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**IQE PLC**

**Report and Financial Statements**

**31 December 1999**

**Deloitte & Touche  
Blenheim House  
Fitzalan Court  
Newport Road  
Cardiff CF24 0TS**



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**REPORT AND FINANCIAL STATEMENTS 1999**

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**REPORT AND FINANCIAL STATEMENTS 1999**

**OFFICERS AND PROFESSIONAL ADVISERS**

**DIRECTORS**

Dr A W Nelson  
Dr G H H Ainsworth  
Dr M D Scott  
G Bressner  
S Massie  
T Hierl

**SECRETARY**

J L Coventry

**REGISTERED OFFICE**

Pascal Close  
Cypress Drive  
St Mellons  
Cardiff  
CF3 8EG

**BANKERS**

Barclays Bank plc

**SOLICITORS**

Eversheds

**AUDITORS**

Deloitte & Touche  
Chartered Accountants  
Blenheim House  
Fitzalan Court  
Newport Road  
Cardiff  
CF24 0TS

**CHAIRMAN'S STATEMENT**

1999 has seen a meteoric rise in interest for compound semiconductor materials with a number of important developments in the fields of fibre-optic and mobile telecommunications, data storage devices, automotive products and display technologies. IQE has been uniquely placed to capitalise on advances in all of these rapidly growing market sectors and, against a background of limited production capacity product development and process qualification, has achieved a 20% increase in turnover from £15.8m in 1998 to £19.0m in 1999. Over the same period, excluding merger costs, the group has realised a 143% increase in post tax profits.

Formed in April 1999 through the merger of Epitaxial Products International of Cardiff, UK and Quantum Epitaxial Designs of Bethlehem, PA, USA, IQE has established itself as the largest pure-clay merchant epitaxy foundry worldwide, supplying specialised compound semiconductor wafers to many of the world's largest component manufacturers. The merger between EPI and QED and to form IQE has given our customers multi-level access to the two leading technologies that are fundamental to the growth of the compound semiconductor industry. Each company brought to the merged group over ten years of valuable experience in the manufacture of compound semiconductor materials. Since IQE went public on 27<sup>th</sup> May 1999, the value of our shares had more than tripled by the end of the year, giving a market capitalisation of over £300 million. profits.

Compound semiconductors are the enabling technology behind many of today's advanced electronic and opto-electronic devices. Epitaxy is the key technology in the manufacture of compound semiconductors. One example where our products are absolutely key is in the telecommunications revolution, which continues to gain pace rapidly. Until recently, data communication activities such as the internet, used the telephone system as the vehicle to transmit and receive data. This very concept is changing as the volume of data is already exceeding that of speech over the traditional telephone system,. In the future, voice communications will be a relatively small activity that will happen over the "datacomms" network. Both hand based and mobile communications are relying more and more on our products in the form of emitters and detectors for fibre optic systems and in high speed, low power consumption components for mobile communications devices. IQE is ideally placed to take maximum advantage of the explosion in the communications infrastructure, required to support the dramatic growth in internet and datacomms. In addition, a host of other exciting developments including the "lighting revolution" where today's bulbs will be replaced by compound semiconductor high brightness LEDs will continue to drive exceptional demand for our products for many years to come.

We have put in place an aggressive capacity expansion plan which anticipates our customer demands for a variety of products. Our core objective is to utilise the largest and most advanced production platforms available to reduce our per wafer costs and offer an exceptional service to our customers. We look forward to the future with great anticipation.



Dr Drew Nelson  
Chair

**DIRECTORS' REPORT**

The directors present their annual report and the audited financial statements for the year ended 31 December 1999.

**ACTIVITIES**

The principal activity of the group during the year was the manufacture of advanced semi conductor materials.

**REVIEW OF DEVELOPMENTS AND FUTURE PROSPECTS**

The company was incorporated on 1 April 1999 as Filbuk 566 Public Limited Company. The name was changed to IQE plc on 26 April 1999. IQE plc acquired the entire share capital of EPI Holdings Limited and Quantum Epitaxial Designs Inc on 3 May 1999 via a share for share exchange. IQE plc was floated on EASDAQ on 27 May 1999.

A review of developments within the group during 1999 is contained in the Chairman's Report. Having established itself as the worlds largest pure-play merchant epitaxy foundry, the group achieved a 20% increase in turnover during the year £19,034K (1998: £15,856K) despite being constrained by limited production capacity at its sites in the UK and America. Post tax profits also increased significantly to £842K (1998: £552K) despite charging exceptional costs of £499K (1998: £nil) associated with the merger of EPI Holdings Limited and Quantum Epitaxial Designs Inc.

