



IQE PLC

Report and Financial Statements

31 December 2000

**Deloitte & Touche
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Fitzalan Court
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REPORTING TIMETABLE

21 March Announcement of Fourth Quarter Results and Preliminary Annual Statement

12 April Publication of Annual Accounts and Notice of Annual General Meeting

08 May Annual General Meeting

23 May Announcement of First Quarter Results

22 August Announcement of Second Quarter Results and Interim Half Yearly Statement

21 November Announcement of Third Quarter Results

FIVE YEAR FINANCIAL SUMMARY

	2000 £'000	1999 £'000	1998 £'000	1997 £'000	1996 £'000
Turnover	30,117	19,043	15,856	11,806	10,405
Operating profit before goodwill and exceptional items	1,995	1,454	1,170	(54)	382
Exceptional items	-	(171)	-	(299)	(76)
Goodwill amortisation	(209)	-	-	-	-
Operating profit	1,786	1,283	1,170	(353)	306
Net interest receivable / (payable)	1,208	(590)	(388)	(323)	(135)
Profit / (loss) on ordinary activities before taxation	2,994	693	782	(676)	171
Taxation	(1,184)	149	(230)	(178)	(269)
Profit / (loss) for the financial year	1,810	842	552	(854)	(98)
Earnings per ordinary share	1.24p	0.63p	0.53p	(0.82)p	(0.09)p
Diluted earnings per ordinary share	1.18p	0.59p	0.49p	(0.74)p	(0.08)p
Earnings before interest, taxation, depreciation and amortisation (EBITDA)	4,834	2,792	2,607	1,112	1,686
Employment of shareholders' funds:					
Tangible fixed assets	47,848	11,483	5,498	4,968	4,862
Goodwill	36,453	-	-	-	-
Net current assets	2,052	6,320	258	1,298	1,696
Other liabilities	(1,659)	(424)	(477)	(462)	(464)
Net cash/(borrowings)	32,813	3,571	(4,648)	(5,787)	(5,264)
Shareholders' funds	117,597	20,950	631	17	830
Free cash flow	(25,265)	(10,290)	1,554	(14)	(3,197)
Interest, tax and dividends	343	(872)	(599)	(509)	(596)
Net cash flow	(24,922)	(11,162)	955	(523)	(3,793)
Acquisitions, disposals, share issues and translation	54,164	19,381	184	-	5,030
Movement in net cash/(borrowings)	29,242	8,219	1,139	(523)	1,237
Key ratios:					
Operating profit as % of:					
Turnover	6.6%	6.7%	7.4%	(0.5)%	3.7%
Shareholders' funds* (average)	3.9%	11.9%	361.1%	(12.8)%	46.0%
Interest cover (times)	-	2.2	3.0	-	2.3
Net borrowings as % of shareholders' funds* excluding borrowings	-	-	88.0%	99.7%	86.4%

*excluding goodwill

IQE Plc was established in April 1999 for the purpose of acquiring EPI Holdings Limited (and its subsidiaries IQE (Europe) Limited, formerly Epitaxial Products International Limited, and Epitaxial Products Inc) and IQE Inc Limited (formerly Quantum Epitaxial Designs Inc.) in May 1999. The acquisitions were accounted for under merger accounting, whereby the financial information is disclosed as if the companies had always been part of the group.

REPORT AND FINANCIAL STATEMENTS 2000

OFFICERS AND PROFESSIONAL ADVISERS

DIRECTORS

Dr A W Nelson (Chairman and Chief Executive Officer)

Dr M D Scott

T L Hierl

R J G Clarke

S Byars

S T Massie

M S M Lamb

Dr G H H Ainsworth (Non-Executive)

G Bressner (Non-Executive)

SECRETARY

J L Coventry

REGISTERED OFFICE

Pascal Close

Cypress Drive

St Mellons

Cardiff

CF3 0EG

PRINCIPAL BANKERS

Barclays Bank plc

AUDITORS

Deloitte & Touche

Chartered Accountants

Blenheim House

Fitzalan Court

Newport Road

Cardiff

CF24 0TS

REPORT AND FINANCIAL STATEMENTS 2000**DIRECTORS' AND OFFICERS' BIOGRAPHIES****Dr Andrew W Nelson** *Age 46* Chairman and Chief Executive Officer

Drew Nelson joined BT Research Laboratories in 1981 leading the Group responsible for the development of MOVPE technology for the manufacture of opto-electronic devices for optical fibre communications. He subsequently managed the technology transfer from BT to BT&D (now Agilent Optoelectronics Ipswich), a leading manufacturer of fibre optic communication devices. Together with Mike Scott, he founded EPI in 1988, becoming Managing Director in 1991 and Chairman and CEO in 1996. Following the merger with QED which formed IQE plc, Dr Nelson became Chairman and CEO of the new Group. Drew Nelson was educated at Sheffield University and holds a First Class BSc Honours degree in electronic engineering as well as a PhD in semiconductor technology.

Dr Michael D Scott *Age 43* Sales and Marketing Director

Mike Scott joined GEC Plessey Research (Caswell) in 1982 and led the development group working on MOVPE for InP based materials. After founding EPI with Drew Nelson in 1988, he became Technical Director and subsequently Sales and Marketing Director in 1996. After the merger he was appointed Sales and Marketing Director of the combined Group. Dr Scott gained a BSc in chemistry and physics, followed by a PhD in semiconductor technology at University of Wales, Aberystwyth.

Thomas L Hierl *Age 49* Technical Director

After working for Loral Corporation and Varian Associates, Tom Hierl joined GAIN Electronics where, as Manager of Semiconductor Materials, he established the first domestic US source of MBE wafers for the merchant market. In 1988 he was a founder of QED, acting as Chief Executive Officer of that Company up until the merger with EPI in 1999. Since the merger, he has been the Group's Chief Technical Officer. Mr Hierl has more than twenty years experience in the GaAs semiconductor industry and has BSEE and MEE degrees from Cornell University.

Richard J G Clarke *Age 45* Finance Director

Richard Clarke qualified as a Chartered Accountant with Ernst & Young in 1980 and subsequently joined Dowty Aerospace where he held various senior financial roles in the UK, USA and Singapore, including a period at the Group head office. In 1994 he was appointed Finance Director of Avimo Group Limited, an international group of electro-optical businesses listed on the Singapore Stock Exchange. He was appointed CFO of IQE plc on 8 March 2001. Mr Clarke is a Fellow of the Institute of Chartered Accountants in England and Wales, and has a BSc in economics from University College, London and an MBA from the University of Bath.

REPORT AND FINANCIAL STATEMENTS 2000**DIRECTORS' AND OFFICERS' BIOGRAPHIES (continued)**

Stephen Byars *Age 43* Managing Director, IQE (Europe) Limited

Steve Byars has over 22 years experience in the semiconductor industry, having worked in a variety of senior management roles both in the UK and overseas. His experience includes acting as Chief Executive Officer of the European operations of QPL International Holdings, a Hong Kong based group providing advanced materials and sub-contract services to the semiconductor industry. Prior to joining IQE he spent 8 years as Chief Executive Officer of Europe's largest dedicated silicon foundry, during which time he successfully led a management buyout of the Company. Mr Byars joined IQE (Europe) Limited as Managing Director in August 2000 and was appointed to the Board of IQE plc in January 2001.

Scott T Massie *Age 39* President, IQE Inc

Scott Massie joined QED in 1993 as Director of Contract Research and was responsible for obtaining a number of government-funded development programmes. He was appointed Vice President, Operations in 1996 with responsibility for manufacturing and contract research, and Chief Operating Officer in 1998. Subsequent to the merger with EPI, he was appointed President of IQE Inc. Mr Massie holds a BS in mathematics and a BS and MS in physics from Virginia Polytechnical Institute and State University, where he also completed his doctoral studies in physics.

Martin S M Lamb *Age 40* Managing Director, Wafer Technology Limited

Martin Lamb joined GEC Plessey Research (Caswell) in 1982 as a Research Scientist working on the characterisation of III-V semiconductor materials and devices. In 1985 he joined Wafer Technology Limited, becoming Quality Assurance Manager in 1986. In 1994 he was a key member of the management buy-out team which acquired the Company from MCP Ltd and was subsequently appointed Manufacturing Director. He became Managing Director in 2000. Following the acquisition of Wafer Technology Ltd by IQE plc, he was appointed to the Board on 22 November 2000. Mr Lamb graduated from the University of Durham in 1982 with a BSc in applied physics and electronics. He obtained an MBA from the University of Leicester in 1995.

Dr Godfrey H H Ainsworth *Age 45* Non-Executive Director, Chairman of the Audit Committee

Godfrey Ainsworth qualified as a Chartered Accountant and was employed by Coopers & Lybrand before becoming an audit partner and then corporate finance partner with Spicer & Oppenheim. Following a period as Finance Director of the Human Resource Consulting Group, in 1992 he founded Gambit Corporate Finance, a practice specialising in the provision of corporate finance services. He has held several Non-Executive Directorship appointments, including assignments for 3i plc and the Welsh Development Agency. He has provided advice to EPI since its inception and was appointed to the Board in 1997. Following the merger with QED he was appointed to the Board of IQE plc. Dr Ainsworth is a Fellow of the Institute of Chartered Accountants in England and Wales and has a First Class BSc Honours degree and a PhD in plant sciences from University College, Cardiff.

