UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

# FORM 10-Q

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

For the quarterly period ended SEPTEMBER 30, 1996

or

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

For the transition period from _______ to ________.

COMMISSION FILE NUMBER: 1-5740

DIODES INCORPORATED
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| DELAWARE | 95-2039518 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| 3050 EAST HILLCREST DRIVE<br>WESTLAKE VILLAGE, CALIFORNIA | 91362 |
| (Address of principal executive offices) | (Zip Code) |

Registrant's telephone number, including area code: (805) 446-4800

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No

The number of shares of the registrant's Common Stock outstanding as of November 7, 1996, was 5,675,794 including 717,115 shares of treasury stock.

THIS REPORT INCLUDES A TOTAL OF 23 PAGES
THE EXHIBIT INDEX IS ON PAGE 21

DIODES INCORPORATED

INDEX

PART I - FINANCIAL INFORMATION
ITEM 1 - CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

DIODES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED BALANCE SHEET

ASSETS

| | SEPTEMBER 30, 1996 (UNAUDITED) | DECEMBER 31, 1995 |
|---|---|---|
| CURRENT ASSETS | | |
| Cash | S1,464,000 | $478,000 |
| Accounts receivable | | |
| Customers | 9,630,000 | 7,794,000 |
| Related party and other | 331,000 | 427,000 |
| | 9,961,000 | 8,221,000 |
| Less allowance for doubtful receivables | 238,000 | 177,000 |
| | 9,723,000 | 8,044,000 |
| Inventories | 14,041,000 | 16,295,000 |
| Deferred income taxes | 893,000 | 893,000 |
| Prepaid expenses and other | 875,000 | 173,000 |
| Total current assets | 26,996,000 | 25,883,000 |
| PROPERTY, PLANT, AND EQUIPMENT - at cost, net | 4,635,000 | 1,527,000 |
| INVESTMENT IN JOINT VENTURE | -- | 1,878,000 |
| OTHER ASSETS | | |
| Advances to affiliated entity | 2,587,000 | -- |
| Other assets | 883,000 | 75,000 |
| TOTAL ASSETS | $35,101,000 | $29,363,000 |

See accompanying notes

DIODES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED BALANCE SHEET

LIABILITIES AND STOCKHOLDERS' EQUITY

| | SEPTEMBER 30, 1996 (UNAUDITED) | DECEMBER 31, 1995 |
|---|---|---|
| CURRENT LIABILITIES | | |
| Notes payable | $3,000,000 | $3,916,000 |
| Accounts payable | 3,278,000 | 6,075,000 |
| Accrued liabilities | 3,672,000 | 1,954,000 |
| Income taxes payable | 112,000 | 637,000 |
| Current portion of long-term debt | 37,000 | 38,000 |
| Total current liabilities | 10,099,000 | 12,620,000 |
| LONG-TERM OBLIGATION, less current maturities | 5,215,000 | 244,000 |
| MINORITY INTEREST IN JOINT VENTURE | 1,130,000 | -- |
| STOCKHOLDERS' EQUITY | | |
| Class A convertible preferred stock - par value $1 per share; 1,000,000 shares authorized; no shares issued and outstanding | -- | -- |
| Common stock - par value $0.66 2/3 per share; 9,000,000 shares authorized; 5,675,794 and 5,675,619 shares issued and outstanding at September 30, 1996 and, December 31, 1996, respectively. | 3,784,000 | 3,784,000 |
| Additional paid-in capital | 5,768,000 | 5,768,000 |
| Retained earnings | 10,887,000 | 8,729,000 |
| | 20,439,000 | 18,281,000 |
| Less: Treasury stock - 717,115 common shares, at cost | 1,782,000 | 1,782,000 |
| Total stockholders' equity | 18,657,000 | 16,499,000 |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | $35,101,000 | $29,363,000 |

