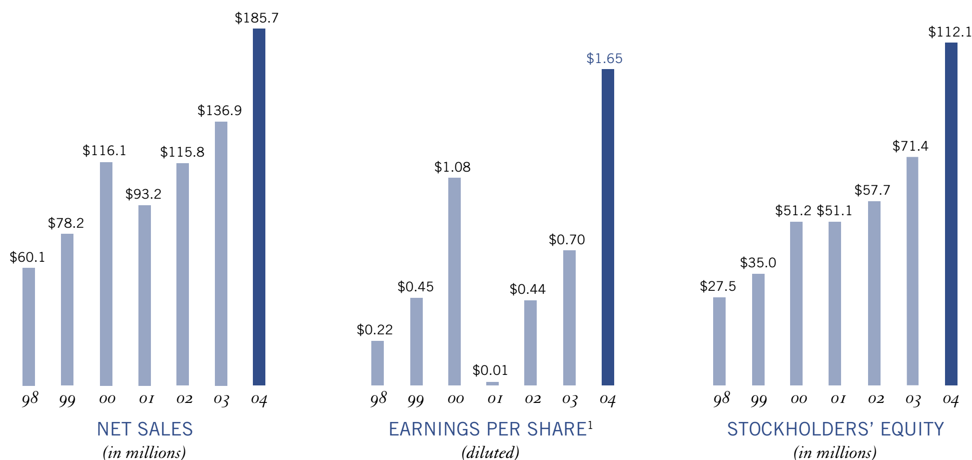
Diodes Incorporated   Annual Report 2004

TRANSFORMING THE FUTURE

FINANCIAL HIGHLIGHTS

(in thousands, except per share data)	*1998*	*1999*	*2000*	*2001*	*2002*	*2003*	*2004*
Net sales	$60,121	$78,245	$116,079	$ 93,210	$115,821	$136,905	$185,703
Gross profit	15,402	20,948	37,427	14,179	26,710	36,528	60,735
Selling, general and administrative expenses	11,016	13,670	18,814	13,711	16,228	19,586	23,503
Research and development expenses	–	–	141	592	1,472	2,049	3,422
Non-reoccurring expenses	–	–	–	8	43	1,037	14
Total operating expenses	11,016	13,670	18,955	14,311	17,743	22,672	26,939
Income (loss) from operations	4,386	7,278	18,472	(132)	8,967	13,856	33,796
Interest expense, net	281	292	940	2,074	1,183	860	637
Other income (expense)	93	182	501	785	67	(5)	(418)
Income (loss) before taxes and minority interest	4,198	7,168	18,033	(1,421)	7,851	12,991	32,741
Income tax benefit (provision)	(1,511)	(1,380)	(2,496)	1,769	(1,729)	(2,460)	(6,514)
Minority interest	(14)	(219)	(642)	(224)	(320)	(436)	(676)
Net income	2,673	5,569	14,895	124	5,802	10,095	25,551
Earnings per share: [1]							
Basic	$ 0.24	$ 0.49	$ 1.23	$ 0.01	$ 0.47	$ 0.79	$ 1.91
Diluted	0.22	0.45	1.08	0.01	0.44	0.70	1.65
Number of shares: [1]							
Basic	11,315	11,438	12,107	12,216	12,277	12,731	13,404
Diluted	12,085	12,306	13,833	13,322	13,297	14,406	15,471
Total assets	$45,389	$62,407	$112,950	$103,258	$105,010	$123,795	$167,801
Working capital	16,639	15,903	17,291	19,798	20,831	27,154	49,571
Long-term debt	8,102	6,984	30,857	29,497	18,417	12,583	11,347
Stockholders' equity	27,460	34,973	51,253	51,124	57,678	71,450	112,148
Return on assets	6.4%	10.3%	17.0%	0.1%	5.6%	8.8%	17.5%
Return on equity	10.3%	17.8%	34.5%	0.2%	10.7%	15.6%	27.8%



[1] Adjusted for the effect of 3-for-2 stock splits in July 2000 and November 2003.

Corporate Profile

Headquartered in Southern California with operations in North America, Asia, and Europe, Diodes Incorporated is a leading manufacturer and supplier of high quality discrete semiconductor products to industry leaders in multiple-end markets, serving the computer, industrial, consumer electronics, communications and automotive markets.

Proven Management Team

The Company has an experienced management team that combines significant operational track records with entrepreneurial and technological vision.

Product Development and Manufacturing Focus

Diodes' manufactures and supplies devices that are essential building blocks of the electronics industry, providing support and making electrical connections to integrated circuits, for use in such products as notebook computers, flat panel displays, digital audio players and cameras, mobile handsets, set top boxes, DC to DC converters, automotive applications, and more.

Diodes Incorporated...

...is a world class manufacturer of high performance Schottky rectifiers, including industry-leading high efficiency, low V_F and high voltage types.

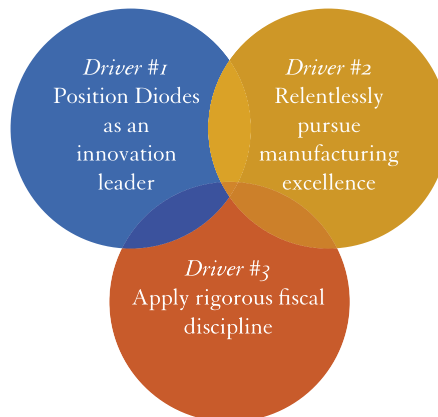
...offers a comprehensive portfolio of high density diode, transistor, and application specific arrays in a variety of multi-pin sub-miniature surface mount packages.

...is a leader in Zener technology, providing performance tight tolerance and low test current types.

...specializes in high power density packaging, and has recently patented several breakthrough PowerDI rectifier packages for a variety of Schottky, Superfast and Standard Recovery Rectifiers, Zener and TVS product types.

...brings to market a variety of Bipolar Junction Transistors, Prebiased Transistors, Small Signal MOSFETs and Transient Protection technologies; Thyristor Surge Protection Devices, Silicon TVS, and ESD protection arrays that round out Diodes' product portfolio.

[THREE DRIVERS OF DIODES' CORPORATE STRATEGY]



Transforming through

INNOVATION LEADERSHIP

Diodes' Corporate Strategy – Driver #1:

To position Diodes as an innovation leader for discrete devices, by investing in developing next-generation technologies that deliver meaningful improvements in performance, size and power consumption – for compact convenience products that define our modern world, keeping us connected or surrounding us with orchestra-quality songs, and more.

As consumers' needs increase for compact audio solutions, mobile communications, interactive high-definition TVs and more, so does the demand for discrete devices that deliver performance in smaller packages. We are bringing to market a broad range of products that offer size and performance benefits for the growing number of next-generation portable and mobile electronics that are vital to today's busy lifestyles. Recognizing that product diversification is a key to long-term success, we are growing our markets both vertically and horizontally.

[DIODES INCORPORATED] + [BOSE CORPORATION]

=

[SMALLER PACKAGE, LARGER SOUND]

[Diodes is intensifying research and development *initiatives in such innovative product areas as application-specific multi-chip component arrays and sub-micro packaging to support our customers' advancing technologies.*]

Transforming through

MANUFACTURING EXCELLENCE

Diodes' Corporate Strategy – Driver #2:

To relentlessly pursue manufacturing excellence to ensure that our product quality, cost structure, and ability to swiftly respond to changing customer demands are the best in industry. To continue the pursuit of uncompromising dedication to quality and innovation throughout every aspect of Diodes' product development chain.

From engineering to manufacturing and quality assurance, we meet and surpass rigorous industry standards, while focusing on cost efficiencies and market requirements. Our relentless pursuit of excellence has earned us quality certifications and customer recognition. With our R&D expertise and first-tier packaging and wafer manufacturing capabilities, we are a fully integrated manufacturer and total solution provider of discrete semiconductors. By controlling the entire product lifecycle and developing new chip technologies, we are producing wafer process and packaging technology breakthroughs in performance discretes while introducing proprietary products to the marketplace.

[DIODES INCORPORATED] + [DANGER, INC]

=

[COOLER COMMUNICATIONS]

[By integrating research and development *and wafer fabrication capabilities with our manufacturing, we have become a total solution provider that can drive new product innovations and support our customers with application-specific designs.*]

Transforming through

FISCAL DISCIPLINE

Diodes' Corporate Strategy – Driver #3:

To apply strict financial discipline to maintain tight controls over overhead, optimize working capital management, and deploy capital judiciously. At Diodes, we ensure that every dollar we invest in capital equipment and research and development earns multiple returns for you, our Shareholders.

Exercising rigorous fiscal discipline with absolute transparency, according to the highest ethical standards of corporate governance, is of paramount importance to us. Our ongoing investment in the development of next-generation technologies, delivering meaningful improvements in performance, size, and power consumption, has positioned us as the go-to company when looking for a total solution provider in the semiconductor industry. Streamlined production processes, lean management structures, and conservative financial policies enable us to build the resources needed to strategically develop and expand our business, yielding maximum shareholder value.

[DIODES INCORPORATED] + [ECHOSTAR COMMUNICATIONS]

=

[ON-DEMAND VIEWING]

[We provide top quality solutions *at economical prices – that's why Diodes' discrete semiconductor components are the building blocks for success.*]

DEAR SHAREHOLDERS

We are pleased to inform you that 2004 was another remarkable year for Diodes Incorporated.

While the semiconductor industry generally experienced a year of solid demand, we again yielded record results. Our 36% growth in revenues for 2004 once again exceeded the discrete semiconductor sector by a factor of nearly two times. We continued to strengthen our balance sheet and generate positive cash from operations even as we built working capital in support of our growth and invested over $26 million in capital expenditures to expand our manufacturing capacity for next-generation devices.

Our strong performance is based on a core operating strategy that has served us well in both strong and weak markets over the past several years. This strategy has three essential elements:

First, to position Diodes as an innovation leader for discrete devices and provider of integrated solutions. We have stepped up the pace of development of core intellectual property that enables us to transcend the current limits of performance, size and power consumption.

Second, to continually pursue manufacturing excellence in order to establish an industry-leading cost structure, maintain the flexibility to rapidly respond to changing customer needs, and sustain our unmatched reputation for product quality.

Third, to exercise rigorous fiscal discipline in order to ensure that our organization is lean, we optimize our working capital performance, and every dollar we invest in capital equipment and research and development earns multiple returns for our shareholders.

These are the fundamental principles that have been behind Diodes' success in recent years – and we believe they offer a compelling formula for sustained performance in the future.

Our fiscal results are the tangible expression of this success. In the past year:

- Revenues increased 35.6% to a record $185.7 million. This compares to the 2004 discrete semiconductor growth of 18.1%.
- Sales of new products reached a record level of 16% of total sales.
- We continued to diversify into higher-margin product lines, improving our gross profit margin 600 bps to 32.7%.

Raymond Soong
Chairman of the Board

C. H. Chen
President and
Chief Executive Officer

- Selling, general and administrative expenses were among the lowest in our industry at 12.7% of revenue.

- Investment in research and development increased 67% to $3.4 million or 1.8% of revenue.

- Net income improved 153% to a record $25.6 million, or $1.65 per share.

Our balance sheet is strong: in 2004, Diodes generated cash flow from operations of $29.3 million, a 56% increase from 2003, which we used, in part, to reduce our total debt by $3.6 million. We ended the year with $19 million in cash and unused and available credit facilities of $32 million. Finally, shareholders' equity increased to $112.1 million, a 57% increase.

These financial results reflect our continued dedication to our strategy of producing leading-edge technology and running efficient, streamlined operations. In all we do, dedication and commitment are key. On the technology side, our products keep getting smaller and more energy-efficient while offering the same powerful – and oftentimes even increased – performance. We are bringing to market a broad range of products that offer very real benefits in both size and performance for a growing number of next-generation portable and mobile electronics that are vital to our end-consumers' busy lives: Diodes' products are used in computers, consumer electronics, industrial, automotive, and communications devices in many of the conveniences that have become staples in our modern world. We realized early on that diversification is another significant factor in long-term success, and we have thus pursued a policy of growing our markets both vertically and horizontally.

We are also responding to an increasing demand, especially from Europe and Asia, for environmentally-friendly products by eliminating lead (Pb) from lead plating. Therefore, as we continue to listen and respond to our customers' needs…

…We Are Transforming The Future.

You cannot talk of the future without revisiting the past. So let us first review the highlights of the year 2004.

On the technological side, we developed a series of sophisticated new products during the year:

- We launched a new line of subminiature SOT-563 discrete semiconductor components, continuing our range of subminiature discretes and arrays targeted to markets including mobile phone, digital-audio player, and portable handheld electronics.

- We introduced the patent-pending PowerDI™123 Compact Power Package. This high-current density package type is one of the most thermally efficient compact rectifier packages available on the market.

- We released the new high-voltage PDS3200 and PDS5100H Schottky Barrier Rectifiers in a new high-current density package type, patent-pending PowerDI™5. Able to accommodate larger die sizes and higher amperage, it broadens the range of Diodes' high-performance next-generation discrete devices.

On the logistics and sales side, we partnered with several strategically important distribution partners. In addition to our long-standing relationships with All American, Arrow, Avnet, Digi-Key, Future, and Jaco we:

- Signed a contract with Mouser Electronics, Inc., one of the largest suppliers and distributors of electronic components in North America whose on-line catalog allows us the fastest 'time to market' approach for our customer solutions and application-specific products.

- Expanded our distribution agreement with Arrow Electronics into Southern Europe, adding 12 Mediterranean countries to our portfolio of global markets. After first entering the European market in 2001, we have consistently grown our sales and market share each year so this agreement was the logical extension of our European activities.

PowerDI is a trademark of Diodes Incorporated.

After this recapitulation of the 2004 highlights, let us now focus on some specifics that have shaped this past year and will continue to transform the future:

Our Path to Becoming A Total Solutions Provider

Reviewing our path in the last ten years, we see a stunning transformation. First, we went from being a distributor of other companies' products to a fully integrated manufacturer with a state-of-the-art packaging facility in Mainland China. Then we acquired a wafer fabrication facility that gave us the capability to control the entire product lifecycle and provided us with a base to develop new chip technologies. And just in the past three years, we have built a full scale R&D program that has produced breakthroughs in both wafer processes and packaging technologies that enables Diodes to extend the envelope of discrete performance and introduce a number of proprietary products to the discrete marketplace.

