MAGNACHIP SEMICONDUCTOR LLC
Form 10-K
March 31, 2006
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark one)

x **Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the fiscal year ended December 31, 2005

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 333-126019-09

MAGNACHIP SEMICONDUCTOR LLC

(Exact name of Registrant as specified in its charter)

Delaware	**83-0406195**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
c/o MagnaChip Semiconductor S.A.	
74, rue de Merl, B.P. 709, L-2017	
Luxembourg, Grand Duchy of Luxembourg	**Not Applicable**

(Address of principal executive offices) **(Zip Code)**

Registrant s telephone number, including area code: (352) 45-62-62

Securities registered pursuant to Section 12(b) of the Act: None.

Securities registered pursuant to Section 12(g) of the Act: None.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes x No ¨

Note Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Exchange Act from their obligations under those Sections.

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 ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer x

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

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant s most recently completed second fiscal quarter. **Not applicable.**

As of March 1, 2006, the registrant had 53,108,569.672 of the registrant s common units outstanding.

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Supplemental Information to be Furnished With Reports Filed Pursuant to Section 15(d) of the Act by Registrants Which Have Not Registered Securities Pursuant to Section 12 of the Act

No annual report or proxy statement, form of proxy or other proxy soliciting material with respect to any annual or other meeting of security holders has been sent to security holders.

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MAGNACHIP SEMICONDUCTOR LLC

2005 FORM 10-K ANNUAL REPORT

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PART I

INDUSTRY AND MARKET DATA

In this report, we rely on and refer to information regarding the semiconductor market from iSuppli, DisplaySearch, and other third party sources. Market data attributed to iSuppli are from CCD and CMOS Image Sensors: to the Handset and Beyond, Consumer Platforms Topical Report Q3 2005 dated October 2005. Market data attributed to DisplaySearch are from Quarterly Worldwide Flat Panel Forecast Report dated October 19, 2005. Although we believe that this information is reliable, we cannot guarantee the accuracy and completeness of the information and have not independently verified it. As a result, you should be aware that market and other similar data set forth herein, and estimates and beliefs based on such data, may not be reliable. We do not have any obligation to announce or otherwise make publicly available updates or revisions to these forecasts. In many cases, we have made statements in this report regarding our industry and our position in the industry based on our experience in the industry and our own investigation of market conditions. We cannot assure you that any of these assumptions are accurate or that our assumptions correctly reflect our position in our industry.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report includes 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. These forward-looking statements represent expectations or beliefs of ours concerning future events, and no assurance can be given that the results described in this report will be achieved. These forward-looking statements can generally be identified by the use of statements that include words such as estimate, project, believe, expect, anticipate, intend, plan, likely, may, will, should or other similar words or phrases. All forward-looking statements are based upon information available to us on the da of this report.

These forward-looking statements are subject to risks, uncertainties and other factors, many of which are outside of our control, that could cause actual results to differ materially from the results discussed in the forward-looking statements, including, among other things, the matters discussed in this report in the sections captioned: Business, Risk factors and Management s discussion and analysis of financial condition and results of operations. There may be other factors that could cause our actual results to differ materially from the results referred to in the forward-looking statements. All forward-looking statements attributable to us or persons acting on our behalf apply only as of the date of this report and are expressly qualified in their entirety by the cautionary statements included in this report. We undertake no obligation to publicly update or revise forward-looking statements to reflect events or circumstances after the date made or to reflect the occurrence of unanticipated events. Readers are urged to carefully review and consider the various disclosures made in this report which attempt to advise interested parties of the risks and factors that may affect our business, financial condition, results of operations and prospects.

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Item 1. Business.

BUSINESS

OVERVIEW

MagnaChip Semiconductor LLC (MagnaChip) is a leading designer, developer and manufacturer of mixed-signal and digital multimedia semiconductors addressing the convergence of consumer electronics and communications devices. We focus on Complementary Metal-Oxide Semiconductor (CMOS) image sensors and flat panel display drivers, which are complex, high-performance mixed-signal semiconductors that capture images and enable and enhance the features and capabilities of both small and large flat panel displays. Our solutions are used in a wide variety of consumer and commercial mass market applications, such as mobile handsets, including camera-equipped mobile handsets, flat panel monitors and televisions, consumer home and mobile displays, portable and desktop computer displays, handheld gaming devices, PDAs and audio-visual equipment such as DVD players. We serve consumer markets that we believe will have higher growth rates than those of the overall semiconductor industry.

We manufacture our products using our proprietary process technology, which we believe provides our products with cost advantages over those of our competitors. We have approximately 11,900 registered and pending patents, which we believe is one of the largest patent portfolios in the semiconductor industry. We believe that our proprietary CMOS image sensor technology provides brighter, sharper, more colorful picture quality in image-capture applications such as camera-equipped mobile handsets. Our flat panel display drivers enable our customers to deliver higher image quality, thinner and more power-efficient small panel displays for use in mobile handsets, handheld gaming devices and PDAs and large panel displays for use in portable and desktop computer monitors and digital televisions. We are also a leading provider of wafer foundry services whereby we leverage our specialized process technologies and low cost manufacturing facilities to produce semiconductors for third parties using their product designs.

We own and operate five wafer fabrication facilities, or fabs, which have a combined production capacity of over 116,000 eight-inch equivalent wafers per month. Our fabs provide us with large-scale, cost-effective and flexible capacity, enabling us to rapidly scale to high volume to meet shifts in demand by our end customers. Our fabs also provide us with the ability to further develop our differentiated process technologies for our own product development and manufacturing. The location of our manufacturing sites and research and development resources in Korea, Japan, and the United States provide close geographical proximity to many of our largest customers and to the core of the worldwide consumer electronics supply chain.

We sell our solutions to leading original equipment manufacturers, or OEMs, which include major branded customers as well as contract manufacturers. Our CMOS image sensors are currently designed into products offered by leading global mobile handset manufacturers. Our flat panel display drivers are currently incorporated into products offered by top flat panel display manufacturers.

During the year ended December 31, 2005, we sold over 1,800 products to more than 300 customers. We generated actual net sales of $937.7 million for the twelve-month period ended December 31, 2005.

In the three-month period ended December 31, 2004, and the fiscal year ended December 31, 2005, we derived respectively 23.8% and 17.4% of our consolidated revenue from CMOS image sensors, 24.8% and 34.8% from flat panel display drivers, and 44.3% and 42.2% from semiconductor manufacturing services.

THE ORIGINAL ACQUISITION

Our business was named MagnaChip Semiconductor when it was acquired from Hynix Semiconductor Inc. on October 6, 2004, by Citigroup Venture Capital Equity Partners, L.P., or CVC, Francisco Partners L.P., or Francisco Partners, CVC Asia Pacific Limited, or CVC Asia Pacific, certain members of management and other investors, following discussions with Hynix that began in late 2001 and the execution of a definitive agreement

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in June 2004. Previously, we were the System IC division within Hynix which, in 1999, had been formed from the Hyundai Electronics and LG Semiconductor System IC businesses and can trace its history back to the late 1970s. Although we were previously part of Hynix, we had a history of operating autonomously within Hynix and had a separate global sales force and management structure.

In connection with the acquisition transaction, we entered into several definitive agreements with Hynix regarding key raw materials, campus facilities, research and development equipment and information technology, and factory automation and wafer foundry services. We also entered into a non-exclusive cross license with Hynix which provides us with access to certain of Hynix s intellectual property for use in the manufacture and sale of non-memory semiconductor products. We believe that these arrangements with Hynix provide significant mutual operational advantages, for example, allowing us to leverage the significant historical investments in our capital equipment and providing for shared resources and other key benefits. All agreements with Hynix under which we obtain essential materials or services are multi-year contracts. We refer to the acquisition transaction, including the related definitive agreements with Hynix, as the Original Acquisition. See Certain relationships and related transactions the Original Acquisition.

RECENT DEVELOPMENTS

On January 31, 2006, we completed the sale of our application processor business to ABOV Semiconductor Co., Ltd., a new independent entity formed by the investors in GreenChips Co., Ltd., a Korean semiconductor solution provider. We had entered into a definitive agreement for the sale on December 28, 2005. The application processor business primarily included assets, staff and intellectual property related to MagnaChip s 8-bit and 32-bit microcontroller, SmartCard controller, microperipheral IC, and linear IC product lines. MagnaChip retained a three percent equity stake in the new entity.

COMPETITIVE STRENGTHS

We believe that our competitive strengths include:

Leading Technology and Intellectual Property. We believe our advanced process technology and portfolio of approximately 11,900 registered and pending patents provide us with key competitive advantages in the following areas:

CMOS image sensors: Our CMOS image sensors feature low power consumption and currently up to 3.2 megapixel resolution with auto-focus and auto-zoom options; features which provide important benefits to products incorporating our solutions, including increased battery life, enhanced image quality and ease of use.

Flat panel display drivers: We believe that our flat panel display drivers offer superior performance in shaping image signals and transmitting those signals to flat panel displays. These technical features result in sharper, brighter and higher-quality colored images in our customers end products. Furthermore, we believe that our flat panel display drivers enable thinner and more power-efficient flat panels that are easily integrated by our customers into their products.

Semiconductor manufacturing services: We have developed high-voltage, analog power and embedded memory specialty manufacturing process technologies that enable us to manufacture differentiated, high performance integrated semiconductor devices. For example, we developed the first high-voltage, high-performance CMOS 0.18 μm process, which enables us to manufacture more integrated, and thus smaller and more cost-efficient, semiconductor products. We believe that our proprietary process technology allows us to meet a wide variety of the specialty semiconductor manufacturing needs of our customers.

Flexible In-House Manufacturing. Our in-house wafer manufacturing capacity allows us to provide dependable delivery and quality of integrated semiconductor products to our customers. We have the ability to ramp quickly to high volumes to meet the variable needs of our customers. We have significant wafer

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manufacturing capacity as a result of our former parent s investments in our wafer fabrication facilities. Because we offer specialty process technologies that do not require expensive investment in leading edge smaller geometry process equipment, we are able to keep our capital expenditures relatively low.

Significant Cost Advantages. We maintain price competitiveness on our products through our low cost operating structure. The Asian location of our primary manufacturing and research and development facilities provides us with a number of cost advantages relative to operating in other regions in the world. Additionally, we believe that our history of competing in the highly cost-sensitive markets in which we operated when we were a unit of Hynix required us to refine our manufacturing processes for optimal cost efficiency.

Established Relationships with Key Consumer Electronics OEMs. Our long history of operating in Asia and our proximity to leading communications and consumer OEMs facilitates our close customer relationships with leading innovators in the consumer electronics market. We have active local applications and engineering work support programs and collaborate closely with our customers in the design and manufacturing of their products.

Significant Management and Board Expertise. Our management and board of directors have significant previous experience with advanced semiconductor companies both in Asia and worldwide. Our top executives have many years in equivalent positions at such leading companies as Hynix, Samsung, Fairchild Semiconductor, ChipPAC, and Agilent Technologies. In addition, two of our equity sponsors, CVC and Francisco Partners, have a long history of investments in semiconductor companies. We believe that their understanding of semiconductor system solutions, relationships, and credibility with key customers provides us with a key competitive advantage.

BUSINESS STRATEGY

Our goal is to build upon our position as a leading provider of mixed-signal and digital multimedia semiconductors addressing the convergence of consumer electronics and communications devices. Our business strategy emphasizes the following key elements:

Leverage Our Substantial Intellectual Property. We intend to use our broad patent portfolio and specific end market expertise to deliver system-level products with higher levels of integration and performance to customers in our existing and new markets. In CMOS image sensors, we intend to leverage our strong pixel design and manufacturing expertise to introduce higher resolution, more integrated and cost-effective solutions for camera-equipped mobile handsets and to penetrate emerging applications for image sensors in the automotive, medical and industrial markets over time. In flat panel display drivers, we intend to leverage our broad library of circuit building blocks, our embedded memory capabilities, our understanding of the major flat panel display types and our process technology to continue to reduce time to market and introduce new products that enhance image quality and operate with greater power efficiency. Our manufacturing process expertise and related intellectual property underlies and supports many of the advances in our technology.

Strengthen Collaboration With Key Customers. We intend to continue strengthening and deepening relationships with our key customers by collaborating on critical design and product development roadmaps. We believe such collaborative relationships will solidify our position with our customers, further our competitive differentiation and accelerate our drive for deeper customer and new market penetration. For example, close collaboration with our mobile handset customers has allowed us to deliver improved interfaces between baseband and image processors, which have resulted in solutions with smaller form factor and improved image quality.

Increase Large Account Penetration. We have a global customer base consisting of leading consumer electronics OEMs and contract manufacturers. Many of our customers have multiple product variations that use image-capture and processing. We will seek to increase our customer penetration by taking advantage of our broad product portfolio and existing relationships to cross-sell existing products to our customers and to penetrate product variations where our solutions are currently not used.

Broaden Our Customer Base. We intend to expand our customer base across various applications and geographic locations by leveraging our position as a supplier to many of the largest global consumer electronics

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companies and delivering to potential customers proven, innovative solutions. We also believe that as consumer electronics and communications applications converge and proliferate, we will increasingly have opportunities to sell our products into new markets such as the automotive, medical and industrial markets. We also intend to expand our global sales presence to penetrate new accounts worldwide and grow existing account relationships. We will leverage our sales representatives and distributors located in Korea, Japan, China, Taiwan, Hong Kong, Germany, Italy, France, the United Kingdom and the United States to further these goals.