See accompanying notes

DIODES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED STATEMENTS OF INCOME
(Unaudited)

| | THREE MONTHS ENDED SEPTEMBER 30, | | NINE MONTHS ENDED SEPTEMBER 30, | |
|---|---|---|---|---|
| | 1996 | 1995 | 1996 | 1995 |
| Net sales | $14,394,000 | $15,356,000 | $41,050,000 | $44,134,000 |
| Cost of goods sold | 10,893,000 | 10,924,000 | 30,381,000 | 31,621,000 |
| Gross profit | 3,501,000 | 4,432,000 | 10,669,000 | 12,513,000 |
| Selling, general and administrative expenses | 2,388,000 | 2,483,000 | 7,397,000 | 7,363,000 |
| Income from operations | 1,113,000 | 1,949,000 | 3,272,000 | 5,150,000 |
| Other income (expense) | | | | |
| Interest income | 55,000 | 3,000 | 144,000 | 22,000 |
| Interest expense | (149,000) | (76,000) | (421,000) | (120,000) |
| Commissions and other | 88,000 | 190,000 | 265,000 | 388,000 |
| Minority interest in joint venture | 71,000 | -- | 83,000 | -- |
| | 65,000 | 117,000 | 71,000 | 290,000 |
| Income before income taxes | 1,178,000 | 2,066,000 | 3,343,000 | 5,440,000 |
| Provision for income taxes | 423,000 | 805,000 | 1,185,000 | 2,074,000 |
| Net income | $ 755,000 | $ 1,261,000 | $ 2,158,000 | $ 3,366,000 |
| Earnings per share | | | | |
| Primary | $ 0.14 | $ 0.24 | $ 0.40 | $ 0.65 |
| Fully-diluted | $ 0.14 | $ 0.24 | $ 0.40 | $ 0.64 |
| Weighted average shares outstanding | | | | |
| Primary | 5,235,179 | 5,276,127 | 5,390,866 | 5,206,042 |
| Fully-diluted | 5,293,366 | 5,276,127 | 5,390,866 | 5,255,624 |

See accompanying notes

DIODES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(Unaudited)

| | NINE MONTHS ENDED SEPTEMBER 30, 1996 | NINE MONTHS ENDED SEPTEMBER 30, 1995 |
|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net income | $ 2,158,000 | $ 3,366,000 |
| Adjustments to reconcile net income to net cash provided (used) by operating activities: | | |
| Depreciation and amortization | 224,000 | 238,000 |
| Increase in allowance for doubtful accounts | 61,000 | 34,000 |
| Gain on sale of property, plant and equipment, net | -- | (73,000) |
| (Increase) decrease in operating assets: | | |
| Accounts receivable | (1,740,000) | (3,795,000) |
| Inventories | 2,254,000 | (5,256,000) |
| Prepaid taxes, expenses and other | (702,000) | (652,000) |
| (Decrease) increase in operating liabilities: | | |
| Accounts payable | (2,797,000) | 344,000 |
| Accrued liabilities | 1,718,000 | 1,064,000 |
| Income taxes payable | (525,000) | (231,000) |
| Deferred compensation payable | -- | (14,000) |
| Minority interest in joint venture earnings | (83,000) | -- |
| Net cash provided (used) by operations | 568,000 | (4,975,000) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchase of property, plant and equipment | (1,454,000) | (289,000) |
| Proceeds from sale of equipment | -- | 147,000 |
| Acquisition of other assets | (808,000) | -- |
| Advances to affiliates | (2,587,000) | |
| Minority interest contribution to joint venture | 1,213,000 | -- |
| Net cash provided (used) by investing activities | (3,636,000) | (142,000) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Advances (payments) on line of credit, net | (917,000) | 3,551,000 |
| Proceeds from issuance of stock | -- | 344,000 |
| Proceeds from (repayments of) long-term obligations | 4,971,000 | (39,000) |
| Net cash provided (used) by financing activities | 4,054,000 | 3,856,000 |
| INCREASE (DECREASE) IN CASH | $ 986,000 | $(1,261,000) |
| CASH AT BEGINNING OF PERIOD | $ 478,000 | $ 1,733,000 |
| CASH AT END OF PERIOD | $ 1,464,000 | $ 472,000 |
| SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION | | |
| Non-Cash Investing Activities | | |
| Conversion of joint venture investment to plant and equipment | $ 1,878,000 | $ -- |

See accompanying notes

DIODES INCORPORATED AND SUBSIDIARIES
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(Unaudited)

NOTE A - BASIS OF PRESENTATION

The accompanying unaudited consolidated, condensed financial statements have been prepared in accordance with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the financial position and results of operations have been included. Operating results for interim periods are not necessarily indicative of the results that may be expected for the full year. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 1995.