Our ongoing investment in the development of next-generation technologies that deliver meaningful improvements in performance, size, and power consumption has positioned us as the go-to company in quest of a total solution provider in the semi-conductor industry. And our unwavering efforts to offer the best, most innovative package of products and service in the industry were acknowledged with several prestigious customer, industry and media awards in 2004, such as Digi-Key's "Top Ten Supplier Award" and Samsung's "Outstanding Supplier Award". We were also listed in *Forbes Magazine*'s "200 Best Small Companies," recognized by Deloitte Technology as part of the "Fast 50 Among the Fastest Growing Technology Companies in Los Angeles," and included in the *Business 2.0 Magazine*'s "Fastest Growing Technology Companies."

Commitment to Quality and Manufacturing Excellence

Hand in hand with an innovation leadership role goes the dedication to quality. Quality is one of the founding principles on which this Company is built, and we realized from the beginning that it is one of the non-negotiable elements of long-term success. It is also the theme that runs through every step of the design, engineering, and quality control process. We relentlessly pursue manufacturing excellence to ensure that product quality, cost structure and our ability to flexibly and swiftly respond to changing customer demands are the best in the industry. This uncompromising dedication to quality and innovation has over time earned us a number of ISO certifications.

Corporate Governance and Financial Discipline

Despite the rapid growth and evolution of our Company, we never lose sight of those who are the driving force behind our endeavors: you, the investor. We understand clearly that we owe you absolute transparency and the highest ethical standards of Corporate Governance. Ensuring that the financial results fairly reflect the results of our operations is of paramount importance to us and to our investors. We have always been diligent in maintaining compliance with our established financial accounting policies, which are consistent with requirements of Generally Accepted Accounting Principles (GAAP), and in reporting our results with objectivity and the highest degree of integrity. Our financial information is transparent, timely, complete, relevant, and accurate.

We are equally committed to rigorously and diligently exercising our oversight responsibilities throughout the Company, managing our affairs consistent with the highest principles of business ethics, and exceeding the Corporate Governance requirements of both federal law and the NASDAQ Stock Market. Our culture demands integrity and an unyielding commitment to strong internal practices and policies.

We appreciate our shareholders' confidence in our future and work hard to not only deliver outstanding results quarter for quarter but we also believe in enhancing the return of capital through increased accountability.

While we are proud of our achievements over the years, we will not rest on our laurels but will continuously strive to surpass existing achievements and to identify areas that will benefit from improvements. We are looking forward to this year 2005 and to bringing continued positive results to you – our shareholders, customers, suppliers, and employees.

Sincerely,

Raymond Soong

Chairman of the Board

C.H. Chen

President and
Chief Executive Officer

Corporate Governance Highlights

Investor confidence in public companies is essential to the functioning of the global economy. To enlist and sustain investor confidence in Diodes Incorporated, the Company maintains an investor website at *www.diodes.com* to provide public access to information about our corporate governance policies. These policies provide a framework for the proper operation of our Company, consistent with the best interests of you, our Shareholders, and the requirements of the law.

Key information about our corporate governance policies and commitments includes:

- Majority of Board members and Board committee members are independent

- Board adopted a Code of Business Conduct

- Board committee charters clearly establish respective roles and responsibilities

- Audit Committee established policies for auditor independence

- Moss Adams LLP, our independent accountants, report directly to the Audit Committee, and any non-audit services performed do not interfere with their independence

- Audit Committee conducts an appropriate review of all related party transactions for potential conflict of interest situations on an ongoing basis and approves such transactions

- Audit Committee members meet regularly with internal and external auditors, without the presence of the Company's management

- Internal Audit Manager reports directly to Audit Committee

- Through internal audit control function, we monitor compliance with our global financial policies and practices over critical areas, including: internal controls, financial accounting and reporting, fiduciary accountability, and safeguarding of our corporate assets

- A whistle-blower hotline has been established as a confidential means for employees to address issues to the Audit Committee regarding our Company's accounting, internal accounting controls and auditing practices

- The Board adopted a Code of Ethics for the Chief Executive Officer and all members of our finance department, including the principal financial/ accounting officer

- Compensation Committee makes recommendations to the Board regarding compensation, benefits and incentive arrangements for officers

- Nominating Committee recommends director nominees to be selected by the Board

Our culture demands integrity and an unyielding commitment to strong internal practices and policies.

We thank you for the confidence you have placed in us.

Distribution Network

Through innovative marketing strategies and sophisticated logistics, we work with world-class distributors to assist our customers in advancing their technologies.

Photo of Bose® Lifestyle® 48 DVD home entertainment system on page 3 courtesy of Bose Corporation
Photo of the Hiptop2 on page 5 courtesy of Danger, Inc.
Photo of Dish Player DVR 510 on page 7 courtesy of EchoStar Communications Corporation

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of the Company's financial condition and results of operations should be read together with the consolidated financial statements and the notes to consolidated financial statements included elsewhere in this Form 10-K. Except for the historical information contained herein, the matters addressed in this Item 7 constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements may be identified by the use of words such as "anticipate," "believe," "continue," "estimate," "expect," "intend," "may," "project," "will" and similar expressions. Such forward-looking statements are subject to a variety of risks and uncertainties, including those discussed above under the heading "Cautionary Statement for Purposes of the "Safe Harbor" Provision of the Private Securities Litigation Reform Act of 1995" and elsewhere in this Annual Report on Form 10-K, that could cause actual results to differ materially from those anticipated by the Company's management. The Private Securities Litigation Reform Act of 1995 (the "Act") provides certain "safe harbor" provisions for forward-looking statements. All forward-looking statements made in this Annual Report on Form 10-K are made pursuant to the Act. The Company does not undertake to update its forward-looking statements to reflect actual events and outcomes or later events.

Overview

We sell a wide variety of discrete semiconductor products, as well as silicon wafers used in the manufacture of these products, primarily to manufacturers in the communications, computing, industrial, consumer electronics and automotive markets, and to distributors of electronic components to end-customers in these markets. Our technologies include high density diode and transistor arrays in multi-pin surface-mount packages; PowerDI™, high-performance surface-mount packages; performance Schottkys, switching and rectifier diodes; single and dual pre-biased transistors; performance tight tolerance and low current zener diodes; subminiature surface-mount packages; transient voltage suppressors (TVS and TSPD); small signal transistors and MOSFETs; and standard, fast, ultra-fast, and super-fast rectifiers.

PowerDI is a trademark of Diodes Incorporated.

Our products are designed into a broad range of end-products such as notebook computers, flat-panel displays, set-top boxes, game consoles, digital cameras, cellular phones, PDAs, power supplies, security systems, network routers and switches, as well as into automotive safety controls, GPS navigation, satellite radios and audio/video players.

The Company rapidly responds to the demands of the global marketplace by continuing to increase its investment in research and development, and by focusing on expanding its product portfolio and closely controlling product quality and time-to-market. As a result of the Company shifting development priorities toward specialized configurations, such as the Company's high-density array devices, the Company is introducing a range of new products that improve the trade-off between size, performance and power consumption for surface-mount packages.

The majority (66% in 2004) of our sales are to major OEMs such as Intel Corporation, Cisco Systems Incorporated, Sony Corporation, Nortel Networks Corporation, Delphi Automotive, Bose Corporation, Scientific Atlanta Incorporated, Samsung Electronics, Asustek Computer, Inc., Quanta and LG Electronics, Inc. Our distribution network (34% of 2004 sales) includes major distributors such as Arrow Electronics, Inc., Avnet, Inc., Digi-Key Corporation, Future Electronics, Ltd., Jaco Electronics, Inc., Reptron Electronics, Inc., and All American Semiconductor, Inc.

Because of the electronics industry trend towards moving manufacturing to lower operating cost countries in Asia, the Company has focused primarily on customers in China, Taiwan, Korea and Hong Kong. We sell to Asian customers (59% of 2004 sales) primarily through our wholly owned subsidiaries, Diodes-Taiwan and Diodes-Hong Kong. The Asian discrete semiconductor market is the largest and fastest growing market in which the Company participates. An increase in the percentage of sales in Asia is expected as we have significantly increased our sales presence there and believe there is greater potential to increase market share in that region due to the expanding base of electronics product manufacturers.

Our corporate headquarters located just outside Los Angeles in Westlake Village, California, which provides sales, marketing, engineering, logistics and warehousing functions, sells primarily to North American manufacturers and distributors (38% of 2004 sales). Due to the manufacturing shift, the North American discrete semiconductor market is now the smallest market and its growth rate is far less than all other markets. The majority of our applications engineers are located in the U.S. in order to work with the customers' design engineers. Whether the end-application is ultimately manufactured in the U.S. or in Asia, our world-wide sales organization is well positioned to provide sales and support to the customer.

In order to take advantage of the relatively robust European market, offices in Toulouse, France and Hattenheim, Germany support our European sales expansion (3% of 2004 sales).

Asian sales are also generated from Shanghai KaiHong Electronics Co., Ltd. ("Diodes-China" or "KaiHong"), and Diodes-Shanghai, 95% owned manufacturing facilities in Shanghai, China, with offices in Shanghai and Shenzhen, China, as well as from FabTech Incorporated ("Diodes-FabTech" or "FabTech"), a silicon wafer manufacturer acquired in December 2000 located near Kansas City, Missouri.

Revenues were derived from the following countries (*All Others* represents countries with less than 8% of total revenues each) (in thousands):

2003	*Revenue*	*% of Total Revenue*
United States	$ 41,593	30.4
Taiwan	38,087	27.8
China	25,908	18.9
Korea	14,455	10.6
All Others	16,862	12.3
Total	$ 136,905	100.0

2004	*Revenue*	*% of Total Revenue*
United States	$ 53,204	28.6
Taiwan	50.716	27.3
China	44,311	23.9
Korea	16,447	8.9
All Others	21,025	11.3
Total	$ 185,703	100.0

Manufacturing and Significant Vendors

Diodes-China and Diodes-Shanghai, both located in Shanghai, China, are our 95% owned joint venture manufacturing facilities. Since Diodes-China's inception in 1995, we have invested approximately $77 million in plant and state-of-the-art equipment in China. Both factories manufacture product for sale by our U.S. and Asian operations, and also sell to external customers as well.

At Diodes-China and Diodes-Shanghai, silicon wafers are received and inspected in a highly controlled "clean room" environment awaiting the assembly operation. At the first step of assembly, the wafers are sawn with very thin, high speed diamond blades into tiny semiconductor "dice", numbering as many as 200,000 per 5" diameter wafer. Dice are then loaded onto a handler, which automatically places the dice, one by one, onto lead frames, which are package specific, where they are bonded to the lead frame pad. Next, automatic wire bonders make the necessary electrical connections from the die to the leads of the lead frame, using micro-thin gold wire. The fully automatic assembly machinery then molds the epoxy case around the die and lead frame to produce the desired semiconductor product. After a trim, form, test, mark and re-test operation, the parts are placed into special carrier housings and a cover tape seals the parts in place. The taped parts are then spooled onto reels and boxed for shipment.

Acquired from Lite-On Semiconductor Corporation ("LSC"), our largest shareholder, in December 2000, our wafer foundry, Diodes-FabTech, is located in Lee's Summit, Missouri. Diodes-FabTech manufactures primarily 5-inch silicon wafers, which are the building blocks for semiconductors. FabTech purchases polished silicon wafers and then, by using various technologies and patents, in conjunction with many chemicals and gases, fabricates several layers on the wafers, including epitaxial silicon, ion implants, dielectrics and metals, with various patterns. Depending upon these layers and the die size (which is determined during the photolithography process and completed at the customer's packaging site where the wafer is sawn into square or rectangular die), different types of wafers with various currents, voltages and switching speeds are produced.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

In 2004, our largest external supplier of products was LSC, a related party. Approximately 17.2% and 17.3% of our sales were from product manufactured by LSC in 2004 and 2003, respectively. Also, in 2004 and 2003, approximately 3.5% and 4.6%, respectively, of our sales were from product manufactured by companies owned by Keylink International (a related party). In addition, sales of products manufactured by Diodes-China and Diodes-FabTech were approximately 49% and 20% in 2004, respectively, versus 39% and 23% in 2003, respectively. We anticipate that Diodes-China will become an increasingly valuable supplier. No other manufacturer of discrete semiconductors accounted for more than 4% and 9% of our sales in 2004 and 2003, respectively.

All of the raw materials we use in our manufacturing operations are available both domestically and abroad. Although we believe alternative sources exist for the products of any of our suppliers, the loss of any one of our principal suppliers or the loss of several suppliers in a short period of time could have a materially adverse effect on our financial statements until an alternate source is located and has commenced providing such products or raw materials.

Related Parties

We conduct business with two related party companies, LSC (and its subsidiaries) and Keylink International (formerly Xing International) (and its subsidiaries). LSC, a 32.3% shareholder, is our largest shareholder, and Keylink International is owned by our 5% joint venture partner in Diodes-China and Diodes-Shanghai. C.H. Chen, our President and Chief Executive Officer, and a member of our Board of Directors, is also Vice-Chairman of LSC. M.K. Lu, a member of our Board of Directors, is President of LSC, while Raymond Soong, our Chairman of the Board, is the Chairman of the Lite-On Group, a significant shareholder of LSC.

In addition to being our largest external supplier of products, in 2004, we sold silicon wafers to LSC totaling 11.1% (10.7% in 2003) of our total sales, making LSC our largest customer. The Company has a long-standing sales agreement where the Company is the exclusive North American distributor for certain of LSC product lines. In addition, the Company leases warehouse space from LSC for its operations in Hong Kong. Such transactions are on terms no less favorable to the Company than could be obtained from unaffiliated third parties. The Audit Committee of the Board of Directors has approved the contracts related to the transactions.

In December 2000, the Company acquired the wafer foundry, FabTech, Inc., from LSC. As part of the purchase price, at December 31, 2004, LSC holds a subordinated, interest-bearing note for approximately $3.8 million. In May 2002, the Company renegotiated the terms of the note to extend the payment period from two years to four years, and therefore, monthly payments of approximately $208,000 plus interest began in July 2002. In connection with the terms of the acquisition, LSC entered into a volume purchase agreement to purchase wafers from FabTech. In addition, as per the terms of the stock purchase agreement, the Company has entered into several management incentive agreements with members of FabTech's management. The agreements provide members of FabTech's management guaranteed annual payments as well as contingent bonuses based on the annual profitability of FabTech, subject to a maximum annual amount. Any portion of the guaranteed and contingent liability paid by FabTech is reimbursed by LSC. Year 2004 is the final year of the management incentive agreements, with final payment by March 31, 2005.

In addition to the 3.5% of our sales of product manufactured by companies owned by Keylink International, in 2004, the Company sold silicon wafers to companies owned by Keylink International totaling 0.9% (1.1% in 2003) of the Company's total sales. In addition, Diodes-China and Diodes-Shanghai both lease their manufacturing facilities from, and subcontract a portion of its manufacturing process (metal plating and environmental services) to Keylink International. The Company

also pays a consulting fee to Keylink International. Such transactions are on terms no less favorable to the Company than could be obtained from unaffiliated third parties. The Audit Committee of the Board of Directors has approved the contracts related to the transactions.