Leverage Our Capital Light Business Model. We acquired significant proprietary process technologies and wafer manufacturing capacity from our former parent, Hynix. We intend to leverage these investments made by Hynix to drive our growth and margin improvement. Furthermore, we plan to continue to keep our capital expenditures relatively low by maintaining our focus on specialty process technologies that do not require expensive investment in leading edge technologies. If needed, we will access other foundries that provide such technology in the future. We believe this approach will lead to a higher return on invested capital.

PRODUCTS AND SERVICES

We have a balanced portfolio of products that address many of the most rapidly growing consumer electronics markets. We provide products and services in the following three principal areas: CMOS image sensors, flat panel display drivers, and wafer foundry services.

CMOS Image Sensors. Our highly integrated image sensors are designed to be cost effective and to provide brighter, sharper, more colorful and, thus enhanced, image quality for use primarily in applications that require small form factors, low power consumption, effective heat dissipation and high reliability. Our image sensors fully satisfy these key criteria and are used in image capture applications such as camera-equipped mobile handsets and personal computer cameras. Our in-house manufacturing capabilities enable us to continuously fine tune our CMOS process technology to deliver improved image-capture sensitivity and accuracy.

CMOS image sensors are typically less expensive to produce and consume less power than other types of image sensors. Historically, CMOS image sensors were primarily used for low-cost applications for which high-image quality was not a priority. Recently, advances in semiconductor manufacturing processes and design techniques have led to improvements in CMOS image sensor performance and quality. As a result, CMOS image sensors have become useful, relatively low-cost solutions for use in applications such as camera-equipped mobile handsets and PDAs, where high-image quality, low power consumption, small size and low-cost are important considerations.

According to iSuppli, total worldwide image sensor revenue is expected to grow from $6.4 billion to $8.4 billion from 2005 to 2009, while unit shipments for area sensors such as our products will grow from 632 million units in 2005 to 1.1 billion units in 2009. Image sensor revenues for mobile communications are forecasted by iSuppli to grow from 28.7% of the total revenue in 2005 to 50.8% by 2009. Conversely, revenues for consumer electronics will drop from 45.9% to 26.2% of the total. The CMOS image sensor market is primarily driven by sales of camera-equipped mobile handsets. According to iSuppli, camera-equipped mobile handsets are the dominant application for CMOS image sensors and account for 89% and 86% of total shipments in 2005 and 2009 respectively. CMOS image sensor market for camera-equipped mobile handsets is predicted to increase from 435 million units in 2005 to 827 million units by 2009.

Our CMOS image sensors are characterized by a high level of integration. Many CMOS image sensors systems are made up of at least two integrated circuits: the CMOS image sensor itself and a separate image signal processor, or ISP. With the continuing demand for ever smaller camera-enabled devices, small size has become an increasingly important consideration for manufacturers of camera phones and similar products. Our products meet this demand for smaller form factors by integrating both our proprietary image sensor and image signal processor onto a single chip, thus occupying approximately half of the space required by multiple chip solutions, while providing equivalent or even superior image quality with lower power consumption and a lower overall cost.

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We offer CMOS image sensors with resolutions of VGA, 1.0MP (megapixels), 1.2MP, 1.3MP, 2.1MP and 3.2MP. Our solutions enable small form factor camera module implementations which are required for today s demanding industrial designs, such as very thin mobile phones. All of our solutions support both video and still capture modes, and provide sub-sampling modes to enable preview modes of operation with reduced power consumption. The choice of resolution by an OEM customer may involve many factors such as size, power and cost target. By offering a full line of solutions, we can service our customer s requirements across the multiple end products they may offer.

Flat Panel Display Drivers. Our flat panel display driver solutions are used in a wide variety of displays for mass market and commercial applications such as mobile handsets, handheld gaming devices, PDAs, displays for desktop and mobile computer monitors and flat panel televisions. We produce highly integrated flat panel display driver solutions and have pioneered developments in embedded memory and in the design and manufacturing of display drivers, enabling our customers to provide improved picture quality through thinner, smaller, more power-efficient displays.

Display drivers are the critical semiconductor components that enable the display s functionality. A display driver operates by interfacing with the host processor to generate the precise analog voltages and currents required to create images on the display. The performance characteristics of a display driver are critical to the quality and visual appeal of the images and text generated on the display and, in mobile devices, the power efficiency of the device. Our display drivers are highly integrated semiconductors that are customized for the particular needs of our customers. We believe that our design engineering expertise, technology leadership, manufacturing process expertise and library of functional building blocks produce display drivers that enable a wide variety of display types with high-impact visual performance.

The overall end market for flat panel display drivers is composed of a multitude of consumer electronics device markets such as television, laptop and desktop computers and portable consumer devices, including mobile handsets. This overall market can be broken down into several distinct sub-markets which we serve. These sub-markets include large panel TFTs, typically used in flat panel televisions and computer displays, small panel TFTs, typically used in mobile handsets, OLEDs and Color STNs. According to DisplaySearch, total worldwide flat panel display market unit shipments are projected to grow from 2.24 billion units in 2005 to 2.8 billion units in 2008.

We provide display drivers for use in several different types of display technologies and for a variety of end-market applications as discussed below.

TFT-LCD. TFT is an advanced active matrix LCD technology that uses a matrix of transistors embedded on a thin film of silicon to change the transparency of the LCD when voltage is applied. TFT-LCD technology is currently widely used for notebook computers and large scale flat panel monitors (Large TFT) as well as for displays for high-end mobile devices such as advanced mobile handsets (Small TFT). We currently provide Large TFT display drivers for use in mobile and desktop computer displays and in stand-alone flat panel television displays. We also provide Small TFT display drivers for use in mobile handsets, PDAs and in other consumer devices such as handheld gaming devices.

Color STN. Color STN is a low-power, low-cost solution based on passive matrix LCD technology and is widely used in color mobile displays available in the market today. Our Color STN display drivers are used in mobile applications such as mobile handsets, PDAs and handheld gaming devices.

Organic Light Emitting Diode or OLED. OLED is a relatively new display technology used in both mobile displays as well as in larger displays. OLED technology provides enhanced picture quality, low power consumption and long product life; it also has fast image response time, making it an ideal solution for displaying motion pictures on mobile devices. We currently offer display drivers for OLED displays used in mobile handsets and other mobile devices.

Semiconductor Manufacturing Services. We provide semiconductor manufacturing services primarily to semiconductor companies that do not have their own fabs. We target the market for diversified semiconductor

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products that require differentiated specialty process technologies for their manufacture including CMOS high-voltage, embedded memory, analog, power, and mixed-signal processes, which in general are not targeted by high-volume pure-play participants in the foundry market. We focus on specialty process technologies that do not require significant recurring capital investment, and we are able to better differentiate ourselves through the depth of our intellectual property portfolio and process technology skills.

The increasing trend toward the outsourcing of semiconductor manufacturing has resulted in a rapid increase in the size of this market. According to iSuppli, the worldwide foundry service market is projected to grow from in excess of $21.8 billion in 2005 to $39.2 billion in 2009, a compound annual growth rate of 15.8%.

Typical applications serviced by our semiconductor manufacturing services business are mixed-signal, high-voltage, power, and logic products for consumer, computer, network and communication, industrial and military end-markets. Our internal wafer fab facilities serve both our in-house product design groups and external foundry customers, allowing for both specialty process technology expertise and flexible manufacturing capacity. We target to be the primary-source provider of semiconductor manufacturing services for specialty process technologies for our foundry customers.

CUSTOMERS

During the year ended December 31, 2005, we sold over 1,800 products to more than 300 customers. In the year ended December 31, 2005, our 10 largest customers accounted for approximately 57.7% of our net sales. In the year ended December 31, 2005, our two largest customers, a group of LG affiliates including LG.Philips LCD, and a group of Samsung affiliates, represented 26.4% and 10.0% of our net sales, respectively. See Risk Factors A significant portion of our sales comes from a relatively limited number of customers.

Revenue classified by geography is determined by the headquarters locations of our customers. During the three-month period ended December 31, 2004, we received revenues of $9.3 million from external customers in the United States and $234.3 million from all foreign countries, of which 54.3% was from Korea, 16.2% from Japan, 12.8% from Taiwan, and 13.5% from China, Hong Kong, and Macau. During the year ended December 31, 2005, we received revenues of $45.5 million from external customers in the United States and $892.2 million from all foreign countries, of which 57.4% was from Korea, 11.0% from Japan, 16.0% from Taiwan, and 11.8% from China, Hong Kong, and Macau.

SALES, MARKETING AND DISTRIBUTION

We sell our products through a direct sales force and a network of authorized agents and distributors located throughout Asia, the United States, and Europe. We have strategically located our sales and technical support offices near concentrations of major customers.

Our direct sales force consists primarily of representatives located in our headquarters in Korea, as well as representatives located elsewhere throughout Asia, the United States, and Europe. Our network of authorized agents and distributors consists of agents in the United States and Europe and distributors and agents in the Asia Pacific region. During the year ended December 31, 2005, we derived approximately 68% of net sales through our direct sales force and 32% of net sales through our network of authorized agents and distributors.

Our product inventory is primarily located in Korea. Outside of Korea, we maintain limited amounts of product inventory, and our sales representatives generally relay orders to our headquarters for fulfillment. Some of the product inventory maintained by sales representatives is subject to return privileges or stock rotation. Our agreements with our authorized agents and distributors are usually terminable by either party on relatively short notice.

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RESEARCH AND DEVELOPMENT

Our expenditures for research and development were $107.6 million, representing 11.5% of net sales for the year ended December, 31, 2005, and $97.8 million, representing 9.0% of net sales for the year ended December 31, 2004. Our research and development efforts focus on process technology, design methodology and intellectual property for our semiconductor products and foundry services. As a result, we have implemented improvements to our manufacturing processes, design software and design libraries, including releasing our 0.18 μm high-voltage process and library. We also work closely with our major customers in many research and development activities, including joint intellectual property development, to increase the likelihood that our products will be more easily designed into the customers products and consequently achieve rapid and lasting market acceptance. In CMOS image sensors, we are focusing on pixel size reduction, thereby enabling smaller form factors and higher resolution sensors. In flat panel display drivers, we are focusing on further integration. In semiconductor manufacturing services, our research and development work allows us to add features such as mixed-signal, high voltage, embedded memory and power devices.

RAW MATERIALS

We use processes that require specialized raw materials that are generally available from a limited number of suppliers. We are currently attempting to qualify additional suppliers for many of our raw materials, including chemicals, gases, and tape, which is one of the process materials for our display drivers. Although we have not experienced any significant raw material shortages in the past, it is possible that going forward our business and results of operations could be adversely affected due to supply shortages or price increases for raw materials.

INTELLECTUAL PROPERTY

As of March 7, 2006, our portfolio of intellectual property assets included approximately 11,900 registered and pending patents. Our patents expire at various times over the next 18 years. While these patents are in the aggregate important to our competitive position, no single registered or pending patent is material to us.

Pursuant to the intellectual property license agreement that we entered into with Hynix in connection with the Original Acquisition, we obtained from Hynix a non-exclusive license to certain intellectual property of Hynix that is mostly patent-related, and we granted to Hynix a non-exclusive license to certain of our intellectual property. Additionally, we have entered into exclusive and non-exclusive licenses and development agreements with third parties relating to the use of intellectual property of the third parties in our products and our design processes, including licenses related to embedded memory technology, design tools, process simulation tools, circuit designs, and ARM s ARM7 and ARM9 core-based System-on-Chip.

In addition, we rely on proprietary know-how, continuing technological innovation and other trade secrets to develop products and maintain our competitive position. We attempt to protect our proprietary know-how and our other trade secrets by executing, when appropriate, confidentiality agreements with our customers and employees. We cannot assure you that our competitors will not discover comparable or the same knowledge and techniques through independent development or other means.

COMPETITION

We operate in highly competitive markets. Although no one company competes with us in all of our product lines, we face significant competition in each of our market segments.

Our competitors include other manufacturers and designers of system semiconductors, standard products, and semi-standard programmable digital logic semiconductor products, as well as customers who design their own semiconductors that are manufactured at third party foundries.

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We compete with other semiconductor providers based on design experience, the ability to service customer needs from the design phase to the shipping of a completed product, length of design cycle, longevity of technology support and sales and technical support personnel. Our ability to successfully compete depends on internal and external variables, both within and outside of our control. These variables include, but are not limited to, the timeliness with which we can develop new products and technologies, product performance and quality, manufacturing yields and availability, customer service, pricing, industry trends and general economic trends.

EMPLOYEES

Our worldwide workforce consisted of 3,858 employees (full- and part-time) as of March 1, 2006, of which 438 were involved in sales, general and administrative, 494 were in research and development, 110 were in quality, reliability and assurance and 2,816 were in manufacturing (comprised of 493 in engineering and 2,323 in operations). As of March 1, 2006, 2,389 employees, or approximately 62% of our workforce, were represented by the MagnaChip Semiconductor Labor Union, which is a member of the Federation of Korean Metal Workers Trade Unions.