The consolidated financial statements include the accounts of the Company, its wholly-owned subsidiary, Diodes Taiwan Co., Ltd. (a foreign subsidiary), and the accounts of the Shanghai Kai Hong Electronics Co., Ltd. ("Kai Hong") joint venture in which the Company has a 70% controlling interest. All significant inter-company balances and transactions have been eliminated.

NOTE B - INCOME TAXES

Income taxes are accounted for using an asset and liability method. This method requires the recognition of deferred tax assets and liabilities for both the expected future tax impact of differences between the financial statement and tax basis of assets and liabilities, and for the expected future tax benefit to be derived from tax loss carryforwards. Additionally, this method requires the establishment of a valuation allowance to reflect the likelihood of realization of deferred tax assets.

Accordingly, the Company has recorded a net deferred tax asset resulting from net deductible temporary differences in the amount of $893,000. This deferred tax asset results primarily from inventory reserves and expense accruals which are not currently deductible for federal income tax purposes.

PART I - FINANCIAL INFORMATION

ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Except for the historical information contained herein, the matters addressed in this Item 2 constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Such forward-looking statements are subject to a variety of risks and uncertainties, including those discussed below under the heading "Factors That May Affect Future Results" and elsewhere in this Report on Form 10-Q, that could cause actual results to differ materially from those anticipated by the Company's management. The Private Securities Litigation Reform Act of 1995 (the "Act") provides certain "safe harbor" provisions for forward-looking statements. All forward-looking statements made on this Quarterly Report on Form 10-Q are made pursuant to the Act.

FINANCIAL CONDITION

Net sales for the three months and nine months ended September 30, 1996 were, $14.4 million and $41.1 million, respectively, representing decreases of approximately 6.3% and 7.0%, respectively, compared to the same periods in 1995. Primary earnings per share were $0.14 and $0.40 for the three months and nine months ended September 30, 1996, representing decreases of 41.7% and 38.5%, respectively, compared to the same periods in 1995. Although net sales and earnings were below that of last year, they showed considerable improvement over the immediately preceding quarter as earnings per share increased 27.3% on a 7.0% increase in net sales. Price erosion due to continuing excess inventories throughout the industry adversely affected the Company's net sales and gross margins in the third quarter of 1996. Gross profit margins for the three and nine months ended September 30, 1996 were 24.3% and 26.0%, respectively versus 28.9% and 28.4% in the comparable periods in 1995, primarily due to industry-wide pricing pressures. With decreased sales and competitive pricing, there can be no assurance that the Company will be able to maintain these gross profit margins.

The Semiconductor Industry Association has reported that book-to-bill ratios (the dollar value of new orders scheduled versus the dollar value of orders shipped) throughout the industry fell in early 1996, reaching a nine year low in March. In the third quarter of 1996, the Company continued to experience a decrease in orders compared to the same period last year, primarily due to a slow down in the personal computer and related industries. Although the industry book-to-bill ratio is recovering somewhat, there can be no assurance that such recovery will continue or be maintained. However, based upon higher than forecasted October 1996 net sales, and provided industry conditions continue to improve, the Company is cautiously optimistic that it will continue to see improvements in net sales.

Selling, general and administrative expenses ("SG&A") for the three and nine months ended September 30, 1996, as a percentage of net sales, was 16.6% and 18.0%, respectively, versus 16.2% and 16.7% for the comparable periods last year, and 19.0% and 18.8% for the comparable periods last quarter, respectively. Planned increases in SG&A accounted for the majority of the increase including three items in particular: (i) higher promotional expenses for a new product line of leading-technology surface-mount (SO-8) power MOSFETs; (ii) additional operating costs associated with the Company's controlling interest in Kai Hong, a previously-announced investment on mainland China for the manufacture of SOT-23 related parts; and (iii) ongoing costs associated with the Company's goal of achieving ISO 9002 certification. The ISO 9002 certification includes a subcontractor qualification program and is designed to maximize product quality, enhance customer service, and strengthen the Company's image in the marketplace.

The Company has been successful in controlling total inventory and overhead expenses, which have been reduced by 13.8% since the beginning of the year, and 6.4% since last quarter, respectively.

The Company has used approximately $3.3 million ($2.8 million as equity contribution and $500,000 as a short-term loan) of its credit line to fund equity contribution for the previously announced Kai Hong joint venture. The Kai Hong facility is operational, has begun shipping product, and the first phase is expected to be at full capacity in the fourth quarter of 1996. The Company's third quarter and year-to-date net interest expense increased $21,000 and $179,000, respectively, from the comparable periods last year.