REPORT AND FINANCIAL STATEMENTS 2000**DIRECTORS' AND OFFICERS' BIOGRAPHIES (continued)**

Glen Bressner *Age 40* Non-Executive Director, Chairman of the Remuneration Committee

Glen Bressner is a general partner of the Mid-Atlantic Venture Funds, having been with the firm since shortly after its inception in 1985. Prior to this, he managed the Boston office for Key Venture Capital Corporation. Mr Bressner is a member of the Boards of Innovative Solutions & Support, Inc. (NASDAQ:ISSC), MicroE, Inc., Sprockets, Inc., Hurwitz Group, Inc., CarrierChoice, Inc and Midas Vision Systems, Inc. He has been a Non-Executive Director of QED since 1998 and was appointed to the Board of IQE plc after the merger with EPI. Mr Bressner holds a BSBA, *cum laude*, from Boston University and an MBA from Babson College.

J Leslie Coventry *Age 55* Company Secretary

Leslie Coventry has acted as Accountant and Company Secretary for a number of companies including British Oxygen, British Shipbuilders, Hydro Aluminium and Seagram Distillers. He joined EPI in 1992 as Commercial Manager/Company Secretary, becoming Finance Director in 1998. After the merger with QED he was appointed Company Secretary of IQE plc. Mr Coventry qualified as a Chartered Accountant with the Institute of Chartered Accountants in Scotland in 1967.

CHAIRMAN'S STATEMENT

Introduction

I am very pleased to report that the Group has again achieved record sales during 2000 of over £30.1m despite severe capacity constraints in the early part of the year. The results represent an increase of 58% over 1999 revenues while pre-tax profits increased by 332% to £2.994m. This is against the backdrop of the current state of technology markets, which have seen dramatic falls in confidence during the second half of 2000, particularly in the last quarter, with many technology businesses reporting reduced sales and substantially downgraded forecasts for 2001. I believe our achievement provides a clear signal to the marketplace that we are well on track at IQE with our ongoing expansion programme.

The first year of the new millennium heralded a number of key milestones for the Group. On 19 May, IQE was admitted to the Official List of the London Stock Exchange, and in June, the International Headquarters at Cardiff was officially opened by his Royal Highness the Duke of Edinburgh. During the year we brought on significantly increased capacity as our investment programme began to come to fruition, resulting in a very strong growth in revenues over the year, and in November we made two major corporate announcements:

The acquisition of Wafer Technology International Limited which ensures the Group's ability to source its key raw materials and provides additional market channels for our epi-wafer products; and

The establishment of IQE Silicon Compounds Limited to provide sophisticated epitaxy services to the silicon industry.

The integration of Wafer Technology has progressed smoothly, and IQE Silicon Compounds has generated exceptionally strong customer interest and is progressing ahead of schedule.

Results

Sales for the year were a record £30.117m, up 58% compared with 1999 (£19.043m). In spite of the additional financial burden of introducing new reactors into production, the gross margin was maintained at 34%, resulting in a gross profit of £10.332m, up 59% compared with 1999 (£6.485m). Distribution and administrative expenses increased to £6.467m (1999: £3.729m) as a result of significant recruitment, particularly in senior level staff, infrastructure improvements, and added sales and marketing activity. Research and development costs increased more slowly, from £1.302m in 1999 to £1.870m in 2000, representing 6.2% of turnover, primarily because most resources were devoted to production, especially in the first three quarters.

Consequently, operating profit excluding goodwill and exceptionals increased by 37% to £1.995m from £1.454m in 1999. Profit after tax more than doubled to £1.810m (1999: £0.842m) an increase of 115% on the previous year. The effective tax rate for the year excluding goodwill amortisation was 37%, driven by the distribution of profits within the Group and the current capital structure of the US subsidiaries which resulted in unrelieved tax losses arising in the US. However, as these losses are available for carry forward, the Group expects to receive a tax benefit in future years.

Earnings Per Share for the year, excluding goodwill, were 1.38 pence, up 119% compared with the previous year (1999 : 0.63 pence). After goodwill amortisation, Earnings Per Share were 1.24 pence (1999 : 0.63p).

CHAIRMAN'S STATEMENT (continued)**Operations**

Several new reactors were successfully brought into production during the year, enabling the Group to substantially increase wafer output to satisfy growing demand for the Group's products. During the year a total of twelve additional high volume tools were delivered of which four new MOCVD reactors were brought on line, two new MBE reactors contributed to increased production output in the UK and US. Delivery of other systems on order has continued according to plan. We were successful in transferring a number of existing products to the larger capacity platforms, allowing much more flexibility in catering for customers' diverse needs and increasing our productivity. As a consequence, we were also able to dedicate certain resources to new product development.

This has resulted in bringing a number of new and exciting products close to market, particularly in the areas of vertical cavity surface emitting lasers (VCSELs), which are highly versatile devices and crucial for a number of rapidly growing applications such as high speed Gigabit Ethernet systems. IQE has a very strong position and long history in VCSEL development and manufacture, and has now successfully developed structures at a variety of different wavelengths, thereby increasing the range of applications that can be addressed by this technology. We have also developed a range of Inf-based electronic products essential for next generation communication systems, which require even faster devices and integrated circuits. Not only have we achieved industry-leading results using conventional InP substrates, we have also been successful in developing this technology on GaAs substrates, allowing these advanced devices to be manufactured on 6" GaAs wafers. Our customers have reported world-leading results using our technology, which has subsequently been the subject of a highly significant technology press release.

The acquisition of Wafer Technology has progressed well' with additional capacity being added for substrate production and new routes being exploited into the marketplace for epi-wafer supply. Rapid progress has also been made at IQE Silicon Compounds, with completion of the cleanrooms and delivery of the first reactors being achieved before the year end. Customer interest in the epi services being offered by this unit has continued at a very high level, and initial customer qualifications are due to begin ahead of our initial estimate.

Order activity continued at a high level with more than £12.3 million booked during the last quarter, resulting in an order book at the year end of over £24.0m for the Group.

Capital expenditure during the year, including equipment leased and deposits on new equipment, was £36.2m, in line with our revised plans which were significantly accelerated to cope with customer demand for additional production and development activity.

Management

We continued to strengthen the management team, making a number of key appointments, including:

Richard Clarke (CFO, IQE plc) previously with Dowty Group and Avimo; Steve Byars (CEO, Europe) previously CEO with ESM, Europe's largest silicon outsource foundry; and Ren Jenkins (VP Sales & Marketing North America), previously with Lucent.

CHAIRMAN'S STATEMENT (continued)

Trading Prospects

Although there have been well-documented areas of weakness, such as the wireless handset market, our products and services overall continue to be in strong demand particularly in opto-electronics, where demand has remained strong in materials for dense wavelength division multiplexing (DWDM) optical fibre systems for long haul and metro networks; short haul optical fibre links; optical storage systems; and the electronic materials required to support such systems.

At first sight, the current strength of our business may seem at odds with the gloomy short term outlook for high technology markets but IQE's strategy has always been to develop a broad product portfolio which ensures a lack of dependence on any one sector of the industry. Moreover, our outsource business model is attractive to many companies and particularly so during times of recession as many companies are loath to invest heavily in capital equipment at a low point of the business cycle but still require materials for both production and development. Our broad product range enables companies to quickly change their own product mixes to address more rapidly growing markets.

Overall, therefore, our business is continuing to grow and we confidently expect the first quarter of 2001 to show further progress compared with the fourth quarter of 2000. Given the current market turmoil, it is difficult to predict when a general turnaround in confidence will occur. However, we have a strong product range, a powerful manufacturing and development capability, a robust business model and a strong balance sheet, and as a result we remain both cautiously optimistic for the remainder of 2001 and highly confident of our long term prospects.



Dr Drew Nelson
Chairman and CEO

20 March 2001

OPERATIONS REVIEW**GROUP STRUCTURE***Expansion programme*

Despite an aggressive capacity expansion programme at both the UK and US manufacturing sites that saw a total of twelve additional high volume tools installed during the year, continued strong demand for compound semiconductor materials resulted in severe capacity constraints during most of the year 2000. These constraints were exacerbated by delivery delays of up to three months on three of the MBE tools that were installed at the US plant although the installation programme is now completely back on schedule.

When planning installation of new machines, the IQE model assumes three months to install and sign off the installation of each system, a further three months to qualify the process to IQE quality standards and three months for customer product qualification. The first of the multiwafer platforms made a contribution to revenues during the third quarter as scheduled.

IQE Silicon Compounds Limited

In November 2000, the launch of a new subsidiary was announced. IQE Silicon Compounds Ltd was set up to provide sophisticated epitaxy services targeted towards the silicon industry. The operation was started in August 2000 at a brown-field site adjacent to the Group headquarters and manufacturing site at St Mellons, Cardiff. The 1,000m² manufacturing facility is being funded primarily through lease finance and with assistance from the National Assembly for Wales in the form of Regional Selective Assistance.

IQE Silicon Compounds is planned to contribute to revenue by the third quarter of 2001 and is expected to employ around 40 people by the end of the year. The operation has already installed the first two low pressure ASM Epsilon CVD reactors that have been committed to servicing the first long term customer contract. Non disclosure agreements and epitaxy structures have been provided by a further thirteen European customers but will not be serviced until further capacity is available from the next four reactors due to be delivered by the end of the first half of 2001.

At present, many European semiconductor plants are outsourcing epitaxial processes but the only viable supplier is based in the US. IQE will therefore offer the first and only European outsource epitaxy service for silicon based products. Initially, product areas will include silicon germanium (SiGe) HBTs, High-end Bi-CMOS semiconductor processes and silicon on insulator (SOI) for MEMs applications.

OPERATIONS REVIEW (continued)

SiGe devices are well positioned to address the market for electronics that serve wireless and land-based voice, data and video applications as well as Bluetooth devices. The overall market for SiGe electronic devices is expected to grow from US\$194 million in 2000 to US\$5.97 billion in 2005.

IQE Silicon Compounds Ltd is a wholly owned subsidiary of IQE plc.