In order to address the issue of production capacity, the group has embarked upon an aggressive capital expenditure program to significantly increase the range of reactors at both sites and has already installed and placed into production several new machines in the last quarter of 1999 and the first quarter of 2000. These, together with further expansion scheduled for later in the current year and into 2001, will enable the group to meet rapidly increasing customer demand for its variety of products. The directors are confident that the combination of reduced per wafer costs and exceptional customer service will strengthen the group's position at the forefront of the industry, and they therefore can look forward to the future with great anticipation.

**DIVIDENDS**

The directors do not recommend the payment of a dividend. Dividends totalling £140,000 are shown in the profit and loss account for the year ended 31 December 1998. These represent dividends paid by EPI Holdings Limited prior to IQE plc acquiring this company. These are included in the 1998 profit and loss under the merger accounting provisions as explained in Note 1 to the accounts.

**DIRECTORS**

The directors in office throughout the year and their beneficial interests in the company's issued ordinary share capital were as follows:

	Ordinary shares of 10p each	
	1999 No.	On incorporation/ appointment No.
Dr A W Nelson (appointed 13 April 1999)	2,998,590	-
Dr G H H Ainsworth (appointed 22 April 1999)	541	-
Dr M D Scott (appointed 13 April 1999)	2,998,590	-
G Bressner (appointed 30 April 1999)	-	-
S Massie (appointed 30 April 1999)	20,568	-
T Hierl (appointed 30 April 1999)	1,902,228	-

**DIRECTORS' REPORT (continued)**

S Massie held options for 144,996 unissued ordinary shares at 31 December 1999. No other director held share options. Further details are given in note 4 to the accounts.

Filbuk Nominees Limited and Filbuk (Secretaries) Limited were appointed as directors on incorporation. Both resigned on 14 April 1999.

**YEAR 2000**

Following their initial review, the directors continue to be alert to the potential risks and uncertainties surrounding the year 2000 issue. As at the date of this report, the directors are not aware of any significant factors which have arisen, or that may arise, which will affect the activities of the business, however the situation is still being monitored. Any future costs associated with this issue cannot be quantified but are not anticipated to be significant.

**RESEARCH AND DEVELOPMENT**

During the year the group incurred costs in respect of research and development of £1,302,338 (1998: £1,529,316). All research and development expenditure is charged to the profit and loss account in the period it is incurred.

**PAYMENT TERMS**

During the year ended 31 December 1999, it was the group's policy to follow the "Better Payment Practice Code" which was issued on 27 October 1988 on supplier payment. The group will adhere to the principles of this document that is available by telephoning 0870 150 2500. The group agrees payment terms in advance with individual suppliers and abides by the terms. The group's average number of days purchases outstanding in respect of trade creditors at 31 December 1999 was 38 days (1998 – 56 days).

**AUDITORS**

Deloitte & Touche were appointed first auditors to the company on 13 April 1999 have expressed their willingness to continue in office as auditors and a resolution to reappoint them will be proposed at the forthcoming Annual General Meeting.

Approved by the Board of Directors  
and signed on behalf of the Board



J.L. Coventry

Secretary

20 March 2000

## STATEMENT OF DIRECTORS' RESPONSIBILITIES

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and the group as at the end of the financial year and of the profit or loss of the group for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the company and the group and to enable them to ensure that the financial statements comply with the Companies Act. They are also responsible for safeguarding the assets of the company and the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

## AUDITORS' REPORT TO THE MEMBERS OF IQE PLC

We have audited the financial statements on pages 7 to 26 which have been prepared under the accounting policies set out on page 12 and 13.

### Respective responsibilities of directors and auditors

As described on page 5 the company's directors are responsible for the preparation of financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

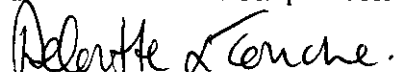
### Basis of opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's and group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

### Opinion

In our opinion the financial statements give a true and fair view of the state of the affairs of the company and the group as at 31 December 1999 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

  
Deloitte & Touche

Chartered Accountants and Registered Auditors

Date 20 March 2000

**CONSOLIDATED PROFIT AND LOSS ACCOUNT**  
Year ended 31 December 1999

	Note	1999 £'000	1998 £'000
<b>TURNOVER</b>	2	19,043	15,856
Cost of sales		(12,558)	(10,170)
<b>GROSS PROFIT</b>		6,485	5,686
Administrative expenses:			
Research and development		(1,302)	(1,529)
Other administrative expenses		(3,974)	(3,032)
		(5,276)	(4,561)
Other operating income		74	45
<b>OPERATING PROFIT</b>	3	1,283	1,170
Other interest receivable and similar income		327	17
Interest payable and similar charges	5, 10	(917)	(405)
<b>PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION</b>		693	782
Tax on profit on ordinary activities	6	149	(230)
<b>PROFIT FOR THE FINANCIAL YEAR</b>		842	552
<b>DIVIDENDS</b>	7	-	(140)
<b>RETAINED PROFIT FOR THE FINANCIAL YEAR</b>		842	412
Earnings per ordinary share	9	6.34p	5.31p
Diluted earnings per ordinary share	9	5.87p	4.86p

All the activities derive from continuing operations.