In accordance with generally accepted accounting principles, the Company has accounted for this majority owned joint venture on a consolidated basis. During the first half of 1996, the Kai Hong joint venture has capitalized pre-operating and start-up costs of approximately $755,000 which are classified in the consolidated balance sheet as "Other assets".

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 1996 AND 1995

The following table sets forth, for the periods indicated, the percentage which 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 THREE MONTHS ENDED SEPTEMBER 30, | | PERCENTAGE DOLLAR INCREASE (DECREASE) |
|---|---|---|---|
| | 1996 | 1995 | '95 TO '96 |
| Net sales | 100.0% | 100.0% | (6.3)% |
| Cost of goods sold | (75.7) | (71.1) | (0.3) |
| Gross profit | 24.3 | 28.9 | (21.0) |
| Operating expenses | (16.6) | (16.2) | (3.8) |
| Income from operations | 7.7 | 12.7 | (42.9) |
| Interest expense, net | (0.6) | (0.5) | 28.8 |
| Other income and Minority interest | 1.1 | 1.3 | (16.3) |
| Income before taxes | 8.2 | 13.5 | (43.0) |
| Income taxes | 3.0 | 5.3 | (47.5) |
| Net income | 5.2 | 8.2 | (40.1) |

The following discussion explains in greater detail the consolidated operating results and financial condition of the Company. This discussion should be read in conjunction with the consolidated financial statements and notes thereto appearing elsewhere in this quarterly report.

| | 1996 | 1995 |
|---|---|---|
| NET SALES | $ 14,394,000 | $ 15,356,000 |

The Company's $962,000 or 6.3% decrease in net sales for the three months ended September 30, 1996, compared to the three months ended September 30, 1995, was primarily attributed to price erosion due to continuing excess inventories throughout the industry. The Semiconductor Industry Association has reported that book-to-bill ratios throughout the industry fell in early 1996, reaching a nine year low in March. In the fourth quarter of 1995, the Company experienced a slowing of orders, primarily due to a slow down in the personal computer and related industries. Although the industry book-to-bill ratio is recovering somewhat, there can be no assurance that such recovery will continue or be maintained. However, based upon higher than forecasted October 1996 net sales, and provided industry conditions continue to improve, the Company is cautiously optimistic that it will continue to see improvements in net sales.

| | 1996 | 1995 |
|---|---|---|
| GROSS PROFIT | $ 3,501,000 | $ 4,432,000 |
| GROSS PROFIT MARGIN PERCENTAGE | 24.3% | 28.9% |

The Company's gross profit for the three months ended September 30, 1996 decreased approximately $931,000 or 21.0%. This decrease was primarily due to the 6.3% decrease in net sales and industry-wide pricing pressures, as well as to inventory reserves recorded by the Company. As a percentage of net sales, the Company's gross profit decreased to 24.3% from 28.9% for the comparable periods in 1995, primarily due to industry-wide pricing pressures.

| | 1996 | 1995 |
|---|---|---|
| SG&A | $ 2,388,000 | $ 2,483,000 |

The Company's SG&A for the three months ended September 30, 1996 decreased approximately 3.8% compared to the same period last year. This $95,000 decrease was primarily attributable to cost controls, partly offset by planned increases in SG&A including three items in particular: (i) higher promotional expenses for a new product line of leading-technology surface-mount (SO-8) power MOSFETs; (ii) additional operating costs associated with the Company's controlling interest in Kai Hong, a previously-announced investment on mainland China for the manufacture of SOT-23 type products; and (iii) ongoing costs associated with the Company's goal of achieving ISO 9002. ISO 9002 certification includes a subcontractor qualification program and is designed to maximize product quality, enhance customer service, and strengthen the Company's image in the marketplace.