Wafer Technology Limited

IQE also announced, in November 2000, the acquisition of Wafer Technology Ltd. The acquisition was key to IQE's overall strategy as a pure-play materials supplier and reflected some major changes occurring within the industry. During the year, many existing substrate manufacturers announced links with epitaxy foundries and in some cases with device manufacturers. This was seen by IQE as leading to possible long term supply constraints and potentially conflicting interests. The acquisition of Wafer Technology demonstrates a clear commitment to maintain a secure supply for our customers. The company also supplies raw feedstock to other substrate manufacturers. Wafer Technology also supplies many in-house epitaxy facilities that are potential customers for epitaxial as well as services and substrates. The acquisition therefore gives IQE access to a wider customer base for epiwafers and allows some integration of sales and marketing functions. Wafer Technology Ltd is a wholly owned subsidiary of IQE plc.

Market overview

Growth in both optical and wireless mobile telecommunications has been a key driver in the demand for the properties of compound semiconductors as has a range of consumer products from DVD and Minidisc through to satellite, lighting, display and automotive applications. The compound semiconductor industry has experienced an average CAGR of 35% over the last ten years and in 2000 accounted for estimated sales of US\$13.5 billion, exceeding earlier forecasts and representing more than 10% of the total semiconductor market.

In addition to the estimated continued growth in the compound semiconductor market as a whole there are two key factors that are influencing IQE's growth potential.

First there is the increasing trend towards outsourcing within the "foundry model". At present, outsourcing accounts for less than 20% of all compound semiconductor epitaxy production which was valued at around US\$2.5 billion in 2000. Driving this trend are factors such as cost savings, reduced financial risk and access to latest technology. Evidence for this growing trend towards outsourcing is also stated in a recent report by Cahners In-Stat Group who found that while the overall semiconductor industry grew by 36.8% in 2000, leading foundries grew even faster with the largest achieving growth rates in the 60-125% range. The report concludes that "Foundries will have a major impact on the new hybrid semiconductor development strategy."

OPERATIONS REVIEW (continued)

The second factor influencing IQE's growth is the tendency towards more complex epitaxial structures, thereby increasing the value added at the epitaxial materials stage. The VCSEL structures serve as a good example of this trend. VCSELs comprise many interlaced layers, each of which is just a few atoms thick, to produce a mirror that acts in the vertical plane. The end result is a laser where the light output emanates from the material's surface rather than from the edge which leads to simplified subsequent testing and fabrication. Amongst the many advantages of this structure is the potential to integrate arrays of lasers or even electronic and optical components onto a single chip.

Principal applications

Connectivity: Compound semiconductors provide connectivity solutions from basic mobile telephone handsets to connected Personal Digital Assistants (PDAs) and wireless networks whilst the emergence of short distance wireless technology in the form of Bluetooth is another key driver for compound semiconductor devices.

Photonics (Communications): Demand for increased bandwidth continues to drive the requirements for InP based compound semiconductor structures for telecommunications lasers and detectors. As we edge towards the 10-Gigabit Ethernet, the technology roadmap for IQE's Vertical Cavity Surface Emitting Laser (VCSEL) technology includes Terabit Ethernet devices for metro and access networks over distances of up to 50Km. Potential future applications also include devices for optical backplane and board-to board communications.

Photonics (Data storage): Laser emitters and receivers are the key enabling technology behind CD, DVD and Minidisc systems for audio, video and data storage. DVD is already the fastest growing consumer electronics product in history, with the number of units sold increasing from zero in 1996 to 19 million in 2000. Although most visible laser diodes used in CD and DVD players are of traditional "edge emitting" design, there is a trend towards the more complex epitaxial structure used in the VCSEL design because of lower overall manufacturing costs.

Lighting and display: The optical properties that can be achieved using compound semiconductors such as AlInGaP and GaN based materials lend themselves readily to high brightness Light Emitting Diodes from the red through to the blue end of the visible spectrum. Already, arrays of red, yellow and green LEDs are being employed as traffic signals throughout the world. Although more expensive than incandescent bulbs, the lower power consumption and virtually maintenance free LEDs often have a payback period of less than one year. Sports arenas, stadiums, airports and city centre information boards are increasingly using high brightness LEDs for large area, full colour displays that are visible even in direct sunlight.

Satellite communications:

High speed, short wavelength RF components with low power consumption are essential in satellite to Earth communications devices. Similarly, high efficiency solar panels provide the power source to drive the satellites' electronics systems. Both the RF components and solar panels found in satellite systems make extensive use of the electronic and optical properties of compound semiconductors.

OPERATIONS REVIEW (continued)

Automotive and medical: Sensors for safety features such as airbags, ABS and collision avoidance radar are examples in the automotive sector where the properties of compound semiconductors are utilised, as are LED brake lights and GPS navigation systems. In the medical sector a number of non-invasive surgical and monitoring techniques have been developed using compound semiconductor technology.

Dr Drew Nelson
Chief Executive

FINANCIAL REVIEW

INTRODUCTION

Following the Company's listing on the London Stock Exchange in May 2000, the format and content of this year's Annual Report and Accounts have been modified to comply with the requirements of the Listing Rules. The Group, however, continues to report under UK GAAP and there have been no changes to the Group's accounting policies.

As stated in Note 2 to the Accounts, the Group does not produce a segmental analysis of its business by geographical location and class of business as the Board believes that to do so would be seriously prejudicial to the interests of the Group.

ANALYSIS OF RESULTS

IQE achieved strong growth in 2000, with sales from continuing operations increasing by 52.5% to £29.0m (1999: £19.0m). A first year contribution from Wafer Technology of £1.0m brought total sales for the year to £30.1m. The principal markets for compound semiconductors demonstrated strong growth throughout the year with demand continuing to exceed available capacity, in particular for opto-electronic products. Against this background, substantial investment in additional capacity, much of which came on stream in the third and fourth quarters, resulted in strong sales growth in the second half of the year.

Despite the substantial increase in sales, the Group's gross profit margin remained largely unchanged at 34.3% (1999: 34.1%). This was mainly due to the additional costs associated with the rapid capacity expansion in both the UK and the US, in particular those resulting from bringing a total of six new reactors on line during the year.

Other administrative expenses were significantly higher in 2000, partly due to high recruitment and training costs to support the growth in capacity and also as a result of increased sales and marketing effort. Profit before interest and tax for the continuing businesses was £1.5m (1999: £1.3m), while Wafer Technology contributed a further £0.3m, their result being enhanced by the sale of waste material for recycling in the last month of the year.

INTEREST

The Group earned £1.6m of interest on cash deposits during the year, which was partly offset by £0.4m of interest payable. Details of the Group's borrowings are set out in Note 19 to the Accounts.

TAXATION

The effective tax rate for the Group in 2000 was 37% (1999: tax credit). This high rate was due to unrelieved tax losses arising in the US operations resulting from the weak operating performance, exacerbated by the capital structure in the US. Measures have been taken since the year end to address both these issues and it is expected that in 2001 the tax charge will reduce to a more normal level, particularly as the US tax losses will be relievable against future profits.

FINANCIAL REVIEW (continued)**CORPORATE DEVELOPMENTS**

In November 2000 the Group completed the acquisition of Wafer Technology Limited. Wafer Technology, based in Milton Keynes, UK, is a leading manufacturer of substrates for the compound semiconductor industry, principally gallium arsenide and indium phosphide. The consideration payable at completion (inclusive of acquisition costs) amounted to £40.3m, £14.5m of which was paid in cash and the balance in new IQE plc shares. There is an additional element of deferred consideration payable in new IQE shares in March 2002, which is estimated at £1.0m. In accordance with the requirements of FRS10, the goodwill arising on the acquisition, which amounted to £36.8m, has been capitalised and is being amortised over twenty years.

Also in November 2000 the Group established a new subsidiary in Cardiff, UK, IQE Silicon Compounds Limited, which is the first independent provider in Europe of outsourced epitaxial services to the silicon based semiconductor industry. Total investment in the venture up to the year end amounted to £6.0m, of which £2.6m was provided through new lease financing. Significant further investment will be made in 2001 and the project has been awarded an Industrial Development Grant of £1.7m by the National Assembly for Wales.

INVESTMENT

Group capital expenditure increased sharply to £36.2m (1999: £9.5m). In addition to the initial investment in IQE Silicon Compounds noted above, both the IQE (Europe) and IQE Inc facilities were expanded and additional plant and equipment brought on line. At IQE (Europe), six new MOVPE reactors were purchased during the year while IQE Inc also acquired six MBE reactors with deposits placed on a further three. The cleanroom facilities for wafer cleaning and characterisation were also significantly enhanced at both sites.

In addition to capital expenditure, the Group invests significant amounts through the profit and loss account in new product and process development and marketing. Total research and development spend amounted to £1.9m in the year (1999: £1.3m), which was equivalent to 6.2% of sales (1999: 6.8% of sales).

CASH AND CASH FLOW

Cash balances stood at £39.5m (1999: £8.1m) at the year end. Over the year cash increased by £31.4m with some £10.8m generated from operations and £67.0m raised from share issues, which more than offset £33.6m of capital expenditure and the net cash cost of the acquisition of Wafer Technology Limited at £13.5m. Interest and tax amounted to a net credit of £1.2m due to the high level of interest income.

CAPITAL STRUCTURE AND FUNDING

The Group's balance sheet was substantially strengthened in the year, with shareholders' funds increasing by £96.6m to £117.6m, principally as a result of share issues. Some 12.6m shares were issued in May at the time of the listing on the London Stock Exchange with a further 3.2m shares issued to index tracker funds in September. In November, 8.7m shares were issued in connection with the acquisition of Wafer Technology Limited.