**CONSOLIDATED STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES**  
Year ended 31 December 1999

	1999 £'000	1998 £'000
Profit for the financial year	842	412
Currency translation differences on foreign currency net investments	96	1
	<u>938</u>	<u>413</u>
Total recognised gains and losses relating to the year	<u>938</u>	<u>413</u>

**COMBINED STATEMENT OF MOVEMENTS IN SHAREHOLDERS' FUNDS AND  
STATEMENT OF MOVEMENTS ON RESERVES**  
Year ended 31 December 1999

	Issued share capital £'000	Share premium £'000	Merger reserve £'000	Profit and loss account £'000	Exchange rate reserve £'000	Total 1999 £'000	Total 1998 £'000
<b>THE GROUP</b>							
Balance at 1 January 1999	1,040	-	(760)	439	(88)	631	17
Shares issued	319	20,121	-	-	-	20,440	-
Cost of shares issued	-	(1,214)	-	-	-	(1,214)	-
Adjustment in respect of further share capital issued by subsidiary	-	-	155	-	-	155	201
Foreign exchange translation difference	-	-	-	-	96	96	1
Profit attributable to members of the group	-	-	-	842	-	842	412
	<u>1,359</u>	<u>18,907</u>	<u>(605)</u>	<u>1,281</u>	<u>8</u>	<u>20,950</u>	<u>631</u>
Balance at 31 December 1999	<u>1,359</u>	<u>18,907</u>	<u>(605)</u>	<u>1,281</u>	<u>8</u>	<u>20,950</u>	<u>631</u>
<b>THE COMPANY</b>							
Balance at 1 January 1999	-	-	-	-	-	-	-
Shares issued	1,359	20,121	-	-	-	21,480	-
Cost of shares issued	-	(1,214)	-	-	-	(1,214)	-
Profit attributable to members of the company	-	-	-	692	-	692	-
	<u>1,359</u>	<u>18,907</u>	<u>-</u>	<u>692</u>	<u>-</u>	<u>20,958</u>	<u>-</u>
Balance at 31 December 1999	<u>1,359</u>	<u>18,907</u>	<u>-</u>	<u>692</u>	<u>-</u>	<u>20,958</u>	<u>-</u>

**CONSOLIDATED BALANCE SHEET**  
31 December 1999

	Note	1999 £'000	1998 £'000
<b>FIXED ASSETS</b>			
Tangible assets	11	11,483	5,498
<b>CURRENT ASSETS</b>			
Stocks	13	2,573	1,591
Debtors	14	7,743	2,759
Cash at bank		8,117	763
		18,433	5,113
<b>CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR</b>	15	(4,518)	(4,835)
<b>NET CURRENT ASSETS</b>		13,915	278
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>		25,398	5,776
<b>CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR</b>	16	(4,117)	(4,678)
<b>PROVISION FOR LIABILITIES AND CHARGES</b>	18	(331)	(467)
		20,950	631
<b>CAPITAL AND RESERVES</b>			
Called-up share capital	19	1,359	1,040
Merger reserve		(605)	(760)
Share premium		18,907	-
Profit and loss account		1,281	439
Exchange rate reserve		8	(88)
<b>TOTAL EQUITY SHAREHOLDERS' FUNDS</b>		20,950	631

These financial statements were approved by the Board of Directors on 20 March 2000.  
Signed on behalf of the Board of Directors

Dr A W Nelson

Director

**PARENT COMPANY BALANCE SHEET**  
31 December 1999

	Note	1999 £'000
<b>FIXED ASSETS</b>		
Investments	12	1,039
<b>CURRENT ASSETS</b>		
Debtors	14	13,197
Cash at bank and in hand		6,871
		20,068
<b>CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR</b>		
	15	(149)
<b>NET CURRENT ASSETS</b>		
		19,919
<b>TOTAL NET ASSETS</b>		
		20,958
<b>CAPITAL AND RESERVES</b>		
Called-up share capital	19	1,359
Share premium account		18,907
Profit and loss account		692
<b>TOTAL EQUITY SHAREHOLDERS' FUNDS</b>		
		20,958

These financial statements were approved by the Board of Directors on 20 March 2000  
Signed on behalf of the Board of Directors