Currently, members of the Korea Federation of Trade Unions, representing the employees of two subcontractors that we retained for only three months in 2004, have demonstrated and may continue to demonstrate at our campus in Cheongju, Korea. The Korea Federation of Trade Unions is requesting that MagnaChip directly hire approximately 90 employees of the former subcontractors. These demonstrations have required additional interim expenses and may have a continuing negative impact on our operations in the future.

ENVIRONMENTAL MATTERS

Our operations are subject to a variety of environmental, health and safety laws and regulations in each of the jurisdictions in which we operate, governing, among other things, air emissions, wastewater discharges, the generation, use, handling, storage and disposal of, and exposure to, hazardous substances (including asbestos) and wastes, soil and groundwater contamination and employee health and safety. These laws and regulations are complex, constantly changing and have tended to become more stringent over time. We cannot assure you that we have been, or will be at all times, in complete compliance with all these laws and regulations or that we will not incur material costs or liabilities in connection with these laws and regulations in the future. The adoption of new environmental, health and safety laws, the failure to comply with new or existing laws, or issues relating to hazardous substances could subject us to material liability (including substantial fines or penalties), impose the need for additional capital equipment or other process requirements upon us, curtail our operations, or restrict our ability to expand operations.

FOR MORE INFORMATION

We file periodic reports with the Securities and Exchange Commission. Copies of our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, and Current Reports on Form 8-K, including any amendments to these reports, are available on our website at www.magnachip.com. The public may also read and copy any materials we file with the SEC at the SEC s Public Reference Room at 100 F Street, NE, Washington, D.C. 20549, or on the SEC s website at www.sec.gov. For information on the operation of the Public Reference Room, please call the SEC at 1-800-SEC-0330.

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Item 1A. Risk Factors.

The cyclical nature of the semiconductor industry may limit our ability to maintain or increase net sales and profit levels during industry downturns.

The semiconductor industry is highly cyclical and periodically experiences significant economic downturns characterized by diminished product demand, resulting in production overcapacity and excess inventory in the markets we serve, which can result in rapid erosion of average selling prices. The industry has experienced significant downturns, often in connection with, or in anticipation of, maturing product cycles of both semiconductor companies and their customers products and the decline in general economic conditions.

We have experienced these conditions in our business in the past and may experience renewed, and possibly more severe and prolonged, downturns in the future as a result of such cyclical changes. This may reduce our profitability and the value of our business.

Customer demand is difficult to accurately forecast.

We make significant decisions, including determining the levels of business that we will seek and accept, production schedules, component procurement commitments, personnel needs and other resource requirements, based on our estimates of customer requirements. The short-term nature of commitments by many of our customers and the possibility of rapid changes in demand for their products reduces our ability to accurately estimate future customer demand. On occasion, customers may require rapid increases in production, which can challenge our resources and reduce margins. We may not have sufficient capacity at any given time to meet our customers increased demand for our product. Conversely, downturns in the semiconductor industry may cause and have caused our customers to significantly reduce the amount of products ordered from us. Because many of our costs and operating expenses are relatively fixed, a reduction in customer demand may decrease our gross margins and operating income.

Our customers may cancel their orders, change production quantities or delay production.

We generally do not obtain firm, long-term purchase commitments from our customers. Customers may cancel their orders, change production quantities or delay production for a number of reasons. Cancellations, reductions or delays by a significant customer or by a group of customers, which we have experienced as a result of the recent downturn in the semiconductor industry, have adversely affected and may continue to adversely affect our results of operations. In addition, while we do not obtain long-term purchase commitments, we generally agree to the pricing of a particular product for the entire lifecycle of the product, which can extend over a number of years. If we underestimate our costs when determining the pricing, our margins and results of operations would be adversely affected.

A significant portion of our sales comes from a relatively limited number of customers.

If we were to lose key customers or if customers cease to place orders for our high volume devices, our financial results will be adversely affected. While we served more than 300 customers in the twelve-month period ended December 31, 2005, net sales to our 10 largest customers represented approximately 57.7% of our net sales for the period. We had one individual customer and two groups of affiliated customers that each represented greater than 10% of our net sales during the year ended December 31, 2005. Significant reductions in sales to any of these customers, the loss of major customers or the curtailment of orders for our high-volume devices within a short period of time would adversely affect our business.

Our industry is highly competitive.

The semiconductor industry is highly competitive and includes hundreds of companies, a number of which have achieved substantial market share. Current and prospective customers for our products evaluate our

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capabilities against the merits of our direct competitors. Some of our competitors are well-established as independent companies and have substantially greater market share and manufacturing, financial, research and development and marketing resources than we do. We also compete with emerging companies that are attempting to sell their products in specialized markets, and with the internal capabilities of many of our significant customers. We expect to experience continuing competitive pressures in our markets from existing competitors and new entrants. Any consolidation among our competitors could enhance their product offerings and financial resources, further enhancing their competitive position. Our ability to compete successfully depends on a number of factors, including the following: our ability to offer cost effective products on a timely basis using our technologies; our ability to accurately identify and respond to emerging technological trends and demand for product features and performance characteristics; product introductions by our competitors; our ability to adopt or adapt to emerging industry standards; and the number and nature of our competitors in a given market. Many of these factors are outside of our control. In the future, our competitors may capture our existing or potential customers and our customers may satisfy more of their requirements internally. As a result, we may experience declining revenues and profits.

A decline in average selling prices could decrease our profits.

In the past, our industry has experienced a decline in average selling prices. A decline in average selling prices for our products, if not offset by reductions in the costs of producing such products, would decrease our gross profits and could have a material adverse effect on our business, financial condition and results of operations.

Growth in the consumer electronics and other end markets for our products is an important component in our success.

Our continued success will depend in part on the growth of various consumer electronics markets and other end markets that use our semiconductors and on general economic growth. To the extent that we cannot offset recessionary periods or periods of reduced growth that may occur in these markets through greater penetration of these markets, our sales may decline and our business, financial condition and results of operations may suffer as a result.

We depend on successful technological advances for growth.

Our industry is subject to rapid technological change and product obsolescence as customers and competitors create new and innovative products and technologies. Products or technologies developed by other companies may render our products or technologies obsolete or noncompetitive and we may not be able to access leading edge process technologies or to license or otherwise obtain essential intellectual property required by our customers. Our inability to continue identifying new product opportunities, or manufacturing technologically advanced products on a cost-effective basis, may result in decreased revenues and a loss of market share to our competitors.

We may not be able to attract or retain the technical or management employees necessary to remain competitive in our industry.

We depend on our ability to attract and retain skilled technical and managerial personnel. We could lose the services of, or fail to recruit, skilled personnel, which could hinder our research and product development programs or otherwise have a material adverse effect on our business.

If we encounter future labor problems, we may fail to deliver our products in a timely manner which could adversely affect our revenues and profitability.

As of March 1, 2006, approximately 62% of our employees were represented by the MagnaChip Semiconductor Labor Union, which is a member of the Federation of Korean Metal Workers Trade Unions. We

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cannot assure you that issues with the labor union and other employees will be resolved favorably for us in the future, that we will not experience significant work stoppages in future years or that we will not record significant charges related to those work stoppages.

We may incur costs to engage in future business combinations or strategic investments and the anticipated benefits of those transactions may not be realized.

As part of our business strategy, we may seek to enter into business combinations, investments, joint ventures and other strategic alliances with other companies in order to maintain and grow revenue and market presence as well as to provide us with access to technology, products and services. Those transactions would be accompanied by risks that may harm our business, such as difficulties in assimilating the operations, personnel and products of an acquired business or in realizing the projected benefits; disruption of our ongoing business; potential increases in our indebtedness and contingent liabilities; and charges if the acquired company or assets are later worth less than the amount paid for them in the Original Acquisition. In addition, our senior secured credit facility and the indentures governing our notes may prohibit us from making acquisitions that we may otherwise wish to pursue.

We depend on high utilization of our manufacturing capacity.

As many of our costs are fixed, a reduction in capacity utilization, together with other factors such as yield and product mix, could reduce our profit margins and adversely affect our operating results. A number of factors and circumstances may reduce utilization rates, including periods of industry overcapacity, low levels of customer orders, operating inefficiencies, mechanical failures and disruption of operations due to expansion or relocation of operations, power interruptions, fire, flood or other natural disasters or calamities.

The failure to achieve acceptable manufacturing yields could adversely affect our business.

The manufacture of semiconductors requires precision, a highly-regulated and sterile environment and expensive equipment. We may have difficulty achieving acceptable yields in the manufacture of our products. Slight impurities or defects in the masks used to print circuits on a wafer or other factors can cause significant difficulties, particularly in connection with the production of a new product, the adoption of a new manufacturing process or any expansion of our manufacturing capacity and related transitions.

We rely on certain subcontractors.

The majority of our net sales are derived from semiconductor devices assembled in advanced packages. The packaging of semiconductors is a complex process requiring, among other things, a high degree of technical skill and advanced equipment. We outsource our semiconductor packaging to subcontractors, most of which are located in Korea and Southeast Asia. We rely on these subcontractors to package our devices with acceptable quality and yield levels. If our semiconductor packagers experience problems in packaging our semiconductor devices or experience prolonged quality or yield problems, our operating results could be adversely affected.

We depend on successful parts and materials procurement for our manufacturing processes.

We use a wide range of parts and materials in the production of our semiconductors, including silicon, processing chemicals, processing gases, precious metals and electronic and mechanical components. We procure materials and electronic and mechanical components from domestic and foreign sources and original equipment manufacturers. As a division of Hynix, we were able to take advantage of Hynix s size and purchasing power in procuring parts and materials. As an independent company, we are smaller and less diversified than Hynix, and we may be unable to obtain parts and materials at prices and on terms as favorable as those available to us prior to the separation from Hynix in October 2004. If we cannot obtain adequate materials in a timely manner or on favorable terms for the manufacture of our products, either or both of our revenues or profits will decline.

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We face product liability risks and the risk of negative publicity if our products fail.

Our semiconductors are incorporated into a number of end products, and our business is exposed to product liability risk and the risk of negative publicity if our products fail. Although we maintain insurance for product liability claims, the amount and scope of our insurance may not be adequate to cover a product liability claim that is asserted against us. In addition, product liability insurance could become more expensive and difficult to maintain and, in the future, may not be available on commercially reasonable terms or at all.

In addition, we are exposed to the product liability risk and the risk of negative publicity affecting our customers and suppliers. Our sales may decline if any of our customers are sued on a product liability claim. We may also suffer a decline in sales from the negative publicity associated with such a lawsuit or with adverse public perceptions in general regarding our customers products.

Our ability to compete successfully and achieve future growth will depend, in part, on our ability to protect our proprietary technology, as well as our ability to operate without infringing the proprietary rights of others.

We seek to protect our proprietary technologies and know-how through the use of patents, trade secrets, confidentiality agreements and other security measures. The process of seeking patent protection takes a long time and is expensive. We cannot assure you that patents will issue from pending or future applications or that, if patents issue, they will not be challenged, invalidated or circumvented, or that the rights granted under the patents will provide us with meaningful protection or any commercial advantage. Some of our technologies are not covered by any patent or patent application. The confidentiality agreements on which we rely may be breached and may not be adequate to protect our proprietary technologies. We cannot assure you that other countries in which we market our services will protect our intellectual property rights to the same extent as the United States.

Our ability to compete successfully depends on our ability to operate without infringing the proprietary rights of others. We have no means of knowing what patent applications have been filed in the United States until they are published. In addition, the semiconductor industry is characterized by frequent litigation regarding patent and other intellectual property rights. Although we have never received any notices of infringement of a third party patent, we cannot assure you that third parties will not tender notices of patent infringement or assert infringement claims against us in the future. Litigation, which could result in substantial costs to us and diversion of our resources, may also be necessary to enforce our patents or other intellectual property rights or to defend against claimed infringement of the rights of others. In the event of an adverse outcome in any such litigation, we may be required to pay substantial damages, indemnify customers for damages they may suffer if the products they purchase from us violate the intellectual property rights of others, stop our manufacture, use, sale or importation of infringing products, expend significant resources to develop or acquire non-infringing technologies, discontinue processes or obtain licenses to the intellectual property we are found to have infringed. We cannot assure you that we would be successful in such development or acquisition or that such licenses would be available under reasonable terms, or at all.

As a business segment of Hynix, we were the beneficiary of some of Hynix s intellectual property arrangements, including cross-licensing arrangements with other leading semiconductor companies and licenses from third parties of technology incorporated in our products and used to operate our business. We are no longer a beneficiary under some of these agreements and arrangements. There may be third parties who had refrained from asserting intellectual property infringement claims against our products or processes while we were a business segment of Hynix that elect to pursue such claims against us now that we are an independent company. In addition, some of our technologies have been sublicensed from Hynix on a non-exclusive basis and Hynix may sublicense such technologies to others. We have cross-licensed most of our technologies to Hynix. This cross-license is subject to the non-competition provision of the Hynix business transfer agreement. Our competitors may develop, patent or gain access to similar know-how and technology. Failure to protect our

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existing intellectual property rights may result in the loss of valuable technologies or having to pay other companies for infringing on their intellectual property rights.

We are subject to many environmental laws and regulations that could affect our operations or result in significant expenses.