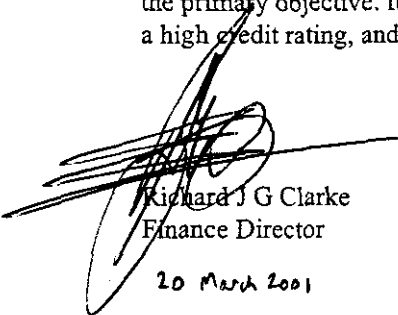
FINANCIAL REVIEW (continued)

TREASURY

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 US dollar and Yen inflows from sales to customers in these currencies and these to some extent provide a natural hedge. Any surplus or shortfall arising over a rolling period of up to twelve months is constantly monitored and the risk fixed through forward currency contracts taken out with the Group's bankers. Other currencies in which the Group trades from time to time are also monitored and material imbalances are fixed as the need arises. It is not the Board's policy to speculate in currency fluctuations.

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

The Board has a conservative policy toward the investment of surplus cash, with the protection of principal being the primary objective. Its guidelines require that cash should be invested with a number of different institutions with a high credit rating, and on fixed deposit maturity not exceeding 6 months.



Richard J G Clarke
Finance Director

20 March 2001

DIRECTORS' REPORT

The Directors present their annual report and the audited financial statements for the year ended 31 December 2000.

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 Group's activities and future prospects are detailed in the Chairman's Statement, the Operations Review and the Financial Review (pages 10 to 16) and should be read as part of this report.

DIVIDENDS

The Directors do not recommend the payment of a dividend.

DIRECTORS

The Directors in office during the year and their beneficial interests in the Company's issued ordinary share capital were as follows:

	Ordinary shares of 1p each 2000 No.	Ordinary shares of 10p each 1999 No.
Dr A W Nelson	26,057,970	2,998,590
Dr M D Scott	26,057,970	2,998,590
T L Hierl	16,489,230	1,902,228
S T Massie	108,620	20,568
M S M Lamb (appointed 22 November 2000)	3,341,250	See below
Dr G H H Ainsworth	5,410	541
G Bressner	-	-

S Byars was appointed a Director on 1 January 2001 and R J G Clarke was appointed a Director on 8 March 2001.

On appointment M S M Lamb held 3,341,250 1p ordinary shares in the Company.

S T Massie held options for 1,258,300 unissued ordinary 1p shares at 31 December 2000 (1999 – 125,830 options for unissued 10p ordinary shares) and Dr G H H Ainsworth held options for 75,000 unissued ordinary 1p shares at 31 December 2000 (1999 – nil). No other Director held share options at 31 December 2000. Further details are given in Note 5 to the accounts.

RESEARCH AND DEVELOPMENT

During the year the Group incurred costs in respect of research and development of £1,870,000 (1999 - £1,302,000). 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 2000, it was the Group's policy to follow the "Better Payment Practice Code". 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 2000 was 45 days (1999 – 38 days).

DIRECTORS' REPORT (continued)**EMPLOYMENT POLICIES**

It is the policy of the Group that there should be no discrimination in considering applications for employment including those from disabled persons. All employees, including the disabled, are given equal opportunities in terms of career development and promotion. Appropriate training is arranged for disabled persons, including retraining for alternative work of employees who become disabled, to promote their career development within the organisation.

The Group remains committed to its policy of keeping employees fully informed about all matters which concern them. Formal communications are used to achieve this objective, including notice board announcements and newsletters. Employee involvement takes different forms in each subsidiary, ranging from formal committee meetings to less formal discussion groups.

Schemes have been implemented to ensure that employees are properly rewarded for performance and loyalty.

GOING CONCERN

The Directors, after making enquiries, have deliberated on the future prospects of the Group and have a reasonable expectation that it will have adequate resources to continue operating for the foreseeable future and therefore the going concern basis has been adopted in preparing these accounts.

EURO

Directors and senior staff of the Group have continued to review the business in the light of the new European currency. The Group will continue to experience Sterling/Euro exchange rate fluctuations with customers and suppliers whilst the UK remains outside the Euro.

AUDITORS

Deloitte & Touche 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.

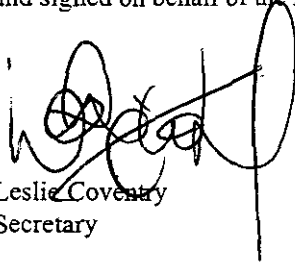
STATEMENT OF DIRECTORS' RESPONSIBILITIES

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 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.

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



Leslie Coventry
Secretary

20 March 2001

REPORT OF THE REMUNERATION COMMITTEE

THE COMMITTEE

The Remuneration Committee consists of the Non-Executive Directors (as detailed on page 3) and is chaired by G Bressner. The Committee complies with Schedule A of the Best Practice Provisions annexed to the Listing Rules of the London Stock Exchange.

The Committee is responsible for the determination of remuneration policy for the Executive Directors. It has access to and takes professional advice.

The fees of the Non-Executive Directors are determined by the Board.

POLICY

In establishing its policy, the Committee has given full consideration to Schedule B of the Best Practice Provisions annexed to the Listing Rules of the London Stock Exchange. The basic objective of the policy is that Executive Directors should receive remuneration which is appropriate to their position of responsibility, and which will attract, motivate and retain Executives of the necessary calibre. Remuneration of the Executive Directors consists of annual salary, bonus, taxable benefits in kind and pension contributions.

BASIC SALARY AND PERFORMANCE BONUS

There is an annual review at which the Committee approves the basic salary for each Executive Director. Details of Directors' salaries, benefits, bonuses and share options can be found on the following page.

BENEFITS

Benefits for Executive Directors comprise fully expensed Company cars, medical health insurance and daily allowances for domestic and foreign business travel.

SHARE OPTIONS

Executive Directors hold share options under The IQE plc Share Option Scheme. Share options held and granted during the year ended 31 December 2000 are shown on page 21. The Committee grants options to Executive Directors and other employees to encourage long term commitment to the Company.

SERVICE CONTRACTS

The Executive Directors have entered into service agreements with the Company which are terminable by either party on twelve months' notice. Each of the agreements contains post termination restrictive covenants which place limitations of solicitation of customers and employees of the Group and on acting in competition with the business of the Group.

PENSIONS

The Executive Directors are members of the Group pension schemes. Their dependants are eligible for dependants' pensions and the payment of a lump sum in the event of death in service.

There have been no changes in the terms of Directors' pension entitlements during the year. There are no unfunded pension promises or similar arrangements for Directors.

REPORT OF THE REMUNERATION COMMITTEE (continued)

REMUNERATION

	Salary 2000 £'000	Fees 2000 £'000	Bonus 2000 £'000	Benefits 2000 £'000	Total 2000 £'000	Total 1999 £'000	Pension contributions 2000 £'000	Pension contributions 1999 £'000
Executive Directors								
Dr A W Nelson	104	-	*59	7	170	87	7	7
Dr M D Scott	73	-	*28	12	113	85	7	7
T L Hierl	117	-	-	-	117	118	-	-
S T Massie	102	-	-	-	102	84	-	-
M S M Lamb (appointed 22 November 2000)	4	-	-	1	5	-	1	-
Non-Executive Directors								
Dr G H H Ainsworth	-	10	-	-	10	9	-	-
G Bressner	-	-	-	-	-	-	-	-
	400	10	87	20	517	374	15	14

Dr Nelson's salary includes a car allowance of £24,500 (1999 - £nil) in lieu of a fully expensed company car.

* Includes adjustment in respect of prior years

SHARE OPTIONS

At 31 December 2000 the following Directors' share options were in existence:

Director	1 January 2000	Granted	10 for 1 share split	Number of options 31 December 2000	Exercise price	Date from which exercisable	Expiry date
S T Massie	33,610	-	302,490	336,100	\$0.130	24.10.98 to 24.10.01	24.10.07
S T Massie	67,220	-	604,980	672,200	\$0.130	14.12.99 to 14.12.02	14.12.08
S T Massie	25,000	-	225,000	250,000	\$1.410	5.11.02	5.11.09
Dr G H H Ainsworth	-	7,500	67,500	75,000	£4.13	16.5.03 to 16.5.10	16.5.10

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

No other Director held share options at any point during the year.

No Directors exercised any options during the year.

CORPORATE GOVERNANCE REPORT

CORPORATE GOVERNANCE

The Combined Code on Corporate Governance, issued by the UK Listing Authority, brings together the recommendations of the Cadbury, Greenbury, Hampel and Turnbull committees and establishes Principles of Good Governance and the Code of Best Practice for listed companies. The paragraphs below, together with the Report of the Remuneration Committee set out on pages 20 to 21, describe how these principles are applied within the Group.

THE BOARD AND ITS COMMITTEES

The Board comprises seven Executive and two Non-Executive Directors. Biographies of the Board members are set out on pages 4 to 6. In the opinion of the Board, the two Non-Executive Directors, Dr G H H Ainsworth and Mr G Bressner, are independent of management and, notwithstanding Note 27 to the Accounts, free from any business or other relationship which could materially interfere with the exercise of their independent judgement.

Dr Nelson currently acts as Chairman and Chief Executive Officer of the Company and the Board believes that this is appropriate at the present time given that there is a Non-Executive element to the Board. Dr Ainsworth is the recognised senior independent Non-Executive Director to whom concerns can be conveyed as required by the Code of Best Practice.

The Board normally meets at least four times a year, in advance of its quarterly reporting dates and where possible at least one meeting is held at the site of each of the Group's operating subsidiaries. A week before the Board meeting the Directors are supplied with comprehensive briefing papers on financial and commercial matters of a standard sufficient to enable the Board to discharge its duties.