Dr A W Nelson

- Director

**CONSOLIDATED CASH FLOW STATEMENT**  
**Year ended 31 December 1999**

	Note	1999 £'000	1998 £'000
Net cash inflow from operating activities	20	(2,877)	3,558
<b>Returns on investments and servicing of finance</b>			
Interest received		327	-
Interest paid		(917)	(336)
<b>Net cash outflow from returns on investments and servicing of finance</b>		(590)	(336)
<b>Taxation</b>			
United Kingdom corporation tax paid		(282)	(123)
<b>Capital expenditure and financial investment</b>			
Payments to acquire tangible fixed assets		(9,540)	(1,988)
Proceeds from sale of tangible fixed assets		2,127	-
<b>Net cash outflow from capital and financial investment</b>		(7,413)	(1,988)
<b>Equity dividends paid</b>		-	(140)
<b>Financing</b>			
Issue of ordinary share capital		19,381	184
Advances of new loans		3,032	3,807
Repayment of loans		(3,475)	(4,642)
<b>Net cash outflow from financing</b>		18,938	(651)
<b>Increase/(decrease) in cash</b>	21	7,776	320

## NOTE TO THE ACCOUNTS

### Year ended 31 December 1999

#### 1. ACCOUNTING POLICIES

The financial statements are prepared in accordance with applicable accounting standards under UK GAAP. The particular accounting policies adopted are described below.

##### Accounting convention

The financial information is prepared under the historical cost convention and in accordance with applicable accounting standards, which have been applied on a consistent basis during the period under review.

##### Turnover

Turnover represents amount invoiced, exclusive of value added taxation.

##### Tangible fixed assets

Tangible fixed assets are stated at cost less accumulated depreciation.

Depreciation has been calculated so as to write down the cost of assets to their residual values over the following estimated useful economic lives:

Short leasehold improvements	5 – 27 years
Plant and machinery	5 - 7 years
Fixtures and fittings	4 – 5 years
Motor vehicles	4 years
Freehold land and buildings	25 years

No depreciation is provided on assets in the course of construction.

##### Basis of consolidation

The financial information consolidates the financial statements information of the Company and all of its subsidiaries.

The acquisition of EPI Holding Limited and Quantum Epitaxial Designs, Inc. by IQE plc, a new holding company established for that purpose, on 16 May 1999 has been accounted for under merger accounting, whereby the financial information is disclosed as if the companies had always been part of the Group.

The acquisition of Epitaxial Products International Limited and its subsidiary Epitaxial Products Inc by EPIH, a new company established for that purpose, on 27 March 1996 has been accounted for under acquisition accounting, whereby these companies became part of the Group on the date of acquisition.

##### Goodwill

On the acquisition of a business, fair values are attributed to the Group's share of the net tangible assets acquired. Where the cost of acquisition exceeds the values attributable to such net assets, the difference is treated as purchased goodwill and is written off directly to reserves in the year of acquisition. Following the issue of Financial Reporting Standard 10, goodwill arising in accounting periods ending in or after 23 December 1998 must be classified as an asset on the balance sheet and amortised over its useful life.

##### Stocks

Stocks are stated at the lower of cost and net realisable value.

##### Research and development

Research and development expenditure is fully written off when incurred.

**NOTE TO THE ACCOUNTS**  
**Year ended 31 December 1999****1. ACCOUNTING POLICIES (continued)****Foreign currencies**

Transactions in foreign currencies during the period are recorded in sterling at the rates of exchange ruling at the date of the transaction. Monetary assets and liabilities in foreign currencies are translated into sterling at the rates ruling at the balance sheet date. All exchange differences are taken to the profit and loss account.

The balance sheets of Quantum Epitaxial Design Inc. are translated into sterling at the closing rates of exchange for each year whilst the profit and loss accounts are translated into sterling at the average rates of exchange for the period. The resulting translation differences are taken direct to reserves.

**Pension costs**

The Group operates a defined contribution pension scheme. Contributions are charged in the profit and loss account as they become payable in accordance with the rules of the schemes.

**Deferred taxation**

Deferred taxation is provided in full on timing differences relating to pension and other post retirement benefits calculated at the rates at which it is expected that tax will arise. Deferred taxation is provided on other timing differences, arising from the different treatment of items for accounting and taxation purposes, which are expected to reverse in the future without replacement, calculated at the rates at which it is expected that will arise.

**Government grants**

Government grants receivable in connection with expenditure on tangible fixed assets are accounted for as deferred income which is credited to the profit and loss account by instalments over the expected useful economic life of the related assets on a basis consistent with the depreciation policy.

Revenue grants for the reimbursement of costs incurred are deducted from the costs to which they related, in the period in which the costs are incurred.

**Leases**

Assets held under finance leases and hire purchase contracts are capitalised at their fair value on the inception of the leases and depreciated over the shorter of the period of the lease and the estimated useful economic lives of the assets. The finance charges are allocated over the period of the lease in proportion to the capital amount outstanding and are charged to the profit and loss account.