Income taxes

In accordance with the current taxation policies of the People's Republic of China (PRC), Diodes-China received preferential tax treatment for the years ended December 31, 1996 through 2004. Earnings were subject to 0% tax rates from 1996 through 2000, and 12% from 2001 through 2004. Due to a $15.0 million permanent re-investment of Diodes-China earnings in 2004, earnings from 2005 through 2007 will continue to be taxed at 12% (one half the normal central government tax rate). Also due to the permanent re-investment, the Company recorded a $1.2 million tax refund (net of U.S. taxes) in the fourth quarter of 2004. Earnings of Diodes-China are also subject to tax of 3% by the local taxing authority in Shanghai. The local taxing authority waived this tax from 2001 through 2004, and is expected to waive this tax in 2005, but can re-impose the tax at its discretion. For 2004, Diodes-Shanghai's effective tax rate was 15%. As an incentive for the establishment of Diodes-Shanghai, beginning in 2005, earnings will be exempted from income tax for two years. Then, beginning in 2007, earnings will be subject to 50% of the standard 15% tax rate for the following three years.

Earnings of Diodes-Taiwan are currently subject to a tax rate of 35%, which is comparable to the U.S. Federal tax rate for C corporations. Earnings of Diodes-Hong Kong are currently subject to a 17.5% tax for local sales and/or local source sales, all other sales are foreign income tax-free.

In accordance with United States tax law, the Company receives credit against its U.S. Federal tax liability for corporate taxes paid in Taiwan and China. The repatriation of funds from Taiwan and China to the Company may be subject to Federal and state income taxes.

As of December 31, 2004, accumulated and undistributed earnings of Diodes-China are approximately $44.2 million, including $25.0 million of restricted earnings (which are not available for dividends). Through March 31, 2002, the Company had not recorded deferred U.S. Federal or state tax liabilities (estimated to be $8.9 million as of March 31, 2002) on these cumulative earnings since the Company, at that time, considered this investment to be permanent, and had no plans or obligation to distribute all or part of that amount from China to the United States. Beginning in April 2002, the Company began to record deferred taxes on a portion of the earnings of Diodes-China in preparation of a dividend distribution. In the year ended December 31, 2004, the Company received a dividend of approximately $5.7 million from its Diodes-China subsidiary, for which the tax effect is included in U.S. Federal and state taxable income. As of December 31, 2004, the Company has recorded $2.0 million in deferred taxes on the cumulative earnings of Diodes-China.

The Company is evaluating the need to provide additional deferred taxes for the future earnings of Diodes-China, Diodes-Shanghai, and Diodes-Hong Kong to the extent such earnings may be appropriated for distribution to the Company's corporate office in North America, and as further investment strategies with respect to foreign earnings are determined. Should the Company's North American cash requirements exceed the cash that is provided through the domestic credit facilities, cash can be obtained from the Company's foreign subsidiaries. However, the distribution of any unappropriated funds to the U.S. will require the recording of income tax provisions on the U.S. entity, thus reducing net income.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

On October 22, 2004, the President of the United States signed the American Jobs Creation Act (AJCA) into law. Originally intended to repeal the extraterritorial income (ETI) exclusion, which had triggered tariffs by the European Union, the AJCA expanded to cover a wide range of business tax issues. Among other items, the AJCA establishes a phased repeal of the ETI, a new incentive tax deduction for U.S. corporations to repatriate cash from foreign subsidiaries at a reduced tax rate (a deduction equal to 85% of cash dividends received in the year elected that exceeds a base-period amount) and significantly revises the taxation of U.S. companies doing business abroad.

At December 31, 2004, the Company made a minimum estimate for repatriating cash from its subsidiaries in China and Hong Kong of $8.0 million under the AJCA, and recorded an income tax expense of approximately $1.3 million. Under the guidelines of the AJCA, the Company will develop a required domestic reinvestment plan, covering items such as U.S. bank debt repayment, U.S. capital expenditures and U.S. research and development activities, among others, to cover the $8.0 million minimum dividend repatriation. In addition, the Company will complete a quantitative analysis of the benefits of the AJCA, the foreign tax credit implications, and state and local tax consequences of a dividend to maximize the tax benefits of a 2005 dividend.

Available Information

Our website address is http://www.diodes.com. We make available, free of charge through our website, our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, Proxy Statements, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission ("the SEC").

Our filings may also be read and copied at the SEC's Public Reference Room at 450 Fifth Street, NW, Washington, DC 20549. Information on the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330. The SEC also maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The address of that site is www.sec.gov.

To support our global customer-base, particularly in Asia and Europe, our website is language-selectable into English, Chinese, Japanese, Korean and German, giving us an effective marketing tool for worldwide markets. With its extensive online Product (Parametric) Catalog with advanced search capabilities, our website facilitates quick and easy product selection. Our website provides easy access to worldwide sales contacts and customer support, and incorporates a distributor-inventory check to provide component inventory availability and a small order desk for overnight sample fulfillment. Our website also provides access to current and complete investor financial information and corporate governance information including our Code of Business Conduct, SEC filings and press releases, as well as stock quotes.

Critical Accounting Policies and Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an on-going basis, we evaluate our estimates, including those related to revenue recognition, allowance for doubtful accounts, inventory reserves and income taxes, among others. Our estimates are based upon historical experiences, market trends and financial forecasts and projections, and upon various other assumptions that management believes to be reasonable under the circumstances and at that certain point in time. Actual results may differ, significantly at times, from these estimates under different assumptions or conditions.

We believe the following critical accounting policies and estimates affect the significant estimates and judgments we use in the preparation of our consolidated financial statements, and may involve a higher degree of judgment and complexity than others.

Revenue Recognition

Revenue is recognized when there is persuasive evidence that an arrangement exists, when delivery has occurred, when our price to the buyer is fixed or determinable and when collectibility of the receivable is reasonably assured. These elements are met when title to the products is passed to the buyers, which is generally when our product is shipped to both original equipment manufacturers (OEMs) and electronics component distributors.

We reduce revenue in the period of sale for estimates of product returns, distributor price adjustments and other allowances, the majority of which are related to our North American operations. Our reserve estimates are based upon historical data as well as projections of revenues, distributor inventories, price adjustments, average selling prices and market conditions. Actual returns and adjustments could be significantly different from our estimates and provisions, resulting in an adjustment to revenues.

Inventory Reserves

Inventories are stated at the lower of cost or market value. Cost is determined principally by the first-in, first-out method. On an on-going basis, we evaluate our inventory, both finished goods and raw material, for obsolescence and slow-moving items. This evaluation includes analysis of sales levels, sales projections, and purchases by item, as well as raw material usage related to our manufacturing facilities. Based upon this analysis, as well as an inventory aging analysis, we accrue a reserve for obsolete and slow-moving inventory. If future demand or market conditions are different than our current estimates, an inventory adjustment may be required, and would be reflected in cost of goods sold in the period the revision is made.

Accounting for Income Taxes

As part of the process of preparing our consolidated financial statements, we are required to estimate 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 bases of the Company's assets and liabilities. Significant management judgment is required in determining our provision for income taxes, deferred tax assets and liabilities. Management continually evaluates its deferred tax asset as to whether it is likely that the deferred tax assets will be realized. If management ever determined that its deferred tax asset was not likely to be realized, a write-down of the asset would be required and would be reflected as an expense in the accompanying period.

Allowance for Doubtful Accounts

Management evaluates the collectability of our accounts receivable based upon a combination of factors, including the current business environment and historical experience. If we are aware of a customer's inability to meet its financial obligations to us, we record an allowance to reduce the receivable to the amount we reasonably believe we will be able to collect from the customer. For all other customers, we record an allowance based upon the amount of time the receivables are past due. If actual accounts receivable collections differ from these estimates, an adjustment to the allowance may be necessary with a resulting effect on operating expense.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Impairment of Long-lived Assets

As of December 31, 2004, goodwill was $5.1 million ($4.2 million related to the FabTech acquisition, and $0.9 million related to Diodes-China). Beginning in fiscal 2002 with the adoption of SFAS No. 142 (*"Goodwill and Other Intangible Assets"*), goodwill is no longer amortized, but instead tested for impairment at least annually. As a result of the Company's adoption of SFAS No. 142, an independent appraiser hired by the Company performed the required impairment tests of goodwill annually and has determined that the goodwill is fully recoverable.

We assess the impairment of long-lived assets, including goodwill, on an ongoing basis and whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Our impairment review process is based upon (i) an income approach from a discounted cash flow analysis, which uses our estimates of revenues, costs and expenses, as well as market growth rates, and (ii) a market multiples approach which measures the value of an asset through an analysis of recent sales or offerings or comparable public entities. If ever the carrying value of the goodwill is determined to be less than the fair value of the underlying asset, a write-down of the asset will be required, with the resulting expense charged in the period that the impairment was determined.

Results of Operations

The following table sets forth, for the periods indicated, the percentage that certain items in the statement of income bear to net sales and the percentage dollar increase (decrease) of such items from period to period.

	Percent of Net Sales Year Ended December 31,					Percentage Dollar Increase (Decrease) Year Ended December 31,			
	2000	2001	2002	2003	2004	'00 to '01	'01 to '02	'02 to '03	'03 to '04
Net sales	100.0 %	100.0 %	100.0 %	100.0 %	100.0 %	(19.7) %	24.3 %	18.2 %	35.6 %
Cost of goods sold	(67.8)	(84.8)	(76.9)	(73.3)	(67.3)	0.5	12.8	12.6	24.5
Gross profit	32.2	15.2	23.1	26.7	32.7	(62.1)	88.4	36.8	66.3
Operating expenses [1]	(16.3)	(15.4)	(15.4)	(16.6)	(14.5)	(24.5)	24.0	27.8	18.8
Income (loss) from operations	15.9	(0.2)	7.7	10.1	18.2	(100.7)	6,893.2	54.5	143.9
Interest expense, net	(0.8)	(2.2)	(1.0)	(0.6)	(0.3)	120.6	(43.0)	(27.3)	(25.9)
Other income (expense)	0.4	0.8	0.1	0.0	(0.2)	56.7	(91.5)	(107.5)	8,260.0
Income (loss) before taxes and minority interest	15.5	(1.6)	6.8	9.5	17.7	(107.9)	652.5	65.5	152.0
Income tax benefit (provision)	(2.2)	1.9	(1.5)	(1.8)	(3.5)	(29.1)	(2.3)	42.3	164.8
Minority interest	(0.6)	(0.2)	(0.3)	(0.3)	(0.4)	(65.1)	42.9	36.3	54.9
Net income	12.7	0.1	5.0	7.4	13.8	(99.2)	4,578.9	74.0	153.1

(1) Operating expenses include loss on sale and impairment of fixed assets of $43,000, $1,037,000 and $14,000 in 2002, 2003 and 2004, respectively.

The following discussion explains in greater detail the consolidated financial condition of the Company. This discussion should be read in conjunction with the consolidated financial statements and notes thereto appearing elsewhere herein. Earnings per share discussion reflects three-for-two stock split in November 2003. All per share amounts have been adjusted to reflect the stock split.

Year 2004 Compared to Year 2003

Net sales for 2004 increased $48.8 million to $185.7 million from $136.9 million for 2003. The 35.6% increase was due primarily to an approximately 40.0% increase in units sold as a result of increased demand for the Company's products, as well as a more favorable pricing environment compared to 2003. In 2004, average selling prices ("ASPs") for discrete products increased approximately 1% while ASPs for wafers fell approximately 9%; consequently, overall ASPs decreased approximately 3% from 2003.

Cost of goods sold increased $24.6 million, or 24.5%, for 2004 compared to 2003. As a percent of sales, cost of goods sold decreased from 73.3% for 2003 to 67.3% for 2004. The Company's average unit cost ("AUP") for discrete devices decreased approximately 7% from 2003, and AUPs for wafer products decreased approximately 12%. These cost decreases were due primarily to improved manufacturing efficiencies.

Gross profit for 2004 increased 66.3% to $60.7 million from $36.5 million for 2003. Of the $24.2 million increase, $13.0 million was due to the 600 basis point increase in gross profit margin from 26.7% in 2003 to 32.7% in 2004, while $11.2 million was due to the 35.6% increase in net sales. Gross profit increases in Asia were the primary contributor to the gross profit increase in 2004. Gross profit margin in the both the third and fourth quarter of 2004 increased to 33.9% due to enhanced capacity utilization, continuing manufacturing efficiencies, relatively stable pricing, and a product mix that continues to shift towards higher-value performance discretes and arrays.

For 2004, selling, general and administrative expenses ("SG&A") increased $3.9 million to $23.5 million from $19.6 million for 2003. The 20.0% increase in SG&A was due primarily to higher sales commissions, incentives, marketing and royalty expenses associated with the 35.6% increase in sales, and higher labor and benefit expenses. Also contributing to the increased SG&A were higher corporate and administrative expenses, including legal and accounting fees associated with Sarbanes-Oxley compliance. However, as a percentage of sales, SG&A decreased to 12.7% for 2004 from 14.3% last year.

Research and development expenses ("R&D") increased to $3.4 million, or 1.8% of sales, in 2004 from $2.0 million, or 1.5% of sales, in 2003. R&D expenses are primarily related to new product development at the silicon wafer level, and, to a lesser extent, at the packaging level. We continue to seek to hire qualified engineers who fit our focus on next-generation discrete processes and packaging technologies. Our goal is to expand R&D to 3% of revenue as we bring proprietary technology and advanced devices to the market.

Net interest expense for 2004 decreased $223,000 to $637,000 from $860,000 in 2003, due primarily to a decrease in the use of the Company's credit facilities, as well as lower interest rates. In 2004, the Company paid down $3.6 million on its credit facilities, reducing the balance from $21.1 million to $17.5 million.

Other expense for 2004 increased $413,000 compared to last year, primarily due to approximately $400,000 in currency exchange losses related to the weakened U.S. dollar, primarily versus the Taiwan dollar recorded in the fourth quarter of 2004.

The effective tax rate in 2004 was 19.9% compared to 18.9% in 2003. The Company recorded a provision for income taxes in the amount of $6.5 million for the year 2004, compared to $2.5 million for 2003. Included in the tax provision in 2004 is $1.3 million in deferred taxes recorded in the fourth quarter for a minimum $8 million planned foreign dividend distribution in 2005 under the American Jobs Creation Act of 2004, offset by a $1.2 million foreign investment tax refund (net of U.S. taxes), and a $0.5 million research and development tax credit.