Under the Company's Articles of Association each of the Directors is required ordinarily to retire by rotation once every three years.

Specific responsibilities have been delegated to the following Board Committees:

Audit Committee: The Audit Committee comprises the Non-Executive Directors, Dr G H H Ainsworth and G Bressner, under the chairmanship of Dr Ainsworth. The Audit Committee meets at least four times a year and more frequently if required. The Audit Committee has specific written terms of reference which deal with its authority and duties. The Group's external auditors normally attend the meetings by invitation. The Committee receives and considers reports relating to the monitoring of the adequacy of the Group's internal controls, the suitability of its accounting policies and financial reporting, the audit arrangements and matters arising from the external auditors' work. Where appropriate, the Committee makes recommendations to the Board on these matters. Although there is currently no internal audit function, the Audit Committee regularly reviews the need to implement one.

Remuneration Committee: The Remuneration Committee comprises the Non-Executive Directors, Dr G H H Ainsworth and G Bressner, under the chairmanship of G Bressner, and meets periodically as required. The Remuneration Committee has specific written terms of reference which deal with its authority and duties. It is responsible for providing advice and recommendations to the Board on Executive Directors' remuneration, and the terms of service and setting the remuneration of the Executive Directors.

The Board has not established a Nomination Committee as the Board considers itself to be small. However, the Remuneration Committee is responsible for Nominations.

CORPORATE GOVERNANCE REPORT (continued)**SHAREHOLDER COMMUNICATIONS**

The Chief Executive, supported by senior management, regularly meets with, and makes presentations to major institutional shareholders. Institutional shareholders are also invited to visit the Group's operating subsidiaries. The Board is aware that not all of the Company's private investors have access to market information. Shareholders are sent copies of annual and interim reports and, when appropriate, circulars. Notice is given in the Annual Report and Accounts of the date and location of the Annual General Meeting at which shareholders are invited to ask questions concerning the Company's business.

The Company has a web site on which it publishes quarterly financial data and other significant announcements as well as providing details on the Group's facilities and products. The web site address is shown on the back cover of the Annual Report and Accounts.

INTERNAL CONTROL

The Board seeks to maintain a sound system of internal control to safeguard shareholders' investments and the Group's assets.

The Board attaches considerable importance to the Group's system of internal control and risk management and acknowledges that it is responsible for the system and for reviewing its effectiveness. Such a system can only provide reasonable assurance and not absolute assurance against material misstatement or loss, as it is designed to manage rather than to eliminate risk.

The Directors have reviewed the effectiveness of the system of financial control for the year and have taken account of material developments up to the date of signing and rely on the following established framework.

The Board undertakes a series of reviews and regular meetings with the Audit Committee and external auditors to ensure that an ongoing process for identifying, evaluating and managing significant risks faced by the Group is in place. These risks include credit risk, market risk, operational risk and legal and compliance risk. This system has been in place since prior to the flotation on the London Stock Exchange on 19 May 2000 and up to the date of approval of the annual report and accounts. It is regularly reviewed by the Board and is in accordance with the Turnbull guidance.

The reviews cover all controls, including financial, operational and compliance controls and risk management.

Control Procedures: The key procedures that the Directors have established with a view to providing effective financial control are as follows:

The Board considers the Group's strategic plan annually and, within the framework of the plan, approves an annual budget. Operational and financial performance are monitored monthly against this budget and explanations are obtained for significant variances.

Monthly accounts which include key performance indicators are produced and circulated and reviewed against forecast. Results are analysed and discussed at frequent Board meetings.

Regular re-forecasting is carried out and reviewed by the Board.

All major investments, including acquisitions and major items of capital expenditure, are subject to detailed financial review and authorisation by the Board.

CORPORATE GOVERNANCE REPORT (continued)

INTERNAL CONTROL (continued)

There is no internal audit function in place, although annual reviews are carried out to assess the need for one.

A formal framework of appropriate responsibility and authorisation is in place and is regularly reviewed for compliance and completeness.

The Directors confirm that they have carried out a review of the effectiveness of internal control as it operated during the year.

Risk Management: Significant areas of risk have been identified by the Directors and senior managers of the Group and have been discussed and evaluated. Review and implementation of procedures to measure and reduce the risk areas are given a high priority by the Board and the Audit Committee and reviews are regularly carried out.

COMPLIANCE

Prior to the Company's listing on the London Stock Exchange on 19 May 2000, the Board reviewed those areas of Corporate Governance where the Company did not fully comply with the recommendations of the Combined Code because the necessary steps needed further consideration. The Board is satisfied that the Company complied throughout the year, and during the subsequent period up to and including the date of this report, with the Code provisions set out in Section 1 of the Combined Code on Corporate Governance issued by the Financial Services Authority except as set out below:

Combined Code Provision A.1.6

Training: The Company does not have a formal training programme for Directors either on appointment or subsequently, although all Directors are encouraged to obtain such training as they consider necessary at the expense of the Company.

Combined Code Provision A.2.1

Chairman and CEO: At the present stage of the Company's development, the Board considers it appropriate to combine the positions of Chairman and CEO. However, as explained in the Listing Particulars issued by the Company at the time of its admission to the Official List of the London Stock Exchange, the Company is actively seeking to appoint an additional independent Non-Executive Director who would act as Chairman.

Combined Code Provision A.3.1

Board Composition: Non-Executive Directors consist of less than one third of the Board. However, as stated above, the Board is seeking to appoint a further Non-Executive Director.

Combined Code Provision D.3.1

Audit Committee: The Audit Committee comprises the two Non-Executive Directors, which is less than the three prescribed by the Combined Code. However, as noted above, the Company is currently seeking to appoint an additional independent Non-Executive Director who would serve on the Committee.

AUDITORS' REPORT TO THE MEMBERS OF IQE PLC

We have audited the financial statements on pages 26 to 50 which have been prepared under the accounting policies set out on page 31 to 33.

Respective responsibilities of directors and auditors

The Directors are responsible for preparing the Annual Report, including as described on page 19 preparation of the financial statements, which are required to be prepared in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established by statute, the Auditing Practices Board, the UK Listing Authority, and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you, if in our opinion, the Directors' report is not consistent with the financial statements, if the Group has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law or the Listing Rules regarding Directors' remuneration and transactions with the Company and other members of the Group is not disclosed.

We review whether the corporate governance statement on pages 22 to 24 reflects the Group's compliance with the seven provisions of the Combined Code specified for our review by the UK Listing Authority and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report, including the corporate governance statement, and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

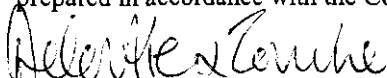
Basis of opinion

We conducted our audit in accordance with United Kingdom 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 2000 and of the profit of the Group 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 2001

CONSOLIDATED PROFIT AND LOSS ACCOUNT
Year ended 31 December 2000

	Note	2000 £'000	1999 £'000
TURNOVER	3		
Continuing operations		29,128	19,043
Acquisitions		989	-
		<hr/>	<hr/>
Total turnover		30,117	19,043
Cost of sales	3	(19,785)	(12,558)
		<hr/>	<hr/>
GROSS PROFIT	3	10,332	6,485
Operating expenses before goodwill and exceptional items:			
Distribution expenses	3	(2,052)	(1,414)
Administrative expenses:			
Research and development	3	(1,870)	(1,302)
Other administrative expenses	3	(4,415)	(2,315)
		<hr/>	<hr/>
		(8,337)	(5,031)
		<hr/>	<hr/>
OPERATING PROFIT BEFORE GOODWILL AND EXCEPTIONAL ITEMS		1,995	1,454
Other operating expenses			
Goodwill amortisation	3	(209)	-
Exceptional items	3, 11	-	(171)
		<hr/>	<hr/>
OPERATING PROFIT	4		
Continuing operations		1,503	1,283
Acquisitions		283	-
		<hr/>	<hr/>
Total operating profit		1,786	1,283
Other interest receivable and similar income		1,630	327
Interest payable and similar charges	6, 11	(422)	(917)
		<hr/>	<hr/>
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION		2,994	693
Tax on profit on ordinary activities	7	(1,184)	149
		<hr/>	<hr/>
PROFIT FOR THE FINANCIAL YEAR		1,810	842
DIVIDENDS	8	-	-
		<hr/>	<hr/>
RETAINED PROFIT FOR THE FINANCIAL YEAR		1,810	842
		<hr/>	<hr/>
Earnings per ordinary share	10	1.24p	0.63p
		<hr/>	<hr/>
Diluted earnings per ordinary share	10	1.18p	0.59p
		<hr/>	<hr/>

CONSOLIDATED STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

Year ended 31 December 2000

	2000	1999
	£'000	£'000
Profit for the financial year	1,810	842
Currency translation differences on foreign currency net investments	680	96
Total recognised gains and losses relating to the year	<u>2,490</u>	<u>938</u>