SG&A as a percentage of net sales increased from 16.2% for the three months ended September 30, 1995 to 16.6% in the comparable period in 1996. The Company continues to manage SG&A by implementing cost controls, but believes that the industry-wide slowdown is temporary and thus will continue to implement its plan for future growth.

| | 1996 | 1995 |
|---|---|---|
| INCOME FROM OPERATIONS | $ 1,113,000 | $ 1,949,000 |

The Company's fiscal 1996 comparative decrease in income from operations of approximately $836,000, or 42.9%, is primarily the net result of the Company's 6.3% decrease in net sales, 21.0% decrease in gross profit, and 0.4 percentage point increase in SG&A as a percentage of net sales.

| | 1996 | 1995 |
|---|---|---|
| INTEREST INCOME | $ 55,000 | $ 3,000 |
| INTEREST EXPENSE | $ 149,000 | $ 76,000 |

The Company's interest income for the three months ended September 30, 1996 increased approximately $52,000 compared to the same period last year as the Company is advancing funds to FabTech and Kai Hong. The interest income is primarily the interest charged to FabTech under the Company's loan agreement. The Company's interest expense for 1996 increased $73,000 or 96.1%, primarily as a result of an increase in the Company's usage of its credit facility to finance additional agreements, primarily FabTech and Kai Hong.

| | 1996 | 1995 |
|---|---|---|
| OTHER INCOME AND MINORITY INTEREST IN JOINT VENTURE | $ 159,000 | $ 190,000 |

The Company's other income for the three months ended September 30, 1996 decreased approximately $31,000 or 16.3% primarily as a result of a 53.7% decrease in commissions earned by the Company's Taiwan subsidiary on drop shipment sales in Asia as well as the discontinuation of commissions from ITT.

The minority interest in joint venture represents the Company's 70% controlling interest in the Kai Hong joint venture. All of the Kai Hong joint venture earnings are consolidated within the Company's financial statements. The $71,000 represents the minority investor's share of the joint venture loss.

| | 1996 | 1995 |
|---|---|---|
| NET INCOME | $ 755,000 | $ 1,261,000 |
| PRIMARY EARNINGS PER SHARE | $ 0.14 | $ 0.24 |

The Company's net income for the three months ended September 30, 1996 decreased 40.1% or approximately $506,000 compared to the same period in 1995. Primary earnings per share decreased approximately 41.7% for the three months ended September 30, 1996, compared to the three months ended September 30, 1995. Decreases in both net income and earnings per share are primarily attributable to a 6.3% decrease in net sales, a 0.4 percentage point decrease in SG&A as a percentage of net sales, combined with a $21,000 increase in net interest expense.

RESULTS OF OPERATIONS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 1996 AND 1995.

The following table sets forth, for the periods indicated, the percentage which 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 NINE MONTHS ENDED SEPTEMBER 30, | | PERCENTAGE DOLLAR INCREASE (DECREASE) |
|---|---|---|---|
| | 1996 | 1995 | '95 TO '96 |
| Net sales | 100.0% | 100.0% | (7.0)% |
| Cost of goods sold | (74.0) | (71.6) | (3.9) |
| Gross profit | 26.0 | 28.4 | (14.7) |
| Operating expenses | (18.0) | (16.7) | 0.5 |
| Income from operations | 8.0 | 11.7 | (36.5) |
| Interest expense, net | (0.7) | (0.2) | 182.7 |
| Minority interest and Other income | 0.8 | 0.8 | (10.3) |
| Income before taxes | 8.1 | 12.3 | (38.5) |
| Income taxes | 2.8 | 4.7 | (42.9) |
| Net income | 5.3 | 7.6 | (35.9) |

The following discussion explains in greater detail the consolidated operating results and financial condition of the Company. This discussion should be read in conjunction with the consolidated financial statements and notes thereto appearing elsewhere in this quarterly report.

| | 1996 | 1995 |
|---|---|---|
| NET SALES | $ 41,050,000 | $ 44,134,000 |

The Company's 7.0% decrease in net sales for the nine months ended September 30, 1996, compared to the nine months ended September 30, 1995, was primarily attributed to a decline in customer demand resulting in a decrease in the number of units shipped, as well as price erosion, both due to continuing excess inventories throughout the industry. Although the industry book-to-bill ratio is recovering somewhat, there can be no assurance that such recovery will continue or be maintained. However, based upon higher than forecasted October 1996 net sales, and provided industry conditions continue to improve, the Company is cautiously optimistic that it will continue to see improvements in net sales.

| | 1996 | 1995 |
|---|---|---|
| GROSS PROFIT | $ 10,669,000 | $ 12,513,000 |
| GROSS PROFIT MARGIN PERCENTAGE | 26.0% | 28.4% |