The minority interest in joint venture represents the minority investor's share of the Diodes-China and Diodes-Shanghai joint venture's income for the period. The increase in the joint venture earnings for 2004 is primarily the result of increased sales of higher margin products. The joint venture investment is eliminated in consolidation of the Company's financial statements, and the activities of Diodes-China and Diodes-Shanghai are included therein. As of December 31, 2004, the Company had a 95% controlling interest in the joint ventures.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The Company generated net income of $25.6 million (or $1.91 basic earnings per share and $1.65 diluted earnings per share) in 2004, as compared to $10.1 million (or $0.79 basic earnings per share and $0.70 diluted earnings per share) for 2003. This 153% increase is due primarily to the 35.6% sales increase at gross profit margins of 32.7% compared to gross profit margins of 26.7% in 2003.

Year 2003 Compared to Year 2002

Net sales for 2003 increased $21.1 million to $136.9 million from $115.8 million for 2002. The 18.2% increase was due primarily to a 19.5% increase in units sold as a result of increased demand for the Company's products, as well as a more favorable pricing environment compared to 2002. In 2003, ASPs for discrete products increased 4% while ASPs for wafers fell 7%; consequently, overall ASPs decreased 1%.

Gross profit for 2003 increased 36.8% to $36.5 million from $26.7 million for 2002. Of the $9.8 million increase, $5.0 million was due to the increase in gross profit margin from 23.1% in 2002 to 26.7% in 2003, while $4.8 million was due to the 18.2% increase in net sales. Gross profit increases in Asia were the primary contributor to the gross profit increase in 2003. Gross profit margin in the fourth quarter of 2003 increased to 29.5% due to increased capacity utilization, continuing manufacturing efficiencies, relatively stable pricing, and a product mix that continues to shift towards higher-value performance discretes and arrays.

For 2003, SG&A increased $3.4 million to $19.6 million from $16.2 million for 2002. The 20.7% increase in SG&A was due primarily to higher sales commissions associated with the 18.2% increase in sales, and higher labor benefits expenses. Also contributing to the increased SG&A were higher corporate and administrative expenses, including legal and accounting fees associated with Sarbanes-Oxley compliance. SG&A, as a percentage of sales, increased to 14.3% for 2003 from 14.0% in 2002.

R&D expenses increased to $2.0 million, or 1.5% of sales, in 2003 from $1.5 million, or 1.3% of sales, in 2002. R&D expenses are primarily related to new product development at the silicon wafer level, and, to a lesser extent, at the packaging level.

In 2003, operating profit margins were negatively affected by a $1.0 million reserve for fixed asset impairment, primarily as a result of the re-engineering of our wafer production lines. During the year, we took advantage of opportunities to purchase more efficient equipment at discounts. As a result, we retired un-depreciated equipment that was replaced.

Net interest expense for 2003 decreased $323,000 to $860,000 from $1.2 million in 2002, due primarily to a decrease in the use of the Company's credit facilities, as well as lower interest rates. In 2003, the Company paid down $5.8 million on its long-term debt, reducing the balance, net of current portion from $12.6 million to $6.8 million.

Other expense for 2003 increased $72,000 compared to last year, primarily due to the discontinuance of income Diodes-FabTech was receiving from an external company's use of its testing facilities in 2002, a decrease in high-technology grant income received at Diodes-China in 2003, and currency exchange losses primarily in Asia in 2003, partly offset by a severance payment in accordance with the terms of a separation agreement in 2002, as well as the reduction in the expense recorded for the management incentive agreement at Diodes-FabTech in 2003.

The effective tax rate in 2003 was 18.9% compared to 22.0% in 2002, due primarily to a higher proportion of income earned by our Asian subsidiaries in lower tax jurisdictions. The Company is benefiting from its Diodes-Hong Kong subsidiary, established in 2002, not only due to its lower tax rates, but also as another entry point into the Asia market. The Company recorded a provision for income taxes in the amount of $2.5 million for the year 2003, compared to $1.7 million for 2002. Included in the tax provision in 2003 is $840,000 in deferred taxes recorded for a portion of the 2003 earnings at Diodes-China, and $200,000 for a portion of the 2003 earnings at Diodes-Hong Kong.

The minority interest in joint venture represents the minority investor's share of the Diodes-China joint venture's income for the period. The increase in the joint venture earnings for 2003 is primarily the result of increased sales. The joint venture investment is eliminated in consolidation of the Company's financial statements, and the activities of Diodes-China are included therein. As of December 31, 2003, the Company had a 95% controlling interest in the joint venture.

The Company generated net income of $10.1 million (or $0.79 basic earnings per share and $0.70 diluted earnings per share) in 2003, as compared to $5.8 million (or $0.47 basic earnings per share and $0.44 diluted earnings per share) for 2002. This 74.0% increase is due primarily to the 18.2% sales increase at gross profit margins of 26.7% compared to gross profit margins of 23.1% in 2002.

Financial Condition

Liquidity and Capital Resources

The Company's liquidity requirements arise from the funding of its working capital needs, primarily inventory, work-in-process and accounts receivable, as well as capital expenditures. The Company's primary sources for working capital and capital expenditures are cash flow from operations and borrowings under the Company's bank credit facilities. Any withdrawal of support from its banks could have adverse consequences on the Company's liquidity. The Company's liquidity depends, in part, on customers paying within credit terms, and any extended delays in payments or changes in credit terms given to major customers may have an impact on the Company's cash flow. In addition, any abnormal product returns or pricing adjustments may also affect the Company's source of short-term funding.

At December 31, 2004 the Company had cash and cash equivalents totaling $19.0 million, an increase of $6.1 million from December 31, 2003. Cash provided by operating activities in 2004 was $29.3 million compared to $18.8 million in 2003 and $20.0 million in 2002. The primary sources of cash flows from operating activities in 2004 were net income of $25.6 million and depreciation and amortization of $13.2 million. The primary sources in 2003 were depreciation and amortization of $11.1 million and net income of $10.1 million. The primary sources of cash flows from operating activities in 2002 were depreciation and amortization of $9.7 million and net income of $5.8 million. The primary use of cash flows from operating activities in 2004 was an increase in accounts receivable of $13.2 million and an increase of inventory of $6.1 million. The primary use of cash flows from operating activities in 2003 was an increase in accounts receivable of $8.5 million. The primary use of cash flows from operating activities in 2002 was an increase in accounts receivable of $4.8 million.

For the year ended December 31, 2004, accounts receivable increased 43.2% compared to the 35.6% increase in sales, as days sales outstanding increased from 70 to 82 days due primarily to a trend in longer payment terms, primarily from Far East customers as well as major distributors. The Company continues to closely monitor its credit terms, while at times providing extended terms as required. The ratio of the Company's current assets to current liabilities on December 31, 2004 was 2.16 to 1, compared to a ratio of 1.67 to 1 and 1.69 to 1 as of December 31, 2003 and 2002, respectively.

Cash used by investing activities was $26.1 million in 2004, compared to $15.3 million in 2003 and $6.8 million in 2002. The primary investments were for additional manufacturing equipment and expansion at the Diodes-China and Diodes-Shanghai manufacturing facilities, and to a lesser extent, for capacity increases at Diodes-FabTech.

On December 1, 2000, the Company purchased all the outstanding capital stock of FabTech Incorporated, a 5-inch wafer foundry located in Lee's Summit, Missouri from LSC, the Company's largest stockholder. The acquisition purchase price consisted of approximately $5 million in cash, plus FabTech was obligated to repay an aggregate of approximately $19 million of debt, consisting of (i) an approximately $13.6 million note payable to LSC, (ii) an approximately $2.6 million note payable to the Company, and (iii) an approximately $3.0 million note payable to a financial institution (which was repaid on December 4, 2000 with the proceeds of a capital contribution by the Company). The acquisition was financed internally and through bank credit facilities.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

In June 2001, according to the Company's U.S. bank covenants, Diodes-FabTech was not permitted to make regularly scheduled principal and interest payments to LSC on the remaining $10.0 million payable related to the FabTech acquisition note, but was, however, able to renegotiate with LSC the terms of the note. Under the terms of the amended and restated subordinated promissory note, monthly payments of approximately $417,000 plus interest were scheduled to begin again in July 2002, provided the Company met the terms of its U.S. bank's covenants. In May 2002, the Company renegotiated the terms of the note with LSC to extend the payment period from two years to four years, and accordingly, monthly payments of approximately $208,000 plus interest began in July 2002.

Cash provided by financing activities was $2.2 million in 2004, compared to $1.9 million in 2003, and cash used by financing activities of $14.0 million in 2002. The primary source of cash in 2004 was the receipt of $5.8 million from stock option exercises. At December 31, 2004, the Company's total bank credit facility of $46.5 million encompasses one major U.S. bank, three banks in Mainland China and five in Taiwan. As of December 31, 2004, the total credit lines were $12.5 million, $25.0 million, and $9.0 million, for the U.S. facility secured by substantially all assets, the unsecured Chinese facilities, and the unsecured Taiwanese facilities, respectively. As of December 31, 2004, the available credit was $5.1 million, $19.0 million, and $9.0 million, for the U.S. facility, the Chinese facilities, and the Taiwanese facilities, respectively.

In February 2003, the Company and its U.S. bank renewed its $7.5 million revolving credit line, extending it for two years. In July 2004, Diodes-FabTech obtained a $5.0 million credit facility to be used for capital expenditure requirements at its wafer fabrication facility. This $5.0 million facility brought the Company's total credit facility to $46.5 million, with the total available and unused credit at December 31, 2004 of $32.3 million.

The credit agreements have certain covenants and restrictions, which, among other matters, require the maintenance of certain financial ratios and operating results, as defined in the agreements, and prohibit the payment of dividends. The Company was in compliance with its covenants as of December 31, 2004.

The Company has used its credit facilities primarily to fund the capacity expansion at Diodes-China and Diodes-Shanghai and to a lesser extent Diodes-FabTech, as well as for the FabTech acquisition, and to support all operations. The Company believes that the continued availability of these credit facilities, together with internally generated funds, will be sufficient to meet the Company's current foreseeable operating cash requirements.

The Company had entered into an interest rate swap agreement with a major U.S. bank which expired November 30, 2004, to hedge its exposure to variability in expected future cash flows resulting from interest rate risk related to a portion of its long-term debt. The interest rate under the swap agreement was fixed at 6.8% and is based on the notional amount. The swap contract was inversely correlated to the related hedged long-term debt and was therefore considered an effective cash flow hedge of the underlying long-term debt. The level of effectiveness of the hedge is measured by the changes in the market value of the hedged long-term debt resulting from fluctuation in interest rates. As a matter of policy, the Company does not enter into derivative transactions for trading or speculative purposes.

Total working capital increased 82.6% to $49.6 million as of December 31, 2004, from $27.2 million as of December 31, 2003. The Company believes that such working capital position will be sufficient for foreseeable operations and growth opportunities. The Company's total debt to equity ratio improved to 0.50 at December 31, 2004, from 0.73 at December 31, 2003. It is anticipated that this ratio may increase should the Company use its credit facilities to fund additional inventory sourcing opportunities.

The Company has no material plans or commitments for capital expenditures other than in connection with manufacturing expansion at Diodes-China, Diodes-Shanghai and Diodes-FabTech. However, to ensure

that the Company can secure reliable and cost effective inventory sourcing to support and better position itself for growth, the Company is continuously evaluating additional internal manufacturing expansion, as well as additional outside sources of products. The Company believes its financial position will provide sufficient funds should an appropriate investment opportunity arise and thereby, assist the Company in improving customer satisfaction and in maintaining or increasing market share. Based upon plans for new product introductions, product mixes, capacity restraints on certain product lines and equipment upgrades, the Company anticipates that year 2005 capital expenditures for the manufacturing facilities will be $12-16 million.

Off-Balance Sheet Arrangements

The Company does not have any transactions, arrangements and other relationships with unconsolidated entities that will affect our liquidity or capital resources. We have no special purpose entities that provided off-balance sheet financing, liquidity or market or credit risk support, nor do we engage in leasing, hedging (except for the interest rate swap agreement), or research and development services, that could expose us to liability that is not reflected on the face of the financial statements.

Contractual Obligations

The following table represents the Company's contractual obligations as of December 31, 2004:

	Payments due by period (in thousands)				
Contractual Obligations	*Total*	*Less than 1 year*	*1-3 years*	*3-5 years*	*More than 5 years*
Long-term debt	$11,347	$ 3,514	$ 7,250	$ 583	$ 0
Capital leases	2,777	230	460	460	1,627
Operating leases	13,498	3,461	6,420	3,617	0
Purchase obligations	2,927	2,927	0	0	0
Total obligations	$30,549	$10,132	$14,130	$4,660	$1,627

Inflation did not have a material effect on net sales or net income in fiscal years 2002 through 2004. A significant increase in inflation could affect future performance.

Recently Issued Accounting Pronouncements and Proposed Accounting Changes

In November 2004, the Emerging Issues Task Force (EITF) reached a consensus on EITF Issue No. 03-13, *Applying the Conditions in Paragraph 42 of FASB Statement No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," in Determining Whether to Report Discontinued Operations*. The consensus provides guidance in determining: (a) which cash flows should be taken into consideration when assessing whether the cash flows of the disposal component have been or will be eliminated from the ongoing operations of the entity, (b) the types of involvement ongoing between the disposal component and the entity disposing of the component that constitute continuing involvement in the operations of the disposal component, and (c) the appropriate (re)assessment period for purposes of assessing whether the criteria in paragraph 42 have been met. The consensus was ratified by the FASB at their November 30, 2004 meeting and should be applied to a component of an enterprise that is either disposed of or classified as held for sale in fiscal periods beginning after December 15, 2004. The Company does not anticipate a material impact on the financial statements from the adoption of this consensus.

In December 2004, the FASB issued FASB Statement No. 153, *Exchanges of Nonmonetary Assets – An Amendment of APB Opinion No. 29*. The amendments made by Statement No. 153 are based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the narrow exception for nonmonetary exchanges of similar productive assets and replace it with a broader exception for exchanges of nonmonetary assets that do not have "commercial substance." The provisions in Statement No. 153 are effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Adoption of this standard is not expected have a material impact on the consolidated financial statements.

In September 2004, the EITF reached a consensus on EITF Issue No. 04-10, *Applying Paragraph 19 of FAS 131 in Determining Whether to Aggregate Operating Segments That Do Not Meet the Quantitative Thresholds*. The consensus states that operating segments that do not meet the quantitative thresholds can be aggregated only if aggregation is consistent with the objective and basic principles of SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*, the segments have similar economic characteristics, and the segments share a majority of the aggregation criteria (a)-(e) listed in paragraph 17 of SFAS No. 131. The effective date of the consensus in this Issue is for fiscal years ending after October 13, 2004. If the Financial Accounting Standards Board (FASB) ratifies EITF Issue No. 04-10, the Company does not anticipate a material impact on the financial statements.