We are subject to requirements of environmental, health and safety laws and regulations in each of the jurisdictions in which we operate, governing, among other things, air emissions, wastewater discharges, the generation, use, handling, storage and disposal of, and exposure to, hazardous substances (including asbestos) and wastes, soil and groundwater contamination and employee health and safety. These laws and regulations are complex, constantly changing and have tended to become more stringent over time. We cannot assure you that we have been, or will be at all times, in complete compliance with all these laws and regulations or that we will not incur material costs or liabilities in connection with these laws and regulations in the future. The adoption of new environmental, health and safety laws, the failure to comply with new or existing laws, or issues relating to hazardous substances could subject us to material liability (including substantial fines or penalties), impose the need for additional capital equipment or other process requirements upon us, curtail our operations, or restrict our ability to expand operations.

We could suffer adverse tax and other financial consequences as a result of changes in, or differences in the interpretation of, applicable tax laws.

Our company organizational structure is based, in part, on assumptions about the various tax laws, including withholding tax, and other laws of applicable non-U.S. jurisdictions. In addition, MagnaChip Korea was granted a limited tax-holiday under Korean law in October 2004, which provides for certain tax exemptions for corporate taxes, withholding tax, acquisition taxes, property and land taxes and other taxes for five years. Our interpretations and conclusions are not binding on any taxing authority, and, if our assumptions about tax and other laws are incorrect or if the authorities were to change or modify the relevant laws, we could suffer adverse tax and other financial consequences or have the anticipated benefits of our company organizational structure materially impaired.

A limited number of persons indirectly control us.

CVC, Francisco Partners, and CVC Asia Pacific, own approximately 34%, 34% and 18%, respectively, of the outstanding voting interests in MagnaChip. By virtue of their ownership of these voting interests, and the securityholders agreement among MagnaChip and its unitholders, these entities have significant influence over our management and will be able to determine the outcome of all matters required to be submitted to the unitholders for approval, including the election of a majority of our directors and the approval of mergers, consolidations and the sale of all or substantially all of our assets.

We may need additional capital in the future and it may not be available on acceptable terms or at all.

We may require more capital in the future to fund our operations, finance investments in equipment and infrastructure, and respond to competitive pressures and potential strategic opportunities. Additional capital may not be available when needed or, if available, may not be available on satisfactory terms. If we are unable to obtain capital on favorable terms, or if we are unable to obtain capital at all, we may have to reduce our operations or forego opportunities and it may have a material adverse effect on our business, financial condition and results of operations.

Our international operations are subject to various risks that may lead to decreases in financial results.

We face risks inherent in international operations, such as unexpected changes in regulatory requirements, tariffs and other market barriers, political, social and economic instability, adverse tax consequences, war, civil disturbances and acts of terrorism, difficulties in accounts receivables collection, extended payment terms and

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differing labor standards, enforcement of contractual obligations and protection of intellectual property. These risks may lead to increased costs or decreased revenue growth, or both.

We are subject to risks associated with currency fluctuations.

Our revenues are denominated in various currencies, specifically, the Korean Won, Japanese Yen, Euro and U.S. dollar. As a result, changes in the exchange rates of these currencies or any other applicable currencies to the U.S. dollar will affect the translated price of products and therefore operating margins and could result in exchange losses.

The majority of our costs are denominated in Korean Won and to a lesser extent in Japanese Yen, U.S. dollar and Euro. Therefore, changes in the exchange rates of these currencies or any other applicable currencies to the U.S. dollar will affect cost of goods sold and operating margins and could result in exchange losses.

We cannot fully predict the impact of future exchange rate fluctuations on our profitability. From time to time, we may have engaged in, and may continue to engage in, exchange rate hedging activities in an effort to mitigate the impact of exchange rate fluctuations. However, we cannot assure you that any hedging technique we implement will be effective. If it is not effective, we may experience reduced operating margins.

Our historical financial information may not be representative of our results as a separate company.

Prior to the Original Acquisition, we operated as a division of Hynix. Historical financial information for periods prior to September 30, 2004, has been derived from Hynix s consolidated financial statements, is presented on a carve-out basis and does not necessarily reflect what our financial position, results of operations or cash flows would have been had we been a separate, stand-alone company during the periods presented. As carve-out financial statements, the financial statements include allocations of the costs of shared activities and overhead of Hynix and of intangible assets and property, plant and equipment shared with Hynix. These allocations are based upon various assumptions and estimates, some of which are subjective. Actual results of our operations had we operated on a stand-alone basis, may differ from those allocations and estimates. Also, as part of the Original Acquisition we did not acquire certain assets that were included in the carve-out financial statements and we assumed certain additional costs and obligations that are not reflected in the carve-out financial statements. Accordingly, the carve-out financial statements should not be relied upon as being representative of our financial position or operating results had we operated on a stand-alone basis, nor may they be representative of our financial position or operating results following the Original Acquisition.

Our expenses could increase if Hynix were unwilling or unable to provide certain services related to our shared facilities with Hynix.

Because we share certain facilities with Hynix, a few services that are essential to our business are provided to us by or through Hynix. These services include electricity, bulk gasses and de-ionized water, campus facilities, wastewater and sewage management, and environmental safety. If any of our agreements with Hynix were terminated or if Hynix were unwilling or unable to fulfill its obligations to us under the terms of these agreements, we would have to procure these services on our own and as a result may experience an increase in our expenses.

In addition, we lease building and warehouse space from Hynix in Cheongju, Korea, and lease to Hynix some of the space we own in Cheongju, Korea. If Hynix were to become insolvent, we could lose our leases on some of our building and warehouse space.

Research and development investments may not yield profitable and commercially viable products and thus will not necessarily result in increases in revenues for us.

We invest significant resources in our research and development. However, research and development efforts may not yield commercially viable products. During each stage of research and development there is a

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substantial risk that we will have to abandon a potential product which is no longer marketable and in which we have invested significant resources. In the event we are able to develop viable new products, a significant amount of time will have elapsed between our investment in the necessary research and development effort and the receipt of any related revenues.

Investor confidence may be adversely impacted if we are unable to comply with Section 404 of the Sarbanes-Oxley Act of 2002.

Beginning with our fiscal year ending December 31, 2007, we will be subject to rules adopted by the SEC pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, which require us to include in our Annual Report on Form 10-K our management s report on, and assessment of the effectiveness of, our internal controls over financial reporting. In addition, our independent auditors will be required to attest to and report on management s assessment of the effectiveness of our internal controls over financial reporting. If we fail to achieve and maintain the adequacy of our internal controls, there is a risk that we will not comply with all of the requirements imposed by Section 404. Moreover, effective internal controls, particularly those related to revenue recognition, are necessary for us to produce reliable financial reports and are important to helping prevent financial fraud. Any of these possible outcomes could result in an adverse reaction in the financial marketplace due to a loss of investor confidence in the reliability of our financial statements, which ultimately could harm our business and could negatively impact the market price of our securities.

Item 1B. Unresolved Staff Comments.

Not Applicable.

Item 2. Properties.

We own and operate five wafer fabrication facilities, or fabs, which have a combined production capacity of over 116,000 eight-inch equivalent wafers per month. We manufacture wafers at our two 8-inch fabs and our 6-inch fab located in Cheongju, Korea and our 8-inch fab and our 5-inch fab located in Gumi, Korea. The Cheongju facilities have three main buildings totaling 164,058 square meters. The Gumi facilities have two main buildings with 50,351 square meters devoted to manufacturing. We also lease from Hynix certain exclusive-use space plus certain common- and joint-use space in several buildings, primarily warehouses, in Cheongju, Korea.

In addition to our fabs located in Cheongju and Gumi, Korea, we lease facilities in Seoul, Korea, and Santa Clara, California. Each of these facilities includes administration, sales and marketing, research and development, and operations functions. We also lease design facilities in Mesa, Arizona, and Osaka, Japan, and sales and marketing offices at our subsidiaries in several other countries.

The ownership of our wafer manufacturing assets is an important component of our business strategy that enables us to develop proprietary, differentiated products and maintain a high level of manufacturing control resulting in high production yields, shortened design and production cycles, adequate manufacturing capacity, and the capture of the wafer manufacturing profit margin.

The table below sets forth information with respect to our manufacturing facilities and technologies:

Manufacturing

Facility	Location	Wafer Size	Technology
F-5	Cheongju	8	0.35 / 0.18 / 0.15µm
F-4	Cheongju	8	0.5 / 0.35 / 0.25µm
F-3	Gumi	8	0.5 / 0.35µm
F-2	Cheongju	6	0.8 / 0.6 / 0.5µm
F-1	Gumi	5	1.2µm

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We outsource most of our back-end manufacturing processes, including assembly, test and packaging to independent providers of these services.

Item 3. Legal Proceedings.

We are subject to lawsuits and claims that arise in the ordinary course of business and intellectual property litigation and infringement claims. Intellectual property litigation and infringement claims, in particular, could cause us to incur significant expenses or prevent us from selling our products. We are currently not involved in any legal proceedings, the outcome of which we believe would have a material adverse effect on our business, financial condition or results of operations.

Item 4. Submission of Matters to a Vote of Security Holders.

Effective December 7, 2005, a proposal by the Company to reserve an additional 1,000,000 common units of the Company, for an aggregate of 7,490,864 common units of the Company, for issuance upon the exercise of Options or SARs granted or Restricted Unit awards offered under the MagnaChip Semiconductor LLC California Equity Incentive Plan and the MagnaChip Semiconductor LLC Equity Incentive Plan was approved, as permitted under the Company s Third Amended and Restated Limited Liability Operating Company Agreement, by written consent of unitholders holding 41,840,446.51 common units of the Company constituting 78.88% of the then-outstanding common units of the Company.

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PART II

Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Market Information

There is currently no established public trading market for our outstanding common equity.

Holders

The approximate number of record holders of our outstanding class of common equity as of March 1, 2006, was 176.

Dividends

We did not pay any dividends in fiscal year 2005. Our ability to pay dividends is restricted by certain covenants contained in our senior credit facilities, as well as certain restrictions contained in our indentures relating to our senior notes and our subordinated notes.

Equity Compensation Plan Information

The information required by this item is incorporated by reference to the information set forth in Item 12 of this Annual Report on Form 10-K.

Recent Sales of Unregistered Securities

In December 2005 and January 2006, certain of our subsidiary s employees and former employees exercised options to acquire an aggregate of 9,062.5 of our common units at an aggregate purchase price of $21,663.13. Because the offering transaction took place outside the U.S. and none of the optionees were U.S. persons, these securities were exempt from registration under Regulation S of the Securities Act of 1933, as amended. On December 9, 2005, ISETEX, Inc., one of our consultants, exercised options to acquire 50,000 of our common units at a purchase price of $100,000.00. These securities were exempt from registration under Section 4(2) of the Securities Act of 1933, as amended, by reason of the fact that the offering was a limited private placement to one knowledgeable investor who agreed not to resell the securities to the public.

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Item 6. Selected Financial Data

	Year ended December 31, 2005	Three months ended December 31, 2004	Nine months ended September 30, 2004	Year ended December 31		
				2003	2002	2001
	(Successor Company)			(Predecessor Company)		
	(in millions of US dollars, except unit data)					
Statement of Operations Data						
Net Sales						
Related parties(1)	$	$	$ 163.8	$ 260.7	$ 306.8	$ 396.6
Others	937.7	243.6	677.8	570.1	393.5	481.1
	937.7	243.6	841.6	830.8	700.3	877.7
Cost of sales	729.0	204.5	654.6	752.5	691.0	768.9
Gross profit	208.7	39.1	187.0	78.3	9.3	108.8
Selling, general and administrative	123.3	29.8	54.0	68.7	61.9	104.8
Research and development	107.6	22.1	75.7	86.6	87.0	59.6
Restructuring and impairment charges	36.2					
Operating income (loss)	(58.4)	(12.8)	57.3	(77.0)	(139.6)	(55.6)
Interest expense, net	(57.2)	(16.7)	(17.7)	(37.8)	(46.8)	(90.9)
Foreign currency gain (loss), net	16.5	30.4	5.3	1.4	8.6	(9.8)
Others, net			1.1	1.1	1.3	1.4
Other income (expenses)	(40.7)	13.7	(11.3)	(35.3)	(36.9)	(99.3)
Income (loss) before income taxes	(99.1)	0.9	46.0	(112.3)	(176.5)	(154.9)
Income tax expenses	1.8	6.7	2.8	1.4	1.8	1.4
Net income (loss)	$ (100.9)	$ (5.8)	$ 43.2	$ (113.7)	$ (178.3)	$ (156.3)
Dividends to preferred unitholders	9.9	13.4	N/A	N/A	N/A	N/A
Net loss attributable to common units	$ (110.8)	$ (19.2)	N/A	N/A	N/A	N/A
Net loss per common unit basic and diluted	$ (2.10)	$ (0.38)	N/A	N/A	N/A	N/A
Weighted average number of units basic and diluted	52,898,497	50,061,910	N/A	N/A	N/A	N/A

On October 6, 2004, MagnaChip Semiconductor LLC completed its acquisition of our business from Hynix. For accounting purposes and consistent with our reporting periods, we have used October 1, 2004 as the effective date of the Original Acquisition since the financial results from October 1, 2004 onwards accrued to our benefit. As a result, we have reported our operating results and financial position for all periods from and after October 1, 2004, as those of the successor company. The predecessor company periods and the successor company periods have different bases of accounting and are therefore not comparable.