The Company's gross profit for the nine months ended September 30, 1996 decreased approximately $1.8 million or 14.7%. This decrease was primarily due to the 7.0% decrease in net sales as well as industry-wide pricing pressures, and inventory reserves recorded by the Company. As a percentage of net sales, the Company's gross profit decreased to 26.0% from 28.4% for the comparable period in 1995, primarily due to industry-wide pricing pressures.

| | 1996 | 1995 |
|---|---|---|
| SG&A | $ 7,397,000 | $ 7,363,000 |

The Company's SG&A for the nine months ended September 30, 1996 increased approximately 0.5% compared to the same period last year. This $130,000 increase was primarily attributable to planned increases in SG&A including three items in particular: (i) higher promotional expenses for a new product line of leading-technology surface-mount (SO-8) power MOSFETs; (ii) additional operating costs associated with the Company's controlling interest in Kai Hong, a previously-announced investment on mainland China for the manufacture of SOT-23s; and (iii) ongoing costs associated with the Company's goal of achieving ISO 9002 certification by year-end, partly offset by cost controls. ISO 9002 certification includes a subcontractor qualification program and is designed to improve product quality, enhance customer service, and strengthen the Company's image in the marketplace.

The total SG&A as a percentage of net sales increased from 16.7% in 1995, to 18.0% in 1996. The Company continues to manage SG&A by implementing cost controls, but believes that the industry-wide slowdown is temporary and thus will continue to implement its plan for future growth.

| | 1996 | 1995 |
|---|---|---|
| INCOME FROM OPERATIONS | $ 3,272,000 | $ 5,150,000 |

The Company's fiscal 1996 comparative decrease in income from operations of approximately $1.9 million or 36.5%, is primarily the net result of the Company's 7.0% decrease in net sales, a 14.7% decrease in gross profit and 1.3 percentage point increase in SG&A as a percentage of net sales.

| | 1996 | 1995 |
|---|---|---|
| INTEREST INCOME | $ 144,000 | $ 22,000 |
| INTEREST EXPENSE | $ 421,000 | $ 120,000 |

The Company's interest income for the nine months ended September 30, 1996, increased approximately $122,000 compared to the same period last year as the Company is advancing funds to FabTech and Kai Hong. The interest income is primarily the interest charged to FabTech under the Company's loan agreement. The Company's interest expense for 1996 increased $301,000, primarily as a result of an increase in the Company's usage of its credit facility to finance additional agreements, primarily FabTech and Kai Hong.

| | 1996 | 1995 |
|---|---|---|
| OTHER INCOME AND MINORITY INTEREST IN JOINT VENTURE | $ 348,000 | $ 388,000 |

The Company's other income for the nine months ended September 30, 1996 decreased approximately $40,000 or 10.3% primarily as a result of a 31.7% decrease in commissions earned by the Company's Taiwan subsidiary on drop shipment sales in Asia as well as the discontinuation of commissions from ITT.

The minority interest in joint venture represents the Company's 70% controlling interest in the Kai Hong joint venture. All of the Kai Hong joint venture earnings are consolidated within the Company's financial statements. The $83,000 represents the minority investor's share of the joint venture loss.

| | 1996 | 1995 |
|---|---|---|
| NET INCOME | $ 2,158,000 | $ 3,366,000 |
| PRIMARY EARNINGS PER SHARE | $ 0.40 | $ 0.65 |

The Company's net income for the nine months ended September 30, 1996 decreased 35.9% or approximately $1.2 million compared to the same period in 1995. Primary earnings per share decreased approximately 38.5% for the nine months ended September 30, 1996, compared to the same period in 1995. Decreases in both net income and earnings per share are primarily attributable to a 7.0% decrease in net sales, a 1.3 percentage point increase in SG&A as a percentage of net sales, combined with a $179,000 increase in net interest expense.

LIQUIDITY AND CAPITAL RESOURCES

Cash provided by operating activities for the nine months ended September 30, 1996 was $568,000 compared to cash used by operating activities of $5.0 million for the comparable period in 1995. The primary sources of cash flows for the nine months ended September 30, 1996 was a $2.2 million net income and an inventory reduction of $2.3 million, while the primary use was a $1.1 million net decrease in accounts payable and accrued liabilities.