COMBINED STATEMENT OF MOVEMENTS IN SHAREHOLDERS' FUNDS AND
STATEMENT OF MOVEMENTS ON RESERVES

	Issued share capital £'000	Share premium £'000	Shares to be issued £'000	Merger reserve £'000	Profit and loss account £'000	Exchange rate reserve £'000	Total 2000 £'000	Total 1999 £'000
THE GROUP								
Balance at 1 January 2000	1,359	18,907	-	(605)	1,281	8	20,950	631
Shares issued	274	94,084	-	-	-	-	94,358	20,440
Cost of shares issued	-	(1,189)	-	-	-	-	(1,189)	(1,214)
Adjustment in respect of further share capital issued by subsidiary	-	-	-	-	-	-	-	155
Deferred consideration on acquisition of subsidiary	-	-	988	-	-	-	988	-
Foreign exchange translation differences	-	-	-	-	-	680	680	96
Profit attributable to members of the Group	-	-	-	-	1,810	-	1,810	842
Balance at 31 December 2000	<u>1,633</u>	<u>111,802</u>	<u>988</u>	<u>(605)</u>	<u>3,091</u>	<u>688</u>	<u>117,597</u>	<u>20,950</u>
THE COMPANY								
Balance at 1 January 2000	1,359	18,907	-	-	692	-	20,958	-
Shares issued	274	94,084	-	-	-	-	94,358	21,480
Cost of shares issued	-	(1,189)	-	-	-	-	(1,189)	(1,214)
Deferred consideration on acquisition of subsidiary	-	-	988	-	-	-	988	-
Profit attributable to members of the Company	-	-	-	-	3,509	-	3,509	692
Balance at 31 December 2000	<u>1,633</u>	<u>111,802</u>	<u>988</u>	<u>-</u>	<u>4,201</u>	<u>-</u>	<u>118,624</u>	<u>20,958</u>

CONSOLIDATED BALANCE SHEET
31 December 2000

	Note	2000 £'000	1999 £'000
FIXED ASSETS			
Intangible assets	12	36,543	-
Tangible assets	13	47,848	11,483
		<u>84,391</u>	<u>11,483</u>
CURRENT ASSETS			
Stocks	15	7,885	2,573
Debtors	16	10,311	7,743
Cash at bank		39,512	8,117
		<u>57,708</u>	<u>18,433</u>
CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR	17	<u>(17,405)</u>	<u>(4,518)</u>
NET CURRENT ASSETS		<u>40,303</u>	<u>13,915</u>
TOTAL ASSETS LESS CURRENT LIABILITIES		124,694	25,398
CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR	18	(5,507)	(4,117)
PROVISION FOR LIABILITIES AND CHARGES	20	<u>(1,590)</u>	<u>(331)</u>
		<u>117,597</u>	<u>20,950</u>
CAPITAL AND RESERVES			
Called-up share capital	21	1,633	1,359
Merger reserve		(605)	(605)
Share premium		111,802	18,907
Shares to be issued		988	-
Profit and loss account		3,091	1,281
Exchange rate reserve		688	8
TOTAL EQUITY SHAREHOLDERS' FUNDS		<u>117,597</u>	<u>20,950</u>

These financial statements were approved by the Board of Directors on 20 March 2001.
Signed on behalf of the Board of Directors

Dr A W Nelson

R J G Clarke

PARENT COMPANY BALANCE SHEET
31 December 2000

	Note	2000 £'000	1999 £'000
FIXED ASSETS			
Investments	14	42,340	1,039
CURRENT ASSETS			
Debtors	16	41,648	13,197
Cash at bank and in hand		35,138	6,871
		76,786	20,068
CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR			
	17	(502)	(149)
NET CURRENT ASSETS			
		76,284	19,919
TOTAL ASSETS LESS CURRENT LIABILITIES			
		118,624	20,958
CAPITAL AND RESERVES			
Called-up share capital	21	1,633	1,359
Share premium account		111,802	18,907
Shares to be issued		988	-
Profit and loss account		4,201	692
TOTAL EQUITY SHAREHOLDERS' FUNDS			
		118,624	20,958

These financial statements were approved by the Board of Directors on 20 March 2001.
Signed on behalf of the Board of Directors

Dr A W Nelson

R J G Clarke

CONSOLIDATED CASH FLOW STATEMENT
Year ended 31 December 2000

	Note	2000 £'000	1999 £'000
Net cash inflow/(outflow) from operating activities	22	10,949	(2,877)
Returns on investments and servicing of finance			
Interest received		1,630	327
Interest paid		(422)	(917)
Net cash inflow/(outflow) from returns on investments and servicing of finance		1,208	(590)
Taxation			
United Kingdom corporation tax paid		(144)	(282)
Capital expenditure			
Payments to acquire tangible fixed assets		(33,566)	(9,540)
Proceeds from sale of tangible fixed assets		-	2,127
Net cash outflow from capital expenditure		(33,566)	(7,413)
Acquisitions and disposals			
Payments to acquire investments in subsidiaries	12	(14,501)	-
Net cash acquired with subsidiary	12	533	-
Net cash outflow from acquisitions and disposals		(13,968)	-
Financing			
Issue of ordinary share capital		67,357	19,381
Advances of new loans		-	3,032
Repayment of loans		(441)	(3,475)
Net cash inflow from financing		66,916	18,938
Increase in cash	23	31,395	7,776

NOTES TO THE ACCOUNTS

Year ended 31 December 2000

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 year under review.

Basis of consolidation

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

The acquisition of EPI Holdings Limited and IQE Inc (formerly 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 IQE Europe Limited (formerly known as Epitaxial Products International Limited) and its subsidiary Epitaxial Products Inc by EPI Holdings Limited, a new company established for that purpose, on 27 March 1996 and the acquisition of Wafer Technology International and its subsidiary Wafer Technology Limited on 22 November 2000 have been accounted for under acquisition accounting, whereby these companies became part of the Group on the date of acquisition.

Turnover

Turnover represents amounts invoiced, exclusive of value added taxation.

Tangible fixed assets

Tangible fixed assets are stated at cost less accumulated depreciation. Cost comprises all costs that are directly attributable to bringing the asset into working condition for its intended use, as defined by Financial Reporting Standard Number 15.

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

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

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

NOTES TO THE ACCOUNTS**Year ended 31 December 2000****1. ACCOUNTING POLICIES (continued)****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. The goodwill arising on the acquisition of Epitaxial Products International Limited and its subsidiary Epitaxial Products Inc, by EPI Holdings Limited was written off directly to reserves in the year of acquisition. Goodwill of £284,000 remains eliminated in the profit and loss reserve and will be charged to the profit and loss account on the subsequent disposal of IQE (Europe) Limited (formerly Epitaxial Products International Limited) and its subsidiary Epitaxial Products Inc. Following the issue of Financial Reporting Standard 10, goodwill arising in accounting periods ending on or after 23 December 1998 must be classified as an asset on the balance sheet and amortised over its useful life. The goodwill arising on the acquisition of Wafer Technology International Limited and its subsidiary Wafer Technology Limited has been capitalised and is being amortised over its useful life which is considered by the Directors to be 20 years.

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.

Foreign currencies

Transactions in foreign currencies during the year 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 IQE Inc, (formerly 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 year. The resulting translation differences are taken direct to reserves.

Pension costs

The Group operates defined contribution pension schemes. 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 on 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 tax 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 year 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.

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

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

1. ACCOUNTING POLICIES (continued)

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 prejudicial to the interests of the Group (Schedule 4, Part III, Section 55(5) Companies Act 1985 and Statement of Standard Accounting Practice Number 25).

3. ANALYSES OF CONTINUING AND ACQUIRED OPERATIONS

	2000			1999
	£'000			£'000
	Continuing	Acquisitions	Total	Continuing
Turnover	29,128	989	30,117	19,043
Cost of sales	(19,230)	(555)	(19,785)	(12,558)
Gross profit	9,898	434	10,332	6,485
Operating expenses				
Distribution expenses	2,027	25	2,052	1,414
Research and development	1,848	22	1,870	1,302
Other administrative expenses	4,311	104	4,415	2,315
Goodwill amortisation	209	-	209	-
Exceptional items	-	-	-	171
	8,395	151	8,546	5,202
Operating profit	1,503	283	1,786	1,283

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

4. OPERATING PROFIT

	2000 £'000	1999 £'000
Operating profit is after charging/(crediting):		
Depreciation of tangible fixed assets:		
Owned assets	2,616	1,479
Leased assets	223	30
Amortisation of goodwill	209	-
Auditors' remuneration		
- Audit fees	112	45
- Company audit fees	3	3
- Other services	358	346
Operating lease rentals		
- Plant and machinery	423	71
- Other	210	133
Exchange losses/(gains)	51	(74)
	<u> </u>	<u> </u>

5. INFORMATION REGARDING DIRECTORS AND EMPLOYEES

Directors' emoluments:

	Salary 2000 £'000	Fees 2000 £'000	Bonus 2000 £'000	Benefits 2000 £'000	Total 2000 £'000	Total 1999 £'000	Pension contributions	
	£'000	£'000	£'000	£'000	£'000	£'000	2000 £'000	1999 £'000
Executive Directors								
Dr A W Nelson	104	-	*59	7	170	87	7	7
Dr M D Scott	73	-	*28	12	113	85	7	7
T L Hierl	117	-	-	-	117	118	-	-
S T Massie	102	-	-	-	102	84	-	-
M S M Lamb (appointed 22 November 2000)	4	-	-	1	5	-	1	-
Non-Executive Directors								
Dr G H H Ainsworth	-	10	-	-	10	9	-	-
G Bressner	-	-	-	-	-	-	-	-
	<u>400</u>	<u>10</u>	<u>87</u>	<u>20</u>	<u>517</u>	<u>383</u>	<u>15</u>	<u>14</u>

Dr Nelson's salary includes a car allowance of £24,500 (1999 - £nil) in lieu of a fully expensed company car.

* Includes adjustment in respect of prior year

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

5. INFORMATION REGARDING DIRECTORS AND EMPLOYEES (continued)

Directors' share options

	1 January 2000	Granted	10 for 1 share split	Exercised	Lapsed	31 December 2000
Director						
S T Massie	33,610	-	302,490	-	-	336,100
S T Massie	67,220	-	604,980	-	-	672,200
S T Massie	25,000	-	225,000	-	-	250,000
Dr G H H Ainsworth	-	7,500	67,500	-	-	75,000

Directors' share options

	31 December 2000	Exercise price	Date from which exercisable	Expiry date
Director				
S T Massie	336,100	\$0.130	24.10.98 to 24.10.01	24.10.07
S T Massie	672,200	\$0.130	14.12.99 to 14.12.02	14.10.08
S T Massie	250,000	\$1.410	05.11.02	05.11.09
Dr G H H Ainsworth	75,000	£4.13	16.5.03 to 16.5.10	16.5.10

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

On 11 September 2000 the Company carried out a 10 for 1 share split.