The information contained in this table should be read in conjunction with Item 7. Management s discussion and analysis of financial condition and results of operations and our historical financial statements and the accompanying notes thereto included elsewhere in this Form 10-K.

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	Year ended December 31, 2005	Three months ended December 31, 2004	Nine months ended September 30, 2004	Year ended December 31		
				2003	2002	2001
	(Successor Company)			(Predecessor Company)		
	(in millions of US dollars, except unit data)					
Balance Sheet Data						
Cash and cash equivalents	$ 86.6	$ 58.4	$	$	$	$
Working capital(2)	141.4	129.3	75.9	21.7	3.1	(43.7)
Total assets	1,040.6	1,154.5	653.8	790.0	1,077.8	1,299.5
Total indebtedness(3)	750.0	750.7	252.6	468.1	631.7	705.2
Preferred units	106.5	96.5				
Owners equity	N/A	N/A	206.7	155.3	268.3	412.1
Unitholders equity	(46.5)	55.9	N/A	N/A	N/A	N/A
Foreign exchange rate (KRW/USD)(4)						
Average exchange rate	1,023.8	1,090.8	1,163.3	1,191.8	1,250.3	1,292.0
End-of-period exchange rate	1,010.0	1,035.1	1,152.0	1,192.0	1,186.3	1,313.5

(1) Primarily relates to wafer foundry contract manufacturing services to Hynix Semiconductor, Inc., Hynix Display Technology and other related parties during the predecessor company period when the Company was the System IC division within Hynix.

(2) Working capital is calculated as current assets less current liabilities.

(3) Total indebtedness is calculated as long and short-term borrowings, including the current portion of long-term borrowings.

(4) As majority of the Company s revenue is incurred in KRW functional currency, conversion to US Dollar reporting currency is required at the end of each reporting period in order to follow the methodology prescribed in SFAS No. 52*, Foreign Currency Translation*.

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Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations

The following Management s Discussion and Analysis of Financial Condition and Results of Operations contain forward-looking statements within the meaning of the federal securities laws that involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors set forth elsewhere in this Form 10-K and in prior Company public filings with the SEC. In addition, other factors have been or may be discussed from time to time in the Company s SEC filings. These forward looking statements are made based upon management s expectations and beliefs concerning future events impacting the Company and, therefore, involve a number of risks and uncertainties. The Company s management cautions that forward looking statements are not guarantees and that actual results could differ materially from those expressed or implied in the forward looking statements. The following discussion should be read in conjunction with the audited consolidated financial statements and related notes included elsewhere in this Form 10-K. While the Company periodically reassesses material trends and uncertainties affecting the Company s results of operations and financial condition in connection with the preparation of Management s Discussion and Analysis of Financial Condition and Results of Operations and certain other sections contained in the Company s quarterly, annual or other reports filed with the SEC, the Company does not intend to review or revise any particular forward looking statement in light of future events.

Overview

We are a leading designer, developer and manufacturer of mixed-signal and digital multimedia semiconductors addressing the convergence of consumer electronics and communication devices. We focus our core business on CMOS image sensors and flat panel display drivers, which are complex, high-performance mixed-signal semiconductors that capture images and enable and enhance the features and capabilities of both small and large flat panel displays. We also provide wafer foundry services whereby we leverage our specialized process technologies and low cost manufacturing facilities to produce semiconductors for third parties using their product designs. Our solutions are used in a wide variety of consumer and commercial mass market applications, such as mobile handsets, including camera-equipped mobile handsets, flat panel monitors and televisions, consumer home and mobile displays, portable and desktop computer displays, handheld gaming devices, PDAs and audio-visual equipment such as DVD players.

We derive our net sales from products and services in three principal areas: CMOS imaging solutions, display solutions, and semiconductor manufacturing services.

CMOS imaging solutions: Our CMOS image sensor solutions are used in image-capture applications such as camera-equipped mobile handsets and personal computer cameras. Our highly integrated image sensors are designed to be cost-effective and to provide brighter, sharper, more colorful, and thus enhanced, image quality.

Display solutions: Our flat panel display drivers are used in several major types of large and small flat panel displays, including TFT-LCD, Color-STN and OLED displays. Our flat panel display solutions are used in applications such as mobile handsets, flat panel televisions, displays for portable and desktop computers, handheld gaming devices and PDAs.

Semiconductor manufacturing services: We use our process technology and manufacturing facilities to manufacture semiconductor wafers for third parties based on their designs. Our five fabs have a combined capacity of over 116,000 eight-inch equivalent wafers per month and are located in Cheongju and Gumi, Korea. Our fabs provide us with large scale, cost-effective and flexible capacity enabling us to rapidly scale to high volume to meet shifts in demand by our end customers.

Our business was named MagnaChip Semiconductor when it was acquired from Hynix Semiconductor Inc. on October 6, 2004, by CVC, Francisco Partners, CVC Asia Pacific, certain members of management and other investors, following discussions with Hynix that began in late 2001 and the execution of a definitive agreement

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in June 2004. Previously, we were the System IC division within Hynix which, in 1999, had been formed from a merger between the Hyundai Electronics and LG Semiconductor System IC businesses and can trace its history back to the late 1970s. Although we were previously part of Hynix, our business had a history of operating autonomously within Hynix and had a separate global sales force and management structure.

Basis of Presentation

Prior to October 1, 2004, our consolidated financial statements were prepared on a carve-out basis from the consolidated financial statements and accounting records of Hynix using the actual results of operations and actual basis of assets and liabilities of our business. The consolidated statements of operations include allocations of certain raw materials, other assets and accounts payable which our business has historically shared with Hynix, and allocations of certain manufacturing costs, general and administrative, sales and marketing, and other miscellaneous expenses. These allocations were made on a specifically identifiable basis or using the relative percentages, as compared to Hynix s other businesses, of sales, headcount, raw material consumption or other reasonable methods. Hynix and MagnaChip considered these allocations to be a reasonable reflection of the utilization of services provided. Our expenses as a separate, stand alone company may be higher or lower than the amounts reflected in the consolidated statements of operations.

We believe the assumptions underlying the consolidated financial statements are reasonable. However, the consolidated financial statements may not necessarily reflect our results of operations, financial position and cash flows in the future or what our results of operations, financial position and cash flows would have been, had we been a separate stand-alone company during the historical carve-out periods presented. As part of the Original Acquisition, we did not acquire certain assets that were included in the carve-out financial statements and we assumed certain additional obligations that are not reflected in the carve-out financial statements. Accordingly, the carve-out financial statements should not be relied upon as being representative of our financial position or operating results had we operated on a stand alone basis, nor may they be representative of our financial position or operating results following the Original Acquisition.

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RESULTS OF OPERATIONS

Comparison of Years Ended December 31, 2005 and December 31, 2004

	Year ended December 31, 2005 (Successor Company)		Three months ended December 31, 2004	Year ended December 31, 2004 Nine months ended September 30, 2004 (Predecessor Company)		Change 2005 vs. 2004	
	Amount	% of net sales	Amount	Amount	Amount	Amount	%
				(in millions of US dollars)			
Net sales							
Related party	$		$	$ 163.8	$ 163.8	15.1%	$ (163.8)	(100.0)%
Others	937.7	100.0%	243.6	677.8	921.4	84.9%	16.3	1.8%
	937.7	100.0%	243.6	841.6	1,085.2	100.0%	(147.5)	(13.6)%
Cost of sales	729.0	77.7%	204.5	654.6	859.1	79.2%	(130.1)	(15.1)%
Gross profit	208.7	22.3%	39.1	187.0	226.1	20.8%	(17.4)	(7.7)%
Selling, general and administrative expenses	123.3	13.1%	29.8	54.0	83.8	7.7%	39.5	47.1%
Research and development expenses	107.6	11.5%	22.1	75.7	97.8	9.0%	9.8	10.0%
Restructuring and impairment charges	36.2	3.9%					36.2	n/a
Operating income (loss)	(58.4)	(6.2)%	(12.8)	57.3	44.5	4.1%	(102.9)	(231.2)%
Interest expense, net	(57.2)	(6.1)%	(16.7)	(17.7)	(34.4)	(3.2)%	(22.8)	66.3%
Foreign currency gain (loss), net	16.5	1.8%	30.4	5.3	35.7	3.3%	(19.2)	(53.8)%
Others, net				1.1	1.1	0.1%	(1.1)	n/a
Income (loss) before income taxes	(99.1)	(10.5)%	0.9	46.0	46.9	4.3%	(146.0)	(311.3)%
Income tax expenses	1.8	0.2%	6.7	2.8	9.5	0.9%	(7.7)	(81.1)%
Net income (loss)	$ (100.9)	(10.7)%	$ (5.8)	$ 43.2	$ 37.4	3.4%	$ (138.3)	(369.8)%

Net Sales. Net sales for the year ended December 31, 2005 were $937.7 million, a $147.5 million or 13.6% decrease from $1.1 billion in 2004, which consisted of $841.6 million for the nine months ended September 30, 2004 and $243.6 million for the three months ended December 31, 2004. The reduction from prior-year revenue was primarily due to a decrease of $133.4 million or 72.8% in our DRAM foundry business with Hynix. This reduction was due to our strategic decision to focus manufacturing capacity and processes on expanding CMOS image sensor capability, which should help improve prospects for increased profitability and growth in the long term. The effect of this decision was a reduction in available capacity to supply Hynix with memory products and lower sales.

Revenues from our core business in 2005 increased $17.0 million or 2.1% from $817.8 million in 2004, driven by an increase of $66.9 million or 25.8% from our display solution business, partially offset by decreases of $36.8 million in CMOS imaging solution and $13.1 million in semiconductor manufacturing services. The increase of revenue in our display solution business was mainly due to an increase in market demand. Revenue decreases in our imaging solution business and semiconductor manufacturing services were attributable to lower average sales prices and increased competition in the market. Our Application Processor revenue decreased by

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$35.6 million or 43.1% as a result of the repositioning this product line, de-emphasizing optical storage device products to focus on consumer appliance and mobile device application areas.

Net sales to related parties during the year 2005 decreased by $163.8 million compared to 2004. Subsequent to the Original Acquisition date, all sales made to Hynix were classified as third party customer sales as the two companies are now separate and do not require related party revenue classification. Net sales to others in 2005 increased by $16.3 million or 1.8% compared to 2004.

Cost of Sales. Cost of sales was $729.0 million in 2005, a $130.1 million or 15.1% decrease from aggregate cost of sales of $859.1 million in 2004, which included $654.6 million for the nine months ended September 30, 2004 and $204.5 million for the three months ended December 31, 2004. The decrease was primarily due to a lower revenue base coupled with a reduction in depreciation expenses associated with the application of purchase accounting from the Original Acquisition. Cost of sales as a percentage of net sales decreased by 1.5% to 77.7% in the current year from 79.2% in the prior year.

Selling, General and Administrative Expenses. Selling, general and administrative expenses were $123.3 million or 13.1% of net sales in 2005. This represents a $39.5 million or 47.1% increase from a total of $83.8 million or 7.7% of net sales in 2004, which consisted of $54.0 million for the nine months ended September 30, 2004 and $29.8 million for the three months ended December 31, 2004. The increase in selling, general and administrative expenses was primarily attributable to amortization of intangible assets recorded upon the application of purchase accounting as a result of the Original Acquisition. We also recognized increased professional fees related to consulting and infrastructure build-out as well as additional warranty reserves to cover possible exposure of future claims from customers.

Research and Development Expenses. Research and development expenses in 2005 were $107.6 million, a $9.8 million or 10.0% increase from $97.8 million in 2004, which consisted of $75.7 million for the nine months ended September 30, 2004 and $22.1 million for the three months ended December 31, 2004. The increase in research and development expenses was mainly due to our reinforcement of research and development centers worldwide through our merger and acquisition and process development to support next generation products. As a percentage of net sales, research and development expense increased to 11.5% in 2005 from 9.0% in 2004.

Restructuring and Impairment Charges. During the year ended December 31, 2005, the Company recorded a one-time charge of $36.2 million of restructuring and impairment charges associated with the Company s initiative to focus on its core businesses and streamline the organization. The amount included $33.5 million for asset impairment and $2.7 million for restructuring.

Operating Income (loss). Operating loss in 2005 was $58.4 million, a $102.9 million or 231.2% decrease from an operating income of $44.5 million in 2004. Operating loss as a percentage of net sales was 6.2% in 2005 compared to the operating income as a percentage of net sales of 4.1% in 2004. The operating loss in 2005 was primarily attributable to lower revenue base and higher operating expenses including one-time charges, partially offset by improved gross margins.

Net Interest Expense. Net interest expense was $57.2 million in 2005, a $22.8 million or 66.3% increase from aggregated interest expense of $34.4 million in 2004, which consisted of $17.7 million for the nine months ended September 30, 2004 and $16.7 million for the three months ended December 31, 2004. The increase in net interest expense was primarily due to interest expenses incurred on the long-term debt of $750.0 million, which was issued in December 2004 and outstanding throughout the year 2005.

