

Registered Number 03745726

IQE PLC

Statutory reports and accounts

for the year ended 31 December 2009

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Five year financial summary

	IFRS 2009 £'000	IFRS 2008 £'000	IFRS 2007 £'000	IFRS 2006 £'000	UK GAAP 2005 £'000
Turnover	52,652	60,485	50,065	32,421	20,890
EBITDA (see below)	8,051	8,407	3,891	(1,702)	(4,197)
Operating profit/(loss)					
- Before exceptional items	3,044	4,000	613	(3,956)	(6,064)
- After exceptional items	3,044	69	174	(3,701)	(4,327)
Retained profit/(loss)					
- Before exceptional items	2,058	2,546	(423)	(4,245)	(6,029)
- After exceptional items	2,058	(1,385)	(862)	(3,990)	(4,292)
Net cash flow from operations					
- Before exceptional items	8,139	8,526	2,043	(4,418)	(5,062)
- After exceptional items	7,712	7,461	1,828	(4,418)	(5,062)
Free cash flow*					
- Before exceptional items	3,906	690	(7,066)	(5,820)	(5,921)
- After exceptional items	3,479	(375)	(7,281)	(5,820)	(5,921)
Net (debt)/funds	(14,931)	(18,135)	(14,159)	(5,918)	860
Shareholders' funds	29,837	30,218	22,960	23,840	12,322
EPS					
- Before exceptional items	0 47p	0 59p	(0 10p)	(1 18p)	(1 89p)
- After exceptional items	0 47p	(0 32p)	(0 20p)	(1 14p)	(1 36p)
Diluted EPS	0 44p	(0 32p)	(0 20p)	(1 14p)	(1 36p)

* Free cash flow is defined as net cash flow before acquisitions, financing and net interest paid

EBITDA has been calculated as follows

	IFRS 2009 £'000	IFRS 2008 £'000	IFRS 2007 £'000	IFRS 2006 £'000	UK GAAP 2005 £'000
Profit/(loss) after tax	2,058	(1,385)	(862)	(3,990)	(4,292)
Interest	986	1,454	1,036	289	(35)
Share based payments	898	884	571	501	308
Exceptional items	-	3,931	439	(255)	(1,737)
Depreciation	3,372	3,076	2,400	1,612	1,559
Amortisation of intangible assets	737	447	307	141	-
EBITDA	8,051	8,407	3,891	(1,702)	(4,197)

**Officers and professional advisers for the year ended
31 December 2009**

IQE plc is a public limited company incorporated in England and Wales

Directors

Dr G H H Ainsworth	(Chairman, Non-Executive)
Dr A W Nelson OBE	(President and Chief Executive Officer)
S J Gibson OBE	(Non-Executive)
P J Rasmussen	(Finance Director and Company Secretary)
Dr H R Williams	(Operations Director)

Registered office

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Principal Bankers

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Auditors

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Legal advisers

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Directors' biographies**Dr Godfrey H H Ainsworth BSc, PhD, FCA**

Age 54, Chairman, 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 a human resource consulting group, he founded Gambit Corporate Finance in 1992, a practice specialising in the provision of corporate finance services where he was Managing Partner until his retirement from the firm on 30 November 2009. 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. He was appointed to the Board of IQE Plc in April 1999, and was appointed Chairman in February 2002.

Dr Andrew W Nelson OBE, BSc, PhD, FREng

Age 55, President and Chief Executive Officer

Drew Nelson joined BT Research Laboratories in 1981, leading the group responsible for the development of MOCVD technology for the manufacture of opto-electronic devices for optical fibre communications. He subsequently managed the technology transfer from BT to Agilent. Together with Mike Scott, he founded EPI in 1988, becoming Managing Director in 1991 and Chairman and Chief Executive Officer in 1996. He was appointed Chairman and Chief Executive Officer of IQE Plc in April 1999 and became Chief Executive Officer in February 2002 when he split his role and Dr Godfrey Ainsworth was appointed to the role of Chairman. Dr Nelson has held several Non-Executive Directorship appointments and is currently non-Executive Chairman of AIM listed Enfis plc.

Phillip J Rasmussen BSc, ACA

Age 39, Group Finance Director and Company Secretary

Phillip Rasmussen qualified as a Chartered Accountant in the audit practice of Coopers and Lybrand, a predecessor firm of PricewaterhouseCoopers LLP ("PwC"). During his career with PwC he spent two years in Toronto, Canada and gained significant experience of working with and advising a broad range of companies in a variety of sectors, including multinational main market and AIM listed companies. Before joining IQE, Mr Rasmussen was Director of Transaction Services with PwC in Bristol and worked with IQE on two major acquisitions during 2006. He was appointed to the Board of IQE Plc in March 2007 and as Company Secretary in January 2009.

Dr Howard R Williams BSc, PhD, CEng, MIMechE, MCIBSE

Age 55, Operations Director

Howard Williams has held a number of positions within both Manufacturing and Service industry sectors, with roles ranging from Engineering Management to General Management. He was a member of the founding team of EPI in 1988 and was appointed Operations Director for EPI in 1996. He was appointed General Manager of IQE Inc in 2002 and General Manager of IQE (Europe) Limited in 2003. He was subsequently appointed Chief Operations Officer in 2004 and was appointed to the Board of IQE Plc as Operations Director in December 2004.

Simon J Gibson OBE

Age 52, Non-Executive Director, Chairman of the Remuneration Committee

Simon Gibson is currently President and Chief Executive Officer of Wesley Clover Wales Limited, a private holding company with assets in technology, the leisure sector and commercial real estate. Prior to joining Wesley Clover, Simon was co-founder, President and Chief Executive Officer of Ubiquity Software Corporation, a pioneer in the creation of SIP based telecommunications services for Global Service Providers. Mr Gibson has also been a senior member of the management teams at Newbridge Networks and Mitel, following an initial career at British Telecommunications (BT), and currently holds a number of private and public board appointments. He was appointed to the Board of IQE Plc in January 2002.

Chairman's Review

Dear Shareholder,

2009 was a year of continued progress for IQE, against the backdrop of the most severe and prolonged global recession in living memory. The Group's excellent performance during the adverse economic climate is due to management having the foresight and courage to take action at the earliest opportunity to reduce exposure to changing demands and to ensure the business was in a position of strength to benefit from the economic recovery.

At a strategic level, we achieved a number of significant milestones, including

- Achieving our goal of qualifying with all of the major wireless chip makers. This puts us in an excellent position to continue to grow our market share organically, and at the same time mitigate our exposure to shifts in market share at customer level.
- Continuing to drive progress through innovation by securing competitive advantage through powerful intellectual property. In particular, we filed a number of patents to protect the intellectual property that we have developed in the emerging solar power and advanced electronics markets.
- Completing the acquisition of NanoGaN Limited (NanoGaN), which brought exciting new talent and patented intellectual property to IQE, accelerating our progress against our technology roadmap for solid state lighting (residential and commercial lighting using LEDs) and advanced laser applications (laser projection systems for mobile phones, digital cameras and office applications).

Furthermore, from the outset, we identified that the global economic downturn presented us with an opportunity to strengthen, invest and build on our leadership position in a number of ways, namely

- We have been successful in attracting the best talent from throughout the industry, to add to a team that is second to none in the advanced semi-conductor world. This included a number of high profile appointments into our technical, sales and group management teams.
- We are engaged in a number of new product qualifications as customers have sought security of supply in an uncertain world, and also to access the advantages that IQE offers as the market leader - technology leadership, cost leadership and an unparalleled 'multi-site, multi-platform' service offering. We expect these qualifications to deliver further gains in market share as these projects complete during the course of 2010.
- As expected, the trend to outsource epitaxy continues to accelerate as chip companies continue to constrain their capital expenditure and take advantage of the critical mass that IQE has created as the leading outsource epitaxy provider.

At an operational level, the painful contraction in volumes that we experienced in the last quarter of 2008 continued into 2009. However, thanks to the hard work and professionalism of our workforce, we were successful at operating lean during the fallow period without jeopardising our ability to return rapidly to high volumes once the destocking came to an end. We achieved this recovery with remarkable success, confirming our customers well placed confidence in IQE, and reflecting the dedication and commitment of our people.

And finally, in financial terms, this year marked our return to bottom line profitability and cash generation. The swift and decisive actions of the management team in 2008 protected our profits when volumes remained depressed in the first half, allowing us to deliver a first half EBITDA profit of £1.9m. As volumes returned in the second half, our high operational gearing and careful management allowed us to more than treble our EBITDA to £6.2m for the second half, and reduce net debt by £4.1m to £14.9m at the year end. This translated into a full year retained profit of £2.1m, and EPS of 0.47p per share.

Our outlook looks similarly exciting. The wireless market is set to enjoy a period of sustained rapid growth as the emerging BRIC economies rapidly adopt wireless technology, and the penetration of smartphones accelerates. The solar market is poised for rapid growth as this emerging industry anticipates the move from field trials into large scale production. Solid state lighting remains the only credible long term solution as governments across the globe ban incandescent lighting in order to reduce their carbon footprints, and new mass market advanced laser applications are emerging, enabled by the advanced properties of new semi-conductor materials such as gallium nitride.

Finally, I would like to thank the many people that make our business the success that it has become, firstly to the management and staff for their commitment and dedication, upon whom our business depends for its continued success, our customers and suppliers for their unfailing support through the difficult times, and for their enduring partnership as we move ahead together to share a prosperous future, and finally, to our shareholders for their continued support and confidence in our prospects and potential.

Dr Godfrey H H Ainsworth
Chairman
23 March 2010

Chief Executive's Review

Overview

It is with much pride in the IQE team that I present our 2009 accounts. This was a year of strong progress against our strategic, operational and financial objectives, despite the tough economic environment.

After a challenging start to the year, the full year returned a strong financial performance, demonstrating the resilience of the organisation and the strength of our highly operationally geared business model.

As predicted, the rapid destocking that began in the fourth quarter of 2008 caused a severe reduction in volumes across all of our primary markets. Inevitably, the impact of the destocking continued into 2009, but started to ease towards the end of the first half.

Whilst we took decisive and proactive steps at an early stage to mitigate the impact of the destocking, we also recognised that in order to be able to respond to the upturn in business and to emerge from the downturn in a position of strength, we needed to continue to invest in people and technology. We have been successful on both of these fronts.

As the market leader we have achieved a virtuous circle. We have been successful in attracting exciting new talent, drawn by our market presence, our financial success, and our technology leadership. This strengthening of our talent pool further consolidates our leadership position, which is attractive to customers and suppliers, so completing the circle. This consolidation and emergence of a clear leading player is the hallmark of a maturing industry.

On a technical front, I am extremely pleased with the progress that we have made this year as we have continued to invest. In collaboration with our customers, our product development is continuing to improve the efficiencies of CPV solar cells, which in turn is continuing to drive down the cost of this technology in preparation for mass production. Furthermore, the intellectual property that we have acquired through our acquisition of NanoGaN in October 2009 has put IQE on the 'fast track' to take advantage of the emerging markets for solid state lighting (residential and commercial lighting using LEDs) and advanced laser applications (laser projection systems for mobile phones, digital cameras and office applications).

We are at a very exciting time in the Group's history. We continue to make excellent progress in our core wireless business, which is projecting sustained strong growth in profits and cash generation. At the same time we continue to build an IP rich advanced semi-conductor 'power house' that is uniquely positioned to take advantage of the high growth markets that are emerging.

Financial Review

The well-documented destocking adversely affected the Group's financial performance during the first half of 2009, but a strong recovery during the second half saw a 46% half on half increase in sales to give total revenue for the year of £52.7m. Inevitably, as a result of the slow first half, full year sales were lower than the prior year (£60.5m).

Gross profit margins, (before exceptional items) improved from 19% to 22% year on year, despite lower volumes, reflecting strong cost control and the benefit of improved efficiencies as a result of the restructuring undertaken in 2008.

Selling, general and administrative expenses remained tightly controlled at £8.5m (2008: £8.5m), and EBITDA was only slightly down to £8.1m (2008: £8.4m).

Operating profit was £3.0m (2008: £69,000 or £4.0m before exceptional items).

The Group reported a pretax profit of £2.1m (2008: loss £1.4m or £2.5m profit before exceptional items). At the end of 2009 the Group had an unrecognised deferred tax asset of £29.5m largely relating to historic tax losses. These losses will be utilised to reduce the tax payable on future profits of certain UK and US business units.

Earnings per share were 0.47p (2008: loss 0.32p or profit 0.59p before exceptional items).

In cash flow, the Group converted the EBITDA of £8.1m (2008: £8.4m) into a cash inflow from operations of £8.1m (2008: £8.5m), a 100% cash conversion rate (2008: 101%) before exceptional items.

IQE invested £2.3m (2008: £1.5m) in development expenditure, relating to the qualification of new wireless products and the development of new solar and gallium nitride products. These development activities are expected to generate increased sales as projects are completed in the near future.

The Group also invested £1.4m in capital expenditure compared with £6.6m in the prior year. The cash outflow for capital expenditure was £1.7m (2008: £6.4m) when taking into account a £0.3m reduction (£0.2m increase) in capital creditors. The year-on-year reduction in capital expenditure reflects the completion of a major capital investment programme in 2008 and the return to a maintenance level of capital expenditure in 2009.

The strong operating cash flow and low level of capital expenditure contributed to a significant improvement in free cash flow (net cash flow before acquisitions, financing activities and debt service), which increased from £0.7m in 2008 to £3.9m in 2009 (before exceptional items). With the absorption of £1.3m of free cash during the first half, the free cash generation in the second half was £5.2m.

The strong free cash generation resulted in a £3.2m year-on-year reduction in net debt to £14.9m (2008: £18.1m) and a reduction of £4.1m during the second half.

Strategy

IQE's strategy is to focus on high-growth, high-volume technologies. During 2009, the Group's major markets were focused in particular on high-speed wireless communications and rapidly emerging technologies such as advanced solar cells, ultra-efficient LEDs and ultra-high-speed microprocessor and memory-chip materials.

The global emphasis on green technologies is expected to create high demand for some of these new technologies, particularly CPV solar cells for highly efficient energy generation and consumer optoelectronics. IQE's capabilities in these fields have been enhanced with the acquisition of some significant new intellectual property in a number of key technologies.

In order to provide customers with the most competitive global wafer outsourcing service, IQE has established, including

- a complete range of products covering all major applications,
- global multi-site production capabilities in the primary manufacturing platforms to allow efficient capacity planning and for disaster scenario contingency,
- a broad contact base with access to all the key global markets,
- benefits from economies of scale including purchasing power and research and development efficiencies,
- improved operating and cost efficiencies from sharing best practices and innovation, and
- providing surge capacity to meet the expected growth in demand in the mobile device sector and other high volume activities.