Accounts receivable increased 20.9% as the Company has experienced a slight slowing trend in cash receipts in both U.S. and overseas operations. The Company, through refined customer service has, in some cases, extended terms to assist customers. The Company's inventories have decreased 13.8% as the Company's continues its commitment to provide timely delivery of product to customers while controlling inventory levels.

The ratio of the Company's current assets to current liabilities on September 30, 1996, was 2.7 to 1 compared to a ratio of 2.1 to 1 as of December 31, 1995.

Cash used by investing activities was $3.6 million for the nine months ended September 30, 1996, compared to $142,000 in 1995. The Company has provided approximately $3.3 million ($2.8 million as equity contribution and $500,000 as a short-term loan) to Kai Hong - for the construction of a new facility for the manufacture of SOT-23 related parts; and loaned approximately $2.6 million to FabTech - to be used in upgrading, reconfiguring, and starting up operations at an existing wafer fabrication facility. The Company has a 70% interest in the Kai Hong joint venture, is responsible for production and management, and currently receives 100% of the production. Additional capital contributions will be made in several phases over three years. Both alliances are indicative of the Company's desire to participate in the sourcing of advanced-technology discrete components, and to enhance its ability to procure products in a timely fashion and at reasonable cost.

Cash provided by financing activities was $4.1 million as of September 30, 1996, compared to $3.9 million in 1995. Long-term obligations increased from $244,000 at December 31, 1995 to $5.2 million as of September 30, 1996. The Company used its credit facility to fund the advances to FabTech and Kai Hong as well as for working capital.

In August 1996, the Company entered into a banking agreement with Union Bank of California who will provide a credit facility of $23 million. The credit facility, will be used for working capital, financing for the Kai Hong joint venture, as well as for future growth. As collateral security, the Company has granted to the lender a lien in all of its property, other than real property. The Company is subject to certain restrictive covenants, including, but not limited to, prohibitions on certain mergers or sales of assets, restrictions as to incurring additional liens or indebtedness, limitations on certain capital expenditures in excess of $1.0 million, restrictions on the making of loans, guarantees, investments and advances, and restrictions on the retirement of the Company's stock. The credit agreement was filed with the Company's second quarter 1996 Form 10-Q.

The Company anticipates it will continue to utilize such credit facility to support its operations. The Company believes that the continued availability of this credit facility and internally generated funds will be sufficient to meet the Company's currently foreseeable operating cash requirements. The Company's cash balance at September 30, 1996 increased $986,000 compared to the December 31, 1995 balance.

Property, plant and equipment increased approximately $3.1 million since December 31, 1995 primarily due to property, plant, equipment and machinery at the Kai Hong facility.

The Company changed the accounting method for the Kai Hong joint venture from an equity method at December 31, 1995 (which resulted in a single line item "Investment in Joint Venture" of $1.8 million) to a full consolidation presentation, when the Kai Hong agreement was changed from a compensation trade agreement to a joint venture effective March 18, 1996.

The Company's total working capital increased 27.1% to $16.9 million as of September 30, 1996 from $13.3 million as of December 31, 1995, and Company believes that its working capital position will be sufficient for its requirements for the foreseeable future.

As of September 30, 1996, the Company has no material plans or commitments for capital expenditures other than disclosed in the Kai Hong and FabTech agreements previously mentioned. However, to ensure that the Company can secure reliable and cost effective sourcing to support and better position itself for growth, the Company is continuously evaluating additional sources of products. The Company believes its credit and financial position will provide sufficient access to funds should an appropriate investment opportunity arise and, thereby, assist the Company in improving customer satisfaction and in maintaining or increasing product market penetration.

The Company's debt to equity ratio increased to 0.88 at September 30, 1996 from 0.78 at December 31, 1995. The Company anticipates this ratio may increase as the Company continues to use its credit facilities to fund additional sourcing opportunities.

FACTORS THAT MAY AFFECT FUTURE RESULTS

All forward-looking statements contained in this Item 2 are subject to, in addition to the other matters described in this Report on Form 10-Q, a variety of significant risks and uncertainties. The following discussion highlights some of these risks and uncertainties. Further, from time to time, information provided by the Company or statements made by its employees may contain forward-looking information. The Company cautions the reader that there can be no assurance that actual results or business conditions will not differ materially from those projected or suggested in such forward-looking statements as a result of various factors, including those discussed below.