Income Tax Expense. Income tax expense was $1.8 million in 2005, compared to $6.7 million for the nine months ended September 31, 2004 and $2.8 million for the three months ended December 31, 2004, which on an aggregate basis totals $9.5 million for the year ended December 31, 2004. Income tax expense for the year ended December 31, 2005 was primarily attributable to $5.2 million of Korean withholding tax on the interest income

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paid to our Korean subsidiary s parent company. Income tax expense including this withholding tax was partially offset by the recognition of a deferred tax asset based on expected future utilization of the Company s temporary difference.

Comparison of Years Ended December 31, 2004 and December 31, 2003

	Year ended December 31, 2004						Change	
	Three months ended December 31, 2004	Nine months ended September 30, 2004	Year ended December 31, 2004		Year ended December 31, 2003		2004 vs. 2003	
	Amount (Successor Company)	Amount (Predecessor Company)	Amount	% of net sales	Amount	% of net sales	Amount	%
	(in millions of US dollars)							
Net sales								
Related party	$	$ 163.8	$ 163.8	15.1%	$ 260.7	31.4%	$ (96.9)	(37.2)%
Others	243.6	677.8	921.4	84.9%	570.1	68.6%	351.3	61.6%
	243.6	841.6	1,085.2	100.0%	830.8	100.0%	254.4	30.6%
Cost of sales	204.5	654.6	859.1	79.2%	752.5	90.6%	106.6	14.2%
Gross profit	39.1	187.0	226.1	20.8%	78.3	9.4%	147.8	188.8%
Selling, general and administrative expenses	29.8	54.0	83.8	7.7%	68.7	8.3%	15.1	22.0%
Research and development expenses	22.1	75.7	97.8	9.0%	86.6	10.4%	11.2	12.9%
Restructuring and impairment charges								n/a
Operating income (loss)	(12.8)	57.3	44.5	4.1%	(77.0)	(9.3)%	121.5	(157.8)%
Interest expense, net	(16.7)	(17.7)	(34.4)	(3.2)%	(37.8)	(4.5)%	3.4	(9.0)%
Foreign currency gain (loss), net	30.4	5.3	35.7	3.3%	1.4	0.2%	34.3	2,450.0%
Others, net		1.1	1.1	0.1%	1.1	0.1%		n/a
Income (loss) before income taxes	0.9	46.0	46.9	4.3%	(112.3)	(13.5)%	159.2	(141.8)%
Income tax expenses	6.7	2.8	9.5	0.9%	1.4	0.2%	8.1	578.6%
Net income (loss)	$ (5.8)	$ 43.2	$ 37.4	3.4%	$ (113.7)	(13.7)%	$ 151.1	(132.9)%

Net Sales. Net sales were $841.6 million for the nine-month period ended September 30, 2004 and $243.6 million for the three-month period ended December 31, 2004, which on an aggregate basis totals $1.1 billion in 2004, a $254.4 million or 30.6% increase from $830.8 million in 2003. This increase in net sales was primarily attributable to expansion of the camera-equipped mobile handset market and the increased demand for flat panel displays. Revenues from the CMOS image sensor and display solution businesses increased 193.2% and 39.2%, respectively, in 2004 versus the prior year. Semiconductor manufacturing services also grew by 69%. These increases in our three largest product groups were offset by declining revenue in application processors and DRAM foundry revenue.

Net sales to related parties were $163.8 million for the year ended December 31, 2004, a $96.9 million or 37.2% decrease from the prior year sale of $260.7 million. This decrease was largely due to the execution of our strategic plan to reduce our memory wafer production and realign capacity to address more profitable business opportunities.

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Net sales to others were $677.8 million for the nine-month period ended September 30, 2004 and $243.6 million for the three-month period ended December 31, 2004, which on an aggregate basis totals $921.4 million for the year ended December 31, 2004, a $351.3 million or 61.6% increase from the prior year net sales to others of $570.1 million. This increase was largely attributable to increased demand for camera-equipped mobile handsets and an increase in flat panel display market share.

Cost of Sales. Cost of sales were $654.6 million for the nine-month period ended September 30, 2004 and $204.5 million for the three-month period ended December 31, 2004, which on an aggregate basis totals $859.1 million for the year ended December 31, 2004, a $106.6 million or 14.2% increase from the prior year cost of sales of $752.5 million. Cost of sales as a percentage of net sales decreased to 79.2% for the year ended December 31, 2004 compared to 90.6% for the year ended December 31, 2003. The decrease in cost of sales as a percentage of net revenue was primarily attributable to increased volume and factory utilization, as well as improved product yields, that drove improved per unit costs. Depreciation costs were reduced for the three-month period ended December 31, 2004 as a result of the valuation of assets using purchase accounting. Improvements in the cost of procuring raw materials were partially offset by increases in labor and outsourcing costs.

Selling, General and Administrative Expenses. Selling, general and administrative expenses were $54.0 million for the nine-month period ended September 30, 2004 and $29.8 million for the three-month period ended December 31, 2004, which on an aggregate basis totals $83.8 million for the year ended December 31, 2004, a $15.1 million or 22.0% increase from the prior year amount of $68.7 million or 8.3% of net sales in the year ended December 31, 2003. The increase in SG&A expenses for the year ended December 31, 2004 was primarily attributable to increases in payroll and bonus expenses, infrastructure costs, professional fees, option expenses and amortization of intangible assets due to purchase accounting.

Research and Development Expenses. Research and development expenses were $75.7 million for the nine-month period ended September 30, 2004 and $22.1 million for the three-month period ended December 31, 2004, which on an aggregate basis totals $97.8 million for the year ended December 31, 2004, a $11.2 million or 12.9% increase from $86.6 million in 2003. This increase in research and development expenses was primarily attributable to the increase in labor costs, development tools and maintenance contracts. Research and development expenses as a percentage of net sales decreased to 9.0% in 2004 from 10.4% in 2003.

Operating Income (Loss). Aggregate operating income of $44.5 million for the year ended December 31, 2004 consisted of operating income of $57.3 million for the nine-month period ended September 30, 2004 and operating loss of $12.8 million for the three-month period ended December 31, 2004, a $121.5 million or 157.8% increase from $77.0 million of operating loss in 2003. Operating income as a percentage of net sales increased to 4.1% for the year ended December 31, 2004 from operating loss as a percentage of net sales of 9.3% for the year ended December 31, 2003. The increase in operating income and operating income as a percentage of net sales was principally due to an improvement in net sales that helped absorb fixed costs and improvements in gross profit.

Net Interest Expense. Net interest expense was $17.7 million for the nine-month period ended September 30, 2004 and $16.7 million for the three-month period ended December 31, 2004, which on an aggregate basis totals $34.4 million for the year ended December 31, 2004, a $3.4 million or 9.0% decrease from $37.8 million in 2003. Net interest expense for the year ended December 31, 2004 included the allocation of debt and related expense of $17.7 million on a carve-out basis as well as the interest expense on the bank loan and others of $16.2 million plus interest incurred on $750 million debt of $1.3 million.

Income Tax Expense. Income tax expense was $2.8 million for the nine-month period ended September 30, 2004 and $6.7 million for the three-month period ended December 31, 2004, which on an aggregate basis totals $9.5 million for the year ended December 31, 2004, a $8.1 million increase from the income tax expense of $1.4 million in 2003. The increase was principally attributable to the effect of the business transfer that occurred in the

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fourth quarter of fiscal year 2004. The Company decided not to recognize deferred tax assets for its temporary tax differences due to its uncertainty of realization, and this led to higher income tax expense in 2004.

Liquidity and Capital Resources

Our principal capital requirements are to fund working capital needs, meet required debt payments, including debt service payments on the notes and, if drawn upon, the senior credit facility, to invest in research and development and capital expenditures. We anticipate that operating cash flow, together with available borrowing capacity under our senior credit facility, will be sufficient to meet our working capital needs, our research and development and capital expenditures and service requirements on our debt obligations for the foreseeable future. As of December 31, 2005 we had total long-term debt outstanding of $750.0 million.

We generated cash from operating activities of $103.6 million during the year 2005, which principally reflects the Company s net loss of $100.9 million adjusted by non-cash depreciation and amortization expenses of $202.9 million. Cash from operating activities was reduced by $225.9 million or 68.6% from $329.5 million in 2004, which consisted of $312.2 million for the nine months ended September 30, 2004 and $17.3 million for three months ended December 31, 2004. The decrease in cash from operating activities between the two periods was primarily due to a 13.6% decrease in sales coupled with 47.1% increase in operating expenses.

Our working capital balance as of December 31, 2005 was $141.4 million compared to $129.3 million as of December 31, 2004. The increase of $12.1 million in working capital balance was primarily attributable to a higher balance in cash and cash equivalents at December 31, 2005. We had lower capital expenditures towards the end of 2005 compared to 2004, which led to increases in cash and cash equivalents at December 31, 2005.

For investing activities, we used cash of approximately $68.7 million for the year 2005 compared to $611.3 million for the year 2004 which consisted of $85.3 million for the nine months ended September 30, 2004 and $526.0 million for the three months ended December 31, 2004. The decrease in cash used for investing activities was primarily due to higher cash spending in 2004 associated with the Original Acquisition compared to cash spending on the acquisitions of ISRON Corporation and IC Media Corporation in 2005.

For financing activities, we used $12.8 million for the year ended December 31, 2005 and $216.8 million for the year ended December 31, 2004. In 2004, cash outflows of $226.8 million for the nine months ended September 30, 2004 was partially offset by cash inflows of $10.0 million for the three months ended December 31, 2004. The current year cash outlay was mainly due to repayment of short-term borrowings in the amount of $12.9 million. Cash outflow in 2004 is primarily due to the application of carve-out accounting, which assumed that cash flows from all other activities were used to repay any outstanding borrowings.

Capital Expenditures. For the year ended December 31, 2005, capital expenditures totaled $64.5 million compared to $110.2 million for the year ended December 31, 2004. Capital expenditure in 2004 composed of $86.7 million for the nine months ended September 30, 2004 and $23.5 million for the three months ended December 31, 2004. The year over year decrease was a result of managing capital expenditure timing in order to better support the growth of business from new customers and to optimize return on investment.

Future Financing Activities. Our primary future capital requirements on a recurring basis will be funding working capital needs, meeting required debt payments and funding research and development and capital expenditures. Specifically, going forward, we expect to expand our research and development headcount and make investments in advanced software and hardware design tools that increase our design engineer productivity. In addition, we plan to add design centers in key geographical locations near our strategic customers. We anticipate that operating cash flows, together with available borrowings under our senior credit facility, will be sufficient to meet these capital requirements for the foreseeable future. We may from time to time incur additional debt.

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We may need to incur additional debt or issue equity to make strategic acquisitions of investments. However, we cannot assure you that such financing will be available to us on acceptable terms or that such financing will be available at all.

Contractual Obligations

Summarized in the table below are our obligations and commitments to make future payments under debt obligations and minimum lease payment obligations as of December 31, 2005.

	Payments Due by Period							
	Total	2006	2007	2008	2009	2010	Thereafter	Interest expense
	(in millions of US Dollars)							
Revolving credit facility(*)								
Secured notes and subordinated notes(*)	750.0						750.0	
Operating lease	62.5	14.6	12.2	11.9	11.9	11.9		
Others	13.1	8.3	5.3	0.1				(0.6)

(*) Excludes interest obligations on revolving credit facility and notes.
The Floating Rate Second Priority Senior Secured Notes ($300 million) and Second Priority Senior Secured Notes ($200 million) mature in 2011, while Senior Subordinated Notes ($250 million) mature in 2014. Interest rates are 3 month LIBOR + 3.25%, 6 7/8% and 8%, respectively. These notes will be paid in full upon maturity.

Each indenture governing the notes contains covenants that limit the ability of the Company and its subsidiaries to (i) incur additional indebtedness, (ii) pay dividends or make other distributions on its capital stock or repurchase, repay or redeem its capital stock, (iii) make certain investments, (iv) incur liens, (v) enter into certain types of transactions with affiliates, (vi) create restrictions on the payment of dividends or other amounts to the Company by its subsidiaries, and (vii) sell all or substantially all of its assets or merge with or into other companies.

Unit/Stock-based Compensation Expense

For options granted to employees on or after October 6, 2004, we record a compensation charge equal to the excess, if any, of the deemed fair value of the stock at the measurement date over the option exercise price, in accordance with Accounting Principles Board Opinion No. 25. *Accounting for Stock Issued to Employees.* All of the option grants during this period reflected an exercise price equal to or higher than the fair value, and therefore, no compensation expense was recorded. For details refer to Note 14. Equity Incentive Plan in Item 8. Financial Statements and Supplementary Data.

Options were previously granted by Hynix to our employees and the related compensation costs are reflected in the historical financials. For the year ended December 31, 2003, and for nine months ended September 30, 2004, we recorded costs of $0.2 million and $3.3 million, respectively. However, none of these options were transferred as part of the Original Acquisition, and therefore, no additional future charges will be required related to these previously issued option grants. On the other hand, we have established new employee option plans and intend to make grants in the future.

Warrant

In connection with the Original Acquisition in October 2004, the Company issued a warrant to Hynix which enables Hynix to purchase 5,079,254 common units in the Company. The value of each unit issuable upon exercise of the warrant is $0.414, which was estimated using the Black-Scholes option pricing model. This warrant expires on the earlier to occur of October 6, 2006, and the date which is 45 days after the Company provides written notice to Hynix that the Company is filing a registration statement providing for a first public offering of its common equity interests. As of December 31, 2005, there had been no exercises of the warrant and the warrant remained outstanding.