Business Review

Living in a material world

The world is changing. Not only is materials technology changing the way we communicate, work, learn and are entertained, it is also providing solutions to major issues of our time with products such as energy efficient lighting and solar power generation to help combat climate change.

IQE is the world leading specialist in the production of advanced semiconductor materials that play an increasingly important role in this changing world.

- IQE's gallium arsenide (GaAs) based products are found at the heart of many wireless enabled devices including mobile handsets, wireless laptops and netbooks, GPS systems, and set-top boxes. Our GaAs materials are also used along with other materials to produce highly efficient concentrator photovoltaic solar cells (CPV) and a range of laser based products for data storage and optical communications, including the fibre optic infrastructure that has enabled the internet revolution.
- Our advanced silicon epitaxial processes are helping chip manufacturers worldwide to enhance the performance of their products, which in turn adds increased functionality, performance and efficiency to a wide range of advanced electronic applications including MEMS (Micro Electrical Mechanical Systems) and advanced computers. Using this technology, IQE is uniquely positioned to develop new products which integrate the advantages of advanced semiconductors with the scale of maturity of today's silicon industry.
- The acquisition of UK based NanoGaN Limited brought a new dimension to our advanced materials capability by introducing key intellectual property for producing high quality gallium nitride (GaN) substrates. This material is critical for a number of emerging high volume applications including solid state lighting and advanced laser applications.

Markets

IQE's product roadmap and strategy continues to be driven by three key market dynamics, all of which have fast growth, high volume prospects.

High-speed wireless communications

Approximately 80% of the group's sales in 2009 were into the wireless market. This is a global market spanning a broad range of applications from mobile phones, mobile laptops, mobile netbooks, wifi enabled devices, GPS devices, mobile infrastructure, and direct broadcast satellite TV. These are high growth markets, which are expected to continue to grow rapidly for the foreseeable future, driven by 3G communications and the unquenchable thirst for mobile internet.

We manufacture advanced semiconductor wafers using a technology called epitaxy. Our semiconductor wafers are used by wireless chip makers to manufacture a variety of radio frequency (RF) chips which are used to detect, amplify and switch RF signals in all forms of wireless and satellite communication. These devices are known as pHEMTs (pseudomorphic High Electron Mobility Transistors), HBTs (Heterojunction Bipolar Transistors) and advanced integrated components combining both pHEMTs and HBTs called BiFETs or BiHEMTs.

The growth in demand for our semiconductor wafers has been fuelled by rapid growth in the number of wireless devices across the globe. This growth has been compounded by the need for an increased number of chips per device as these devices become more sophisticated. These growth drivers are well understood and highly visible, for example:

- Over 1.1 billion mobile handsets were shipped globally in 2009. The long-term growth trend in global handset shipments is expected to remain strong for the foreseeable future driven primarily by growth in the BRIC economies.

- The smartphone segment of this global market has grown rapidly in recent years but still represents less than 15% of the overall market. This segment continued to grow throughout the economic recession of 2008 and 2009, and is expected to grow at an accelerated rate as market penetration of these devices increases over the coming years driven by increases in mobile services such as more apps, social networking and location based services
- There is approximately four to five times more advanced semiconductor material in a 3G smartphone compared with a standard 2G phone

It is estimated that over 60% of wireless chip makers outsource their epitaxy needs. Outsourcing has grown over recent years, as the epitaxial foundries like IQE have consolidated and gained critical mass. It is widely expected that the outsource market will continue to grow as the industry continues to mature, and the chip foundries constrain their capital expenditure.

These are high-growth markets that are expected to grow rapidly for the foreseeable future, driven by 3G communications and increasing demand for mobile internet.

IQE is the largest epitaxial foundry, giving critical mass in an industry where economies of scale enable a wide range of advantages including cost and technology leadership. Industry analysts estimate that IQE's share of the outsource market is approximately 30%. IQE's nearest competitors are estimated to command approximately 15% of the market.

IQE's strategy has been to supply all of the major wireless chip manufacturers in order to mitigate the risk that we lose volume as a result of swings in market share between chip manufacturers. In recent years we have progressively achieved new product qualifications and extended our customer base. This strategy has been successful in more closely aligning demand for our products with demand in the end market for wireless devices. IQE achieved a milestone in 2009 by qualifying with the last remaining chip maker that was previously not a customer. IQE now supplies all of the major chip makers.

Security of wafer supply is critical to the commercial success of our customers. Part of IQE's competitive advantage is that it is the only epitaxial foundry able to provide a full range of advanced semi-conductor materials, and that these can be provided from multiple manufacturing sites. This unique service offering allows our customers to reduce their costs whilst maintaining a secure supply. Furthermore, IQE has the largest available on-line capacity, which makes it unique in its ability to meet rapid surges in customer demand. It is these unique features combined with IQE's technology leadership which are enabling IQE to continue to increase its market share.

There remain excellent growth prospects for IQE in this global market. The overall market is growing, the outsource segment of the market is increasing, and IQE is seeking to increase its market share by leveraging its broad customer base and its unique competitive advantages. These are its technology leadership, cost leadership and the security of supply provided by its multi-site capability and its large installed capacity.

Optoelectronics

This market accounts for approximately 15% of IQE's sales but is expected to increase very rapidly over the next few years. In broad terms, optoelectronics refers to devices that convert electricity into light (lasers and LEDs) or light into electricity (fibre optic communication receivers and solar power generation). It is a diverse market with a broad range of applications including LEDs, lasers for data storage (CD, DVD, Blu Ray), lasers for office applications (laser printers, laser mouse), medical and industrial lasers, and components for fibre-optic communication systems covering all applications from USB cables to long distance telecommunication networks.

IQE's foundations are rooted in this market, and for more than twenty years we have developed a long standing reputation for technology leadership. We continue to push the boundaries of this technology, and are engaged in a number of cutting edge R&D programmes. This technical expertise uniquely positions IQE to take advantage of the high volume markets that are emerging, including optical communications, consumer optoelectronics, solid state lighting, and solar power generation.

Optical communications

The fibre optic communications market is set to enjoy significant growth over the coming years as the proliferation of video streaming and social networking on the internet continue to consume bandwidth at an exponential rate. Governments and corporations are embarking on major investment programmes to increase the bandwidth of fibre optic networks to meet this increasing demand.

Furthermore, demands for higher data volume is also influencing the way in which interconnections take place within electronic devices such as mobile handsets. Currently, highly complex metal interconnects are utilised to transfer data between components within electronic devices but there is a great deal of international effort going into replacing metal interconnectors with fibre optic channels which will rely upon GaAs based materials for lasers and receivers.

Consumer Optoelectronics

This diverse area is set to grow very rapidly in the coming years as optical devices penetrate large segments of the consumer markets, including the following areas:

- *Active Optical Cables and Plastic Optical Fibre (LightPeak)*
The increase in data transfer rates is also driving investment in optical communication at peripheral level. Active Optical Cables (AOC) look set to replace existing interconnects such as USB and HDMI cables, as these traditional cables struggle to meet the increasing demands for data transfer. The current market for USB cables alone is estimated at 3 billion per annum. Intel is leading the way in this area with its recently announced 'Light Peak' project.
- *Optical Storage (Blu Ray, DVD)*
As data storage requirements grow, high density storage media are required, including Blu Ray Disc which used shorter wavelength blue lasers to store large amounts of data. IQE's technology includes red lasers for DVD, and through NanoGaN are developing blue laser technology for both Blu Ray and blue/green lasers for projection systems.
- *Office equipment and Sensing*
This market includes various optical devices for office equipment such as laser printers, high resolution photocopy machines and laser mouse for computer navigation. IQE supplies many of the materials used for such applications.
- *Laser projection*
IQE acquired UK based NanoGaN in October 2009. NanoGaN brings exciting new intellectual property to IQE, including its proprietary nanocolumn technology for producing high quality Gallium Nitride advanced semiconductor materials (GaN). This material is critical for the emerging high growth laser projection (red, green and blue lasers) and solid state lighting (SSL) markets.
Laser projection systems have performance, efficiency and size advantages over conventional projection systems. In particular, this technology will offer high quality miniature projectors that have been termed 'pico projectors', which will extend this application for incorporation into mobile phones and into digital cameras to support mobile video streaming and image projection. Industry analysts predict rapid growth for laser projection, given the scale and growth in mobile devices.

Solid state lighting (SSL)

Global concerns about climate change and the Earth's dwindling natural resources continues to be a priority for governments worldwide. Significant new policies and legislation continue to be introduced in the direction of renewable and highly efficient energy devices.

Already, many continents have introduced wide-ranging legislation to ban incandescent lighting with the sale of incandescent lighting greater than 80W and all frosted light bulbs having been banned from September 2009. Alternative low energy lighting is unpopular because of perceptions of low quality lighting and ongoing issues with heavy metal content including mercury.

Solid state lighting is widely viewed as the only credible long solution to replace the incandescent light bulb. Efficient

energy consumption will remain a key driver in the development and adoption of this technology, but the critical success factor is reducing cost and improving the ambience of these units. High quality gallium nitride provides the route map to achieving this, which will revolutionise residential and commercial lighting around the planet over the coming years.

Solar power generation

The drive to develop clean renewable energy sources is widely understood, driven by environmental concerns and the quest for energy security. Solar power generation is an energy solution which promises to play an increasingly important role in energy diversity over the coming years. Of course, economic reality is that the scale of adoption will ultimately depend upon cost. This is where advanced semiconductors have a distinct advantage.

The efficiency at which solar cells convert sunlight into electricity is a key determinant in their size and cost. Solar cells which use advanced semiconductors (called CPV or Concentrator PhotoVoltaics) provide the most efficient solution by using multiple layers of finely tuned materials to absorb sunlight across a wider range of wavelengths. For example, CPV currently operates at over 40% efficiency, which far exceeds the efficiency of Silicon technology (<15% efficiency), and thin film technology (<10% efficiency). Continued research and development provides the potential for CPV efficiency to reach 50% efficiency and beyond. This is one of the factors which has led industry analysts to predict that CPV will reach cost parity with fossil fuels within the next 2 to 3 years. This will be a key catalyst for large scale adoption, creating a market for epitaxy which could outgrow the current wireless market in only a few years.

Currently, there are a small number of pilot CPV solar farms that are under field trial. Early indications are that these trial sites are achieving all of their milestones, providing utility providers and governments with comfort over the reliability and feasibility of these systems.

IQE is well placed in this industry to exploit the explosive growth that is anticipated as this technology moves from field trial to pilot and mass production. In particular, IQE has developed an extensive network of solar cell and system partners, has developed cutting edge technology which is protected by patent, and has the available capacity to meet the demands of this market.

Electronics

Our electronics business provides advanced epitaxy services on silicon, which account for almost 5% of group sales. Part of this business is engaged in mainstream consumer electronics markets, and accordingly suffered more significantly as a result of the global economic downturn. Recovery in this market sector lagged that of the rest of the business but has seen a pick-up in demand in recent months.

The silicon epitaxy business remains of strategic importance to the group, as the Silicon industry struggles to deal with the physical barriers to improving the performance of Silicon through continued miniaturisation. The key solution to overcoming this barrier is to combine the advanced properties of compound semiconductors with the cost advantages of silicon. IQE has established a powerful position in this technology, working with some of the biggest names in the industry, which is reflected in a number of joint patents awarded in conjunction with Intel for the production of III-V materials on silicon substrates and presented at the International Conference for Electronic Devices and Materials (IEDM) in December 2009.

The Group has also developed a powerful range of engineered wafers based on silicon substrates such as germanium-on-insulator (GeOI), germanium-on-silicon (GeOSi) and silicon-on-sapphire (SOS), which help ensure the continuation of Moore's Law for continuing enhancements to microprocessor performance.

We believe that the intellectual property that we are developing in this field has the potential to revolutionise the semiconductor world, and in doing so create significant long term value to IQE stakeholders.

Research and development

The development of leading edge materials technology is paramount to IQE's success. We have over twenty years of experience, and a culture of innovation, which has enabled us to develop technology and market leadership in the markets in which we operate.

We continue to push the limits of materials technology, constantly improving the quality of existing products whilst developing new and enhanced capabilities. We are engaged in a number of research and development programmes with customers, research institutions and government agencies.

As set out above, our current research and development programmes include developing advanced materials to enable CPV solar cells, solid state lighting, laser projection and advanced microprocessors and memory devices.

Quality & environment

IQE's reputation for quality and excellence in products and service is second to none. A philosophy of total quality is integrated throughout the group's operations and each of the group's manufacturing facilities worldwide is independently accredited to the international standard for Quality Management ISO9001:2008.

IQE is fully committed to creating business growth whilst ensuring that the impact on the environment is minimised and that all activities are conducted safely by appropriately trained and qualified employees. The group works closely with all key stakeholders to ensure that its global facilities, and those activities over which it has influence through its supply chain, operate in a way that is ethical and in accordance with best practice.

Corporate responsibility

The group actively promotes a philosophy of corporate social responsibility across all of its operations and engages in a number of local, national and international initiatives working with a wide range of third party organisations and authorities in areas such as ethical employment policies, educational and community work.

The IQE Board is responsible for developing corporate policies on social, ethical and environmental matters and for reviewing their effectiveness. Each of the group's subsidiaries is responsible for communicating and applying group policies within their businesses taking account of local legislation and potential risks.

As an AIM listed company, IQE is not eligible to participate in the FTSE4Good programme but nevertheless, maintains standards and applies the principles of this index.

We are committed to protecting the environment in which we live and work, and have taken a leading role in the industry by implementing formal environmental policies and management systems. We have received awards from customers and third parties for our commitment to environmental programmes. All of IQE's UK operations and its Singapore facility are independently accredited to the ISO14001:2004 standard for Environmental Management.

The group also actively engages with a number of industry groups, educational bodies and charities to promote science and technology and to help contribute to community causes.

Outlook

IQE is widely recognised as the global market leader in advanced semi conductor materials. The technical, operational and financial successes of recent years provide clear evidence of the group's forward momentum and endorse our strategy, our management, and our execution.

2010 promises to be another exciting year for IQE as it expands its technology leadership and builds market share in new, rapidly growing sectors such as active optical cables, laser projection, LED lighting and CPV solar energy.

The Group's solid financial performance achieved during a particularly difficult year, coupled with an enviable portfolio of products, services and intellectual property underlines the Board's confidence in our ability to increase revenue, profitability and cash generation over the coming years.