There are many factors that could cause the events in such forward looking statements to not occur, including, but not limited to, general or specific economic conditions, the ability and willingness of the Company's customers to purchase products provided by the Company, the perceived absolute or relative overall value of these products by the purchasers, including the features, quality, and price in comparison to other competitive products, the level of availability of products and substitutes, the ability and willingness of purchasers to acquire new or advanced products, pricing, purchasing, financing, operational, advertising and promotional decisions by intermediaries in the distribution channels which could affect the supply of or end-user demands for the Company's products, the amount and rate of growth and the Company's selling, general and administrative expenses, difficulties in obtaining materials, supplies and equipment, difficulties or delays in the development, production, testing and marketing of products, including, but not limited to, failure to ship new products and technologies when anticipated, the failure of customers to accept these products or technologies when planned, and defects in products, any failure of economies to develop when planned, the acquisition of fixed assets and other assets, including inventories and receivables, the making or incurring of any expenditures, the effects of and changes in trade, monetary and fiscal policies, laws and regulations, other activities of governments, agencies and similar organizations and social and economic conditions, such as trade restriction or prohibition, inflation and monetary fluctuation, import and other charges or taxes, the ability or inability of the Company to obtain or hedge against foreign currency, foreign exchange rates and fluctuations in those rates, adaptations of new, or changes in, accounting policies and practices, in the application of such policies and practices, the effects of changes within the Company's organization, and activities of parties with which the Company has an agreement or understanding, including any issues affecting any investment or joint venture in which the Company has an investment, and the amount, and the cost of financing which the Company has, and any changes to that financing.

# PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

There are no matters to be reported under this heading.

ITEM 2. CHANGES IN SECURITIES

There are no matters to be reported under this heading.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

There are no matters to be reported under this heading.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

There are no matters to be reported under this heading.

ITEM 5. OTHER INFORMATION

There are no matters to be reported under this heading.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

| | |
|---|---|
| Exhibit 11 - | Computation of Earnings Per Share for the three months and nine months ended September 30, 1996 and September 30, 1995 |
| Exhibit 27 - | Financial Data Schedule |

(b) Reports on Form 8-K

None

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

DIODES INCORPORATED (Registrant)

/s/ Joseph Liu November 7, 1996

- --------------------------------------------

JOSEPH LIU
Vice President,
Chief Financial Officer
and Secretary
(Principal Financial and Accounting Officer)

INDEX TO EXHIBITS

DIODES INCORPORATED AND SUBSIDIARIES

EXHIBIT - 11

COMPUTATION OF EARNINGS PER SHARE

| | THREE MONTHS ENDED SEPTEMBER 30, | | NINE MONTHS ENDED SEPTEMBER 30, | |
|---|---|---|---|---|
| | 1996 | 1995 | 1996 | 1995 |
| PRIMARY | | | | |
| Weighted average number of common shares outstanding | 4,958,679 | 4,949,050 | 4,958,652 | 4,855,058 |
| Assumed exercise of stock options | 276,500 | 327,077 | 432,214 | 350,984 |
| | 5,235,179 | 5,276,127 | 5,390,866 | 5,206,042 |
| Net income | $ 755,000 | $1,261,000 | $2,158,000 | $3,366,000 |
| Primary earnings per share | $ 0.14 | $ 0.24 | $ 0.40 | $ 0.65 |
| FULLY-DILUTED | | | | |
| Weighted average number of common shares outstanding | 4,958,679 | 4,949,050 | 4,958,652 | 4,855,058 |
| Assumed exercise of stock options | 334,687 | 327,077 | 432,214 | 400,566 |
| | 5,293,366 | 5,276,127 | 5,390,866 | 5,255,624 |
| Net income | $ 755,000 | $1,261,000 | $2,158,000 | $3,366,000 |
| Fully-diluted earnings per share | $ 0.14 | $ 0.24 | $ 0.40 | $ 0.64 |

5

9-MOS
DEC-31-1996
JUL-01-1996
SEP-30-1996
1,464,000
0
9,961,000
238,000
14,041,000
26,996,000
6,246,000
1,611,000
35,101,000
10,099,000
0
0
0
3,784,000
16,655,000
35,101,000
14,394,000
14,394,000
10,893,000
13,281,000
0
0
149,000
1,178,000
423,000
755,000
755,000
0
0
755,000
0.14
0.14