letter Agreement, dated as of August 23, 2021, by and among Magnachip Semiconductor Corporation, South Dearborn Limited and Michigan Merger Sub, Inc. (incorporated by reference to Exhibit 2.1 to our Current Report on Form 8-K filed on August 23, 2021).</u>
31.1 [#]	<u>Certification pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934 of the Chief Executive Officer.</u>
31.2 [#]	<u>Certification pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934 of the Chief Financial Officer.</u>
32.1 [†]	<u>Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, of the Chief Executive Officer.</u>
32.2 [†]	<u>Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, of the Chief Financial Officer.</u>
101.INS [#]	Inline XBRL Instance Document.
101.SCH [#]	Inline XBRL Taxonomy Extension Schema Document.
101.CAL [#]	Inline XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF [#]	Inline XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB [#]	Inline XBRL Taxonomy Extension Label Linkbase Document.
101.PRE [#]	Inline XBRL Taxonomy Extension Presentation Linkbase Document.
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101).

Footnotes:

- [#] Filed herewith
[†] Furnished herewith

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.

MAGNACHIP SEMICONDUCTOR CORPORATION
(Registrant)

Dated: November 5, 2021

By: /s/ Young-Joon Kim
Young-Joon Kim
Chief Executive Officer
(Principal Executive Officer)

Dated: November 5, 2021

By: /s/ Young Soo Woo
Young Soo Woo
Chief Financial Officer
(Principal Financial Officer)

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO
SECTION 302 OF THE
SARBANES-OXLEY ACT OF 2002**

I, Young-Joon Kim, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Magnachip Semiconductor Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: November 5, 2021

/s/ Young-Joon Kim

Young-Joon Kim
Chief Executive Officer
(Principal Executive Officer)

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO
SECTION 302 OF THE
SARBANES-OXLEY ACT OF 2002**

I, Young Soo Woo, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Magnachip Semiconductor Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: November 5, 2021

/s/ Young Soo Woo

Young Soo Woo
Chief Financial Officer
(Principal Financial Officer)

**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**

Pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of Magnachip Semiconductor Corporation (the “**Company**”) hereby certifies, to such officer’s knowledge, that:

(i) the Quarterly Report on Form 10-Q of the Company for the quarterly period ended September 30, 2021 as filed with the Securities and Exchange Commission on the date hereof (the “**Report**”) fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and

(ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of the dates and for the periods expressed in the Report.

Dated: November 5, 2021

/s/ Young-Joon Kim

Young-Joon Kim

Chief Executive Officer

(Principal Executive Officer)

The foregoing certification is being furnished solely pursuant to 18 U.S.C § 1350 and shall not be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or incorporated by reference in any registration statement of the Company filed under the Securities Act of 1933, as amended.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

**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**

Pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of Magnachip Semiconductor Corporation (the “**Company**”) hereby certifies, to such officer’s knowledge, that:

(i) the Quarterly Report on Form 10-Q of the Company for the quarterly period ended September 30, 2021 as filed with the Securities and Exchange Commission on the date hereof (the “**Report**”) fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and

(ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of the dates and for the periods expressed in the Report.

Dated: November 5, 2021

/s/ Young Soo Woo

Young Soo Woo

Chief Financial Officer

(Principal Financial Officer)

The foregoing certification is being furnished solely pursuant to 18 U.S.C § 1350 and shall not be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or incorporated by reference in any registration statement of the Company filed under the Securities Act of 1933, as amended.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.