I would also like to thank my Board colleagues and all the staff of IQE for their tireless support through this very difficult period. It has only been through their hard work, innovation, skill and determination that IQE has emerged from the recession in a position of strength to deliver a strong set of results for 2009 whilst building a clear leadership position within our industry segment. I am proud to be working with such a talented and dedicated team.

Dr Andrew Nelson OBE

President & Chief Executive Officer

23 March 2010

**Directors' report for the year ended
31 December 2009**

The directors present their annual report and the audited financial statements for the year ended 31 December 2009

Activities

The principal activity of the group during the year was the manufacture of advanced semiconductor materials. The principal activity of the company is that of a holding company for the group.

Business review

A review of the group's trading during the year and its position at the year end is provided in the Chief executive's review. The review includes key performance indicators as detailed in the Five Year Financial Summary.

Dividends

The directors do not recommend the payment of a dividend (2008: £nil).

Directors

The directors in office at 31 December 2009 and their beneficial interests in the company's issued ordinary share capital and share options are set out in the remuneration report.

Substantial interests in shares

As at 23 March 2010, the company had been notified pursuant to the Companies Act of the following substantial interests in the shares of the company as defined by the Listing Rules in addition to those disclosed for the directors:

	Percentage of ordinary share capital
AXA Framlington Investment Management	11.04%
Fidelity Investments	8.55%
Nelson A W Dr	6.17%
M&G Investment Management	4.93%
Barclays Stock Brokers Limited	4.79%
Herald Investment Management Limited	4.49%
Scott M D Dr	4.48%
Blackrock Investment Management	4.33%
Universities Superannuation Scheme	3.88%
Invesco Asset Management	3.15%

Research and development

The group incurred costs in respect of research and development during the year of £2,477,000 (2008: £1,784,000) of which £2,210,000 (2008: £1,520,000) has been capitalised in accordance with IAS 38 ("Intangible assets"). The remaining research and development costs totalling £267,000 (2008: £264,000) have been charged to the income statement.

**Directors' report for the year ended
31 December 2009 (continued)**

Donations

The group made charitable donations during the year of £250 (2008 £1,073). No political donations (2008 £nil) were made during the year.

Payment terms

The group seeks to agree favourable credit terms with its suppliers where possible, and adhere to the agreed terms. The group's average number of days' purchases outstanding in respect of trade creditors at 31 December 2009 was 81 days (2008 72 days).

Employment policies

It is the group's policy 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 intranet, e-mail and notice board announcements. 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 considered 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 financial statements.

Statement of directors' responsibilities

The directors are responsible for preparing the annual report, the directors' remuneration report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the group and parent company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. In preparing these financial statements, the directors have also elected to comply with IFRSs, issued by the International Accounting Standards Board (IASB). The financial statements are required by law to give a true and fair view of the state of affairs of the company and the group 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 that the financial statements comply with IFRSs as adopted by the European Union
- Prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the group will continue in business, in which case there should be supporting assumptions or qualifications as necessary. This statement should cover both the parent company and the group as a whole.

The directors confirm that they have complied with the above requirements in preparing the financial statements.

**Directors' report for the year ended
31 December 2009 (continued)**

The directors are responsible for keeping proper accounting records that 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 and the directors' remuneration report comply with the Companies Act 2006. 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.

The directors are responsible for the maintenance and integrity of the group web site, www.iqep.com. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Provision of information to auditors

So far as the directors are aware, there is no relevant audit information of which the company's auditors are unaware. The directors have taken all the steps that ought to have been taken as directors in order to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of that information.

Auditors

A resolution to reappoint PricewaterhouseCoopers LLP will be proposed at the forthcoming Annual General Meeting.

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



Phillip Rasmussen
Finance Director & Company Secretary
23 March 2010

**Remuneration report for the year ended
31 December 2009**

Introduction

This report has been prepared in accordance with the Directors' Remuneration Report Regulations 2002 which introduced new statutory requirements for the disclosure of directors' remuneration. Although not required to, the directors have decided to provide directors' remuneration disclosures similar to those that would be required of a fully listed company. In particular, the Remuneration Report describes how the Board has applied the principles of good governance relating to directors' remuneration set out in the Combined Code. A resolution to approve the report will be proposed at the forthcoming Annual General Meeting of the company.

The report has been divided into separate sections for unaudited and audited information.

Unaudited information

(a) Remuneration Committee

The Board considers itself ultimately responsible for the framework and cost of executive remuneration, but has delegated responsibility for determining the remuneration levels and conditions of service for executive directors and senior executives to the remuneration committee. The committee's approach is fully consistent with the company's overall philosophy that all employees should be competitively rewarded in order to attract and retain their valued skills in the business, as well as supporting corporate strategy by directly aligning executive management with the company's strategic business goals.

The remuneration committee is comprised exclusively of independent non-executive directors of the company who have no personal financial interest, other than as shareholders, in the matters to be decided. The members of the committee throughout the year were Dr G H H Ainsworth and S J Gibson. The Chairman of the committee is S J Gibson.

The committee complies with Schedule A of the Best Practice Provisions annexed to the Listing Rules of the London Stock Exchange, and is responsible for determining the company's policy on compensation of executive directors and the basis of their service agreements with due regard to the interests of shareholders. It also approves the allocation of share options to employees.

The committee operates under clear written terms of reference and has access to and takes independent professional advice as appropriate. The committee met four times during 2009 to review the performance of the executive directors and other senior executives, and set the scale and structure of their remuneration.

(b) Remuneration policy

In establishing its remuneration policy, the committee has given full consideration to Schedule B of the Best Practices Provisions annexed to the Listing Rules of the Financial Services Authority. The remuneration packages for executive directors and senior executives, as determined by the committee, are intended to attract and retain high quality executives, induce loyalty and motivate them to achieve a high level of corporate performance in line with the best interests of shareholders, while not being excessive. The remuneration of the executive directors consists of annual salary, performance bonus, share options, taxable benefits in kind and pension contributions.

There is an annual review at which the committee approves the basic salary and profit sharing bonus scheme for each executive director. The committee receives input from the Chief Executive regarding recommended packages for executive directors and senior executives.

**Remuneration report for the year ended
31 December 2009 (continued)**

(c) Basic salary

Basic salary is determined by reference to individual responsibilities, performance and external market data. As reported last year, the Executive Directors' remuneration was reset from the 1 January 2008 based on independent benchmarking data and remained unchanged from this base in 2009.

In addition, in light of the adverse economic conditions the Executive and Non-Executive Directors elected to accept a 20% pay cut between January and April, and a 10% pay cut during May and June.

(d) Performance bonus

Bonus payments are linked to the executive directors achieving internal annual plan targets in respect of profitability and other non-financial performance criteria.

Bonuses were awarded in respect of 2009 in accordance with this scheme.

(e) Taxable benefits in kind

The company reimbursed all fuel and maintenance costs in respect of the executive directors' private cars, and these costs are treated as taxable benefits in kind. Other taxable benefits comprise medical health insurance.

(f) Share incentive schemes

The company operates a number of share incentive schemes. The IQE Plc Share Option Scheme, as adopted on 26 May 2000 and amended by shareholders at the company's Annual General Meeting on 17 May 2002, allows the company to grant options over up to 15% of the issued share capital and those options are subject to performance conditions.

During the year, the committee approved the grant of 11,127,340 share options to staff (2008: 5,051,362 share options). No options were awarded to directors (2008: 3,762,500 options). As at 31 December 2009, 52,017,091 share options (2008: 43,773,669 share options) have been granted under the IQE Plc Share Option Scheme with exercise prices ranging from nil cost to 458p/option (2008: nil cost to 458p/option). No share options were exercised by directors during the year. The numbers and prices of share options at 31 December 2009 and 31 December 2008 were as follows:

Option price	2009 No of options	2008 No of options
Share options of nil cost to 10p/option	19,971,661	11,176,277
Share options in excess of 10p/option to 20p/option	30,955,788	31,351,750
Share options in excess of 20p/option to 30p/option	922,500	922,500
Share options in excess of 30p/option	167,142	323,142
Total	52,017,091	43,773,669

The company also operates UK and US All Employee Share Ownership Plans whereby employees agree to contribute fixed amounts per month during a fixed annual period which are used to purchase shares in the company. The UK Plan commenced in November 2001 and the US Plan commenced in August 2002. No contributions were made by employees to the UK Plan after 31 March 2003 and to the US Plan after 31 July 2003.

**Remuneration report for the year ended
31 December 2009 (continued)**

As at 31 December 2009, there were 580,079 shares (2008 580,079 shares) in the UK and Offshore Trusts, comprising 289,421 allocated shares (2008 289,421 allocated shares) and 290,658 unencumbered shares (2008 290,658 unencumbered shares). The company has the ability to make option and share awards from the Offshore Trust

(g) Pension arrangements

The executive directors are members of the group defined contribution pension schemes and their pension contributions are based on a percentage of basic annual salary. 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 2009, and there were no unfunded pension promises or similar arrangements for directors at 31 December 2009.

(h) Executive Directors' service contracts

It is the company's policy to appoint executive directors under service agreements which are terminable by either party giving between six and twelve months' notice. Each of the agreements contains post-termination restrictive covenants, which place limitations on solicitation of customers and employees of the group and on acting in competition with the business of the group. There are no predetermined provisions for compensation on termination within executive directors' service agreements. However, the company is against rewards for failure and believes that severance arrangements should be restricted to basic pay and consequential payments such as earned bonus.

(i) Non-Executive Directors' contracts

The non-executive directors have entered into service agreements with the company, and these are terminable by either party on three months' notice. Non-executive directors have specific terms of engagement, and their fees are determined by the Board within the limits set by the company's Articles of Association. Non-executive directors do not take part in discussions on their own remuneration. There were no changes to non-executive remuneration during 2009 except for the temporary reduction in remuneration as set out above.

During the year, the services of Dr G H H Ainsworth were paid in the form of shares in the company based on the weighted average share price throughout the year. The shares were awarded to Gambit Corporate Finance, a firm in which Dr Ainsworth was the Managing Partner until his retirement on 30 November 2009. A total of 782,099 shares (2008 167,790 shares) were awarded to Gambit Corporate Finance for Dr Ainsworth's services, including 195,498 shares (2008 52,806 shares) in respect of services provided in the previous year. No other amounts were paid to Gambit Corporate Finance in respect of fees and expenses for 2009 (£52,433 not paid in the form of shares). VAT was charged on the invoices from Gambit Corporate Finance and this was recovered by the company. At 31 December 2009 a total of £17,477 (excluding VAT) was outstanding to Gambit or to Dr Ainsworth in respect of his services in the final quarter and which was settled by the further issue of 101,915 shares after the year end.

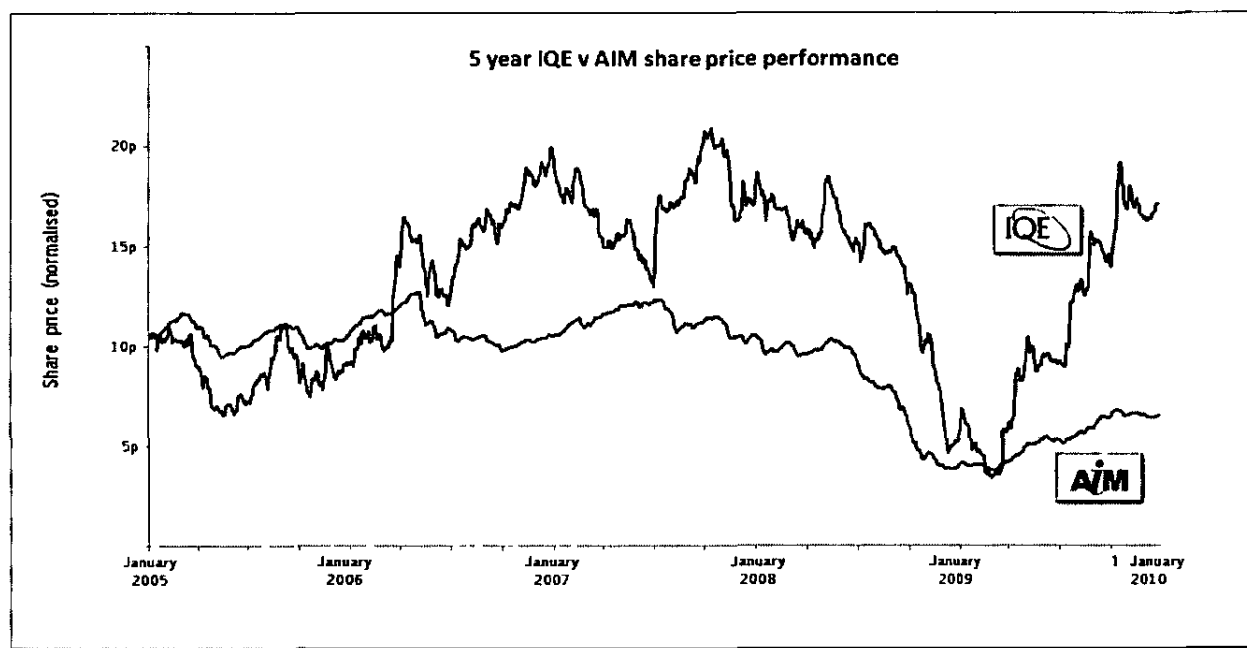
The services of S J Gibson were paid partly in shares in the company based on the weighted average share price throughout the year and partly in cash. A total of 244,289 shares (2008 57,566 shares) were awarded to Fishstone Limited, including 97,875 shares (2008 no shares) awarded in respect of services provided in the previous year. S J Gibson is a shareholder in Fishstone Limited. £18,914 (2008 £26,250), not paid in the form of shares, was paid to Fishstone Limited respectively for his remaining fees and expenses for 2009. VAT was charged on the invoices from Fishstone Limited and this was recovered by the company.

The non-executive directors receive no other pay or benefits, do not participate in the company's share schemes, and are not eligible for pension scheme membership. Neither had any share options in the company at 31 December 2009 and it is not intended that share options will be issued to them in the future in accordance with Best Practice Guidelines issued by the Association of British Insurers.