In March 2004, the EITF reached a consensus on the remaining portions of EITF 03-01, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* with an effective date of June 15, 2004. EITF 03-01 provides new disclosure requirements for other-than-temporary impairments on debt and equity investments. Investors are required to disclose quantitative information about: (i) the aggregate amount of unrealized losses, and (ii) the aggregate related fair values of investments with unrealized losses, segregated into time periods during which the investment has been in an unrealized loss position of less than 12 months and greater than 12 months. In addition, investors are required to disclose the qualitative information that supports their conclusion that the impairments noted in the qualitative disclosure are not other-than temporary. The Company determined that EITF 03-01 would not have a material impact on the financial statements.

In January 2003, the FASB issued Interpretation No. 46, *Consolidation of Variable Interest Entities – an Interpretation of ARB No. 51*, which provides guidance on the identification of and reporting for variable interest entities. Interpretation No. 46 expands the criteria for consideration in determining whether a variable interest Interpretation No. 46 is effective immediately for variable interest entities created after January 31, 2003, and to variable interest entities in which an enterprise obtains an interest after that date. Interpretation No. 46 was effective for the Company in 2004 because the Company entered into a joint venture for Diodes-Shanghai. The Company has a 95% interest. The Interpretation requires unconsolidated variable interest entities to be consolidated by their primary beneficiaries. The primary beneficiary is the party that assumes the majority of the risk, which includes, but is not limited to, the entity's expected losses. Management concluded that its investment in Diodes-Shanghai did not meet the criteria for consolidation under the standard. Based upon our review, we concluded that management's analysis and the conclusions contained therein appeared reasonable.

In December 2004, the FASB also issued SFAS No. 151, "*Inventory Costs, an amendment of ARB No. 43, Chapter 4*," which will become effective for the Company beginning January 1, 2006. This standard clarifies that abnormal amounts of idle facility expense, freight, handling costs and wasted material should be expensed as incurred and not included in overhead. In addition, this standard requires that the allocation of fixed production overhead costs to inventory be based on the

normal capacity of the production facilities. The Company is currently evaluating the potential impact of this standard on its financial position and results of operations, but does not believe the impact of the change will be material.

On October 22, 2004, a new tax law was passed, the American Jobs Creation Act of 2004 (the "Jobs Creation Act"), which raised a number of issues with respect to accounting for income taxes. In response, on December 21, 2004, the FASB issued two FASB Staff Positions (FSP), FSP 109-1 – "*Application of FASB Statement No. 109, Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004*" and FSP 109-2 – "*Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004*," which became effective for the Company upon issuance.

The Jobs Creation Act provides a deduction for income from qualified domestic production activities, to be phased in from 2005 through 2010, which is intended to replace the existing extra-territorial income exclusion for foreign sales. In FSP 109-1, the FASB decided the deduction for qualified domestic production activities should be accounted for as a special deduction under SFAS No. 109, rather than as a rate reduction. Accordingly, any benefit from the deduction will be reported in the period in which the deduction is claimed on the tax return and no adjustment to deferred taxes at December 31, 2004, is required.

The Jobs Creation Act also creates a temporary incentive for U.S. corporations to repatriate accumulated income earned abroad by providing an 85 percent dividends received deduction for certain dividends from controlled foreign corporations. The deduction is subject to a number of limitations and uncertainty remains as to how to interpret numerous provisions in the Act. FSP 109-2 addresses when to reflect in the financial statements the effects of the one-time tax benefit on the repatriation of foreign earnings. Under SFAS No. 109, companies are normally required to reflect the effect of new tax law changes in the period of enactment. FSP 109-2 provides companies additional time to determine the amount of earnings, if any, that they intend to repatriate under the Jobs Creation Act's provisions. See Note 8 for more discussion of the impact of the Jobs Creation Act, including the Company's status on the repatriation of foreign earnings.

In December 2004, the FASB issued SFAS No. 123(R). This new standard requires companies to adopt the fair value methodology of valuing stock-based compensation and recognizing that valuation in the financial statements from the date of grant. Accordingly, the adoption of SFAS No. 123(R)'s fair value method will have a significant impact on the Company's results of operations, although it will have no impact on the Company's overall financial position. The impact of adoption of SFAS No. 123(R) cannot be predicted at this time because it will partially depend on levels of share-based payments granted in the future. However, had the Company adopted SFAS No. 123(R) in prior periods, the impact of that standard would have approximated the impact of SFAS No. 123 as shown in the Stock-based Compensation table (see Note 1). SFAS No. 123(R) also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under current literature. The Company is currently evaluating several option valuation models in order to calculate the required compensation expense. The Company has elected to adopt the provisions of SFAS No. 123(R) on a modified prospective application method effective July 1, 2005, with no restatement of any prior periods. SFAS No. 123(R) is effective for the Company as of the beginning of the first interim reporting period that begins after June 15, 2005.

CONSOLIDATED BALANCE SHEETS

December 31,	2003	2004
Assets		
Current Assets		
Cash	$ 12,847,000	$ 18,970,000
Accounts receivable		
Trade customers	27,010,000	38,682,000
Related parties	3,938,000	5,526,000
	30,948,000	44,208,000
Allowance for doubtful accounts	(375,000)	(432,000)
	30,573,000	43,776,000
Inventories	16,164,000	22,238,000
Deferred income taxes, current	5,547,000	2,453,000
Prepaid expenses and other	2,256,000	4,243,000
Prepaid income taxes	446,000	406,000
Total current assets	67,833,000	92,086,000
Property, Plant and Equipment, net	47,893,000	60,857,000
Deferred Income Taxes, non-current	1,816,000	7,970,000
Other Assets		
Goodwill	5,090,000	5,090,000
Other	1,163,000	1,798,000
Total assets	$123,795,000	$167,801,000
Liabilities and Stockholders' Equity		
Current Liabilities		
Line of credit	$ 8,488,000	$ 6,167,000
Accounts payable		
Trade	14,029,000	17,274,000
Related parties	3,453,000	3,936,000
Accrued liabilities	8,715,000	11,459,000
Current portion of long-term debt		
Related party	2,500,000	2,500,000
Others	3,333,000	1,014,000
Current portion of capital lease obligations	161,000	165,000
Total current liabilities	40,679,000	42,515,000
Long-Term Debt, net of current portion		
Related party	3,750,000	1,250,000
Others	3,000,000	6,583,000
Capital Lease Obligations, net of current portion	2,334,000	2,172,000
Minority Interest in Joint Venture	2,582,000	3,133,000
Stockholders' Equity		
Class A convertible preferred stock – par value $1.00 per share; 1,000,000 shares authorized; no shares issued and outstanding	–	–
Common stock – par value $0.66 2⁄3 per share; 30,000,000 shares authorized; 14,627,284 and 15,763,266 shares issued at 2003 and 2004, respectively	6,502,000	7,260,000
Additional paid-in capital	11,192,000	24,765,000
Retained earnings	55,779,000	81,330,000
	73,473,000	113,355,000
Less:		
Treasury stock – 1,613,508 shares of common stock, at cost	1,782,000	1,782,000
Accumulated other comprehensive loss (gain)	241,000	(575,000)
	2,023,000	1,207,000
Total stockholders' equity	71,450,000	112,148,000
Total liabilities and stockholders' equity	$123,795,000	$167,801,000

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

Diodes Incorporated and Subsidiaries

CONSOLIDATED STATEMENTS OF INCOME

Years ended December 31,	*2002*	*2003*	*2004*
Net Sales	$115,821,000	$136,905,000	$185,703,000
Cost of Goods Sold	89,111,000	100,377,000	124,968,000
Gross profit	26,710,000	36,528,000	60,735,000
Operating Expenses			
Selling, general and administrative	16,228,000	19,586,000	23,503,000
Research and development	1,472,000	2,049,000	3,422,000
Impairment of fixed assets	–	1,000,000	–
Loss on disposal of fixed assets	43,000	37,000	14,000
Total operating expenses	17,743,000	22,672,000	26,939,000
Income from operations	8,967,000	13,856,000	33,796,000
Other Income (Expenses)			
Interest expense, net	(1,183,000)	(860,000)	(637,000)
Other	67,000	(5,000)	(418,000)
Total other expenses	(1,116,000)	(865,000)	(1,055,000)
Income before income taxes and minority interest	7,851,000	12,991,000	32,741,000
Income Tax Provision	(1,729,000)	(2,460,000)	(6,514,000)
Income before minority interest	6,122,000	10,531,000	26,227,000
Minority Interest in Earnings of Joint Venture	(320,000)	(436,000)	(676,000)
Net Income	$ 5,802,000	$ 10,095,000	$ 25,551,000
Earnings Per Share			
Basic	$ 0.47	$ 0.79	$ 1.91
Diluted	$ 0.44	$ 0.70	$ 1.65
Number of shares used in computation			
Basic	12,276,899	12,730,808	13,404,276
Diluted	13,297,490	14,406,054	15,471,438

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

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

Years ended December 31, 2002, 2003, and 2004	*Common Stock*							
	Shares	*Shares in Treasury*	*Amount*	*Common Stock in Treasury*	*Additional Paid-in Capital*	*Retained Earnings*	*Accumulated Other Compre-hensive Gain (Loss)*	*Total*
Balance, December 31, 2001	13,841,496	1,613,508	$6,151,000	$(1,782,000)	$ 7,310,000	$39,882,000	$(437,000)	$ 51,124,000
Comprehensive income, net of tax:								
Net income for the year ended December 31, 2002						5,802,000		5,802,000
Translation adjustments							(40,000)	(40,000)
Change in unrealized loss on derivative instruments, net of tax of $400							(1,000)	(1,000)
Total comprehensive income								5,761,000
Management fee from LSC					375,000			375,000
Exercise of stock options including $98,000 income tax benefit	97,650	–	44,000	–	375,000	–	–	419,000
Balance, December 31, 2002	13,939,146	1,613,508	$6,195,000	$(1,782,000)	$ 8,060,000	$45,684,000	$(478,000)	$ 57,679,000
Comprehensive income, net of tax:								
Net income for the year ended December 31, 2003						10,095,000		10,095,000
Translation adjustments							169,000	169,000
Change in unrealized loss on derivative instruments, net of tax of $27,000							68,000	68,000
Total comprehensive income								10,332,000
Management fee from LSC					286,000			286,000
Exercise of stock options including $1,139,000 income tax benefit	688,138	–	307,000	–	2,846,000	–	–	3,153,000
Balance, December 31, 2003	14,627,284	1,613,508	$6,502,000	$(1,782,000)	$11,192,000	$ 55,779,000	$(241,000)	$ 71,450,000
Comprehensive income, net of tax:								
Net income for the year ended December 31, 2004						25,551,000		25,551,000
Translation adjustments							793,000	793,000
Change in unrealized loss on derivative instruments, net of tax of $9,000							23,000	23,000
Total comprehensive income								26,367,000
Management fee from LSC					180,000			180,000
Exercise of stock options including $8,514,000 income tax benefit	1,135,982	–	758,000	–	13,393,000	–	–	14,151,000
Balance, December 31, 2004	15,763,266	1,613,508	$7,260,000	$(1,782,000)	$24,765,000	$81,330,000	$ 575,000	$112,148,000

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

Diodes Incorporated and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31,	2002	2003	2004
Cash Flows From Operating Activities			
Net income	$ 5,802,000	$ 10,095,000	$ 25,551,000
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	9,747,000	11,073,000	13,173,000
Minority interest earnings	320,000	436,000	676,000
Loss on impairment and disposal of property, plant and equipment	43,000	1,037,000	14,000
Changes in operating assets and liabilities			
Accounts receivable	(4,779,000)	(8,490,000)	(13,203,000)
Inventories	2,139,000	(1,248,000)	(6,074,000)
Prepaid expenses and other	(711,000)	(388,000)	(2,474,000)
Deferred income taxes	646,000	270,000	5,463,000
Accounts payable	3,153,000	5,082,000	3,728,000
Accrued liabilities	3,481,000	–	1,468,000
Income taxes payable	149,000	954,000	978,000
Net cash provided by operating activities	19,990,000	18,821,000	29,300,000
Cash Flows From Investing Activities			
Purchases of property, plant and equipment	(6,777,000)	(15,646,000)	(26,201,000)
Proceeds from sales of property, plant and equipment	3,000	357,000	68,000
Net cash used by investing activities	(6,774,000)	(15,289,000)	(26,133,000)
Cash Flows From Financing Activities			
Advances (repayments) on line of credit, net	(3,478,000)	5,463,000	(2,321,000)
Net proceeds from the issuance of common stock	321,000	2,014,000	5,628,000
Management incentive reimbursement from LSC	375,000	375,000	375,000
Proceeds from long-term debt	–	–	3,583,000
Repayments of long-term debt	(11,080,000)	(5,833,000)	(4,819,000)
Minority shareholder investment in subsidiary	–	–	175,000
Repayments of capital lease obligations	(133,000)	(157,000)	(158,000)
Dividend to minority shareholders	–	–	(300,000)
Net cash provided (used) by financing activities	(13,995,000)	1,862,000	2,163,000
Effect of Exchange Rate Changes on Cash and Cash Equivalents	(40,000)	169,000	793,000
Increase (Decrease) in Cash	(819,000)	5,563,000	6,123,000
Cash, beginning of year	8,103,000	7,284,000	12,847,000
Cash, end of year	$ 7,284,000	$ 12,847,000	$ 18,970,000
Supplemental Disclosure of Cash Flow Information			
Cash paid during the year for:			
Interest	$ 1,229,000	$ 876,000	$ 683,000
Income taxes	$ 965,000	$ 999,000	$ 2,504,000
Non-cash activities:			
Tax benefit related to stock options credited to paid-in capital	$ 98,000	$ 1,139,000	$ 8,514,000
Building acquired through capital lease obligation	$ 2,785,000	$ –	$ –

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

Note 1 – Summary of Operations and Significant Accounting Policies

Nature of operations – Diodes Incorporated and its subsidiaries manufacture and distribute discrete semiconductor devices to manufacturers in the communications, computing, industrial, consumer electronics and automotive markets. The Company's products include small-signal transistors and MOSFETs, transient voltage suppressors (TVSs), zeners, Schottkys, diodes, rectifiers, bridges and silicon wafers. The products are sold primarily throughout North America, Asia and Europe.