Rentals are charged to profit and loss in equal annual amounts over the lease term.

**Financial instruments**

The only derivative instruments utilised by the group are forward exchange contracts. The group does not enter into speculative derivative contracts. Forward exchange contracts are used for hedging purposes to alter the risk profile of an existing underlying exposure of the group in line with the group's risk management policies.

**2. SEGMENTAL ANALYSIS**

Analyses of geographical location and class of business for turnover and analysis of class of business for profit on ordinary activities before taxation have not been given as, in the opinion of the directors, the disclosure of this information would be seriously prejudiced to the interests of the group (Schedule 4, Part III, Section 55(5) Companies Act 1985 and Statement of Standard Accounting Practice Number 25).

**NOTE TO THE ACCOUNTS**  
**Year ended 31 December 1999**

**3. OPERATING PROFIT**

	1999 £'000	1998 £'000
<b>Operating profit is after charging</b>		
Depreciation of tangible fixed assets:		
Owned assets	1,479	1,437
Leased assets	30	-
Auditors' remuneration		
- Audit fees	45	31
- Other services	346	81
Operating lease rentals		
- Plant and machinery	71	64
- Other	133	195
Exchange gains	(74)	(45)
	<u>          </u>	<u>          </u>

**4. INFORMATION REGARDING DIRECTORS AND EMPLOYEES**

	1999 £'000	1998 £'000
<b>Directors' emoluments</b>		
Other emoluments	374	288
Pension contributions	14	14
	<u>          </u>	<u>          </u>
	<u>          </u>	<u>          </u>
	<u>          </u>	<u>          </u>
Remuneration of the highest paid director including pension contributions	<u>          </u>	<u>          </u>
	<u>          </u>	<u>          </u>

Four of the directors are members of the company defined contribution scheme and accrued benefits during the year under that scheme.

NOTE TO THE ACCOUNTS  
Year ended 31 December 1999

## 4. INFORMATION REGARDING DIRECTORS AND EMPLOYEES (continued)

Director	1		Number of options		Exercise price	Date from which exercisable	Expiry date
	January 1999	Granted	Exercised	December 31 1999			
S Massie	13,444	-	-	13,444	\$0.507	02.03.96 to 02.03.99	02.03.05
S Massie	20,166	-	(13,444)	6,722	\$0.72	01.01.97 to 01.01.00	01.01.06
S Massie	33,610	-	-	33,610	\$1.75	24.10.98 to 24.10.01	24.10.97
S Massie	67,220	-	-	67,220	\$1.75	14.12.99 to 14.12.02	14.12.08
S Massie	-	25,000	-	25,000	\$14.05	05.11.02	05.11.09

The above options are granted under a share option scheme adopted on 26 May 1999.

	1999 £'000	1998 £'000
<b>Employee costs</b>		
Wages and salaries	5,104	3,927
Social security costs	813	653
Other pension costs	175	140
	<u>6,092</u>	<u>4,720</u>

The average number of employees, including directors, during the year:

	1999 No	1998 No
	<u>197</u>	<u>155</u>

## 5. INTEREST PAYABLE AND SIMILAR CHARGES

	1999 £'000	1998 £'000
Bank loans, overdrafts and other loans	<u>917</u>	<u>405</u>

**NOTE TO THE ACCOUNTS**  
**Year ended 31 December 1999**

**6. TAXATION**

	1999	1998
	£'000	£'000
United Kingdom corporation tax at 30% (1998 - 31%)	(133)	179
United Kingdom deferred tax	398	60
Overseas deferred tax	(407)	(9)
Adjustments in respect of prior years provision:		
United Kingdom corporation tax	120	-
United Kingdom deferred tax	(127)	-
	<u>(149)</u>	<u>230</u>

The tax credit for the period arises from the release of a provision of overseas deferred tax no longer required.

**7. DIVIDENDS**

No dividend has been paid or proposed in 1999. Dividends totalling £140,000 are shown in the profit and loss account for the year ended 31 December 1998. These represent dividends paid by EPI Holdings Limited prior to IQE plc acquiring this company. These are included in the 1998 profit and loss under the merger accounting provisions as explained in Note 1 to the accounts.

**8. PROFIT OF PARENT COMPANY**

As permitted by Section 230 of the Companies Act 1985, the profit and loss account of the parent company is not presented as part of these accounts. The parent company's profit for the financial year amounted to £692,000.

**9. EARNINGS PER ORDINARY SHARE**

Basic earnings per share is calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares during the year. Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares in issue on the assumption of conversion of all dilutive potential ordinary shares.