**Remuneration report for the year ended
31 December 2009 (continued)**

(j) Share price performance

The IQE plc share price has been compared with the AIM market and TechMark all-share indices for the years 2008 and 2009 as this was considered to be the most representative market group



**Remuneration report for the year ended
31 December 2009 (continued)**

Audited information

(a) Aggregate directors' remuneration

The total amounts paid for directors' remuneration during 2009 were as follows

	2009 £'000	2008 £'000
Basic salaries	498	526
Bonuses	356	-
Non-executive fees	93	105
Sub total salaries and fees	947	631
Car allowances	75	75
Benefits in kind	31	19
Money purchase pension contributions	38	61
Total	1,091	786

(b) Directors' emoluments

The aggregate emoluments paid to each director during 2009 were as follows

Name of director	Salary and fees £'000	Bonus £'000	Car allowance £'000	Benefits in kind £'000	Pensions £'000	2009 Total £'000	2008 Total £'000
Executive							
Dr A W Nelson	224	158	33	21	13	449	302
Dr H R Williams	133	99	21	3	17	273	188
P J Rasmussen	141	99	21	7	8	276	191
Non-Executive							
Dr G H H Ainsworth	64	-	-	-	-	64	70
S J Gibson	29	-	-	-	-	29	35
Total	591	356	75	31	38	1,091	786

Notes

Dr G H H Ainsworth and S J Gibson took their remuneration during 2008 and 2009 partly in the form of company shares calculated on a weighted average share price basis and partly in cash

**Remuneration report for the year ended
31 December 2009 (continued)**

(c) Directors' interests in ordinary shares of IQE Plc

The interests in ordinary shares of IQE Plc of those directors holding office at 31 December 2009 were as follows

Name of director	As at	As at
	1 January 2009	31 December 2009
Executive		
Dr A W Nelson	27,391,303	27,391,303
Dr H R Williams	15,000	15,000
P J Rasmussen	-	-
Non-Executive		
Dr G H H Ainsworth	2,813,919	2,960,569
S J Gibson	57,566	301,855
Total	30,277,788	30,668,727

Dr Ainsworth became interested in a further 52,009 shares after the year end which were issued in part settlement of his Q4 fees. The interests in share options in IQE Plc of those directors who held office at 31 December 2009 were as follows

Name of director	As at 1 January 2009	As at 31 December 2009	Dates from which exercisable
Executive			
Dr A W Nelson	10,412,500	10,412,500	1 Jan 2010 to 1 Jan 2011
Dr H R Williams	4,829,040	4,829,040	1 Jan 2010 to 1 Jan 2011
P J Rasmussen	2,550,000	2,550,000	10 Apr 2010 to 1 Jan 2011
Non-Executive			
Dr G H H Ainsworth	-	-	
S J Gibson	-	-	
Total	17,791,540	17,791,540	

The directors do not hold shares or share options in any group company other than IQE plc

The highest and lowest mid-market share prices in respect of the shares of IQE Plc during 2009 were 19 60p/share and 3 25p/share respectively (2008 18 75p/share and 4 50p/share respectively). The mid-market price of IQE plc shares closed at 17 00p/share as at 31 December 2009 (2008 5 25p/share)

Approval

This report was approved by the Board of Directors on 23 March 2010 and signed on its behalf by



S J Gibson, OBE
Remuneration Committee Chairman

Corporate governance report for the year ended 31 December 2009

Although not required to, the directors have decided to provide corporate governance disclosures similar to those that would be required of a fully listed company

The Board recognises that it is accountable to the group's shareholders for the standard of governance and therefore seeks to maintain high standards in its management of the affairs of the group, seeing it as a fundamental part of discharging its stewardship responsibilities. Accordingly, both the Board and the audit committee continue to keep under review the group's whole system of internal control, which comprises not only financial controls but also operational controls, compliance and risk management

Throughout the year ended 31 December 2009, the company has been in compliance with the Code provisions set out in Section 1 of the June 2008 FRC Combined Code on Corporate Governance

The Board of Directors

The management of the group is directed by the Board of directors, which is responsible for ensuring the development and implementation of the group's overall strategy. The Board of directors comprises the non-executive Chairman Dr G H H Ainsworth, the Chief Executive Dr A W Nelson, two executive directors and one non-executive director. There is a clear division of responsibility between the non-executive Chairman, who is responsible for the running of the Board, and the Chief Executive, who is responsible for the running of the group in accordance with the authority delegated by the Board. This ensures that there is a balance of power and authority such that no one individual has unfettered powers of decision.

The fees of the non-executive directors are paid in cash or in the form of shares in the company based on an agreed weighted average share price formula. The Board considers that the non-executive directors are independent of management and free from any business or other relationship which could materially interfere with the exercise of their independent judgement. The terms and conditions of appointment of the non-executive directors are available for inspection upon request to the Company Secretary.

The non-executive Chairman is recognised as the senior independent non-executive director to whom concerns by staff of any suspected impropriety can be conveyed in private and investigated as required by the Code of Best Practice.

Biographical details of the executive and non-executive directors, including their qualifications, are set out on page 4. Under the Company's Articles of Association each of the directors is required ordinarily to retire by rotation once every three years.

The Board held regular meetings during the year. The Board has a formal schedule of matters referred to it for decision, which includes the approval of interim and annual results, the annual budget, acquisitions and disposals, major items of capital expenditure, share capital issues, governance issues and executive appointments. The Board is provided with appropriate strategic and financial information prior to each meeting together with monthly reports to enable it to monitor the performance of the group. The Chief Executive reviews the performance of the executive directors on an annual basis.

All directors have direct access to the advice and services of the Company Secretary who is responsible for ensuring that Board procedures are followed, and are allowed to take independent professional advice if necessary at the company's expense.

**Corporate governance report for the year ended
31 December 2009 (continued)**

Board committees

The Board has delegated specific responsibilities to the following committees

(a) Executive Committee

The executive committee consists of the executive directors under the chairmanship of Dr AW Nelson and is responsible for the development of strategy, annual budgets and operating plans linked to the management and control of the day-to-day operations of the group. The executive committee is also responsible for monitoring key research and development programmes and for ensuring that the Board policies are carried out on a group-wide basis.

(b) Audit Committee

The audit committee consists of the non-executive directors, Dr G H H Ainsworth and S J Gibson, and meets at least twice a year under the chairmanship of Dr G H H Ainsworth.

The audit committee has specific written terms of reference which deal with its authority and responsibilities and these are available for inspection upon request to the Company Secretary. Its duties include monitoring internal controls throughout the group, approving the group's accounting policies, and reviewing the group's interim and financial statements before submission to the full Board. The audit committee also reviews and approves the scope and content of the group's annual risk assessment programme and the annual audit, and monitors the independence of the external auditors.

During the year the Group introduced an Internal Audit function, with a scope of evaluating and testing the group's financial control procedures. The Internal Audit function reports directly to the chairman of the audit committee, and liaises with the external auditors as appropriate.

The Finance Director, other financial management and the external auditors attend meetings of the audit committee by invitation. The committee also holds separate meetings with the external auditors, as appropriate.

(c) Remuneration and Nominations Committees

The remuneration committee consists of the non-executive directors, Dr G H H Ainsworth and S J Gibson and meets at least twice a year under the chairmanship of S J Gibson. The Chief Executive attends meetings of the remuneration committee by invitation to respond to questions raised by the committee, but he is excluded from any matter concerning the details of his own remuneration.

The remuneration committee has specific terms of reference which deal with its authority and duties and these are available for inspection upon request to the Company Secretary. The remuneration committee is responsible for setting salaries, incentives and other benefit arrangements of executive directors and senior executives and overseeing the group's employee share schemes. The group's policy on directors' remuneration has been in line with the Code provisions throughout the year, full details of which are given in the remuneration report and in note 6 to the financial statements. Members of the remuneration committee do not participate in decisions concerning their own remuneration.

The Board has not established a separate nominations committee and has delegated responsibility for nominations to the remuneration committee. There are currently no plans for further appointments to the Board.

**Corporate governance report for the year ended
31 December 2009 (continued)**

Attendance at meetings

The number of meetings held during 2009 by the Board, the audit committee and the remuneration committee are as shown below. The number of meetings attended by the executive and non-executive directors is also shown below.

	Board	Audit Committee	Remuneration Committee
Number of meetings held in 2009	9	4	4
Number of meetings attended in 2009			
Executive			
Dr A W Nelson	9	1	4
P J Rasmussen	9	4	-
Dr H R Williams	8	-	-
Non-executive			
Dr G H H Arnsworth	9	4	4
S J Gibson	7	3	4

Principal risks and uncertainties

The Board considers that the principal risks and uncertainties facing the group are

Competition

IQE's business model involves building close working relationships with its customers and often involves forming multilevel partnerships from the product design stages through pilot production to volume production. Such arrangements can lead to long qualification timescales but once a product range and relationship is established, it can also create significant barriers to entry for competitors.

In some cases, customers seek second source supply arrangements to meet their own business continuity planning policies. As such, there is a risk that market share may be eroded. IQE's strategy to provide multiple site capabilities for all leading product lines provides an effective mitigation against this risk.

Technological change

Any technology based company faces a threat from technology change that has not been anticipated. IQE actively engages with customers, educational institutions and government agencies on a range of research and development programmes. The company's involvement in R&D activities coupled with its broad range of products and process technologies helps ensure a forward looking approach that positions IQE as a driver of technological change.

Supply chain

Changes in the supply chain such as scarcity of key raw materials could impact the business. IQE builds close relationships with its key suppliers in order to keep well informed about potential supply issues. The raw materials which sustain IQE's products are not scarce resources.

Retention of key employees

The Board recognises that the retention and development of its workforce is critical to its long term success as a leading technology group. Therefore, to promote the development and retention of its staff IQE offers career progression, personal development and a range of benefits and incentives to its staff. This is reflected in low staff turnover, with many employees who have been with the company since it was formed over twenty years ago.

IQE's people are the heart of the business and a whole range of benefits and incentives are offered to help ensure key employees stay with the business. The group was founded over 20 years ago, and a significant proportion of senior management have been with the company since it was formed.

In addition, IQE operates a highly effective, robust, and fully documented quality management system across all of its operations. These systems ensure that all key data and procedures are fully documented, reflecting IQE's "learning organisation" philosophy. These rigorous systems provide IQE and its customers with a high level of confidence in terms of process reproducibility and product traceability, and minimise the potential impact of losing key personnel.

**Corporate governance report for the year ended
31 December 2009 (continued)**

Treasury

IQE operates a central treasury which acts in accordance with specific board policies. Speculative transactions are not permitted.

Interest rate risk

The Board is 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 or currencies.

The group's policy is to regularly review its exposure to interest rate risk, and in particular the mix between fixed and floating rate facilities. The percentage of borrowings on fixed rate terms at 31 December 2009 was 23% (2008: 47%). Floating rate liabilities are primarily indexed to LIBOR, and to a lesser extent SIBOR (being the Singaporean Inter-Bank Offer Rate).

The group did not enter into any interest rate swap instruments during 2009. This remains under regular review.

As a guide to the sensitivity of the group's results to movements in interest rates, a 100 basis point (1%) movement in interest rates would have impacted the 2009 annual interest charge by approximately £90,000.

Credit risk

The majority of the group's revenues are derived from large multinational organisations. Therefore the credit risk is considered to be small.

Where the group does perceive a credit risk, this is dealt with either by up-front payment prior to the shipment of goods or by other credit risk mitigation measures. As a result the group has historically had and continues to have a very low level of payment default.

Currency risk

(a) Cash flow risk

The group's presentational currency is sterling. However, the vast majority of sales are denominated in US dollars. Therefore, the group's cash flows are affected by fluctuations in the rate of exchange between Sterling and the US dollar.

This exposure is managed by a natural currency hedge because a significant portion of the group's cost base is also denominated in US dollars. In particular, the vast majority of the group's raw materials are purchased in US dollars (representing c 50% of the value of sales), and a significant portion of labour and overheads are also denominated in US dollars as two of the group's principal subsidiaries are situated in North America.

To a much lesser extent, the group also generates sales in other currencies including Yen and Euros which are also partially hedged where possible by purchases of some raw materials in these currencies.

The management team monitor foreign currency rates as part of its ongoing evaluation of the cost versus benefit of using forward contracts to manage any residual foreign currency exposure. As a result, during 2009 the group entered into forward currency contracts to exchange US dollars and Japanese yen into sterling. There were no such contracts outstanding at 31 December 2009.

(b) Fair value risk

The group has operations in the UK, North America and Asia. Translation exposures that arise on converting the results of overseas subsidiaries are not hedged. Net assets held in foreign currencies are hedged wherever practical by matching borrowings in the same currency.

As a guide to the sensitivity of the group's results to movements in foreign currency exchange rates, a one cent movement in the US dollar to Sterling rate would impact annual earnings by approximately £100,000.

**Corporate governance report for the year ended
31 December 2009 (continued)**

Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and cash equivalents and the availability of funding through committed credit facilities

Management utilises detailed rolling cashflow forecasts as part of its cash management. This includes weekly forecasts for the next quarter and monthly forecasts for the next 12 months

Capital risk

The group's main objectives when managing capital are to safeguard the group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital

Consistent with others in the industry, the group monitors capital on the basis of the gearing ratio. This ratio is calculated as 'net debt' (see note 25) divided by 'total capital' (calculated as equity in the consolidated balance sheet plus net debt)

The gearing ratio at 31 December 2009 was 33% (2008: 38%) based on net debt of £14.9m (2008: £18.1m), and shareholder equity of £29.8m (2008: £30.2m)

Internal control

The Board acknowledges its responsibility for the group's system of internal control, the effectiveness of which has been reviewed by the audit committee during the year and reported on to the Board. The review has taken account of any material developments up to the date of the signing of the financial statements

The processes to identify and manage key risks to the success of the group are an integral part of the internal control environment. Such processes are ongoing, are regularly reviewed and improved as necessary, and are in accordance with the internal control guidelines for directors in the Combined Code for Corporate Governance. They include strategic planning, the appointment of senior executives, the monitoring on a regular basis of performance, control of capital expenditure and significant revenue investment, and the setting of high standards for health, safety and environmental performance. These processes have been in place throughout the financial year and up to the date of approval of the financial statements

The effectiveness of the control systems and procedures is monitored regularly through management self-assessment. In addition, recognition is given to the external audit findings, which inform the audit committee's views of areas of increased risk

The system of internal control comprises those controls established in order to provide assurance that the assets of the group are safeguarded against unauthorised use or disposal and to ensure the maintenance of proper accounting records and the reliability of financial information used within the business or for publication. Any system of internal control can only provide reasonable, but not absolute, assurance against material misstatement or loss, as it is designed to manage rather than to eliminate the risk of failing to achieve the business objectives of the group

**Corporate governance report for the year ended
31 December 2009 (continued)**

The key procedures that the directors have established with a view to providing effective internal control are as follows

- a clearly defined organisational structure and limits of authority,
- corporate policies and procedures for financial reporting and control, project appraisal, human resources, quality control, health and safety, information security and corporate governance,
- the preparation of annual budgets and regular forecasts which require approval from both the group executive committee and the Board,
- the monitoring of performance against budget and forecasts and the reporting of any variances in a timely manner to the Board,
- regular review and self-assessment of the risks to which the group is exposed, taking steps to monitor and mitigate these wherever possible including, where appropriate, taking out insurance cover, and
- approval by the audit committee of audit plans and, on behalf of the Board, receipt of reports on the group's accounting and financial reporting practices and its internal controls together with reports from the external auditors as part of their normal audit work
- an internal audit function, which is mandated to evaluate and test the Group's financial control procedures, reporting directly to the chairman of the audit committee

Shareholder relations

The Chief Executive and the Finance Director meet on a regular basis with representatives of institutional shareholders to discuss their views and to ensure that the strategies and objectives of the group are well understood. The Chief Executive keeps the Board fully informed of the views of institutional shareholders. Issues discussed with institutional shareholders include the group's performance and the impact of any major transactions. The Chairman has met with individual shareholders on an ad hoc basis.