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Off-Balance Sheet Arrangements

On December 23, 2004, two of the Company s subsidiaries, MagnaChip Semiconductor S.A. and MagnaChip Semiconductor Finance Company entered into a senior credit agreement with a syndicate of banks, financial institutions and other entities providing for a $100 million senior secured revolving credit facility. The undrawn portion of such new senior secured credit line amounted to $82,956 thousand and $86,295 thousand as of December 31, 2005 and 2004, respectively.

Other than the senior credit facility, there are no material off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

Recent Accounting Pronouncements

In December 2004, FASB issued SFAS 123(R), *Share-Based Payment (revised 2004)*. This revision will affect current practice in a number of ways, including the elimination of the alternative to use the intrinsic value method of accounting from Accounting Principles Board (APB) Opinion No. 25 that was provided in FASB Statement No.123 as originally issued. Pursuant to this statement, companies are required to record stock option expenses in its financial statements based on a fair value methodology. This statement will become effective and impact the Company on January 1, 2006. The Company has determined there are no material impacts on its financial statements as a result of the adoption of this proposed FASB Statement.

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs,* an amendment of ARB No. 43, Chapter 4. This Statement amends the guidance in Accounting Research Bulletin (ARB) No. 43, Chapter 4, *Inventory Pricing*, to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage), and requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. The effective date for the Company was January 1, 2005, and there was no material impact on our financial statements resulting from this proposed FASB Statement.

In May 2005, the FASB issued SFAS 154, *Accounting Changes and Error Corrections* a replacement of APB Opinion No. 20 and FASB Statement No. 3. This Statement supersedes APB Opinion No. 20, *Accounting Changes* and FASB Statement No. 3, *Reporting Accounting Changes in Interim Financial Statements*, and changes the requirements for the accounting and reporting for a change in accounting principle. This statement requires retrospective application to prior periods financial statements of changes in accounting principle, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. This standard is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The adoption of this standard will have no impact on our financial statements.

Critical Accounting Policies and Estimates

The preparation of financial statements and related disclosures in conformity with U.S. GAAP requires our management to make significant judgments and estimates that affect our financial position and results of operations. For a summary of our significant accounting policies, including the accounting policies discussed below, see Note 2 to the Consolidated Financial Statements.

Revenue Recognition and Valuation

Our revenue is derived from the sale of semiconductor products we design and the manufacture of semiconductor wafers for third parties. We recognize revenue when persuasive evidence of an arrangement exists, the product has been delivered and title and risk of loss have transferred, the price is fixed and determinable, and collection of resulting receivables is reasonably assured. For certain distributors, standard products are sold to the distributors without rights to return products or stock rotation or price protection rights.

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Generally we recognize revenue on shipment to the distributor or drop shipment to the end customer. Specialty foundry services are performed pursuant to manufacturing agreements and purchase orders. Standard products are shipped and sold based upon purchase orders from customers. All amounts billed to a customer related to shipping and handling are classified as sales, while all costs incurred by us for shipping and handling are classified as expenses. We currently manufacture a substantial portion of our products internally at our five wafer fabrication facilities. In the future, we expect to rely, to some extent, on outside wafer foundries for additional capacity and advanced technologies.

We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make payment. If the financial condition of our customers were to deteriorate, additional allowances may be required. The establishment of reserves for sales discounts is based on management judgment that requires significant estimates of a variety of factors, including forecasted demand, returns and industry pricing assumptions. We record warranty liabilities for the estimated costs that may be incurred under our limited warranty. This warranty covers product defects based on compliance to our specifications and is normally applicable for twelve months from the date of purchase. These liabilities are accrued when revenues are recognized. Warranty costs include the costs to replace the defective product. Factors that affect our warranty liability include historical and anticipated rate of warranty claims on those repairs and cost per claim to satisfy our warranty obligation. As these factors are impacted by actual experience and future expectations, we periodically assess the adequacy of our recorded warranty liabilities and adjust the amounts as necessary.

Inventory Valuation

Inventories are stated at the lower of cost or market, using the average method, which approximates the first in, first out method. If net realizable value is less than cost at the balance sheet date, the carrying amount is reduced to the realizable value, and the difference is recognized as a loss on valuation of inventories. We estimate the net realizable value for such finished goods and work-in-progress based primarily upon the latest invoice prices and current market conditions. Inventory reserves are established when conditions indicate that the net realizable value is less than cost due to physical deterioration, obsolescence, changes in price levels, or other causes. Reserves are also established for excess inventory based on inventory levels in excess of six months of projected demand, as judged by management, for each specific product.

As described above, in connection with the Acquisition and the application of purchase accounting, on October 1, 2004, we made adjustments to inventory to reflect fair value. As a result, the inventory and related reserves for historical periods presented on a carved-out basis, prior to October 1, 2004, are not representative of future levels of inventory and related reserves, after October 1, 2004.

Useful Lives of Tangible and Intangible Assets

We review property, plant and equipment and other long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Recoverability is measured by comparison of its carrying amount with the future net cash flows the assets are expected to generate. If such assets are considered to be impaired, the impaired amount is measured as the amount by which the carrying amount of the asset exceeds the present value of the future net cash flows generated by the respective long-lived assets. Our intellectual property assets represent rights under patents, trademarks and property use rights and are amortized over the periods of benefit, ranging up to 10 years, on a straight-line basis.

Intellectual Property

Our success and future sales growth will depend, in part, on our ability to protect our intellectual property. We rely on a combination of patent, copyright, trademark and trade secret laws, as well as nondisclosure agreements and other methods to protect our proprietary technologies. We have approximately 12,500 registered and pending patents. However, we cannot assure you that any patent will be issued as a result of any applications or, if issued, that any claims allowed will be sufficiently broad to protect our technology. In addition, it is possible that existing or future patents may be challenged, invalidated or circumvented.

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Income taxes

We account for income taxes in accordance with SFAS No. 109, Accounting for Income Taxes. SFAS No. 109 requires recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in a company s financial statements or tax returns. Under this method, deferred tax assets and liabilities are determined based upon the difference between the financial statement carrying amounts and the tax bases of assets and liabilities using enacted tax rates in effect in the years in which the differences are expected to reverse. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized. Income tax expense is the tax payable for the period and the change during the period in deferred tax assets and liabilities.

We established valuation allowances for deferred tax assets at most of our subsidiaries since it is not probable that majority of deferred tax assets other than one subsidiary are realizable. The valuation allowance at this particular subsidiary was not set up since it is expected that the deferred tax assets at this subsidiary is deemed realizable based on the current prospect for its future taxable income.

Contingencies and Litigation

We are subject to the possibility of losses from various contingencies. Considerable judgment is necessary to estimate the probability and amount of any loss from such contingencies. An accrual is made when it is probable that a liability has been incurred or an asset has been impaired and the amount of loss can be reasonably estimated. In such case, we accrue a liability and charges operations for the estimated costs of adjudication or settlement of asserted and unasserted claims existing as of the balance sheet date.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Market risk is the risk that the value of a financial instrument will fluctuate due to changes in market conditions, including changes in interest rates and foreign exchange rates. In the normal course of our business, we are subject to market risk associated with interest rate movements and currency movements on our assets and liabilities.

Foreign Currency Risk. We have exposure to foreign currency exchange-rate fluctuations on net income from our subsidiaries denominated in currencies other than U.S. dollars, as our foreign subsidiaries in Korea, Taiwan, China, Japan and Hong Kong use local currency as their functional currency. From time to time these subsidiaries have cash and financial instruments in local currency. The amounts held in Japan, Taiwan, Hong Kong and China are not material in regards to foreign currency movements. However, based on the cash and financial instruments balance at December 31, 2005 for our Korean subsidiary, a 10% devaluation of the Korean Won against the U.S. dollar would have resulted in a decrease of $6.0 million in our U.S. dollar financial instruments balance and cash balance.

Interest Rate Risk. The $200 million 6 7/8% Second Priority Senior Secured Notes due 2011 and the $250 million 8% Senior Subordinated Notes due 2014 are subject to changes in fair value due to interest rate changes. If the market interest rate had decreased by 10% and all other variables were held constant from their levels at December 31, 2005, we estimate that we would have additional interest expense costs over the market rate of $2.7 million (360 days basis). Our net loss for the year ended December 31, 2005 would have increased by 2.7%. The fair value on these fixed rate notes would have decreased by $10.2 million or increased by $10.6 million with a 10% increase or decrease in the interest rate, respectively.

Cash Flow Interest Rate Risk. During the current year, the Company entered into an interest rate swap agreement to convert the variable interest rate on our Floating Rate Second Priority Senior Secured Notes to a fixed interest rate for the periods to maturity date of June 2008. With this interest rate swap, cash flow interest rate risk was replaced with exposure to interest rate risk. For details, refer to Note 9. Short-term and Long-term Borrowings in Item 8. Financial Statements and Supplementary Data.

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Item 8. Financial Statements and Supplementary Data.

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Unitholders of

MagnaChip Semiconductor LLC (Successor Company)

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, of changes in unitholders equity and of cash flows present fairly, in all material respects, the financial position of MagnaChip Semiconductor LLC and its subsidiaries (the Company) at December 31, 2005 and 2004, and the results of their operations and their cash flows for the year ended December 31, 2005 and for the three-month period ended December 31, 2004 (successor basis), in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits of these statements 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 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

/s/ Samil PricewaterhouseCoopers

Seoul, Korea

March 24, 2006

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Unitholders of

MagnaChip Semiconductor LLC (Predecessor Company)

In our opinion, the accompanying consolidated (carve-out) statements of operations, of changes in owners equity and of cash flows present fairly, in all material respects, the results of operations and cash flows of MagnaChip Semiconductor LLC and its subsidiaries (Predecessor Company) (the Company) for the nine-month period ended September 30, 2004 and for the year ended December 31, 2003 (predecessor basis), in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits of these statements 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 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

/s/ Samil PricewaterhouseCoopers

Seoul, Korea

June 15, 2005

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MagnaChip Semiconductor LLC and Subsidiaries

Consolidated Statements of Operations

(In thousands of US dollars, except unit data)

	Year Ended December 31, 2005	Three months ended December 31, 2004	Nine months ended September 30, 2004	Year Ended December 31, 2003
	(Successor Company)		(Predecessor Company)	
Net sales				
Related party	$	$	$ 163,760	$ 260,739
Others	937,656	243,582	677,828	570,101
	937,656	243,582	841,588	830,840
Cost of sales	728,999	204,461	654,569	752,509
Gross profit	208,657	39,121	187,019	78,331
Selling, general and administrative expenses	123,211	29,784	53,982	68,738
Research and development expenses	107,590	22,058	75,657	86,575
Restructuring and impairment charges	36,234			
Operating income (loss)	(58,378)	(12,721)	57,380	(76,982)
Other income (expenses)				
Interest expense, net	(57,236)	(16,816)	(17,749)	(37,797)
Foreign currency gain (loss), net	16,532	30,437	5,364	1,404
Others			1,070	1,041
	(40,704)	13,621	(11,315)	(35,352)
Income (loss) before income taxes	(99,082)	900	46,065	(112,334)
Income tax expenses	1,816	6,725	2,828	1,389
Net income (loss)	$ (100,898)	$ (5,825)	$ 43,237	$ (113,723)
Dividends accrued on preferred units	9,928	13,428		
Net loss attributable to common units	$ (110,826)	$ (19,253)		
Net loss per common unit Basic and diluted	$ (2.10)	$ (0.38)		
Weighted average number of units Basic and diluted	52,898,497	50,061,910		

The accompanying notes are an integral part of these financial statements

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MagnaChip Semiconductor LLC and Subsidiaries

Consolidated Balance Sheets

(In thousands of US dollars, except unit data)

	December 31, 2005	December 31, 2004 (Successor Company)
Assets		
Current assets		
Cash and cash equivalents	$ 86,574	$ 58,396
Restricted cash	2,837	12,962
Accounts receivable, net	112,053	86,592
Inventories, net	88,677	86,169
Other receivables	9,501	72,918
Other current assets	10,148	6,915
Total current assets	309,790	323,952
Property, plant and equipment, net	485,077	581,636
Intangible assets, net	191,389	211,987
Other non-current assets	54,391	36,955
Total assets	$ 1,040,647	$ 1,154,530
Liabilities and Unitholders Equity		
Current liabilities		
Accounts payable	$ 93,911	$ 66,163
Other accounts payable	35,368	86,462
Accrued expenses	28,968	31,413
Short-term borrowings		749
Other current liabilities	10,102	9,892
Total current liabilities	168,349	194,679
Long-term borrowings	750,000	750,000
Accrued severance benefits, net	55,124	50,714
Other non-current liabilities	7,196	6,731
Total liabilities	980,669	1,002,124
Commitments and contingencies		
Series A redeemable convertible preferred units; 60,000 units authorized, 50,091 units issued and 0 unit outstanding at December 31, 2005 and 2004		
Series B redeemable convertible preferred units; 550,000 units authorized, 450,692 units issued and 93,997 units outstanding at December 31, 2005 and 2004	106,462	96,534
Total redeemable convertible preferred units	106,462	96,534
Unitholders equity		
Common units; 65,000,000 units authorized, 53,091,570 units and 52,533,003 units issued and outstanding at December 31, 2005 and December 31, 2004, respectively	53,092	52,533