Principles of consolidation – The consolidated financial statements include the accounts of the parent company, Diodes Incorporated (Diodes-North America), its wholly-owned subsidiaries; Diodes Taiwan Corporation, Ltd. (Diodes-Taiwan), Diodes Hong Kong, Ltd. (Diodes-Hong Kong) and FabTech, Inc. (FabTech or Diodes-FabTech); and its majority (95%) owned subsidiaries, Shanghai KaiHong Electronics Co., Ltd. (Diodes-China) and Diodes Shanghai Company, Ltd. (Diodes-Shanghai). All significant intercompany balances and transactions have been eliminated in consolidation.

Revenue recognition – Revenue is recognized when there is persuasive evidence that an arrangement exists, when delivery has occurred, when our price to the buyer is fixed or determinable and when collectibility of the receivable is reasonably assured. These elements are met when title to the products is passed to the buyers, which is generally when our product is shipped to both original equipment manufacturers (OEMs) and electronics component distributors. The Company reduces revenue in the period of sale for estimates of product returns and other allowances.

In 2003, Diodes-China received approximately $254,000 in high-technology grants as an incentive for further investment from the local Chinese government. The grants were unrestricted and available upon receipt to fund the operations of Diodes-China. The Company recognized this grant income when received and recorded them within "other income" on the accompanying statements of income. No grant income was received in 2004 and the Company does not expect this type of income in the future.

Product warranty – The Company generally warrants its products for a period of one year from the date of sale. Historically, warranty expense has not been significant.

Inventories – Inventories are stated at the lower of cost or market value. Cost is determined principally by the first-in, first-out method. On an on-going basis both finished goods inventory and raw material inventory is evaluated for obsolescence and slow-moving items. This evaluation includes analysis of sales levels, sales projections, and purchases by item, as well as raw material usage related to our manufacturing facilities. Based upon this analysis, as well as an inventory aging analysis, a reserve for obsolete and slow-moving inventory is accrued (see Note 2).

Property, plant and equipment – Property, plant and equipment are depreciated using straight-line and accelerated methods over the estimated useful lives, which range from 20 to 55 years for buildings and 3 to 10 years for machinery and equipment. Leasehold improvements are amortized using the straight-line method over 3 to 5 years (see Note 3).

Goodwill – Beginning in fiscal 2002 with the adoption of Statement of Financial Accounting Standards (SFAS) No. 142 (*"Goodwill and Other Intangible Assets"*), goodwill is no longer amortized, but instead tested for impairment at least annually. As a result of the Company's adoption of SFAS No. 142, an independent appraiser hired by the Company, performed the required impairment tests of goodwill as of January 1, 2004 and 2005, and has determined that the goodwill is fully recoverable. No goodwill was acquired or impaired during the years ended December 31, 2002, 2003 and 2004. As of December 31, 2004, goodwill for Diodes-FabTech and Diodes-China was $4.2 million and $0.9 million, respectively. Prior to fiscal 2002, goodwill was amortized using the straight-line method over its estimated period of benefit.

Impairment on long-lived assets – Certain long-lived assets of the Company are reviewed at least annually as to whether their carrying values have become impaired in accordance with SFAS No. 144, *"Accounting for the Impairment or Disposal of Long-Lived Assets."*

Management considers assets to be impaired if the carrying value exceeds the undiscounted projected cash flows from operations. If impairment exists, the assets are written down to fair value or the projected discounted cash flows from related operations. As of December 31, 2004, the Company expects the remaining carrying value of assets to be recoverable.

Income taxes – Income taxes are accounted for using an asset and liability approach whereby deferred tax assets and liabilities are recorded for differences in the financial reporting bases and tax bases of the Company's assets and liabilities (see Note 8).

Concentration of credit risk – Financial instruments, which potentially subject the Company to concentrations of credit risk, include trade accounts receivable. Credit risk is limited by the dispersion of the Company's customers over various geographic areas, operating primarily in the electronics manufacturing and distribution industries. The Company performs on-going credit evaluations of its customers and generally requires no collateral from its customers. Historically, credit losses have not been significant.

The Company currently maintains substantially all of its day-to-day operating cash balances with major financial institutions. Cash balances are usually in excess of Federal and/or foreign deposit insurance limits.

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

Stock split – On November 25, 2003, the Company affected a three-for-two stock split for shareholders of record as of November 14, 2003 in the form of a 50% stock dividend. All share and per share amounts in the accompanying financial statements and footnotes reflect the effect of this stock split.

Earnings per share – Earnings per share are based upon the weighted average number of shares of common stock and common stock equivalents outstanding, net of common stock held in treasury. Earnings per share is computed using the "treasury stock method" under the Financial Accounting Standards Board (FASB) Statement No. 128.

For the years ended December 31, 2002, 2003 and 2004, options outstanding for 824,000 shares, 1,195,000 shares, and 0 shares of common stock have been excluded from the computation of diluted earnings per share because their effect was anti-dilutive.

Year Ended December 31,	*2002*	*2003*	*2004*
Net income for earnings per share computation	$ 5,802,000	$10,095,000	$25,551,000
Basic			
Weighted average number of common shares outstanding during the year	12,276,899	12,730,808	13,404,276
Basic earnings per share	$ 0.47	$ 0.79	$ 1.91
Diluted			
Weighted average number of common shares outstanding used in calculating basic earnings per share	12,276,899	12,730,808	13,404,276
Add: additional shares issuable upon exercise of stock options	1,020,591	1,675,246	2,067,162
Weighted average number of common shares used in calculating diluted earnings per share	13,297,490	14,406,054	15,471,438
Diluted earnings per share	$ 0.44	$ 0.70	$ 1.65

Note 1 – Summary of Operations and Significant Accounting Policies *(continued)*

Stock-based compensation – The Company maintains stock-based compensation plans for its board of directors, officers, and key employees, which provide for non-qualified and incentive stock options. The plans are described more fully in Note 9. With the issuance in mid-December 2004 by FASB of SFAS No. 123(R), *"Share-Based Payments,"* which is a revision to SFAS No. 123, *"Accounting for Stock-Based Compensation,"* which was issued in 1995, the Company will begin reporting the fair value of stock-based compensation as an expense in its financial statements beginning in 2005 (see discussion in "Recently Issued Accounting Pronouncements and Proposed Accounting Changes" below). Prior to implementation of this new standard, the Company accounted for those plans under the recognition and measurement principles of APB Opinion No. 25, *"Accounting for Stock Issued to Employees,"* and related Interpretations. No compensation cost was reflected in net income for stock options, as all options granted under those plans have an exercise price equal to or greater than the market value of the underlying common stock on the date of the grant. As required by SFAS No. 148, *"Accounting for Stock-Based Compensation – Transition and Disclosure, an amendment of FASB Statement No. 123,"* the following table illustrates the effect on net income and earnings per common share as if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock-based compensation for each period presented:

For the years ended December 31,

		Amounts Per Share			*Amounts Per Share*			*Amounts Per Share*	
	2002	*Basic*	*Diluted*	*2003*	*Basic*	*Diluted*	*2004*	*Basic*	*Diluted*
Net income	$ 5,802,000	$ 0.47	$ 0.44	$10,095,000	$ 0.79	$ 0.70	$25,551,000	$ 1.91	$ 1.65
Deduct: stock-based compensation expense determined under fair value method, net of tax	(1,918,000)	(0.15)	(0.15)	(1,397,000)	(0.11)	(0.10)	(1,642,000)	(0.13)	(0.10)
Pro forma net income	$ 3,884,000	$ 0.32	$ 0.29	$ 8,698,000	$ 0.68	$ 0.60	$23,909,000	$ 1.78	$ 1.55

The pro forma information recognizes as compensation the value of stock options granted using the Black-Scholes option pricing model which takes into account as of the grant date, the exercise price and expected life of the option, the current price of underlying stock and its expected volatility, expected dividends on the stock, expected forfeitures and the risk-free interest rate for the term of the option. The following is the weighted average of the data used to calculate the estimated fair value:

December 31,	*Risk-free interest rate*	*Expected life*	*Expected volatility*	*Expected forfeitures*	*Expected dividends*
2004	3.64%	5.0 years	68.36%	2.64%	0%
2003	3.31%	5.0 years	66.18%	2.77%	0%
2002	4.03%	5.0 years	75.61%	2.77%	0%

The Company's valuations are based upon a single option valuation approach using the Black-Scholes option valuation model. The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options, which have no vesting restrictions and are fully transferable and negotiable in a free trading market. In addition, option valuation models require the input of highly subjective assumptions, including the expected stock price volatility and expected life of the option. Because the Company's stock options have characteristics significantly different from those of freely traded options, and changes in the subjective input assumptions can materially affect the Company's fair value estimate

of those stock options, in the Company's opinion, existing valuations models, including Black-Scholes, are not reliable single measures and may misstate the fair value of the Company's stock options. Because Company stock options do not trade on a secondary exchange, recipients can receive no value nor derive any benefit from holding stock options under these plans without an increase, above the grant price, in the market price of the Company's stock. Such an increase in stock price would benefit all stockholders commensurately.

Derivative financial instrument – The Company used an interest rate swap agreement to hedge its exposure to variability in expected future cash flows resulting from interest rate risk related to a portion of its long-term debt. The interest rate swap agreement applied to 25% of the Company's long-term debt and expired November 30, 2004. Market value of the swap as of December 31, 2003 and 2004 is included in *"Accumulated Other Comprehensive Loss"*. The swap contract is inversely correlated to the related hedged long-term debt and is therefore considered an effective cash flow hedge of the underlying long-term debt. The level of effectiveness of the hedge is measured by the changes in the market value of the hedged long-term debt resulting from fluctuation in interest rates. As a matter of policy, the Company does not enter into derivative transactions for trading or speculative purposes.

Functional currencies and foreign currency translation – Through its subsidiaries, the Company maintains operations in Taiwan, Hong Kong and China. The Company believes the New Taiwan ("NT") dollar as the functional currency at Diodes-Taiwan most appropriately reflects the current economic facts and circumstances of the operations. The Company continues to use the U.S. dollar as the functional currency in Diodes-China, Diodes-Shanghai and Diodes-Hong Kong, as substantially all monetary transactions are made in that currency, and other significant economic facts and circumstances currently support that position. As these factors may change in the future, the Company will periodically assess its position with respect to the functional currency of its foreign subsidiaries. Included in net income are foreign currency exchange losses of approximately $82,000, $115,000, and $424,000 for the years ended December 31, 2002, 2003 and 2004, respectively.

Comprehensive income – Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income. The components of other comprehensive income include foreign currency translation adjustments and changes in the unrealized loss on derivative instruments from swap liability.

Recently issued accounting pronouncements and proposed accounting changes – In November 2004, the Emerging Issues Task Force (EITF) reached a consensus on EITF Issue No. 03-13, *Applying the Conditions in Paragraph 42 of FASB Statement No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," in Determining Whether to Report Discontinued Operations*. The consensus provides guidance in determining: (a) which cash flows should be taken into consideration when assessing whether the cash flows of the disposal component have been or will be eliminated from the ongoing operations of the entity, (b) the types of involvement ongoing between the disposal component and the entity disposing of the component that constitute continuing involvement in the operations of the disposal component, and (c) the appropriate (re)assessment period for purposes of assessing whether the criteria in paragraph 42 have been met. The consensus was ratified by the FASB at their November 30, 2004 meeting and should be applied to a component of an enterprise that is either disposed of or classified as held for sale in fiscal periods beginning after December 15, 2004. The Company does not anticipate a material impact on the financial statements from the adoption of this consensus.

Note 1 – Summary of Operations and Significant Accounting Policies *(continued)*

In December 2004, the FASB issued FASB Statement No. 153, *Exchanges of Nonmonetary Assets – An Amendment of APB Opinion No. 29.* The amendments made by Statement No. 153 are based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the narrow exception for nonmonetary exchanges of similar productive assets and replace it with a broader exception for exchanges of nonmonetary assets that do not have "commercial substance." The provisions in Statement No. 153 are effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Adoption of this standard is not expected have a material impact on the consolidated financial statements.

In September 2004, the EITF reached a consensus on EITF Issue No. 04-10, *Applying Paragraph 19 of FAS 131 in Determining Whether to Aggregate Operating Segments That Do Not Meet the Quantitative Thresholds.* The consensus states that operating segments that do not meet the quantitative thresholds can be aggregated only if aggregation is consistent with the objective and basic principles of SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*, the segments have similar economic characteristics, and the segments share a majority of the aggregation criteria (a)-(e) listed in paragraph 17 of SFAS No. 131. The effective date of the consensus in this Issue is for fiscal years ending after October 13, 2004. If the Financial Accounting Standards Board (FASB) ratifies EITF Issue No. 04-10, the Company does not anticipate a material impact on the financial statements.

In March 2004, the EITF reached a consensus on the remaining portions of EITF 03-01, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments,* with an effective date of June 15, 2004. EITF 03-01 provides new disclosure requirements for other-than-temporary impairments on debt and equity investments. Investors are required to disclose quantitative information about: (i) the aggregate amount of unrealized losses, and (ii) the aggregate related fair values of investments with unrealized losses, segregated into time periods during which the investment has been in an unrealized loss position of less than 12 months and greater than 12 months. In addition, investors are required to disclose the qualitative information that supports their conclusion that the impairments noted in the qualitative disclosure are not other-than temporary. The Company determined that EITF 03-01 would not have a material impact on the financial statements.

In January 2003, the FASB issued Interpretation No. 46, *Consolidation of Variable Interest Entities – an Interpretation of ARB No. 51*, which provides guidance on the identification of and reporting for variable interest entities. Interpretation No. 46 expands the criteria for consideration in determining whether a variable interest Interpretation No. 46 is effective immediately for variable interest entities created after January 31, 2003, and to variable interest entities in which an enterprise obtains an interest after that date. Interpretation No. 46 was effective for the Company in 2004 because the Company entered into a joint venture for Diodes-Shanghai. The Company has a 95% interest. The Interpretation requires unconsolidated variable interest entities to be consolidated by their primary beneficiaries. The primary beneficiary is the party that assumes the majority of the risk, which includes, but is not limited to, the entity's expected losses. Management concluded that its investment in Diodes-Shanghai did not meet the criteria for consolidation under the standard. Based upon our review, we concluded that management's analysis and the conclusions contained therein appeared reasonable.

In December 2004, the FASB also issued SFAS No. 151, *"Inventory Costs, an amendment of ARB No. 43, Chapter 4,"* which will become effective for the Company beginning January 1, 2006. This standard clarifies that abnormal amounts of idle facility expense, freight, handling costs and wasted material should be expensed as incurred and not included in overhead. In addition, this standard requires that the allocation of fixed production overhead costs to inventory be based on the normal

capacity of the production facilities. The Company is currently evaluating the potential impact of this standard on its financial position and results of operations, but does not believe the impact of the change will be material.