The company also has a manager responsible for investor relations and operates a web site, which provides details of the group's facilities and products and includes a separate investor relations section on which financial data and other significant announcements are published. The web site can be found at www.iqep.com. All shareholders receive a copy of the group's annual report and financial statements and an interim report is issued at the half year.

The Annual General Meeting allows shareholders to raise questions with the Board, although shareholder enquiries and questions are also addressed throughout the year. In accordance with the recommendation of the Hampel Code, the company will advise shareholders attending the Annual General Meeting of the number of proxy votes lodged for each resolution in the categories 'For' and 'Against', together with the numbers 'at the Chairman's discretion' and abstentions. These will be advised after the resolutions have been dealt with on a show of hands.

**Corporate governance report for the year ended
31 December 2009 (continued)**

Audit and related services

The nature of the services provided by the auditors and the amounts paid to them are as detailed below

	Total 2009 £'000	Total 2008 £'000
PricewaterhouseCoopers LLP (group auditors)		
- Company audit and consolidated financial statements	22	25
- Subsidiary companies' audit	65	73
- Tax services	14	18
- Other services	-	8
Ernst and Young (auditors of MBE Technology Pte Limited)		
- Subsidiary companies' audit (2009 SG\$30,000, 2008 SG\$35,000)	14	13
- Tax services	12	-
Total	127	137

The Board is aware of the importance of maintaining the independence of the group auditors, and does not contract for additional services from them which would compromise their audit independence. Additional services are also subject to appropriate market testing.

The Audit Committee keeps under review the nature and extent of audit and non-audit services provided to the group by the auditors in accordance with a policy which it established in 2004. Under this policy, the award to the group's auditors of audit-related services, tax consulting services or other non-audit related services in excess of £10,000 must first be approved by the Chairman of the Audit Committee. In addition, the group's auditors will be required to make a formal report to the Audit Committee annually on the safeguards that are in place to maintain their independence and the internal safeguards in place to ensure their objectivity.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF IQE plc

We have audited the group and parent company financial statements (the "financial statements") of IQE plc for the year ended 31 December 2009 which comprise the Consolidated Income Statement, Consolidated Statement of Comprehensive Income, Consolidated and Parent Company Balance Sheets, Consolidated and Parent Company Cash Flow Statements and the Consolidated Statement of Changes in Equity and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on pages 16 and 17, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements.

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2009 and of the group's profit and group's and parent company's cash flows for the year then ended,
- the group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union,
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006, and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion, the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following

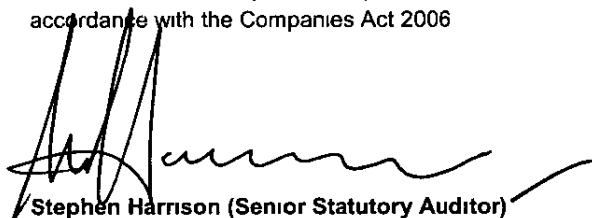
Under the Companies Act 2006 we are required to report to you if, in our opinion

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us, or
- the parent company financial statements are not in agreement with the accounting records and returns, or
- certain disclosures of directors' remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit

Other matters

The directors have requested, (because the company applies Listing Rules 9.8.6R 5 and 6 of the Financial Services Authority as if it were a listed company), that we review the parts of the Corporate Governance Statement relating to the company's compliance with the nine provisions of the June 2008 Combined Code specified for our review by the Listing Rules of the Financial Services Authority. We have nothing to report in respect of this review.

At the request of the directors, we have also audited the Directors' Remuneration Report that is described as having been audited. In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.



Stephen Harrison (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Cardiff

23 March 2010

**Consolidated income statement
for the year ended 31 December 2009**

	Note	2009 £'000	2008 £'000
Revenue	3	52,652	60,485
Cost of sales		(41,073)	(51,898)
Gross profit		11,579	8,587
Gross profit before exceptional items		11,579	11,755
Exceptional items	5	-	(3,168)
Selling, general and administrative expenses		(8,535)	(8,518)
Operating profit		3,044	69
Operating profit before exceptional items		3,044	4,000
Exceptional items	5	-	(3,931)
Finance costs	7	(986)	(1,454)
Profit/(loss) for the period attributable to equity shareholders		2,058	(1,385)
Pre-exceptional earnings per share	10	0 47p	0 59p
Basic earnings per share	10	0 47p	(0 32p)
Diluted earnings per share	10	0 44p	(0 32p)

The notes on pages 39 to 65 form part of these financial statements

Consolidated statement of comprehensive income

		2009 £'000	2008 £'000
Profit/(loss) for the period		2,058	(1,385)
Currency translation differences on foreign currency net investments		(3,859)	7,723
Revaluation gain of initial investment on acquisition	18	28	-
Total comprehensive (expense)/income for the period		(1,773)	6,338

All of the above results relate to continuing activities

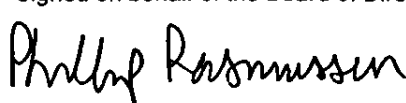
**Consolidated balance sheet
as at 31 December 2009**

	Note	2009 £'000	2008 £'000
Non-current assets			
Intangible assets	11	19,182	14,675
Property, plant and equipment	12	21,365	25,626
Total non-current assets		40,547	40,301
Current assets			
Inventories	14	10,789	11,262
Trade and other receivables	15	13,261	11,671
Cash and cash equivalents		4,233	-
Total current assets		28,283	22,933
Total assets		68,830	63,234
Current liabilities			
Borrowings	17	(6,573)	(8,090)
Trade and other payables	16	(16,770)	(14,798)
Total current liabilities		(23,343)	(22,888)
Non-current liabilities			
Borrowings	17	(12,591)	(10,045)
Deferred consideration	18	(3,014)	-
Deferred income		(45)	(83)
Total non-current liabilities		(15,650)	(10,128)
Total liabilities		(38,993)	(33,016)
Net assets		29,837	30,218
Shareholders' equity			
Ordinary shares	19	4,435	4,333
Share premium		1,150	124
Profit and loss account		20,513	18,455
Other reserves		3,739	7,306
Total shareholders' equity		29,837	30,218

The notes on pages 39 to 65 form part of these financial statements

These financial statements were approved by the Board of Directors on 23 March 2010

Signed on behalf of the Board of Directors



P J Rasmussen



Dr A W Nelson

**Consolidated statement of changes in equity
for the year ended 31 December 2009**

	Share capital	Share premium	Retained earnings	Exchange rate reserve	Other reserves	Total equity
	£'000	£'000	£'000	£'000	£'000	£'000
Balance at 1 January 2009	4,333	124	18,455	5,604	1,702	30,218
Comprehensive income						
Profit for the period	-	-	2,058	-	-	2,058
Foreign exchange translation differences	-	-	-	(3,859)	-	(3,859)
Revaluation gain on business combination	-	-	-	-	28	28
Total comprehensive income	-	-	2,058	(3,859)	28	(1,773)
Transactions with owners						
Employee share option scheme	-	-	-	-	264	264
Shares issued for business combination	58	709	-	-	-	767
Other issues of ordinary shares	44	317	-	-	-	361
Total transactions with owners	102	1,026	-	-	264	1,392
Balance at 31 December 2009	4,435	1,150	20,513	1,745	1,994	29,837
Balance at 1 January 2008	4,310	172,183	(152,441)	(2,119)	1,027	22,960
Comprehensive income						
Loss for the period	-	-	(1,385)	-	-	(1,385)
Foreign exchange translation differences	-	-	-	7,723	-	7,723
Total comprehensive income	-	-	(1,385)	7,723	-	6,338
Transactions with owners						
Employee share option scheme	-	-	-	-	747	747
Issues of ordinary shares	23	222	-	-	(72)	173
Capital reduction	-	(172,281)	172,281	-	-	-
Total transactions with owners	23	(172,059)	172,281	-	675	920
Balance at 31 December 2008	4,333	124	18,455	5,604	1,702	30,218

The notes on pages 39 to 65 form part of these financial statements

**Consolidated cash flow statement
for the year ended 31 December 2009**

	Note	2009 £'000	2008 £'000
Cash flows from operating activities			
Cash inflow from operations	23	7,712	7,461
Cash inflow from operations before exceptional items		8,139	8,526
Exceptional items	5	(427)	(1,065)
Net interest paid		(1,099)	(1,505)
Net cash inflow from operating activities		6,613	5,956
Cash flows from investing activities			
Acquisition of NanoGaN Limited	18	(205)	-
Development expenditure		(2,325)	(1,520)
Investment in other intangible fixed assets		(248)	(134)
Purchase of property, plant and equipment		(1,660)	(6,361)
Proceeds from sale of property, plant and equipment		-	179
Net cash used in investing activities		(4,438)	(7,836)
Cash flows from financing activities			
Issues of ordinary share capital		596	208
Loans and leases received		2,778	1,755
Net cash generated from financing activities		3,374	1,963
Net increase/(decrease) in cash and bank overdrafts		5,549	83
Cash/(bank overdrafts) at 1 January	25	(928)	(1,011)
Exchange losses on cash and bank overdrafts		(388)	-
Cash/(bank overdrafts) at 31 December	25	4,233	(928)

The notes on pages 39 to 65 form part of these financial statements

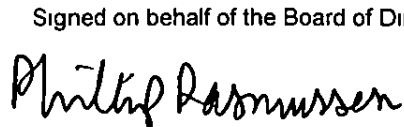
Parent company balance sheet
for the year ended 31 December 2009

	Note	2009 £'000	2008 £'000
Non-current assets			
Intangible assets	11	-	100
Investments in subsidiaries	13	14,717	10,915
Total non-current assets		14,717	11,015
Current assets			
Trade and other receivables	15	25,542	29,499
Cash and cash equivalents		3,196	-
Total current assets		28,738	29,499
Total assets		43,455	40,514
Current liabilities			
Borrowings	17	(2,914)	(9,948)
Trade and other payables	16	(1,053)	(737)
Total current liabilities		(3,967)	(10,685)
Non-current liabilities			
Deferred consideration	18	(3,014)	-
Borrowings	17	(9,834)	(5,609)
Total non-current liabilities		(12,848)	(5,609)
Total liabilities		(16,815)	(16,294)
Net assets		26,640	24,220
Shareholders' equity			
Ordinary shares	19,22	4,435	4,333
Share premium	22	1,150	124
Profit and loss account	22	18,484	17,456
Other reserves	22	2,571	2,307
Total shareholders' equity		26,640	24,220

The notes on pages 39 to 65 form part of these financial statements

These financial statements were approved by the Board of Directors on 23 March 2010

Signed on behalf of the Board of Directors



P J Rasmussen



Dr A W Nelson

Parent company cash flow statement
for the year ended 31 December 2009

	Note	2009 £'000	2008 £'000
Cash flows from operating activities			
Cash inflow/(outflow) from operations	23	6,028	(5,575)
Interest paid		(501)	(1,214)
Net cash outflow from operating activities		5,527	(6,789)
Cash flows from investing activities			
Purchase of investments		(221)	(100)
Net cash used in investing activities		(221)	(100)
Cash flows from financing activities			
Issues of ordinary share capital		596	208
Loans and leases received		(2,706)	6,670
Net cash generated from financing activities		(2,110)	6,878
Net increase/(decrease) in cash and cash equivalents		3,196	(11)
Cash and cash equivalents at 1 January		-	11
Cash and cash equivalents at 31 December		3,196	-

The notes on pages 39 to 65 form part of these financial statements

Notes to the financial statements
year ended 31 December 2009

1 Significant accounting policies

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to all years presented unless otherwise stated.

Basis of preparation

This financial information has been prepared on a going concern basis under the historical cost convention and in accordance with the Companies Act 2006, International Financial Reporting Standards ("IFRS") as adopted by the European Union and IFRIC interpretations expected to be in issue at 31 December 2009. The application of these standards and interpretations necessitates the use of estimates and judgements. The main areas involving estimates are set out below in note 2.

The following new International Accounting standards and amendments have been applied to and impacted the financial information presented:

- IFRS 8 'Operating segments', (effective from 1 January 2009), replacing IAS 14 'Segment reporting'. The historical operating segments reported are in line with those segments used for internal reporting, hence the adoption of this standard has not led to any change in the operating segments reported. The adoption of this standard has changed the required disclosures of geographical information by the group, which are set out in note 3 with full comparative information.
- IAS 1 (revised) 'Presentation of financial statements' (effective from 1 January 2009). The adoption of this standard has led to minor presentational changes to the 'statement of comprehensive income' (formerly the 'statement of recognised income and expense') and the 'statement of changes in equity'.
- IAS 23 (amendment) 'Borrowing costs'. The standard requires the capitalisation of borrowing costs incurred during the construction or development of qualifying tangible and intangible assets using the effective interest method. The standard has been adopted as at 1 January 2009 and therefore applies prospectively to all qualifying assets where construction or development commenced after this date. The impact of adoption of this standard on the 2009 financial statements is not material.

The following new International Accounting standards and amendments have been adopted but have no impact on the financial information presented and have therefore not been analysed in detail:

- IFRS 1 (amendment) 'First time adoption of IFRS' (effective from 1 January 2009)
- IFRS 2 (amendment) 'Share-based payment' (effective from 1 January 2009)
- IAS 19 (amendment) 'Employee benefits' (effective from 1 January 2009)
- IAS 28 (amendment) 'Investments in associates' (effective from 1 January 2009)
- IAS 32 (amendment) 'Financial instruments: Presentation' (effective from 1 January 2009)
- IAS 36 (amendment) 'Impairment of assets' (effective from 1 January 2009)
- IAS 38 (amendment) 'Intangible assets' (effective from 1 January 2009)
- IAS 39 (amendment) 'Financial instruments: Recognition and measurement' (effective from 1 January 2009)

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiary undertakings. Subsidiaries are all entities over which the Group has the power to govern their financial and operating policies.