**NOTE TO THE ACCOUNTS**  
**Year ended 31 December 1999**

**9. EARNINGS PER ORDINARY SHARE (continued)**

	1999	1998
	£'000	£'000
Basic and diluted earnings attributable to ordinary shareholders	842	552
	<u>          </u>	<u>          </u>
	No.	No.
Weighted average number of ordinary shares	13,271,722	10,403,109
Diluted share options	1,074,838	965,387
	<u>          </u>	<u>          </u>
Adjusted weighted average number of ordinary shares	14,346,060	11,368,496
	<u>          </u>	<u>          </u>
Earnings per share	6.34p	5.31p
	<u>          </u>	<u>          </u>
Diluted earnings per share	5.87p	4.86p
	<u>          </u>	<u>          </u>

**10. EXCEPTIONAL ITEM**

Included within other administrative expenses are amounts totalling £171,138 in respect of costs associated with the acquisition of EPI Holdings Limited and Quantum Epitaxial Designs, Inc. by IQE plc and the subsequent flotation of IQE plc.

Included within interest payable are amounts totalling £328,050 in respect of the early settlement of certain bank loans arising out of the acquisition of EPI Holdings Limited and Quantum Epitaxial Designs, Inc. by IQE plc and the subsequent flotation of IQE plc.

NOTE TO THE ACCOUNTS  
Year ended 31 December 1999

## 11. TANGIBLE FIXED ASSETS

The Group	Freehold Land and buildings £'000	Short leasehold improve- ments £'000	Fixtures & Fittings £'000	Plant and machinery £'000	Assets in the course of construction £'000	Total £'000
<b>Cost or valuation</b>						
At 1 January 1999	-	634	817	13,370	1,029	15,850
Additions	2,358	133	587	4,608	1,854	9,540
Disposals	-	(21)	-	(2,127)	-	(2,148)
Transfers	220	(220)	11	2,339	(2,350)	-
Exchange difference	-	10	7	146	-	163
At 31 December 1999	2,578	536	1,422	18,336	533	23,405
<b>Depreciation</b>						
At 1 January 1999	-	256	446	9,650	-	10,352
Charge for the year	55	73	170	1,211	-	1,509
Disposals	-	(21)	-	-	-	(21)
Transfers	87	(87)	5	(5)	-	-
Exchange difference	-	3	5	74	-	82
At 31 December 1999	142	224	626	10,930	-	11,922
<b>Net book value</b>						
At 31 December 1999	2,436	312	796	7,406	533	11,483
At 31 December 1998	-	378	371	3,720	1,029	5,498

The net book value of fixtures and fittings includes £90,640 (1998: £nil) in respect of assets held under finance lease.

## 12. INVESTMENTS HELD AS FIXED ASSETS

	£'000
Cost and net book value at 1 April 1999	-
Additions in the period	1,039
Cost and net book value at 31 December 1999	1,039
The above is represented by investments in the following 100% subsidiaries:	
Quantum Epitaxial Designs Inc.	439
EPI Holdings Limited	600
	1,039

**NOTE TO THE ACCOUNTS**  
Year ended 31 December 1999

**13. STOCKS**

	The Group £'000	1999 The Company £'000	The Group £'000	1998 The Company £'000
Raw materials and consumables	2,239	-	1,384	-
Finished goods	334	-	207	-
	<u>2,573</u>	<u>-</u>	<u>1,591</u>	<u>-</u>

**14. DEBTORS**

	The Group £'000	1999 The Company £'000	The Group £'000	1998 The Company £'000
<b>Amounts falling due within one year</b>				
Trade debtors	3,045	-	2,283	-
Amounts owed by group undertakings	-	13,177	-	-
Other debtors and prepayments	4,565	20	476	-
Corporation tax	133	-	-	-
	<u>7,743</u>	<u>13,197</u>	<u>2,759</u>	<u>-</u>

Amounts owed by group undertakings are due after more than one year.

**15. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR**

	The Group £'000	1999 The Company £'000	The Group £'000	1998 The Company £'000
Bank loans and overdrafts	-	-	743	-
Other loans	504	-	-	-
Trade creditors	3,115	-	2,657	-
Amounts due under hire purchase and finance leases	18	-	-	-
Other creditors including taxation and social security	111	27	162	-
Corporation tax	-	122	162	-
Accruals and deferred income	770	-	1,111	-
	<u>4,518</u>	<u>149</u>	<u>4,835</u>	<u>-</u>



**NOTE TO THE ACCOUNTS**  
**Year ended 31 December 1999**

**17. BORROWINGS (continued)**

The bank loan was repaid in full during this year.

Other loans comprise of a loan from 3i of £1,425,000 a loan from the WDA of £1,482,000 and a loan from Copelco of £1,540,000.