On October 22, 2004, a new tax law was passed, the American Jobs Creation Act of 2004 (the "Jobs Creation Act"), which raised a number of issues with respect to accounting for income taxes. In response, on December 21, 2004, the FASB issued two FASB Staff Positions (FSP), FSP 109-1 – *"Application of FASB Statement No. 109, Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004*" and FSP 109-2 – *"Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004,"* which became effective for the Company upon issuance.

The Jobs Creation Act provides a deduction for income from qualified domestic production activities, to be phased in from 2005 through 2010, which is intended to replace the existing extra-territorial income exclusion for foreign sales. In FSP 109-1, the FASB decided the deduction for qualified domestic production activities should be accounted for as a special deduction under SFAS No. 109, rather than as a rate reduction. Accordingly, any benefit from the deduction will be reported in the period in which the deduction is claimed on the tax return and no adjustment to deferred taxes at December 31, 2004, is required.

The Jobs Creation Act also creates a temporary incentive for U.S. corporations to repatriate accumulated income earned abroad by providing an 85 percent dividends received deduction for certain dividends from controlled foreign corporations. The deduction is subject to a number of limitations and uncertainty remains as to how to interpret numerous provisions in the Act. FSP 109-2 addresses when to reflect in the financial statements the effects of the one-time tax benefit on the repatriation of foreign earnings. Under SFAS No. 109, companies are normally required to reflect the effect of new tax law changes in the period of enactment. FSP 109-2 provides companies additional time to determine the amount of earnings, if any, that they intend to repatriate under the Jobs Creation Act's provisions. See Note 8 for more discussion of the impact of the Jobs Creation Act, including the Company's status on the repatriation of foreign earnings.

In December 2004, the FASB issued SFAS No. 123(R). This new standard requires companies to adopt the fair value methodology of valuing stock-based compensation and recognizing that valuation in the financial statements from the date of grant. Accordingly, the adoption of SFAS No. 123(R)'s fair value method will have a significant impact on the Company's results of operations, although it will have no impact on the Company's overall financial position. The impact of adoption of SFAS No. 123(R) cannot be predicted at this time because it will partially depend on levels of share-based payments granted in the future. However, had the Company adopted SFAS No. 123(R) in prior periods, the impact of that standard would have approximated the impact of SFAS No. 123 as shown in the table above (see discussion in Stock-Based Compensation above). SFAS No. 123(R) also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under current literature. The Company is currently evaluating several option valuation models in order to calculate the required compensation expense. The Company has elected to adopt the provisions of SFAS No. 123(R) on a modified prospective application method effective July 1, 2005, with no restatement of any prior periods. SFAS No. 123(R) is effective for the Company as of the beginning of the first interim reporting period that begins after June 15, 2005.

Reclassifications – Certain prior year amounts as well as unaudited quarterly financial data presented in the accompanying consolidated financial statements have been reclassified to conform to the current year financial statement presentation. These reclassifications had no impact on previously reported net income or stockholders' equity.

Note 2 – Inventories

Inventories, stated at the lower of cost or market value, at December 31 were:

	2003	2004
Finished goods	$ 9,920,000	$13,118,000
Work-in-progress	1,818,000	2,025,000
Raw materials	6,519,000	9,240,000
	18,257,000	24,383,000
Less: reserves	(2,093,000)	(2,145,000)
	$16,164,000	$22,238,000

Note 3 – Property, Plant and Equipment

Property, plant and equipment at December 31 were:

	2003	2004
Buildings and leasehold improvements	$ 5,894,000	$ 7,126,000
Construction in-progress	2,810,000	2,989,000
Machinery and equipment	74,171,000	90,151,000
	82,875,000	100,266,000
Less: Accumulated depreciation and amortization	(35,244,000)	(39,671,000)
	47,631,000	60,595,000
Land	262,000	262,000
	$ 47,893,000	$ 60,857,000

The Company implemented an Enterprise Resource Planning software system for which approximately $2,511,000 and $0 is capitalized within construction in-progress in 2003 and 2004, respectively.

Note 4 – Bank Credit Agreements and Long-Term Debt

Line of credit – The Company maintains credit facilities with several financial institutions through its affiliated entities in the United States and Asia.

The credit unused and available under the various facilities as of December 31, 2004, totals $32.3 million, as follows:

		Outstanding at December 31,	
2004 Credit Facility	*Terms*	*2003*	*2004*
$ 7,500,000	Revolving, collateralized by all assets, variable interest (prime rate, approximately 5.25% at December 31, 2004) due monthly	$ 5,782,000	$ 3,167,000
$ 5,000,000	Term loan, collateralized by all assets, variable interest (LIBOR + variable margin, approximately 3.8% at December 31, 2004) due monthly	3,333,000	4,597,000
$25,000,000	Unsecured, interest at LIBOR plus margin (approximately 2.3% at December 31, 2004) due quarterly	3,000,000	6,000,000
$ 8,960,000	Unsecured, variable interest plus margin (approximately 1.7% to 2.3% at December 31, 2003) due monthly	2,706,000	–
$46,460,000		14,821,000	13,764,000
Less: Long-term debt, net of Related Party (included in table below)		(6,333,000)	(7,597,000)
Line of credit		$ 8,488,000	$ 6,167,000

Long-term debt – The balances remaining as of December 31, consist of the following:

	2003	2004
Note payable to LSC, a major stockholder of the Company (see Note 10), due in equal monthly installments of $208,000 plus interest beginning July 31, 2002, through June 30, 2006. The unsecured note bears interest at LIBOR plus 2% (approximately 4.1% at December 31, 2004) and is subordinated to the interest of the Company's primary lender.	$ 6,250,000	$ 3,750,000
Term note portion of $25,000,000 China credit facility due in 2006.	3,000,000	3,000,000
Note payable to U.S. bank, collateralized by all assets, due in aggregate monthly principal payments of $278,000 plus interest at 6.8% fixed by hedge contract through November 2004.	3,333,000	–
Note payable to U.S. bank, collateralized by all assets, due in aggregate monthly principal payments of $83,000 plus interest at approximately 3.8% at December 31, 2004.	–	4,597,000
	12,583,000	11,347,000
Less: Current portion	(5,833,000)	(3,514,000)
Long-term debt, net of current portion	$ 6,750,000	$ 7,833,000

The credit facilities contain certain covenants and restrictions, which, among other matters, require the maintenance of certain financial ratios and attainment of certain financial results, and prohibit the payment of dividends.

The aggregate maturities of long-term debt for future years ending December 31 are:

2005	$ 3,514,000
2006	5,250,000
2007	1,000,000
2008	1,000,000
2009	583,000
	$11,347,000

In July 2001, the Company entered into an interest rate swap agreement with a bank to hedge its interest exposure. The interest rate under the swap agreement, which expired November 30, 2004, was fixed at 6.8% and based on the notional amount, which was $2,292,000 at December 31, 2003.

Note 5 – Capital Lease Obligations

Future minimum lease payments under capital lease agreements are summarized as follows:

For years ending December 31,	
2005	$ 230,000
2006	230,000
2007	230,000
2008	230,000
2009	230,000
Thereafter	1,627,000
	2,777,000
Less: Interest	(440,000)
Present value of minimum lease payments	2,337,000
Less: Current portion	(165,000)
Long-term portion	$2,172,000

At December 31, 2004, property under capital leases had a cost of $2,785,000, and the related accumulated depreciation amounted to $557,000.

Note 6 – Accrued Liabilities

Accrued liabilities at December 31 were:

	2003	2004
Employee compensation and payroll taxes	$4,501,000	$ 5,779,000
Equipment purchases	1,875,000	2,012,000
Taxes payable	–	978,000
Sales commissions	686,000	437,000
Refunds to product distributors	334,000	219,000
Other	1,319,000	2,034,000
	$8,715,000	$11,459,000

Note 7 – Valuation of Financial Instruments

The Company's financial instruments include cash, accounts receivable, accounts payable, working capital line of credit, and long-term debt. The Company estimates the carrying amounts of all financial instruments described above to approximate fair value based upon current market conditions, maturity dates and other factors.

Note 8 – Income Taxes

The components of the income tax provisions are as follows:

	2002	2003	2004
Current tax provision			
Federal	$ –	$1,167,000	$ 4,922,000
Foreign	1,231,000	1,183,000	4,745,000
State	1,000	40,000	461,000
	1,232,000	2,390,000	10,128,000
Deferred tax expense (benefit)	497,000	70,000	(3,614,000)
Total income tax provision	$1,729,000	$2,460,000	$ 6,514,000

Reconciliation between the effective tax rate and the statutory tax rates for the years ended December 31, 2002, 2003, and 2004 are as follows:

	2002		2003		2004	
	Amount	Percent of pretax earnings	Amount	Percent of pretax earnings	Amount	Percent of pretax earnings
Federal tax	$ 2,669,000	34.0	$ 4,417,000	34.0	$11,131,000	34.0
State franchise tax, net of Federal benefit	455,000	5.8	753,000	5.8	1,588,000	4.8
Foreign income tax rate difference	(1,409,000)	(18.0)	(2,808,000)	(21.6)	(6,629,000)	(20.2)
Other	14,000	0.2	98,000	0.8	424,000	1.3
Income tax provision	$ 1,729,000	22.0	$ 2,460,000	19.0	$ 6,514,000	19.9

In accordance with the current taxation policies of the People's Republic of China (PRC), Diodes-China received preferential tax treatment for the years ended December 31, 1996 through 2004. Earnings were subject to 0% tax rates from 1996 through 2000, and 12% from 2001 through 2004. Due to a $15.0 million permanent re-investment of Diodes-China earnings in 2004, earnings from 2005 through 2007 will continue to be taxed at 12% (one half the normal central government tax rate). Also due to the permanent re-investment, the Company recorded a $1.2 million tax refund (net of U.S. taxes) in the fourth quarter of 2004. Earnings of Diodes-China are also subject to tax of 3% by the local taxing authority in Shanghai. The local taxing authority waived this tax from 2001 through 2004, and is expected to waive this tax in 2005, but can re-impose the tax at its discretion. For 2004, Diodes-Shanghai's effective tax rate was 15%.

As an incentive for the establishment of Diodes-Shanghai, beginning in 2005, earnings will be exempted from income tax for two years. Then, beginning in 2007, earnings will be subject to 50% of the standard tax rate of 15% for the following three years.

Earnings of Diodes-Taiwan are currently subject to a tax rate of 35%, which is comparable to the U.S. Federal tax rate for C corporations. Earnings of Diodes-Hong Kong are currently subject to a 17.5% tax for local sales and/or local source sales, all other sales are foreign income tax-free.

In accordance with United States tax law, the Company receives credit against its U.S. Federal tax liability for corporate taxes paid in Taiwan and China. The repatriation of funds from Taiwan and China to the Company may be subject to Federal and state income taxes.

As of December 31, 2004, accumulated and undistributed earnings of Diodes-China and Diodes-Shanghai are approximately $44.2 million, including $25.0 million of restricted earnings (which are not available for dividends). Through March 31, 2002, the Company had not recorded deferred U.S. Federal or state tax liabilities (estimated to be $8.9 million as of March 31, 2002) on these cumulative earnings since the Company, at that time, considered this investment to be permanent, and had no plans or obligation to distribute all or part of that amount from China to the United States. Beginning in April 2002, the Company began to record deferred taxes on a portion of the China earnings in preparation of a dividend distribution. In the year ended December 31, 2004, the Company received a dividend of approximately $5.7 million from its Diodes-China subsidiary, for which the tax effect is included in U.S. Federal and state taxable income. As of December 31, 2004, the Company has recorded approximately $2.0 million in deferred taxes on the cumulative earnings of Diodes-China and Diodes-Shanghai.

The Company is evaluating the need to provide additional deferred taxes for the future earnings of Diodes-China, Diodes-Shanghai, and Diodes-Hong Kong to the extent such earnings may be appropriated for distribution to the Company's corporate office in North America, and as further investment strategies with respect to foreign earnings are determined. Should the Company's North American cash requirements exceed the cash that is provided through the domestic credit facilities, cash can be obtained from the Company's foreign subsidiaries. However, the distribution of any unappropriated funds to the U.S. will require the recording of income tax provisions on the U.S. entity, thus reducing net income.

On October 22, 2004, the President of the United States signed the American Jobs Creation Act (AJCA) into law. Originally intended to repeal the extraterritorial income (ETI) exclusion, which had triggered tariffs by the European Union, the AJCA expanded to cover a wide range of business tax issues. Among other items, the AJCA establishes a phased repeal of the ETI, a new incentive tax deduction for U.S. corporations to repatriate cash from foreign subsidiaries at a reduced tax rate (a deduction equal to 85% of cash dividends received in the year elected that exceeds a base-period amount) and significantly revises the taxation of U.S. companies doing business abroad.

At December 31, 2004, the Company made a minimum estimate for repatriating cash from its subsidiaries in China and Hong Kong of $8.0 million under the AJCA, and recorded an income tax expense of approximately $1.3 million. Under the guidelines of the AJCA, the Company will develop a required domestic reinvestment plan, covering items such as U.S. bank debt repayment, U.S. capital expenditures and U.S. research and development activities, among others, to cover the $8.0 million minimum dividend repatriation. In addition, the Company will complete a quantitative analysis of the benefits of the AJCA, the foreign tax credit implications, and state and local tax consequences of a dividend to maximize the tax benefits of a 2005 dividend.

At December 31, 2003 and 2004, the Company's deferred tax assets and liabilities are comprised of the following items:

	2003	2004
Deferred tax assets, current		
Inventory cost	$ 272,000	$ 364,000
Accrued expenses and accounts receivable	566,000	702,000
Net operating loss carryforwards, foreign tax credits and other	4,709,000	1,387,000
	$ 5,547,000	$ 2,453,000
Deferred tax assets, non-current		
Plant, equipment and intangible assets	$(2,380,000)	$(2,632,000)
Net operating loss carryforwards, foreign tax credits and other	4,196,000	10,602,000
	$ 1,816,000	$ 7,970,000

At December 31, 2004, the Company had Federal and state net operating loss (NOL) carryforwards of approximately $17.0 million and $20.2 million, respectively, available to offset future regular and alternative minimum taxable income. The Federal NOL carryforwards will begin to expire in 2016 and the state NOL carryforwards will begin to expire in 2006.

Note 8 – Income Taxes (continued)

At December 31, 2004, the Company had Federal and state tax credit carryforwards (primarily relating to foreign tax credits, and to a lesser extent to research and development tax credits) of approximately $6.6 million and $0.1 million, respectively, available to offset future regular income and partially offset alternative minimum taxable income. The Federal credit carryforwards will begin to expire in 2009 and the state credit carryforwards will begin to expire in 2020.