Subsidiaries are consolidated from the date on which control is transferred to the Group and are de-consolidated from the date that control ceases. As permitted by Section 408 of the Companies Act 2006, the income statement of the parent company has not been presented.

Notes to the financial statements
year ended 31 December 2009 (continued)

Business combinations

The acquisition of subsidiaries is accounted for using the purchase method. The cost of an acquisition is measured at the fair value of the consideration plus costs directly attributable to the acquisition. The acquired identifiable assets, liabilities and contingent liabilities are recognised at their fair value at the date of acquisition.

Goodwill

Goodwill arising on an acquisition is recognised as an asset and initially measured at cost, being the excess of the fair value of the consideration and directly attributable costs over the fair value of the identifiable assets, liabilities and contingent liabilities.

Goodwill is not amortised. However, it is reviewed annually for any indication of potential impairment. Any impairment identified is immediately charged to the Consolidated Income Statement. Subsequent reversals of impairment losses for goodwill are not recognised.

Research and development

Expenditure incurred on the development of new or substantially improved products or processes is capitalised, provided that the related project satisfies the criteria for capitalisation, including the project's technical feasibility and likely commercial benefit. All other research and development costs are expensed as incurred.

Capitalised development costs are amortised on a straight line basis over the period during which the economic benefits are expected to be received, which typically range between 2 and 10 years. The estimated remaining useful lives of development costs are reviewed at least on an annual basis.

The carrying value of capitalised development costs is reviewed for potential impairment at least annually. Any impairment identified is immediately charged to the Consolidated Income Statement.

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and any provision for impairment. Cost comprises all costs that are directly attributable to bringing the asset into working condition for its intended use. Depreciation is calculated to write down the cost of fixed assets to their residual values on a straight-line basis over the following estimated useful economic lives:

Freehold buildings	25 years
Leasehold improvements	5 to 27 years
Plant and machinery	5 to 15 years
Fixtures and fittings	4 to 5 years

During the year the estimates of useful economic lives of certain items of plant and machinery were increased to reflect revised expectations of their productive lifetimes. These changes had the impact of reducing the depreciation charge for the current period by £585,000.

No depreciation is provided on land or assets yet to be brought into use.

Impairment of non-current assets

Non-current assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value (less disposal costs) and value in use.

Notes to the financial statements
year ended 31 December 2009 (continued)

Value in use is based on the present value of the future cash flows relating to the asset. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (Cash Generating Units).

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials and, where applicable, direct labour costs and attributable overheads that have been incurred in bringing the inventories to their present location and condition.

Financial instruments

Financial assets and liabilities are recognised on the group's balance sheet when the group becomes a party to the contractual provisions of the financial instrument.

The only financial assets held by the group are receivables and cash and cash equivalents. Receivables do not carry interest and are stated at their nominal value as reduced by appropriate allowances for estimated irrecoverable amounts. Cash and cash equivalent include cash in hand, short term highly liquid investments with original maturity of less than three months and bank overdrafts. Bank overdrafts are presented within borrowings in current liabilities. Trade payables are stated at their nominal value and do not bear interest.

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

Equity instruments issued by the company are recorded at the proceeds received net of any direct issue costs.

Interest bearing loans are recorded at the proceeds received net of any direct issue costs. Finance charges are accounted for on an accrual basis using the effective interest method.

The group does not use derivative financial instruments for speculative purposes. The group uses forward currency contracts as appropriate to manage foreign exchange risk.

Leases

Leases which transfer substantially all the risks and rewards of ownership of an asset are treated as a finance lease. Assets held under finance lease are capitalised at their fair value at the inception of the lease and depreciated over the estimated useful economic life of the asset or lease term if shorter. The finance charges are allocated to the Consolidated Income Statement in proportion to the capital amount outstanding.

All other leases are classified as operating leases. Operating lease rentals are charged to the Consolidated Income Statement in equal annual amounts over the lease term.

Provisions

Provisions are recognised when the group has a legal or constructive obligation as a result of a past event, it is probable that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are calculated based on management's best estimate of the expenditure required to settle the obligation after due consideration of the risks and uncertainties that surround the event.

Notes to the financial statements
year ended 31 December 2009 (continued)

Revenue recognition

Revenue represents the amounts receivable for goods and services provided in the ordinary course of business net of value added tax and other sales related taxes. Revenue is recognised when the risks and rewards of the underlying sale have been transferred to the customer and when collectability of the related receivable is reasonably assured, which is on the delivery of the goods or services supplied and accepted by the customer.

Segmental reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments.

A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of components operating in other economic environments.

Exceptional items

Exceptional items are those significant items which are separately disclosed by virtue of their size or incidence to enable a better understanding of the group's underlying financial performance.

Pension costs

The group operates defined contribution pension schemes. Contributions are charged in the Consolidated Income Statement as they become payable in accordance with the rules of the scheme.

Share based payments

Under the IQE plc Share Option Scheme, the scheme participants are eligible for the grant of share options in the Company. These have vesting periods of between one and four years and can be exercised within ten years from the date of grant, subject to performance criteria relating to profitability and share price growth. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted which is calculated using the Black-Scholes option pricing model.

Under the IQE plc All Employee Share Ownership Plans, the scheme participants are eligible for the grant of matching shares from the Company which are equivalent to the number of partnership shares that the company purchases on their behalf with their monthly contributions.

The matching shares have a three year vesting period. The Company issues its own shares in the open market in order to meet its obligations under the share incentive schemes. Shares held by the Employee Share Ownership Trust's are shown as a deduction from shareholders' funds. The cost of employee share plans is charged to Consolidated Income Statement using the quoted market price of shares at the date of grant and credited to reserves under shares to be issued. The charge is accrued over the vesting period of the shares to the extent that they are projected to vest.

Government grants

Government grants receivable in connection with expenditure on tangible fixed assets are accounted for as deferred income, which is credited to the Consolidated Income Statement 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 charged to the Consolidated Income Statement are credited to the Consolidated Income Statement in the year in which the costs are incurred.

Notes to the financial statements
year ended 31 December 2009 (continued)

Foreign currencies

Items included in the financial statements of each subsidiary are measured using the currency of the primary economic environment in which the subsidiary operates ("the functional currency") The consolidated financial statements are presented in sterling, which is the group's functional currency

Foreign currency transactions are translated into the subsidiaries functional currency at the rates of exchange ruling at the date of the transaction, or at the forward currency hedged rate where appropriate Monetary assets and liabilities in foreign currencies are translated into the subsidiaries functional currency at the rates ruling at the balance sheet date All exchange differences are taken to the income statement

The balance sheets of overseas subsidiaries are translated into sterling at the closing rates of exchange at the balance sheet date, whilst the income statements are translated into sterling at the average rate for the period The resulting translation differences are taken directly to reserves

Foreign exchange gains and losses on the retranslation of foreign currency borrowings that are used to finance overseas operations are accounted for on the 'net investment' basis and are recorded directly in reserves provided that the hedge is 'effective' as defined in IAS 39 "Financial Instruments recognition and measurement"

Taxation

Income tax on the profit or loss for the year comprises current and deferred tax

Current tax is the expected tax payable on the taxable income for the year using rates substantially enacted at the balance sheet date, and any adjustments to tax payable in respect of prior years

Deferred tax is provided in full on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the amounts used for taxation purposes Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised Deferred tax assets are only recognised to the extent that it is probable that future taxable profits will be utilised

Tax is recognised in the Consolidated Income Statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity

Standards and Interpretations that are not yet applicable to the group

At the date of approval of these Financial Statements, the following Standards and Interpretations which have not been applied in these Financial Statements were in issue but not yet effective

IFRIC 9	-	Reassessment of embedded derivatives
IFRIC 16	-	Hedges of a net investment in a foreign operation
IFRIC 17	-	Distribution of non cash assets to owners
IFRIC 18	-	Transfer of assets from customers

Notes to the financial statements
year ended 31 December 2009 (continued)

Revisions and amendments to existing standards

IFRS 2	-	Scope of IFRS 2 and IFRS 3 (revised)
IFRS 3	-	Revised standard regarding Business Combinations
IFRS 5	-	Amendment regarding disclosures relating to held for sale assets
IFRS 8	-	Amendment to clarify required disclosures of segment assets
IAS 1	-	Current/non-current classification of convertible instruments
IAS 7	-	Classification of expenditures on unrecognised assets
IAS 17	-	Classification of leases of land and buildings
IAS 18	-	Determining whether an entity is acting as a principal or as an agent
IAS 36	-	Unit of accounting for goodwill impairment test
IAS 38	-	Additional consequential amendments arising from IFRS 3 (revised)
IAS 39	-	Revisions to clarify interpretations

The directors anticipate that the adoption of these Standards and Interpretations in future periods will have no material impact on the Financial Statements of the group except for changes in the accounting treatment for any business combinations occurring in periods starting on or after 1 January 2010

2 Critical accounting judgements and key sources of estimation uncertainty

The group's principal accounting policies are described in note 1. The application of these policies necessitates the use of estimates and judgements in a number of areas. Accordingly, the actual amounts may differ from these estimates. The main areas involving estimation are set out below.

(a) Impairment of intangible assets

Goodwill on the group's balance sheet is not subject to amortisation because it is assumed to have an indefinite useful life. In accordance with IAS 36 "Impairment of assets", the carrying value of goodwill is assessed at least annually for impairment. This assessment is based on estimated cash flow forecasts. In light of these forecasts the Board has concluded that goodwill is not impaired.

The group capitalises the cost of developing new and substantially improved products and processes if there is a reasonable expectation of obtaining an appropriate economic return. This necessitates an assessment of the future technical viability and future commercial benefits of the product or process. The carrying value for each project is assessed for impairment on an on-going basis.

(b) Impairment of receivables

Trade and other receivables are carried at the contractual amount due less any estimated provision for non-recovery. Provision is made based on a number of factors including the age of the receivable, previous collection experience and the financial circumstances of the counterparty.

(c) Inventory provisions

Inventories are carried at the lower of cost and net realisable value. Provision is made based on a number of factors including the age of inventories, the risk of obsolescence and the expected future usage.

Notes to the financial statements year ended
31 December 2009 (continued)

3 Segmental analysis

The group considers its three key market areas of wireless, opto-electronics and electronics to be its primary reporting segments, based on the reports reviewed by the board of directors that are used to make strategic decisions. The board of directors assesses the performance of the operating segments based on their earnings before interest, tax, depreciation, amortisation and share based payments (EBITDA)

Further detail on the nature of the segments is provided in the Chief executive's review

2009	Wireless £'000	Opto- electronics £'000	Electronics £'000	Total £'000
Income statement				
Revenue	41,598	9,843	1,211	52,652
EBITDA	8,359	(46)	(262)	8,051
Share based payments	(586)	(176)	(136)	(898)
Depreciation	(2,627)	(502)	(243)	(3,372)
Amortisation	(487)	(218)	(32)	(737)
Operating profit/(loss)	4,659	(942)	(673)	3,044
Finance costs				(986)
Retained profit				2,058
Segment assets				
Operating assets	49,863	12,743	1,991	64,597
Cash				4,233
Total assets				68,830
Segment liabilities				
Operating liabilities	(11,924)	(7,166)	(739)	(19,829)
Borrowings				(19,164)
Total liabilities				(38,993)
Other segmental information				
Capital expenditure - intangible assets	1,447	732	284	2,463
Capital expenditure - tangible assets	1,191	202	44	1,437

Costs not directly attributable to one of the segments above have been allocated based on the share of revenue attributable to that segment

Finance costs are not allocated to the segments since this type of activity is driven by central management of the cash and borrowings of the group

Notes to the financial statements year ended
31 December 2009 (continued)

3 Segmental analysis (continued)

2008	Wireless £'000	Opto- Electronics £'000	Electronics £'000	Total £'000
Income statement				
Revenue	48,490	10,169	1,826	60,485
EBITDA before exceptional items	10,729	(1,274)	(1,048)	8,407
Share based payments	(709)	(149)	(26)	(884)
Depreciation	(2,263)	(551)	(262)	(3,076)
Amortisation	(401)	(25)	(21)	(447)
Operating profit/(loss) before exceptional items	7,356	(1,999)	(1,357)	4,000
Exceptional items	(2,975)	(646)	(310)	(3,931)
Operating profit/(loss)	4,381	(2,645)	(1,667)	69
Net finance costs				(1,454)
Retained loss				(1,385)
Segment assets				
Operating assets	52,236	9,256	1,742	63,234
Total assets				63,234
Segment liabilities				
Operating liabilities	(11,497)	(2,927)	(457)	(14,881)
Borrowings				(18,135)
Total liabilities				(33,016)
Other segmental information				
Capital expenditure - intangible assets	1,282	249	123	1,654
Capital expenditure - tangible assets	5,928	585	117	6,630

In the periods set out below, certain customers, all within the Wireless operating segment, accounted for greater than 10% of the Group's total revenues

	2009 £'000	2009 % revenue	2008 £'000	2008 % revenue
Customer 1	11,167	21	10,740	18
Customer 2	5,435	10	13,089	22
Customer 3	4,760	9	6,712	11
Other wireless operating segment customers	20,235	38	17,949	30

There are no customers in the opto-electronics or electronics segments that accounted for greater than 10% of the Group's total revenues

Notes to the financial statements year ended
31 December 2009 (continued)

3 Segmental analysis (continued)

Geographical information

Disclosure of group revenues by location of customer

	2009 £'000	2008 £'000
Americas	33,890	40,318
United States of America	33,602	40,058
Rest of Americas	288	260
Europe, Middle East & Africa (EMEA)	5,664	6,274
France	492	1,168
Germany	1,423	1,171
Israel	1,784	1,275
United Kingdom	1,153	1,552
Rest of EMEA	812	1,108
Asia Pacific	13,098	13,893
People's Republic of China	1,294	782
Japan	5,650	4,808
Taiwan	5,274	7,106
Rest of Asia Pacific	880	1,197
Total revenue	52,652	60,485

Disclosure of non-current assets by location of assets

By location	Property, plant & equipment		Intangible assets	
	2009 £'000	2008 £'000	2009 £'000	2008 £'000
USA	11,421	14,099	6,671	7,018
Singapore	5,756	7,429	5,975	5,987
UK	4,188	4,098	6,536	1,670
	21,365	25,626	19,182	14,675

Notes to the financial statements year ended
31 December 2009 (continued)

4 Analysis of other charges/(credits)

	2009 £'000	2008 £'000
The operating result is stated after charging/(crediting)		
Depreciation of property, plant and equipment	3,372	3,076
Amortisation of non-current intangible assets	737	447
(Gain)/loss on sale of property, plant and equipment	(100)	6
Services provided by auditors	127	137
Plant and machinery lease rentals	55	44
Other lease rentals	1,681	897
Research and development	267	264
Release of government grants	(39)	(39)
Exchange losses/(gains)	107	(534)
Cost of inventories consumed	21,694	28,054

A schedule of services provided by the group's auditors is disclosed in the Corporate Governance Report

5 Exceptional items

	2009 £'000	2008 £'000
Exceptional charges comprise		
Relocation costs	-	2,486
Group restructuring	-	1,445
	-	3,931

The relocation costs in 2008 of £2,486,000 related to the one-off costs incurred in relocating the Singapore operation to a new state-of-the-art facility. The relocation was completed in November 2008. The related cash outflow in 2008 was £990,000.