Additional paid-in capital	2,169	2,100
Accumulated deficit	(130,092)	(19,266)
Accumulated other comprehensive income	28,347	20,505
Total unitholders equity	(46,484)	55,872
Total liabilities, redeemable convertible preferred units and unitholders equity	$ 1,040,647	$ 1,154,530

The accompanying notes are an integral part of these financial statements

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MagnaChip Semiconductor LLC and Subsidiaries

Consolidated Statements of Changes in Unitholders Equity and Owners Equity

(In thousands of US dollars, except unit data)

	Common Units						
	Units	Amount	Additional Paid-In Capital	Owner s Equity	Deferred Stock Compensation	Retained Earnings	Accumulated Other Comprehensive Income (loss)	Total
(Predecessor Company)								
Balance at January 1, 2003				$ 249,504	$ 2,189		$ 16,573	$ 268,266
Comprehensive income (loss) :								
Net loss				(113,723)				(113,723)
Foreign currency translation adjustments							610	610
Total comprehensive loss								(113,113)
Deferred stock compensation					161			161
Balance at December 31, 2003				$ 135,781	$ 2,350		$ 17,183	$ 155,314
Comprehensive income (loss) :								
Net income				43,237				43,237
Foreign currency translation adjustments							4,842	4,842
Total comprehensive loss								48,079
Deferred stock compensation					3,324			3,324
Balance at September 30, 2004				$ 179,018	$ 5,674		$ 22,025	$ 206,717
(Successor Company)								
Balance at October 1, 2004	49,713,286	$ 49,713	$			$ (13)	$ (116)	$ 49,584
Issuance of common units	363,627	364						364
Exercise of unit options	2,456,090	2,456						2,456
Issuance of warrants in connection with Original Acquisition			2,100					2,100
Payment of accumulated accrued dividends						(10,891)		(10,891)
Dividends accrued on Series B redeemable convertible preferred units						(2,537)		(2,537)
Comprehensive income (loss):								
Net loss						(5,825)		(5,825)
Foreign currency translation adjustments							20,621	20,621
Total comprehensive income								14,796
Balance at December 31, 2004	52,533,003	$ 52,533	$ 2,100			$ (19,266)	$ 20,505	$ 55,872
Issuance of common units	504,317	$ 504	$ 10					$ 514
Exercise of unit options	54,250	55	59					114
Dividends accrued on Series B redeemable convertible preferred units						(9,928)		(9,928)
Comprehensive income (loss):								
Net loss						(100,898)		(100,898)
Fair valuation of derivatives							4,534	4,534
Foreign currency translation adjustments							3,308	3,308

Total comprehensive income						(93,056)
Balance at December 31, 2005	53,091,570	$ 53,092	$ 2,169	$ (130,092)	$ 28,347	$ (46,484)

The accompanying notes are an integral part of these financial statements

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MagnaChip Semiconductor LLC and Subsidiaries

Consolidated Statements of Cash Flows

(In thousands of US dollars)

	Year Ended December 31, 2005	Three months ended December 31, 2004	Nine months ended September 30, 2004	Year Ended December 31, 2003
	(Successor Company)		(Predecessor Company)	
Cash flows from operating activities				
Net income (loss)	$ (100,898)	$ (5,825)	$ 43,237	$ (113,723)
Adjustments to reconcile net income (loss) to net cash provided by operating activities				
Depreciation and amortization	202,929	45,855	266,862	338,513
Provision for severance benefits	16,583	3,397	15,353	7,291
Amortization of debt issuance costs	3,432	4,411		
Loss (gain) on foreign currency translation, net	(15,880)	(33,263)	(3,811)	669
Loss (gain) on disposal of property, plant and equipment, net	(829)	(193)	(488)	2,279
Impairment charges	33,576			12
Stock compensation			3,324	161
Others	721	494	3,138	955
Changes in operating assets and liabilities				
Accounts receivable	(25,812)	(43,270)	(7,067)	(35,778)
Inventories	(806)	36,513	(18,070)	(1,454)
Other receivables	62,821	(56,917)	(548)	(628)
Deferred tax assets	(12,935)			
Accounts payable	24,928	(33,061)	(5,719)	(12,740)
Other accounts payable	(66,069)	81,509	18,329	(183)
Accrued expenses	(5,184)	17,711	584	724
Other current assets	2,713	(6,009)	(1,177)	3,082
Other current liabilities	200	9,842	1,450	2,000
Payment of severance benefits	(13,831)	(2,898)	(6,602)	(4,966)
Others	(2,012)	(1,011)	3,376	(4,138)
Net cash provided by operating activities	103,647	17,285	312,171	182,076
Cash flows from investing activities				
Purchase of plant, property and equipment	(62,334)	(23,346)	(84,595)	(22,640)
Purchases of intangible assets, net	(2,174)	(108)	(2,128)	(2,520)
Acquisition of business	(16,369)	(488,152)		
Decrease (increase) in restricted cash	10,307	(12,350)		
Others	1,878	(2,027)	1,392	3,679
Net cash used in investing activities	(68,692)	(525,983)	(85,331)	(21,481)
Cash flows from financing activities				
Proceeds from issuance of Senior Secured and Subordinated Notes		750,000		
Proceeds from long-term borrowings		45,867		79
Proceeds from short-term borrowings		720		28,582
Issuance of common units	628	2,820		
Issuance of redeemable convertible preferred units		3,636		
Repayment of short-term borrowings	(12,883)		(46,978)	(2,665)
Repayment of long-term borrowings		(347,718)	(179,862)	(186,591)
Redemption of redeemable convertible preferred units		(406,786)		
Payment of preferred dividends		(10,891)		

Debt issuance costs paid	(594)	(27,635)		
Others		(16)		
Net cash provided by (used in) financing activities	(12,849)	9,997	(226,840)	(160,595)
Effect of exchange rates on cash and cash equivalents	1,452	10,217		
Net increase (decrease) in cash and cash equivalents	23,558	(488,484)		
Cash and cash equivalents				
Beginning of the period	58,396	546,880		
Net increase in cash and cash equivalents from changes of consolidated subsidiaries	4,620			
End of the period	$ 86,574	$ 58,396	$	$
Supplemental cash flow information				
Cash paid for interest	$ 53,373	$ 11,862	$ 17,791	$ 37,872
Cash paid for income taxes	$ 15,370	$ 76	$ 2,828	$ 1,389

The accompanying notes are an integral part of these financial statements

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MagnaChip Semiconductor LLC and Subsidiaries

Notes to Consolidated Financial Statements

(Tabular dollars in thousands, except unit data)

1. General

The Company

MagnaChip Semiconductor LLC was created on November 26, 2003 and was capitalized on September 10, 2004, with the issuance of 60,822 common units for total cash and stock consideration of $61 thousand. It was created with the sole purpose of acquiring the non-memory business (the Business) of Hynix Semiconductor, Inc (Hynix), which acquisition was completed with effect from October 1, 2004 (the Original Acquisition).

On September 23, 2004, the Company issued 49,727 Series A redeemable convertible preferred units and 447,420 series B redeemable convertible preferred units for a total cash consideration of $49,727 thousand and $447,420 thousand, respectively. During the period from November 26, 2003 through October 1, 2004, MagnaChip Semiconductor LLC owned no assets or liabilities, other than the cash raised from its equity offerings in preparation for the Original Acquisition and the stock of its holding company and acquisition subsidiaries. In addition, during this period, MagnaChip Semiconductor LLC had no operations other than interest income from the cash totaling $22 thousand, and various bank fees and administrative expenses incurred in connection with its formation and the formation of its subsidiaries totaling $35 thousand. The accumulated other comprehensive income of $116 thousand was generated by the translation of the portion of the assets described above in its two consolidated subsidiaries at October 1, 2004, MagnaChip Semiconductor S.A. and MagnaChip Semiconductor B.V. At October 1, 2004, MagnaChip Semiconductor S.A. and MagnaChip Semiconductor B.V. were holding companies, with no significant operations, assets or liabilities other than holding cash raised in the equity offerings described above.

MagnaChip Semiconductor LLC and its subsidiaries (successor company) (the Company) is a designer, developer and manufacturer of mixed-signal and digital multimedia semiconductors addressing the convergence of consumer electronics and communications devices. The Company has five wafer fabrication facilities located in Cheongju and Gumi in the Republic of Korea.

2. Summary of Significant Accounting Policies

Basis of Presentation

The consolidated financial statements are presented in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). Significant accounting policies followed by the Company in the preparation of the accompanying financial statements are summarized below.

For the periods as of and prior to September 30, 2004, the accompanying consolidated financial statements are presented on a carve-out basis reflecting the assets, liabilities, revenues, expenses and changes in owner s equity and cash flows that were directly attributable to the Business of Hynix Semiconductor, Inc. (predecessor company), which was purchased on October 6, 2004. The Company has used October 1, 2004, as the effective date of the Original Acquisition since the financial results from October 1, 2004 onwards accrue to its benefit.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company including its wholly-owned subsidiaries. All significant intercompany transactions and balances are eliminated in consolidation.

Use of Estimates

The preparation of financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the accompanying financial statements and

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MagnaChip Semiconductor LLC and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Tabular dollars in thousands, except unit data)

disclosures. The most significant estimates and assumptions relate to the useful life of property, plant and equipment, allowance for uncollectible accounts receivable, contingent liabilities, inventory valuation, restructuring accrual and impairment of long-lived assets. Although these estimates are based on management s best knowledge of current events and actions that the Company may undertake in the future, actual results may be different from the estimates.

Foreign Currency Translation

The Company has assessed in accordance with Statements of Financial Accounting Standards (SFAS) 52, *Foreign Currency Translation*, the functional currency of each of its subsidiaries in Luxembourg, the Netherlands and the United Kingdom and has designated the U.S. dollar to be their respective functional currencies. The Company and its other subsidiaries are utilizing their local currencies as their functional currencies. The financial statements of the subsidiaries in functional currencies other than the U.S. dollar are translated into the U.S. dollar in accordance with SFAS No. 52. All the assets and liabilities are translated to the U.S. dollar at the end-of-period exchange rates. Capital accounts are determined to be of a permanent nature and are therefore translated using historical exchange rates. Revenues and expenses are translated using average exchange rates. Foreign currency translation adjustments arising from differences in exchange rates from period to period are included in the foreign currency translation adjustment account in accumulated comprehensive income (loss) of unitholders equity. Transactions in currencies other than the functional currency are included as a component of other income (expense) in the statement of operations.

Cash and Cash Equivalents

Cash equivalents consist of highly liquid investments with an original maturity date of three months or less. Restricted cash includes amounts placed in deposits at Korean banks, subject to certain withdrawal restraints for government grants, other payables and checking accounts plus amounts pledged as collateral for the obligations under our senior secured revolving credit facility and our Second Priority Senior Secured Notes.

Accounts receivable reserves

An allowance for doubtful accounts is provided based on the aggregate estimated collectibility of their accounts receivable. The Company records an allowance for cash returns, presented within accounts receivable, based on the historical experience of the amount of goods that will be returned and refunded. In addition, the Company also includes in accounts receivable, an allowance for additional products that may have to be provided, free of charge, to compensate customers for products that do not meet previously agreed yield criteria, the low yield compensative reserve.

Inventories

Inventories are stated at the lower of cost or market, using the average cost method, which approximates the first in, first out method (FIFO). If net realizable value is less than cost at the balance sheet date, the carrying amount is reduced to the realizable value, and the difference is recognized as a loss on valuation of inventories. Inventory reserves are established when conditions indicate that the net realizable value is less than cost due to physical deterioration, obsolescence, changes in price levels, or other causes. Reserves are also established for excess inventory based on inventory levels in excess of six months of projected demand, as judged by management, for each specific product.

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MagnaChip Semiconductor LLC and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Tabular dollars in thousands, except unit data)

Property, Plant and Equipment

Property, plant and equipment are stated at cost, less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets as set forth below.

Buildings	30 - 40 years
Building related structures	10 - 20 years
Machinery and equipment	5 - 10 years
Vehicles and others	5 years

Routine maintenance and repairs are charged to expense as incurred. Expenditures that enhance the value or significantly extend the useful lives of the related assets are capitalized.

Borrowing costs incurred during the construction period of assets are capitalized as part of the related assets.

Impairment of Long-Lived Assets

The Company reviews property, plant and equipment and other long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Recoverability is measured by comparison of its carrying amount with the future net cash flows the assets are expected to generate. If such assets are considered to be impaired, the impaired amount is measured as the amount by which the carrying amount of the asset exceeds the present value of the future net cash flows generated by the respective long-lived assets.

Restructuring Charges

The Company recognizes restructuring charges in accordance with Statements of Financial Accounting Standards (SFAS) 146, *Accounting for Costs Associated with Exit or Disposal Activities.* Certain costs and expenses related to exit or disposal activities are recorded as restructuring charges when liabilities for those costs and expenses are incurred.

Lease Transactions

The Company accounts for lease transactions as either operating leases or capital leases, depending on the terms of the underlying lease agreements. Machinery and equipment acquired under capital lease agreements are recorded at cost as property, plant and equipment and depreciated using the straight-line method over their estimated useful lives. In addition, the aggregate lease payments are recorded as capital lease