Note 9 – Employee Benefit Plans

Employee Savings and Retirement Plans – The Company maintains a 401(k) profit sharing plan (the Plan) for the benefit of qualified employees at its North American locations. Employees who participate may elect to make salary deferral contributions to the Plan up to 100% of the employees' eligible payroll subject to annual Internal Revenue Code maximum limitations. The Company makes a matching contribution of $1 for every $2 contributed by the participant up to 6% (3% maximum matching) of the participant's eligible payroll. In addition, the Company may make a discretionary contribution to the entire qualified employee pool, in accordance with the Plan.

As stipulated by the regulations of the PRC, the Company maintains a retirement plan pursuant to the local Municipal Government for its employees in China. The Company is required to make contributions to the retirement plan at a rate of 22.5% of the employee's eligible payroll.

Pursuant to the Taiwan Labor Standard Law and Factory Law, the Company maintains a retirement plan for its employees in Taiwan. The Company makes contributions at a rate of 6% of the employee's eligible payroll.

For the years ended December 31, 2002, 2003, and 2004, the Company's total contributions to all plans were approximately $917,000, $1,241,000, and $1,428,000, respectively.

Stock Option Plans – The Company maintains stock option plans for directors, officers, and key employees, which provide for non-qualified and incentive stock options. The Compensation and Stock Option Committee of the Board of Directors determines the option price (not to be less than fair market value of the underlying common stock at the date of grant for incentive stock options) at the date of grant. The options generally expire ten years from the date of grant and are exercisable (vested) over the period stated in each option. Approximately 440,600 shares were available for future grants under the plans as of December 31, 2004. A summary of stock option transactions for the plans follows:

	Outstanding Options		
		Exercise Price Per Share	
	Number	*Range*	*Weighted Average*
Balance, December 31, 2001	3,172,641	$ 0.83-15.94	$ 5.85
Granted	515,550	5.69-6.38	5.72
Exercised	(97,650)	0.83-5.55	3.28
Canceled	(5,400)	5.55-5.69	5.62
Balance, December 31, 2002	3,585,141	0.83-15.94	5.90
Granted	502,950	10.63-13.04	13.03
Exercised	(688,141)	0.83-15.94	2.93
Canceled	(15,325)	5.55-15.94	7.84
Balance, December 31, 2003	3,384,625	2.22-15.94	7.56
Granted	526,900	18.32-21.85	18.35
Exercised	(1,136,725)	2.22-15.94	4.96
Canceled	(35,600)	5.55-18.32	13.64
Balance, December 31, 2004	2,739,200	$ 2.22-21.85	$10.63

As of December 31, 2004, approximately 1,737,200 of the 2,739,200 options outstanding were exercisable. The following summarizes information about stock options outstanding at December 31, 2004:

	Range of exercise prices	*Number outstanding*	*Weighted average contractual life (years)*	*Weighted average exercise price*
'93 NQO'	$2.67-15.94	631,950	4.6	$ 9.42
'93 ISO	2.22-15.94	705,400	4.9	7.45
'01 Plan	4.77-21.85	1,401,850	8.6	12.77
Total	$2.22-21.85	2,739,200	6.7	$10.63

The following summarizes information about stock options exercisable at December 31, 2004:

	Range of exercise prices	*Number exercisable*	*Weighted average exercise price*
'93 NQO	$2.67-15.94	630,300	$9.43
'93 ISO	2.22-15.94	668,550	$7.53
'01 Plan	5.55-13.04	438,350	$8.09
Total	$2.22-15.94	1,737,200	$8.36

Stock Bonus Plan – The Company also maintains an incentive stock bonus plan, which reserves shares of stock for issuance to key employees. As of December 31, 2004, there were 279,000 shares available for issuance under this plan. No shares were issued under this incentive bonus plan for years ended December 31, 2002 through 2004.

Note 10 – Related Party Transactions

Lite-On Semiconductor Corporation (LSC) – In July 1997, Vishay Intertechnology, Inc. (Vishay) and the Lite-On Group, a Taiwanese consortium, formed a joint venture – Vishay/Lite-On Power Semiconductor Pte., LTD. (Vishay/LPSC) – to acquire Lite-On Power Semiconductor Corp. (LPSC), a then 37% shareholder of the Company and a member of the Lite-On Group of the Republic of China. The Lite-On Group is a leading manufacturer of power semiconductors, computer peripherals, and communication products.

In March 2001, Vishay agreed to sell its 65% interest in the Vishay/LPSC joint venture to the Lite-On Group, the 35% joint venture partner. Because of this transaction, the Lite-On Group, through LPSC, its wholly-owned subsidiary, indirectly owned approximately 37% of the Company's common stock. In December 2001, LPSC merged with Dyna Image Corporation of Taipei, Taiwan. Dyna Image is the world's largest manufacturer of Contact Image Sensors (CIS), which are used in fax machines, scanners, and copy machines. The combined company is called Lite-On Semiconductor Corporation (LSC). At December 31, 2004, LSC owned approximately 32.5% of the Company's common stock. The Company considers its relationship with LSC to be mutually beneficial and the Company and LSC plans to continue its strategic alliance as it has since 1991.

The Company also leases warehouse space from LSC for its operations in Hong Kong. Such transactions are on terms no less favorable to the Company than could be obtained from unaffiliated third parties. As required by Nasdaq, the Audit Committee of the Board of Directors has approved the contracts associated with the related party transactions. The Company buys product from, and sells products to, LSC.

Net sales to, and purchases from, LSC were as follows for years ended December 31:

	2002	*2003*	*2004*
Net sales	$16,147,000	$14,628,000	$20,675,000
Purchases	14,292,000	18,667,000	22,368,000

Note 10 – Related Party Transactions *(continued)*

As a result of the acquisition of FabTech from LSC, the Company is indebted to LSC in the amount of $3,750,000 as of December 31, 2004. Terms of the debt are indicated in Note 4. As per the terms of the acquisition agreement, LSC entered into a volume purchase agreement with FabTech pursuant to which LSC is obligated to purchase from FabTech, and FabTech is obligated to manufacture and sell to LSC, silicon wafers.

As part of the FabTech acquisition, the Company entered into management incentive agreements with several members of FabTech's management. The agreements provide a guaranteed aggregate $375,000 annual payment as well as contingent bonuses based on the annual profitability of FabTech (subject to a maximum annual amount). Any portion of the guaranteed and contingent liability paid by FabTech is reimbursed by LSC. Guaranteed and maximum contingent bonus payments provided for by the management incentive agreements for the year ended December 31, 2004 (the final year of the agreements) were $375,000 and $1.2 million, respectively. Because the profitability targets were not met, no contingent bonus was earned or paid in the years 2002 through 2004.

Other related party – The Company sells product to, and purchases inventory from, companies owned by its 5% minority shareholder, Keylink International (formerly Xing International), in Diodes-China and Diodes-Shanghai. In addition, Diodes-China and Diodes-Shanghai each leases its manufacturing facilities from, subcontracts a portion of its manufacturing process (metal plating and environmental services) to, and pays a consulting fee to, its 5% minority shareholder. Total amounts for these services for the years ended December 31, 2002, 2003, and 2004 were $2,699,000, $3,464,000, and $4,760,000. Such transactions are on terms no less favorable to the Company than could be obtained from unaffiliated third parties. As required by Nasdaq, the Audit Committee of the Board of Directors has approved the contracts associated with the related party transactions.

Net sales to, and purchases from, companies owned by Keylink International were as follows for years ended December 31:

	2002	2003	2004
Net sales	$1,885,000	$1,484,000	$1,677,000
Purchases	4,394,000	2,961,000	4,789,000

Accounts receivable from, and accounts payable to, related parties were as follows as of December 31:

	2003	2004
Accounts receivable		
LSC	$3,111,000	$4,180,000
Other	827,000	1,346,000
	$3,938,000	$5,526,000
Accounts payable		
LSC	$2,914,000	$3,308,000
Other	539,000	628,000
	$3,453,000	$3,936,000

Note 11 – Geographic Information

An operating segment is defined as a component of an enterprise about which separate financial information is available that is evaluated regularly by the chief decision maker, or decision-making group, in deciding how to allocate resources and in assessing performance. The Company's chief decision-making group consists of the President and Chief Executive Officer, Chief Financial Officer, Vice President of Sales and Marketing, and Senior Vice President of Operations. The Company operates in a single segment, discrete semiconductor devices, through its various manufacturing and distribution facilities.

The Company's operations include the domestic operations (Diodes, Inc. and FabTech) located in the United States and the Asian operations (Diodes-Taiwan located in Taipei, Taiwan, Diodes-China and Diodes-Shanghai both located in Shanghai, China, and Diodes-Hong Kong located in Hong Kong, China). European operations are consolidated within the U.S. operations.

The accounting policies of the operating entities are the same as those described in the summary of significant accounting policies. Revenues are attributed to geographic areas based on the location of the market producing the revenues.

	Asia	*U.S.A.*	*Consolidated*
2004			
Total sales	$185,308,000	$ 92,634,000	$277,942,000
Intercompany sales	(75,527,000)	(16,712,000)	(92,239,000)
Net sales	$109,781,000	$ 75,922,000	$185,703,000
Assets	$116,729,000	$ 51,072,000	$167,801,000
Property, plant & equipment, net	48,589,000	12,268,000	60,857,000
2003			
Total sales	$124,412,000	$ 72,188,000	$196,600,000
Intercompany sales	(48,378,000)	(11,317,000)	(59,695,000)
Net sales	$ 76,034,000	$ 60,871,000	$136,905,000
Assets	$ 82,142,000	$ 41,653,000	$123,795,000
Property, plant & equipment, net	35,941,000	11,952,000	47,893,000
2002			
Total sales	$ 95,081,000	$ 66,338,000	$161,419,000
Intercompany sales	(39,592,000)	(6,006,000)	(45,598,000)
Net sales	$ 55,489,000	$ 60,332,000	$115,821,000
Assets	$ 63,721,000	$ 41,289,000	$105,010,000
Property, plant & equipment, net	32,313,000	12,380,000	44,693,000

Note 12 – Commitments and Contingencies

Operating leases – The Company leases its offices, manufacturing plants and warehouses under operating lease agreements expiring through December 2009. Rent expense amounted to approximately $2,711,000, $2,455,000, and $2,938,000 for the years ended December 31, 2002, 2003, and 2004, respectively.

Future minimum lease payments under non-cancelable operating leases for years ending December 31 are:

2005	$ 3,461,000
2006	3,481,000
2007	2,939,000
2008	2,520,000
2009	1,097,000
	$13,498,000

Note 13 – Selected Quarterly Financial Data (Unaudited)

	Quarter Ended			
	March 31	*June 30*	*Sept. 30*	*Dec. 31*
Fiscal 2004				
Net sales	$41,435,000	$47,017,000	$49,364,000	$47,887,000
Gross profit	12,750,000	15,028,000	16,746,000	16,211,000
Net income	4,856,000	6,123,000	7,242,000	7,330,000
Earnings per share				
Basic	$ 0.37	$ 0.46	$ 0.54	$ 0.53
Diluted	0.32	0.40	0.47	0.47
Fiscal 2003				
Net sales	$29,446,000	$33,316,000	$34,941,000	$39,202,000
Gross profit	7,461,000	8,346,000	9,162,000	11,559,000
Net income	1,923,000	2,172,000	2,563,000	3,437,000
Earnings per share				
Basic	$ 0.15	$ 0.17	$ 0.20	$ 0.27
Diluted	0.14	0.15	0.18	0.23
Fiscal 2002				
Net sales	$26,924,000	$29,946,000	$30,287,000	$28,664,000
Gross profit	4,345,000	7,098,000	7,862,000	7,405,000
Net income	208,000	1,564,000	1,767,000	2,263,000
Earnings per share				
Basic	$ 0.02	$ 0.13	$ 0.14	$ 0.18
Diluted	0.02	0.12	0.13	0.17

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders
Diodes Incorporated and Subsidiaries

We have audited the accompanying consolidated balance sheets of Diodes Incorporated and Subsidiaries as of December 31, 2004 and 2003 and the related consolidated statements of income, stockholders' equity and cash flows for each of the years in the three-year period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Diodes Incorporated and Subsidiaries as of December 31, 2004 and 2003, and the consolidated results of their operations and cash flows for each of the years in the three year period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

Moss Adams LLP

Los Angeles, California
January 28, 2005

CORPORATE INFORMATION

Board of Directors

Raymond Soong [3N]
Chairman of the Board, Diodes Incorporated
Chairman of the Board, The Lite-On Group

C.H. Chen [3N, 4C]
President & Chief Executive Officer, Diodes Incorporated
Vice Chairman, Lite-On Semiconductor Corporation

Michael R. Giordano [1C, 2C, 4]
Senior Vice President, UBS Incorporated

Dr. Keh-Shew Lu [1, 2, 3C, 4]
Retired Senior Vice President, Texas Instruments, Inc.

M.K. Lu
President, Lite-On Semiconductor Corporation

Dr. Shing Mao [3]
Retired Chairman of the Board, Lite-On Incorporated

John M. Stich [1, 2, 3, 4]
President & Chief Executive Officer, The Asian Network
Retired Chief Marketing Officer, Texas Instruments, Inc.– Japan

Executive Officers

C.H. Chen
President & Chief Executive Officer

Joseph Liu
Senior Vice President, Operations

Mark A. King
Vice President, Sales & Marketing

Carl C. Wertz
Chief Financial Officer, Secretary & Treasurer

1 – Member, Audit Committee
2 – Member, Compensation & Stock Options Committee
3 – Member, Nominating Committee
4 – Member, Strategic Planning Committee
C – Committee Chair
N – Non-Voting Member

Shareholder Information

Diodes Incorporated common stock is listed and traded on the Nasdaq National Market (Nasdaq: DIOD).

No cash dividends have been declared or paid. The Company currently intends to retain any earnings for use in its businesses.

Form 10-K

A copy of the Company's Form 10-K, as filed with the U.S. Securities and Exchange Commission, is available at *www.diodes.com* or upon written request to:

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Calendar Quarter Ended	*Closing Sales Price of Common Stock*	
	High	*Low*
Fourth Quarter 2004	$ 29.230	$ 21.590
Third Quarter 2004	25.859	16.830
Second Quarter 2004	24.800	20.840
First Quarter 2004	25.160	19.010
Fourth Quarter 2003	20.600	13.867
Third Quarter 2003	16.053	12.100
Second Quarter 2003	14.360	7.180
First Quarter 2003	8.200	6.367

Independent Accountants

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Financial Information Online

World Wide Web users can access Company information on the Diodes, Inc. Investor page at *www.diodes.com*.

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File Number A5109