The Group restructuring costs in 2008 of £1,445,000 related to the restructuring of the Group's activities and operations to reduce operating costs. This involved a 20% reduction in headcount in addition to a streamlining of certain manufacturing activities. This restructuring was completed by the end of 2008. As a result the Group incurred an exceptional charge of £1,445,000 in 2008, the majority of which was a non-cash charge relating to the write down of assets. The related cash outflow in 2008 was £75,000, with the majority of the exceptional cash outflow of £427,000 in 2009 relating to the settlement of liabilities created by this restructuring.

Of the exceptional costs incurred in 2008, £3,168,000 was charged to cost of sales in the income statement and £763,000 was charged to selling, general and administrative expenses. This allocation was determined by identifying to which classification of expenses each component of the exceptional charge most closely relates.

Notes to the financial statements year ended
31 December 2009 (continued)

6 Employee costs

	2009 £'000	2008 £'000
Employee costs (including directors' remuneration)		
Wages and salaries	11,814	12,433
Social security costs	1,755	1,714
Other pension costs	487	715
Charge for share based payments	798	884
	14,854	15,746
	No	No
The average number of employees, including directors, during the year was as follows	315	367

Directors' emoluments and share option details are disclosed in the Remuneration Report. Key management within the group comprises the executive and non-executive directors and the general managers of the subsidiaries. Compensation to key management, including pensions of £68,000 (2008: £74,000), was £1,747,000 (2008: £1,392,000) and the charge for share-based payments was £476,000 (2008: £490,000).

Included in the prior year costs above are severance costs of £409,000 relating to the group restructuring and included in exceptional costs (see note 5).

7 Finance costs

	2009 £'000	2008 £'000
Bank and other loans	980	1,446
Finance lease interest	6	8
	986	1,454

8. Taxation

	2009 £'000	2008 £'000
United Kingdom corporation tax at 28% (2008: 28%)	-	-
Overseas taxes	-	-
	-	-

**Notes to the financial statements year ended
31 December 2009 (continued)**

8 Taxation (continued)

Factors affecting total tax charge

The tax assessed for the period is different from that resulting from applying the standard rate of corporation tax in the UK 28% (2008 28%) The differences are explained below

	2009 £'000	2008 £'000
Profit/(loss) on ordinary activities before tax	2,058	(1,385)
Tax at 28% thereon (2008 28%)	576	(388)
Effects of		
Expenses not deductible for tax purposes	125	156
Overseas tax rate differences	(1,028)	(145)
Increase in unrecognised tax losses	1,435	283
Other deferred tax movements	(1,108)	94
Total tax charge for the year	-	-

Factors that may affect the future tax charge

A deferred tax asset has not been recognised in respect of timing differences relating to trading losses carried forward and accelerated depreciation as there is currently insufficient evidence that the asset will be recovered The amount of the asset not recognised is £29,506,000 (2008 £28,069,000), this would be recovered if sufficient profits from the same trade arise in future periods

9 Dividends

No dividend has been paid or proposed in 2009 (2008 £nil)

10 Earnings per share

Basic earnings per share is calculated by dividing the profit 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 potential ordinary shares Share options are only considered to be dilutive if they are 'in the money', i.e. that they can result in the purchase of ordinary shares for less than the average mid market share price in the period (2009 10.84p) The group incurred losses in the prior year and, as such, options and warrants that may be converted were considered anti dilutive, since they would reduce the loss per share

Notes to the financial statements year ended
31 December 2009 (continued)

10. Earnings per share (continued)

	2009 £'000	2008 £'000
Basic and diluted profit/(loss) attributable to ordinary shareholders	2,058	(1,385)
	No	No
Weighted average number of ordinary shares	436,881,052	432,207,766
Dilutive share options	26,321,661	-
Adjusted weighted average number of ordinary shares	463,202,713	432,207,766
Pre-exceptional earnings per share	0 47p	0 59p
Earnings/(loss) per share	0 47p	(0 32p)
Diluted earnings/(loss) per share	0 44p	(0 32p)

11 Intangible assets

The Group	Investments £'000	Goodwill £'000	Patents £'000	Development		Total £'000
				costs £'000	Software £'000	
Cost						
At 1 January 2009	100	9,574	-	6,542	157	16,373
Additions	-	-	18	2,210	235	2,463
Acquisitions	-	1,592	127	1,919	-	3,638
Disposals	(100)	-	-	-	-	(100)
Exchange difference	-	(364)	-	(487)	(20)	(871)
At 31 December 2009	-	10,802	145	10,184	372	21,503
Accumulated amortisation and impairment						
At 1 January 2009	-	-	-	1,600	98	1,698
Charge for the year	-	-	-	707	30	737
Exchange difference	-	-	-	(98)	(16)	(114)
At 31 December 2009	-	-	-	2,209	112	2,321
Net book value						
At 31 December 2009	-	10,802	145	7,975	260	19,182
At 31 December 2008	100	9,574	-	4,942	59	14,675

The carrying amount of goodwill relates to the acquisition during the year of NanoGaN Ltd £1,592,000 (2008: £nil) as set out in note 18, the historical acquisition of IQE RF LLC £3,270,000 (2008: £3,634,000) and the historical acquisition of MBE Technology Pte Ltd £5,940,000 (2008: £5,940,000). These amounts have been reviewed for impairment by comparing their carrying value with their value in use. This confirmed that these assets have not been impaired. The value in use was determined using three year projections (based on market trends) and a further seven years for which no growth was assumed, and a discount factor of 10%.

The carrying value of deferred development costs continue to be supported by forecast cash flows. During 2008 the Board decided to impair the carrying value of a number of projects, giving rise to a charge of £521,000 in light of changing economic circumstances.

Notes to the financial statements year ended
31 December 2009 (continued)

The Group	Investments £'000	Goodwill £'000	Development costs £'000	Software £'000	Total £'000
Cost					
At 1 January 2008	-	8,563	3,910	82	12,555
Additions	100	-	1,520	34	1,654
Exchange difference	-	1,011	1,112	41	2,164
At 31 December 2008	100	9,574	6,542	157	16,373
Accumulated amortisation and impairment					
At 1 January 2008	-	-	402	43	445
Charge for the year	-	-	422	25	447
Impairment	-	-	521	-	521
Exchange difference	-	-	255	30	285
At 31 December 2008	-	-	1,600	98	1,698
Net book value					
At 31 December 2008	100	9,574	4,942	59	14,675
At 31 December 2007	-	8,563	3,508	39	12,110

12. Property, plant and equipment

a) The Group	Freehold land and buildings £'000	Short leasehold improve- ments £'000	Fixtures and fittings £'000	Plant and machinery £'000	Total £'000
Cost					
At 1 January 2009	7,760	11,023	4,449	104,306	127,538
Acquisitions	-	-	-	342	342
Additions	23	48	48	1,318	1,437
Disposals	-	-	-	(52)	(52)
Exchange difference	(357)	(463)	(112)	(6,546)	(7,478)
At 31 December 2009	7,426	10,608	4,385	99,368	121,787
Depreciation					
At 1 January 2009	2,421	10,649	4,378	84,464	101,912
Disposals	-	-	-	(44)	(44)
Charge for the year	179	79	162	2,952	3,372
Exchange difference	(18)	(432)	(340)	(4,028)	(4,818)
At 31 December 2009	2,582	10,296	4,200	83,344	100,422
Net book value					
At 31 December 2009	4,844	312	185	16,024	21,365
At 31 December 2008	5,339	374	71	19,842	25,626

As set out in note 1 the useful economic lives of some items of plant and machinery were revised during the period

Notes to the financial statements year ended
31 December 2009 (continued)

b) The Group	Freehold land and buildings £'000	Short leasehold improve- ments £'000	Fixtures and fittings £'000	Plant and machinery £'000	Total £'000
Cost					
At 1 January 2008	6,727	10,550	4,568	82,108	103,953
Additions	18	65	185	6,362	6,630
Disposals	-	(930)	(561)	(928)	(2,419)
Exchange difference	1,015	1,338	257	16,764	19,374
At 31 December 2008	7,760	11,023	4,449	104,306	127,538
Depreciation					
At 1 January 2008	2,218	10,287	4,270	69,935	86,710
Disposals	-	(922)	(548)	(763)	(2,233)
Charge for the year	165	34	379	2,498	3,076
Exchange difference	38	1,250	277	12,794	14,359
At 31 December 2008	2,421	10,649	4,378	84,464	101,912
Net book value					
At 31 December 2008	5,339	374	71	19,842	25,626
At 31 December 2007	4,509	263	298	12,173	17,243

c) The Company	2009 Fixtures and fittings £'000	2008 Fixtures and fittings £000
Cost		
At 1 January and 31 December	140	140
Depreciation		
At 1 January and 31 December	140	140
Net book value		
At 31 December 2009	-	-
At 31 December 2008	-	-

Notes to the financial statements year ended
31 December 2009 (continued)

13. Investments in subsidiaries

	2009 £'000	2008 £'000
The Company		
Cost		
At 1 January	81,353	80,918
Additions (note 18)	3,512	-
Transfer from intangible assets (notes 12, 18)	100	-
Share option costs during the year	190	435
At 31 December	85,155	81,353
Impairment		
At 1 January	70,438	70,438
Impairment provision for the year	-	-
At 31 December	70,438	70,438
Net book value		
At 31 December	14,717	10,915
At 1 January	10,915	10,480

Details of subsidiary undertakings are set out in note 26

14 Inventories

	The Group	
	2009 £'000	2008 £'000
Raw materials and consumables	7,603	7,834
Work-in-progress and finished goods	3,186	3,428
	10,789	11,262

The directors are of the opinion that the replacement values of inventories are not materially different to the carrying values stated above. These carrying values are stated net of impairment provisions of £2,010,000 (2008 £2,032,000)

Notes to the financial statements year ended
31 December 2009 (continued)

15 Trade and other receivables

	2009 Group £'000	2009 Company £'000	2008 Group £'000	2008 Company £'000
Trade receivables	7,616	-	4,277	-
Amounts owed by group undertakings	-	25,371	-	29,447
Other debtors and prepayments	5,645	171	7,394	52
	13,261	25,542	11,671	29,499

As at 31 December 2009, 80% (2008 69%) of trade receivables were within terms. Of the other trade receivables, 71% (2008 84%) were less than 30 days past due. An allowance has been made for estimated irrecoverable amounts from the sale of goods of £14,000 (2008 £170,000). This allowance has been determined by reference to past default experience. Included in other receivables is accrued income of £4,053,000 (2008 £5,581,000).

The carrying values of trade and other receivables also represent their estimated fair values. The maximum exposure to credit risk at the reporting date is the carrying value of each class of receivable as set out above. In terms of trade receivables, the terms of sale provide that the group has recourse to the products sold in the event of non-payment by a customer.

16 Trade and other payables

	2009 Group £'000	2009 Company £'000	2008 Group £'000	2008 Company £'000
Trade creditors	10,959	-	8,842	-
Other taxation and social security	1,311	491	223	-
Accruals and deferred income	4,500	562	5,733	737
	16,770	1,053	14,798	737

The carrying values of trade and other payables also represent their estimated fair values.

Notes to the financial statements year ended
31 December 2009 (continued)

17 Borrowings

The Group	2009 £'000	2008 £'000
Borrowings are analysed as follows		
Overdraft	-	928
Bank loans	11,948	12,351
Deferred consideration	-	1,852
Other borrowings	7,139	2,856
Finance leases	77	148
	19,164	18,135
Borrowings fall due for repayment as follows.		
Within one year	6,573	8,090
Between one and two years	10,366	4,084
Between two and five years	470	3,813
After five years	1,755	2,148
	19,164	18,135
Borrowings are analysed by currency as follows:		
Sterling	12,608	9,341
Euro	-	2,856
US dollar	5,702	3,938
Singapore dollar	854	2,000
	19,164	18,135

The bank loans bear interest of between 1 90% over base and 7 95% fixed. The bank loans are repayable by monthly and quarterly instalments, and are secured by a fixed and floating charge over the assets of IQE plc and its principal subsidiaries.

The deferred consideration related to the acquisition of MBE Technology Pte Ltd ("MBET") This loan was secured by a charge over the issued share capital of MBET and bore interest at 6 5%.

Other borrowings include a revolving credit facility of £7,000,000. This revolving facility is secured by a fixed and floating charge over the assets of IQE plc and its principal subsidiaries, bears interest at 1 90% over LIBOR and falls due for repayment in 2011.

Finance leases bear interest at fixed rates between 2 85% to 3 5% (2008 2 83% to 3 5%) and comprise amounts repayable within one year of £54,000 (2008 £84,000) and amounts repayable between one and two years of £23,000 (2008 £39,000) and amounts repayable in two to five years of £nil (2008 £25,000).

The carrying value of loans approximates to their fair value based on the net present value of future cash flows.

The borrowings of the parent company, all of which are denominated in sterling, comprise bank loans of £5,609,000 (2008 £13,705,000), deferred consideration of £nil (2008 £1,852,000) and other borrowings of £7,139,000 (2008 £nil). The amount payable between one and two years is £9,834,000 (2008 £2,805,000), and the amount payable between two and five years is £nil (2008 £2,804,000). The balance is repayable within one year. The deferred consideration was denominated in Singapore Dollars and the balance is denominated in Sterling.