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

5. INFORMATION REGARDING DIRECTORS AND EMPLOYEES (continued)

	2000 £'000	1999 £'000
Employee costs		
Wages and salaries	7,623	5,104
Social security costs	1,061	813
Other pension costs	243	175
	<u>8,927</u>	<u>6,092</u>
	2000	1999
	No.	No.
The average number of employees, including Directors, during the year was as follows:	<u>322</u>	<u>197</u>

6. INTEREST PAYABLE AND SIMILAR CHARGES

	2000 £'000	1999 £'000
Bank loans	-	107
Other loans	415	803
Finance lease interest	7	7
	<u>422</u>	<u>917</u>

7. TAXATION

	2000 £'000	1999 £'000
United Kingdom corporation tax at 30% (1999 – 30%)	49	(133)
United Kingdom deferred tax	1,141	398
Overseas corporation tax	-	(407)
Adjustments in respect of prior years provision:		
United Kingdom corporation tax	(124)	120
United Kingdom deferred tax	118	(127)
	<u>1,184</u>	<u>(149)</u>

The high taxation charge is due to tax losses available for carry forward within the Group which cannot be recognised as deferred tax assets under UK GAAP.

8. DIVIDENDS

No dividend has been paid or proposed in 2000 (1999 - £nil).

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

9. 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 £3,509,000 (1999 - £692,000).

10. 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.

In September 2000 the Company carried out a 10 for 1 share split. In accordance with the provisions of FRS14 "Earnings Per Share", for the purpose of calculating earnings per share, the number of ordinary shares is adjusted as if the share split had taken place at 1 January 1999.

	2000 £'000	1999 £'000
Basic and diluted earnings attributable to ordinary shareholders	1,810	842
	<u>No.</u>	<u>No.</u>
Weighted average number of ordinary shares	146,203,992	132,717,220
Diluted share options	6,924,456	10,748,380
Adjusted weighted average number of ordinary shares	153,128,448	143,465,600
Earnings per share	1.24p	0.63p
Diluted earnings per share	1.18p	0.59p

11. EXCEPTIONAL ITEMS

Included within other operating expenses are amounts totalling £nil (1999 - £171,138) in respect of costs associated with the acquisition of EPI Holdings Limited and IQE Inc (formerly Quantum Epitaxial Designs, Inc) by IQE plc and the subsequent flotation of IQE plc.

Included within interest payable are amounts totalling £nil (1999 - £328,050) in respect of the early settlement of certain bank loans arising out of the acquisition of EPI Holdings Limited and IQE Inc (formerly Quantum Epitaxial Designs, Inc) by IQE plc and the subsequent flotation of IQE plc.

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

12. INTANGIBLE FIXED ASSETS

The Group	Goodwill £'000
Cost	
At 1 January 2000	-
Additions in the year	36,752
At 31 December 2000	<u>36,752</u>
Accumulated amortisation	
At 1 January 2000	-
Charge for the year	209
At 31 December 2000	<u>209</u>
Net book value	
At 31 December 2000	<u>36,543</u>
At 31 December 1999	<u>-</u>

100% of the issued share capital of Wafer Technology International Limited and Wafer Technology Limited was acquired on 22 November 2000 for a consideration of £41,301,000. This acquisition has been accounted for using the acquisition method of accounting. The amount of goodwill arising as a result of the acquisition is £36,752,000. This has been capitalised in the Group balance sheet. The consideration included a deferred consideration of 500,000 ordinary 1p shares in IQE plc to be issued within 14 days following 28 February 2002. The market value per share at 31 December 2000 was £1.975.

The following table summarises the adjustments made to the book value of the major categories of assets and liabilities acquired to arrive at the fair values included in the consolidated financial statements at the date of acquisition.

	Book amount £'000	Fair value adjustment £'000	Fair value to the Group £'000
Tangible fixed assets	908	1,495	2,403
Current assets	2,894	-	2,894
Creditors	(869)	-	(869)
Taxation	121	-	121
	<u>3,054</u>	<u>1,495</u>	4,549
Goodwill			<u>36,752</u>
			<u>41,301</u>

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

12. INTANGIBLE FIXED ASSETS (continued)

The cash flow effects of the acquisition are:

Net assets acquired:	2000 £'000
Tangible fixed assets	2,403
Stocks	1,299
Debtors	1,062
Cash at bank and in hand	533
Creditors	(869)
Taxation	121
	<hr/>
Goodwill	4,549
	36,752
	<hr/>
	41,301
	<hr/> <hr/>
Satisfied by:	
Cash	14,000
8,750,000 ordinary 1p shares in IQE plc (market value at 22 November 2000, £2.95 per share)	25,812
Deferred consideration:	
500,000 ordinary 1p shares in IQE plc (market value at 31 December 2000, £1.975 per share)	988
Costs of acquisition	501
	<hr/>
	41,301
	<hr/> <hr/>

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

13. TANGIBLE FIXED ASSETS

The Group	Freehold land & buildings £'000	Short leasehold improve- ments £'000	Fixtures & fittings £'000	Plant & machinery £'000	Assets in the course of construction £'000	Total £'000
Cost						
At 1 January 2000	2,578	536	1,422	18,336	533	23,405
Acquired with subsidiary	-	685	164	1,554	-	2,403
Additions	1,095	-	767	7,016	27,278	36,156
Disposals	-	-	-	(29)	-	(29)
Transfers	-	1,146	-	1,422	(2,568)	-
Exchange difference	-	57	37	716	225	1,035
At 31 December 2000	<u>3,673</u>	<u>2,424</u>	<u>2,390</u>	<u>29,015</u>	<u>25,468</u>	<u>62,970</u>
Depreciation						
At 1 January 2000	142	224	626	10,930	-	11,922
Charge for the year	117	223	280	2,219	-	2,839
Exchange difference	-	20	17	324	-	361
At 31 December 2000	<u>259</u>	<u>467</u>	<u>923</u>	<u>13,473</u>	<u>-</u>	<u>15,122</u>
Net book value						
At 31 December 2000	<u>3,414</u>	<u>1,957</u>	<u>1,467</u>	<u>15,542</u>	<u>25,468</u>	<u>47,848</u>
At 31 December 1999	<u>2,436</u>	<u>312</u>	<u>796</u>	<u>7,406</u>	<u>533</u>	<u>11,483</u>

The net book value of fixtures and fittings includes £60,000 (1999: £90,000) and the net book value of plant and machinery includes £3,240,000 (1999: £2,342,000) in respect of assets held under finance leases.

14. INVESTMENTS HELD AS FIXED ASSETS

	2000 £'000
Cost and net book value at 1 January 2000	1,039
Additions in the period	<u>41,301</u>
Cost and net book value at 31 December 2000	<u>42,340</u>

The above additions relate to the acquisition of 100% of the ordinary share capital of Wafer Technology International Limited and the remaining 19% of the ordinary share capital of Wafer Technology Limited not already owned by Wafer Technology International Limited (see note 12).

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

14. INVESTMENTS HELD AS FIXED ASSETS (continued)

The above is represented by investments in the following 100% owned subsidiaries:

	£'000
IQE Inc (formerly Quantum Epitaxial Designs Inc)	439
EPI Holdings Limited	600
Wafer Technology International Limited and Wafer Technology Limited	41,301
	<u>42,340</u>

15. STOCKS

	The Group £'000	2000 The Company £'000	The Group £'000	1999 The Company £'000
Raw materials and consumables	6,796	-	2,239	-
Work in progress and finished goods	1,089	-	334	-
	<u>7,885</u>	<u>-</u>	<u>2,573</u>	<u>-</u>

16. DEBTORS

	The Group £'000	2000 The Company £'000	The Group £'000	1999 The Company £'000
Trade debtors	8,419	-	3,045	-
Amounts owed by Group undertakings	-	41,387	-	13,177
Other debtors and prepayments	1,532	139	4,565	20
Corporation tax	360	122	133	-
	<u>10,311</u>	<u>41,648</u>	<u>7,743</u>	<u>13,197</u>

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

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

17. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR

	The Group £'000	2000 The Company £'000	The Group £'000	1999 The Company £'000
Other loans	508	-	504	-
Trade creditors	13,446	-	3,115	-
Amounts due under hire purchase and finance leases	753	-	18	-
Other taxation and social security	460	131	111	27
Corporation tax	-	-	-	122
Accruals and deferred income	2,238	371	770	-
	<u>17,405</u>	<u>502</u>	<u>4,518</u>	<u>149</u>

18. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR

	The Group £'000	2000 The Company £'000	The Group £'000	1999 The Company £'000
Amounts due under hire purchase and finance leases	1,911	-	81	-
Other loans	3,527	-	3,943	-
Deferred income	69	-	93	-
	<u>5,507</u>	<u>-</u>	<u>4,117</u>	<u>-</u>

19. BORROWINGS

	The Group	
	2000 £'000	1999 £'000
Other loans		
Other loans are payable as follows:		
Within one year	508	504
Between one and two years	661	455
Between two and five years	1,295	1,594
Over five years	1,571	1,894
	<u>4,035</u>	<u>4,447</u>

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

19. BORROWINGS (continued)

	The Group	
	2000 £'000	1999 £'000
Hire purchase and finance lease repayments		
Hire purchase and finance lease repayments are payable as follows:		
Within one year	753	18
Between one and two years	793	25
Between two and five years	1,118	56
	2,664	99
	2,664	99

Other loans comprise a loan from 3i of £1,235,000 (1999 - £1,425,000), a loan from the WDA of £1,482,551 (1999 - £1,482,551) and a loan from Copelco of £1,316,714 (1999 - £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 13 annual instalments of £95,000, which commenced on 31 August 2000. The loan is secured by a fixed and floating charge over the assets of the Group.