Interest is charged on the 3i loan at a rate equal to the base rate and a margin of 2.5% per annum.

The loan is repayable by 15 annual instalments of £95,000, commencing 28 February 2000, with a 6 monthly instalment on 31 August 2000.

The loan is secured by a fixed and floating charge over the assets of the company.

Interest is charged on the WDA loan at a maximum rate of 8.5% per annum. The loan is secured on the company's property. The loan is repayable by 32 instalments, quarterly in arrears, commencing 10 October 2001.

Interest is charged on the Copelco loan at 10.86% per annum. The loan is secured on equipment. The loan is repayable by monthly instalments of \$63,924 per month with a final instalment in January 2003 of \$767,076.

Amounts due under hire purchase and finance leases are secured on the related assets.

**18. DEFERRED TAXATION**

	At 1 January 1998 £'000	Charged/ (released) to profit and loss account £'000	At 31 December 1999 £'000
UK deferred tax	60	271	331
Overseas deferred tax	407	(407)	-
	<u>467</u>	<u>(136)</u>	<u>331</u>

The amounts of deferred taxation provided and unprovided in the accounts are:

	Provided		Unprovided	
	1999 £'000	1998 £'000	1999 £'000	1998 £'000
<b>The Group</b>				
Capital allowances in excess of depreciation	331	467	-	-
<b>The Company</b>				
Capital allowances in excess of depreciation	-	-	-	-

**NOTE TO THE ACCOUNTS**  
Year ended 31 December 1999

**19. SHARE CAPITAL**

	1999		1998	
	Number of shares	£'000	Number of shares	£'000
<b>Authorised</b>				
Ordinary shares of 10p each	19,000,000	1,900	15,500,000	1,550
<b>Allotted, called up and fully paid</b>				
Ordinary shares of 10p each	13,595,517	1,359	10,403,109	1,040

10,389,645 shares were issued in the year to acquire 100% of the ordinary share capital of Quantum Epitaxial Designs Inc, and EPI Holdings Limited.

The share capital of both companies were acquired at par, through a share-for-share exchange.

In the remainder of the year, a further 3,205,872 shares were issued for cash at a total premium of £20,120,989.

Under the company's share option scheme adopted on 26 May 1999, employees held options at 31 December 1999 for 1,074,838 unissued ordinary shares as follows:

No. of shares	Option price/share	Option period ending	No. of shares	Option price/share	Option period ending	Total
17,221	\$0.153	21/05/02	2,016	\$1.750	13/06/08	
47,054	\$0.507	01/03/05	1,008	\$1.750	28/06/08	
6,722	\$0.720	31/12/05	6,722	\$1.750	31/07/08	
222,982	\$0.100	31/12/06	1,344	\$1.750	22/09/08	
7,444	\$1.750	02/02/07	672	\$1.750	03/10/08	
10,083	\$1.750	13/04/07	1,008	\$1.750	15/10/08	
90,218	\$1.750	17/05/07	255,600	\$14.050	04/11/08	
33,610	\$1.750	23/10/07	67,220	\$1.750	13/12/08	
69,544	\$0.100	31/12/07	86,015	\$0.100	31/12/08	
10,083	\$1.750	03/04/08	6,722	\$2.470	24/01/09	
1,008	\$1.750	19/04/08	6,722	\$2.470	31/01/09	
8,821	\$1.750	25/05/08	60,153	\$2.470	14/03/09	
1,344	\$1.750	06/06/08	16,802	\$8.180	06/05/09	
526,134			512,004			1,038,138

During the year 524,045 options were granted and 414,594 options were exercised.

**NOTE TO THE ACCOUNTS**  
**Year ended 31 December 1999**

**20. RECONCILIATION OF OPERATING PROFIT TO NET CASH INFLOW FROM OPERATING ACTIVITIES**

	1999 £'000	1998 £'000
Operating profit	1,283	1,170
Depreciation charges	1,509	1,437
Increase in stocks	(982)	(286)
Increase in debtors	(4,851)	(719)
(Decrease)/increase in creditors	81	1,929
Government grant release received	(29)	(33)
Government grant	112	-
Release of deferred issue costs	-	60
	<u>(2,877)</u>	<u>3,558</u>
Net cash outflow from operating activities	<u>(2,877)</u>	<u>3,558</u>

**21. RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET DEBT**

	1999 £'000	1998 £'000
Increase in cash in the period	7,776	320
Loan repayments	3,611	4,642
Loans received	(2,908)	(3,807)
	<u>8,479</u>	<u>1,155</u>
Change in net debt resulting from cash flows	8,479	1,155
Inception of new finance leases	(124)	-
	<u>8,355</u>	<u>1,155</u>
Net movement for period	8,355	1,155
Net debt at 1 January 1999	(4,648)	(5,870)
Exchange differences	(136)	67
	<u>3,571</u>	<u>(4,648)</u>
Net debt at 31 December 1999	<u>3,571</u>	<u>(4,648)</u>