**Notes to the financial statements year ended
31 December 2009 (continued)**

18. Business combinations

During 2008 the group acquired 3% of the share capital of NanoGaN Limited, an IP rich technology company operating in the United Kingdom. On 7 October 2009, the group acquired the remaining 97% of the share capital and obtained control of NanoGaN Ltd.

Details of net assets acquired and goodwill are as follows

Purchase consideration	£'000
Cash paid for initial investment in prior period (note 11)	100
Cash paid on acquisition	120
Cash paid for direct costs relating to the acquisition	101
Fair value of shares issued (note 19)	277
Fair value of contingent consideration	3,014
Total purchase consideration	3,612

The net cash outflow on acquisition was £205,000, being the cash paid on acquisition (£221,000) less the cash held by NanoGaN at acquisition (£16,000).

As set out in the acquisition agreement the fair value of the shares issued was based on the average published share price of 14.67p for the 3 trading days immediately prior to the offer of acquisition being accepted (1 October 2009).

The contingent consideration becomes payable on the achievement of specific technical and commercial milestones. The consideration is payable in shares or cash at the group's option.

The assets and liabilities as of 7 October 2009 arising from the acquisition are as follows

	Acquiree's carrying amount £'000	Fair value adjustments (provisional) £'000	Fair value £'000
Patents (included in intangibles) (note 11)	127	-	127
Intellectual property (included in intangibles) (note 11)	341	1,584	1,925
Property, plant and equipment (note 12)	405	(51)	354
Cash	16	-	16
Trade and other receivables	7	-	7
Trade and other payables	(108)	(273)	(381)
Fair value of net assets	788	1,260	2,048
Revaluation gain on initial 3% equity interest			(28)
Goodwill (note 11)			1,592
Total purchase consideration			3,612

The group has recognised a revaluation gain in the Statement of Comprehensive Income and Expense as a result of measuring at fair value its initial 3% equity interest before acquisition of the remaining share capital in NanoGaN Limited.

**Notes to the financial statements year ended
31 December 2009 (continued)**

The goodwill of £1,592,000 arising from the acquisition is attributable to technical and commercial synergies generated by the business combination. NanoGaN expect to benefit from the commercial experience, industry reputation and technical skills of the group as they exploit their patented 'nanocolumn' technology for blue/green lasers and solid state lighting applications. The group intend to apply nanocolumn technology to complement, enhance and develop existing and emerging products with applications including wireless, solar power and advanced consumer electronics.

19 Called up share capital

Group and Company	2009 Number of shares	2009 £'000	2008 Number of shares	2008 £'000
Authorised				
Ordinary shares of 1p each	650,000,000	6,500	650,000,000	6,500
Allotted, called up and fully paid				
Ordinary shares of 1p each	443,500,599	4,435	433,263,558	4,333

The movement in the number of ordinary shares during the year was

	2009 No	2008 No
At 1 January	433,263,558	430,952,266
Employee share options	1,444,456	2,085,936
Acquisition of NanoGaN Limited	1,819,134	-
Placing	4,000,000	-
Employee share awards	1,947,063	-
Non-executive directors	1,026,388	225,356
At 31 December	443,500,599	433,263,558

10,237,041 ordinary shares (2008 2,311,292 ordinary shares) were issued during the year for the following considerations

	2009 No of shares	2009 Consideration	2008 No of shares	2008 Consideration
Employee share options	1,444,456	1 00p to 14 00p	2,085,936	1 00p to 10 11p
Acquisition of NanoGaN Limited	1,819,134	14 67p	-	-
Placing	4,000,000	14 00p	-	-
Employee share awards	1,947,063	9 24p	-	-
Non-executive directors	1,026,388	5 05p to 12 44p	225,356	15 17p to 19 47p
	10,237,041		2,311,292	

The group's objectives when managing capital are to safeguard the entity's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders, and provide an adequate return for shareholders.

The group sets the amount of capital in proportion to risk. The group manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the characteristic of the underlying assets. The group monitors capital by reviewing net debt against shareholders' funds. The position of these indicators and the movement during the period is shown in the Five Year Financial Summary and within the Corporate Governance Report.

**Notes to the financial statements year ended
31 December 2009 (continued)**

20 Share based payments

The IQE Plc Share Option Scheme was adopted on 26 May 2000 and amended by shareholders at the Annual General Meeting on 17 May 2002. Under the scheme, the Remuneration Committee can grant options over shares in the company to employees of the group.

Options are granted with a contractual life of ten years and with a fixed exercise price equal to the market value of the shares under option at the date of grant, and they become exercisable between one and three years from date of grant subject to performance conditions, including achievement of positive EBITDA and growth in earnings per share in excess of the retail price index over the same period.

Options are valued using the Black-Scholes option-pricing model and the total amount to be expensed is charged to profit and loss account over the vesting period of the option. No performance conditions are included in the fair value calculations. The principal assumptions used in the calculation of the fair value of share options are as follows:

Principal assumptions	2009	2008
Weighted share price at grant date	6.42p	17.46p
Weighted exercise price	6.34p	10.16p
Weighted number of options granted	1,589,620	2,190,271
Weighted vesting period (years)	3	3
Weighted expected volatility factor	61%	48%
Option life (years)	10	10
Weighted expected life (years)	3	3
Weighted risk free rate	2.39%	4.35%
Dividend yield	0%	0%
Weighted fair value per option	2.77p	7.66p

The expected volatility factor is based on historical share price volatility over the three years immediately preceding the grant of the option. The expected life is the average expected period to exercise. The risk free rate of return is the yield of zero-coupon UK government bonds of a term consistent with the assumed option life. The fair value of options granted during the year ended 31 December 2009 was £307,990 (2008: £1,139,863).

As at 31 December 2009, the total number of options held by employees was 52,017,091 (2008: 43,773,669) as follows:

Option price pence/share	Option period ending	2009 No. of options	2008 No. of options
75.00p - 458.36p	31 December 2010	10,500	10,500
72.92p - 147.40p	31 December 2011	7,000	7,000
1.00p - 86.20p	31 December 2012	2,515,830	3,055,576
6.67p - 10.17p	31 December 2014	8,201,801	9,026,127
6.87p - 10.25p	31 December 2015	1,673,992	2,296,958
10.40p - 18.00p	31 December 2016	11,114,083	11,490,000
13.58p - 19.42p	31 December 2017	8,690,462	9,126,425
0.00p - 18.00p	31 December 2018	8,676,083	8,761,083
1.00p - 17.07p	31 December 2019	11,127,340	-
At 31 December		52,017,091	43,773,669

**Notes to the financial statements year ended
31 December 2009 (continued)**

The movements on share options during the year were as follows

	2009 No of options	2008 No of options
At 1 January	43,773,669	37,808,054
Granted	11,127,340	8,813,862
Exercised	(1,265,416)	(2,085,936)
Cancelled	(1,618,502)	(762,311)
At 31 December	52,017,091	43,773,669

The total amount charged to the income statement in 2009 in respect of share based payments was £898,000 (2008 £884,000)

21 Investments in own shares

The IQE Plc Employee Benefit Trust and the IQE Plc General Benefit Trust were established to manage the IQE Plc All Employee Share Ownership Plans (the Plans) for UK and US employees respectively. The IQE Plc General Benefit Trust was also established to manage a Deferred Share Bonus Plan for UK and US employees by granting shares to employees in lieu of salary and bonus sacrifices. The Trustees of the Plans purchase the company's ordinary shares in the open market with financing provided by the employees. The Trusts contribute matching shares at no cost to the employees which are generated from new issues made by the company to the Trusts. As at 31 December 2009, the company had issued 1,863,079 ordinary shares (2008 1,863,079 ordinary shares) of 1p each to the Trusts to establish the Plans and allocated 1,806,718 matching shares (2008 1,806,718 matching shares).

The market value of shares awarded under the Plans is amortised evenly over the period from the original grant of the particular award to the time of vesting, which is normally a period of three years, and charged to the income statement. Other administrative costs are also charged to the income statement as incurred. As at 31 December 2009, 901,088 shares (2008 901,088 shares) had been issued to employees including 249,967 shares (2008 249,967 shares) under the Deferred Share Bonus Plan.

Group and Company	Shares held in trust No	Nominal value £'000	Cost £'000	Issued £'000	Net book value £'000
At 1 January and 31 December 2009	961,392	12	12	(2)	10

The market value of IQE Plc ordinary shares at 31 December 2009 was 17.00p (2008 5.25p) per share.

Notes to the financial statements year ended
31 December 2009 (continued)

22. Parent company profit and statement of changes in equity

As permitted by Section 408 of the Companies Act 2006, the profit and loss account of the parent company is not presented as part of these financial statements. The parent company's profit for the financial year amounted to £1,028,000 (2008 profit £1,437,000)

	Share capital £'000	Share premium £'000	Retained earnings £'000	Other reserves £'000	Total equity £'000
Balance at 1 January 2008	4,310	172,183	(156,262)	1,632	21,863
Comprehensive income					
Profit for the period	-	-	1,437	-	1,437
Total comprehensive income	-	-	1,437	-	1,437
Transactions with owners					
Employee share option scheme	-	-	-	747	747
Issues of ordinary shares	23	222	-	(72)	173
Capital reduction	-	(172,281)	172,281	-	-
Total transactions with owners	23	(172,059)	172,281	675	920
Balance at 1 January 2009	4,333	124	17,456	2,307	24,220
Comprehensive income					
Profit for the period	-	-	1,028	-	1,028
Total comprehensive income	-	-	1,028	-	1,028
Transactions with owners					
Employee share option scheme	-	-	-	264	264
Shares issued for business combination	58	709	-	-	767
Other issues of ordinary shares	44	317	-	-	361
Total transactions with owners	102	1,026	-	264	1,392
Balance at 31 December 2009	4,435	1,150	18,484	2,571	26,640

Notes to the financial statements year ended
31 December 2009 (continued)

23 Cash generated from operations

	2009 £'000	2008 £'000
The Group		
Operating profit	3,044	69
Depreciation of tangible assets	3,372	3,076
Amortisation of intangible assets	737	447
(Gain)/loss on sale of tangible assets	(100)	6
Government grants released	(39)	(39)
Non cash exceptional costs – impairment of development costs	-	521
Non cash exceptional costs – other costs	-	2,345
Non-cash share based payment costs	898	884
Operating profit before changes in working capital	7,912	7,309
(Increase)/decrease in inventories	(340)	(1,426)
(Increase)/decrease in trade and other receivables	(2,457)	1,618
Increase/(decrease) in trade and other payables	2,597	(40)
Net cash inflow from operations	7,712	7,461

	2009 £'000	2008 £'000
The Company		
Operating profit	1,028	1,437
Non-cash share based payment costs	485	349
Operating profit before changes in working capital	1,513	1,786
Decrease/(increase) in trade and other receivables	4,199	(7,070)
Increase/(decrease) in trade and other payables	316	(291)
Net cash inflow/(outflow) from operations	6,028	(5,575)

Notes to the financial statements year ended
31 December 2009 (continued)

24 Reconciliation of net cash flow to movement in net debt

	2009 £'000	2008 £'000
Increase in cash in the year	4,621	-
Decrease in highly liquid investments in the year	-	(11)
Decrease in overdraft in the year	928	94
Loans received	(10,348)	(9,862)
Loans repaid	7,510	8,174
Leases received	-	(24)
Leases repaid	60	53
Decrease/(increase) in net debt resulting from cash flows	2,771	(1,576)
Net debt at 1 January	(18,135)	(14,159)
Net movement resulting from cash flows	2,771	(1,576)
Non-cash movements	433	(2,400)
Net debt at 31 December	(14,931)	(18,135)

Highly liquid investments represent cash balances placed on deposit terms which are not accessible within one day

25 Analysis of net debt

	At 1 January 2009 £'000	Cash flow £'000	Other non-cash movements £'000	At 31 December 2009 £'000
Cash and cash equivalents	-	4,621	(388)	4,233
Bank overdraft	(928)	928	-	-
Loans due after one year	(9,961)	(5,879)	3,272	(12,568)
Loans due within one year	(7,098)	3,041	(2,462)	(6,519)
Finance leases due after one year	(84)	-	61	(23)
Finance leases due within one year	(64)	60	(50)	(54)
Total borrowings	(18,135)	(1,850)	821	(19,164)
Net debt	(18,135)	2,771	433	(14,931)

Cash and cash equivalents at 31 December 2009 comprised balances held in instant access bank accounts

Notes to the financial statements year ended
31 December 2009 (continued)

26 Principal subsidiary undertakings

Name of company	Class of capital	Proportion of shares held	Activity	Country of incorporation
IQE (Europe) Limited	Ordinary shares of £1	100%*	Manufacture of advanced semiconductor materials	UK
IQE Inc	Common stock of \$0.001	100%*	Manufacture of advanced semiconductor materials	USA
IQE RF LLC	Limited liability company	100%	Manufacture of advanced semiconductor materials	USA
IQE Silicon Compounds Limited	Ordinary shares of £1	100%	Manufacture of silicon epitaxy	UK
MBE Technology Pte Ltd	Preferred shares of S\$1	100%	Manufacture of advanced semiconductor materials	Singapore
	Ordinary shares of S\$1	100%		
Wafer Technology Limited	Ordinary shares of £1	100%*	Manufacture of semiconductor compounds and ultra high purity materials	UK
NanoGaN Limited (see note 18)	Ordinary shares of £0.001	100%	Development of advanced semiconductor materials	UK

* Indirect holdings

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

**Notes to the financial statements year ended
31 December 2009 (continued)**

27 Related party transactions

The group incurred professional fees and expenses during the year of £64,000 (2008 £70,000) payable to Gambit Corporate Finance and £29,000 (2008 £39,000) payable to Fishstone Limited. Dr G H H Ainsworth, who is a director of IQE Plc, was a partner in Gambit Corporate Finance until 30 November 2009. S J Gibson, who is a director of IQE Plc, is also a director of Fishstone Limited. An amount of £26,228 (2008 £30,000) was outstanding to these parties at the year-end.

During the year fees were paid to M and A solicitors of £63,000 (2008 £12,000). Alan Whitely, a partner in Gambit Corporate Finance is also a partner in M and A solicitors.

28 Operating lease commitments

The group was committed at 31 December 2009 and 31 December 2008 to making the following aggregate payments in respect of non-cancellable operating leases:

	2009 £'000	2008 £'000
Due within one year	1,625	1,474
Due between two and five years	6,371	6,525
Due after five years	12,119	13,910
	20,115	21,909

29. Commitments

The group had the following capital commitments at 31 December 2009 and 31 December 2008:

	2009 £'000	2008 £'000
Authorised and contracted for	204	297