Interest is charged on the WDA loan at a maximum rate of 8.5% per annum. The loan is secured on the Group's property. The loan is repayable by 32 instalments, quarterly in arrears, commencing 1 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.

20. DEFERRED TAXATION

	At 1 January 2000 £'000	Charged to profit and loss account £'000	At 31 December 2000 £'000
	UK deferred tax	331	1,259
	331	1,259	1,590
	331	1,259	1,590

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

20. DEFERRED TAXATION (continued)

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

	Provided		Unprovided	
	2000	1999	2000	1999
	£'000	£'000	£'000	£'000
The Group				
Capital allowances in excess of depreciation	1,736	381	(540)	-
Other timing differences	(146)	(50)	-	-
	<u>1,590</u>	<u>331</u>	<u>(540)</u>	<u>-</u>

21. SHARE CAPITAL

	2000		1999	
	Number of shares	£'000	Number of shares	£'000
Authorised				
Ordinary shares of 1p (1999 - 10p) each	<u>250,000,000</u>	<u>2,500</u>	<u>19,000,000</u>	<u>1,900</u>
Allotted, called up and fully paid				
Ordinary shares of 1p (1999 - 10p) each	<u>163,250,498</u>	<u>1,633</u>	<u>13,595,167</u>	<u>1,359</u>

During the year the Company carried out a 10 for 1 share split.

8,750,000 1p ordinary shares were issued in the year to acquire 100% of the ordinary share capital of Wafer Technology Limited and Wafer Technology International Limited at a total premium of £25,725,000.

Also during the year 1,482,222 10p ordinary shares (later split into 14,822,220 1p ordinary shares) and 3,726,608 1p ordinary shares were issued for cash at a total premium of £68,359,000.

The movement in ordinary shares during the year was:

	At 1 January 2000 No.	Shares Issued prior to split No.	10 for 1 share split No.	Shares issued following share split No.	At 31 December No.
Brought forward	13,595,167	-	122,356,503	-	135,951,670
Secondary offering	-	1,263,157	11,368,413	-	12,631,570
Tracker funds	-	-	-	3,230,000	3,230,000
Wafer Technology International Limited acquisition	-	-	-	8,750,000	8,750,000
Options exercised	-	219,065	1,971,585	496,608	2,687,258
	<u>13,595,167</u>	<u>1,482,222</u>	<u>135,696,501</u>	<u>12,476,608</u>	<u>163,250,498</u>

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

21. SHARE CAPITAL (continued)

Under the Company's share option scheme adopted on 26 May 1999, employees held options at 31 December 2000 for 9,328,082 unissued ordinary shares as follows:

Number of shares	Option price per shares £	Option period ending
1,554,562	0.01 – 0.09	31 December 2007
1,659,250	0.01 – 0.09	31 December 2008
1,569,210	0.01 – 2.79	31 December 2009
33,060	0.01	31 December 2010
1,876,000	0.96 – 7.50	31 December 2010

The movements on share options during the year were as follows:

	Options No.
At 1 January 2000	10,380,990
Granted	2,340,560
Exercised	(2,687,258)
Cancelled	(706,210)
At 31 December 2000	<u>9,328,082</u>

22. RECONCILIATION OF OPERATING PROFIT TO NET CASH INFLOW FROM OPERATING
ACTIVITIES

	2000 £'000	1999 £'000
Operating profit	1,786	1,283
Depreciation charges	2,839	1,509
Amortisation of goodwill	209	-
Loss on sale of fixed assets	29	-
Increase in stocks	(4,013)	(982)
Increase in debtors	(1,157)	(4,851)
Increase in creditors	11,280	81
Government grant release	(24)	(29)
Government grant received	-	112
Net cash inflow/(outflow) from operating activities	<u>10,949</u>	<u>(2,877)</u>

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

23. RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET FUNDS

	2000 £'000	1999 £'000
Increase in cash in the year	31,395	7,776
Loan repayments	441	3,611
Loans received	-	(2,908)
	<hr/>	<hr/>
Change in net funds resulting from cash flows	31,836	8,479
Inception of new finance leases	(2,590)	(124)
	<hr/>	<hr/>
Net movement for year	29,246	8,355
Net funds at 1 January 2000	3,571	(4,648)
Exchange differences	(4)	(136)
	<hr/>	<hr/>
Net funds at 31 December 2000	<u>32,813</u>	<u>3,571</u>

24. ANALYSIS OF NET FUNDS

	At 31 December 1999 £'000	Cash flow £'000	Other non-cash movements £'000	At 31 December 2000 £'000
Cash in hand and at bank	8,117	31,395	-	39,512
Debt due after one year	(3,943)	416	-	(3,527)
Debt due within one year	(504)	-	(4)	(508)
Finance leases	(99)	25	(2,590)	(2,664)
	<hr/>	<hr/>	<hr/>	<hr/>
	<u>3,571</u>	<u>31,836</u>	<u>(2,594)</u>	<u>32,813</u>

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

25. ADDITIONAL INFORMATION ON SUBSIDIARY UNDERTAKINGS

Name	Class of capital	Portion of shares held	Activity	Country of incorporation
IQE Inc (formerly Quantum Epitaxial Designs, Inc)	Common Stock of \$0.001	100%	Manufacture of advanced semi-conductor materials	USA
EPI Holdings Limited	£1 ordinary shares	100%	Holding Company	UK
IQE (Europe) Limited (formerly Epitaxial Products International Limited)	£1 ordinary shares	100%*	Manufacture of advanced semi-conductor materials	UK
Epitaxial Products, Inc	Common stock of \$10	100%*	Sales office	USA
Wafer Technology International Limited	£1 ordinary shares	100%	Holding Company	UK
Wafer Technology Limited	£1 ordinary shares	100%*	Manufacture of semi-conductor compounds and ultra high purity materials	UK
IQE Silicon Compounds Limited	£1 ordinary shares	100%	Manufacture of silicon epitaxy	UK

The proportion of voting rights of subsidiaries held by the Group is the same as the proportion of shares held.

* Indirect holdings

26. FINANCIAL INSTRUMENTS

The Group's policies as regards derivatives and financial instruments are set out in the Financial Review on pages 14 to 16 and the accounting policies on pages 31 to 33.

The Group does not trade in financial instruments.

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

26. FINANCIAL INSTRUMENTS (continued)

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 2000 the Group had entered into the following forward contracts in:

	Amount	Period	Rate
Bank to buy	\$4,750,000	Jan/Nov 2001	\$1.4142 / 1.5832
	Yen 170,000,000	Jan/Nov 2001	Y149/162
Bank to sell	Euro 3,040,252	Jan/March 2001	E1.5970

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 4. The currency profile of the Group's trade debtors and trade creditors is as follows:

	Trade debtors £'000	Trade creditors £'000
Sterling	641	1,906
US\$	6,968	5,975
Yen	175	291
Other	635	5,274
	<hr/>	<hr/>
Total	8,419	13,446
	<hr/> <hr/>	<hr/> <hr/>

NOTES TO THE ACCOUNTS
Year ended 31 December 2000

26. FINANCIAL INSTRUMENTS (continued)

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

	Assets floating £'000	Assets fixed rate £'000	Liabilities floating rate £'000	Liabilities fixed rate £'000	Total £'000
Sterling	3,770	33,500	1,235	1,483	39,987
US\$	1,762	295	-	1,317	3,375
Yen	113	-	-	-	113
Other	72	-	-	-	72
	<u>5,717</u>	<u>33,795</u>	<u>1,235</u>	<u>2,800</u>	<u>43,547</u>
Comprising					
Cash at bank	5,717	33,795	-	-	39,512
Other loans	-	-	1,235	2,800	4,035
	<u>5,717</u>	<u>33,795</u>	<u>1,235</u>	<u>2,800</u>	<u>43,547</u>
Total	<u>5,717</u>	<u>33,795</u>	<u>1,235</u>	<u>2,800</u>	<u>43,547</u>

For the fixed rate liabilities the weighted average interest rate is 9.61% and the weighted average period for which interest rates are fixed is 5.6 years.

Further details of the financial liabilities at 31 December 2000 are shown in notes 18 and 19.

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

27. RELATED PARTY TRANSACTIONS

During the year the Group incurred professional fees of £109,798 (1999 - £343,415) and expenses of £8,655 (1999 - £nil) payable to Gambit Corporate Finance. Dr Godfrey Ainsworth, who is a Director of IQE plc, is a partner in Gambit Corporate Finance

28. FINANCIAL COMMITMENTS

At 31 December 2000 the Group was committed to making the following payments during the next year in respect of financial commitments:

	Land and buildings		Plant and machinery	
	2000	1999	2000	1999
	£'000	£'000	£'000	£'000
Annual commitments which expire:				
Within one year	28	-	7	15
In the second to fifth year	373	165	657	597
In more than five years	-	-	-	-
	<u>401</u>	<u>165</u>	<u>664</u>	<u>612</u>

NOTES TO THE ACCOUNTS
Year ended 31 December 2000**29. CAPITAL COMMITMENTS**

The Group had the following capital commitments as at 31 December 2000:

	2000 £'000	1999 £'000
Authorised and contracted for	<u>16,690</u>	<u>14,653</u>