NOTE TO THE ACCOUNTS  
Year ended 31 December 1999

## 22. ANALYSIS OF NET DEBT

	At 31 December 1998 £'000	Cash Flow £'000	Other non-cash movements £'000	At 31 December 1999 £'000
Cash in hand and at bank	763	7,354	-	8,117
Bank overdrafts	(422)	422	-	-
	341	7,776	-	8,117
Debt due after one year	(4,668)	802	(77)	(3,943)
Debt due within one year	(321)	(260)	77	(504)
Finance Leases	-	(99)	-	(99)
	(4,648)	8,219	-	3,571

## 23. ADDITIONAL INFORMATION ON SUBSIDIARY UNDERTAKINGS

Name	Class of Capital	Portion of shares held	Activity	Country of Incorporation
Quantum Epitaxial Designs Inc.	Common Stock of \$0.001	100%	Manufacture of advanced semi conductor materials	USA
EPI Holdings Limited	£1 ordinary shares	100%	Dormant	Great Britain
Epitaxial Products International Limited	£1 ordinary shares	100%	Manufacture of advanced semi conductor materials	Great Britain
Epitaxial Products, Inc.		100%	Manufacture of advanced semi conductor materials	USA

**NOTE TO THE ACCOUNTS**  
**Year ended 31 December 1999**

**24. FINANCIAL INSTRUMENTS**

**Risk Management**

Group cash flows are affected by international currency fluctuations, primarily in respect of the US dollar. A significant amount of the group's purchases of raw materials are sourced in North America and are settled in US dollars. To a lesser extent, purchases of raw materials are also sourced in the Far East and settled in Japanese yen.

However, the group has consistently achieved significant dollar and yen inflows from sales to customers in North America and the Far East, and on this basis the Board considers that these provide a natural hedge to the extent that they cover a significant proportion of the group's currency requirements. Any shortfall over a rolling period of up to twelve months is constantly monitored and the risk is fixed through forward currency contracts with the group's bankers. Other currencies are also monitored and imbalances may be fixed as the need arises. It is not the policy of the Board to speculate in currency fluctuations.

The Board is also mindful of risks associated with changes in interest rates and, where possible, these have been fixed in order to minimise risk. The Board does not speculate on future changes in Bank interest rates.

The group does not trade in financial instruments.

Forward currency contracts are entered into with the group's bankers in order to fix exchange rate risks associated with currency shortfalls over a rolling twelve month period in respect of dollar and yen inflows (and to a lesser extent other currencies). At 31 December 1999, the group had entered into eight forward exchange contracts totalling US\$2,000,000 which are exercisable at exchange rates in the range \$1.5957/£- \$1.6048/£ during the period January to August 2000. There were no material gains or losses brought forward or carried forward at the year end. Gains and losses are recognised in the year and are disclosed in note 3. The currency profile of the group's trade debtors and trade creditors is as follows:

	Trade debtors £'000	Trade creditors £'000
Sterling	293	804
US\$	2,598	2,005
Yen	56	262
Other	98	44
	<hr/>	<hr/>
Total	3,045	3,115
	<hr/> <hr/>	<hr/> <hr/>

**NOTE TO THE ACCOUNTS**  
**Year ended 31 December 1999**

**24. FINANCIAL INSTRUMENTS (continued)**

The interest rate profile of the group's financial assets and liabilities is as follows:

	Assets floating rate £'000	Floating rate £'000	Liabilities fixed rate £'000	Total £'000
Sterling	7,060	1,425	1,483	2,908
US\$	993	-	1,539	1,539
Yen	64	-	-	-
Other	-	-	-	-
Comprising -				
Cash at bank	8,117	-	-	-
Bank overdrafts	-	190	314	504
Bank loans	-	1,235	2,708	3,943
	<u>8,117</u>	<u>1,425</u>	<u>3,022</u>	<u>3,337</u>
Total	<u>8,117</u>	<u>1,425</u>	<u>3,022</u>	<u>3,337</u>

For the fixed rate liabilities the weighted average interest rate is 9.73% and the weighted average period for which interest rates are fixed is 6.2 years.

Further details of the financial liabilities at 31 December 1999 are shown in notes 15 and 16.

There is no significant difference between the book value and the fair value of the group's financial assets and liabilities.

**25. RELATED PARTY TRANSACTIONS**

During the year the group incurred professional fees of £352,415 (1998- £63,750) payable to Gambit Corporate Finance. Dr Godfrey Ainsworth, who is a director of IQE plc, is a partner in Gambit Corporate Finance.