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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2018

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from __________ to __________ .

Commission File Number: 001-34791

MagnaChip Semiconductor Corporation

(Exact name of registrant as specified in its charter)

Delaware	**83-0406195**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

c/o MagnaChip Semiconductor S.A.

1, Allée Scheffer, L-2520

Luxembourg, Grand Duchy of Luxembourg

(352) 45-62-62

(Address, zip code, and telephone number, including area code, of registrant s principal executive offices)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company or an emerging growth company. See the definitions of large accelerated filer, accelerated filer smaller reporting company, and emerging growth company in Rule 12b-2 of the Exchange Act.

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)	Smaller reporting company
Emerging growth company		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of July 31, 2018, the registrant had 34,495,040 shares of common stock outstanding.

MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES

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PART I FINANCIAL INFORMATION

Item 1. Interim Consolidated Financial Statements (Unaudited)

MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS (Unaudited)

	June 30 2018	December 31, 2017
	(In thousands of US dollars, except share data)	
Assets		
Current assets		
Cash and cash equivalents	$ 131,682	$ 128,575
Accounts receivable, net	85,570	92,026
Unbilled accounts receivable	35,857	
Inventories, net	57,456	73,073
Other receivables	8,468	4,292
Prepaid expenses	10,227	9,250
Hedge collateral (Note 7)	10,100	7,600
Other current assets (Notes 7 and 18)	11,023	15,444
Total current assets	350,383	330,260
Property, plant and equipment, net	197,034	205,903
Intangible assets, net	3,966	4,061
Long-term prepaid expenses	13,858	12,791
Other non-current assets	5,851	5,774
Total assets	$ 571,092	$ 558,789
Liabilities and Stockholders Equity		
Current liabilities		
Accounts payable	$ 60,742	$ 65,940
Other accounts payable	11,123	10,261
Accrued expenses	49,506	51,746
Deferred revenue	13,440	8,335
Other current liabilities (Note 7)	5,149	1,860
Total current liabilities	139,960	138,142
Long-term borrowings, net	304,489	303,416
Accrued severance benefits, net	145,542	148,905

Other non-current liabilities (Note 4)	14,894	7,963
Total liabilities	604,885	598,426
Commitments and contingencies (Note 18)		
Stockholders equity		
Common stock, $0.01 par value, 150,000,000 shares authorized, 42,877,395 shares issued and 34,483,754 outstanding at June 30, 2018 and 42,563,808 shares issued and 34,189,599 outstanding at December 31, 2017	429	426
Additional paid-in capital	139,502	136,259
Accumulated deficit	(51,147)	(40,889)
Treasury stock, 8,393,641shares at June 30, 2018 and 8,374,209 shares at December 31, 2017	(102,518)	(102,319)
Accumulated other comprehensive loss	(20,059)	(33,114)
Total stockholders deficit	(33,793)	(39,637)
Total liabilities and stockholders equity	$ 571,092	$ 558,789

The accompanying notes are an integral part of these consolidated financial statements

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MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

	Three Months Ended		Six Months Ended	
	June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
	(In thousands of US dollars, except share data)			
Net sales	$ 199,685	$ 166,685	$ 365,504	$ 328,395
Cost of sales	145,831	120,023	267,069	240,163
Gross profit	53,854	46,662	98,435	88,232
Operating expenses				
Selling, general and administrative expenses	18,935	17,730	36,557	40,878
Research and development expenses	21,005	16,928	40,585	34,886
Restructuring and other gain				(17,010)
Early termination charges		2,262		13,369
Total operating expenses	39,940	36,920	77,142	72,123
Operating income	13,914	9,742	21,293	16,109
Interest expense	(5,489)	(5,441)	(10,952)	(10,614)
Foreign currency gain (loss), net	(27,449)	(11,905)	(26,131)	29,881
Other income (expense), net	(960)	83	(441)	1,694
Income (loss) before income taxes	(19,984)	(7,521)	(16,231)	37,070
Income tax expenses	1,521	538	2,511	1,391
Net income (loss)	$ (21,505)	$ (8,059)	$ (18,742)	$ 35,679
Earnings (loss) per common share				
Basic	$ (0.62)	$ (0.24)	$ (0.55)	$ 1.06
Diluted	$ (0.62)	$ (0.24)	$ (0.55)	$ 0.87
Weighted average number of shares				
Basic	34,420,654	33,952,574	34,337,345	33,808,237
Diluted	34,420,654	33,952,574	34,337,345	43,772,115

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MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (Unaudited)

	Three Months Ended		Six Months Ended	
	June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
	(In thousands of US dollars)			
Net income (loss)	$ (21,505)	$ (8,059)	$ (18,742)	$ 35,679
Other comprehensive income (loss)				
Foreign currency translation adjustments	20,116	9,362	19,633	(25,962)
Derivative adjustments				
Fair valuation of derivatives	(1,870)	(1,594)	(1,937)	909
Reclassification adjustment for gain on derivatives included in net income (loss)	(2,035)	(808)	(4,641)	(1,305)
Total other comprehensive income (loss)	16,211	6,960	13,055	(26,358)
Total comprehensive income (loss)	$ (5,294)	$ (1,099)	$ (5,687)	$ 9,321

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MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY (Unaudited)

(In thousands of US dollars, except share data)	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Accumulated Deficit	Treasury Stock	Accumulated Other Comprehensive Loss	Total
Six Months Ended June 30, 2018:							
Balance at December 31, 2017, as previously reported	34,189,599	$ 426	$ 136,259	$ (40,889)	$ (102,319)	$ (33,114)	$ (39,637)
Impact of adopting the new revenue standard				8,484			8,484
Balance at January 1, 2018, as adjusted	34,189,599	$ 426	$ 136,259	$ (32,405)	$ (102,319)	$ (33,114)	$ (31,153)
Stock-based compensation			2,810				2,810
Exercise of stock options	64,753	1	435				436
Settlement of restricted stock units	248,834	2	(2)				
Acquisition of treasury stock	(19,432)				(199)		(199)
Other comprehensive income, net						13,055	13,055
Net loss				(18,742)			(18,742)
Balance at June 30, 2018	34,483,754	$ 429	$ 139,502	$ (51,147)	$ (102,518)	$ (20,059)	$ (33,793)
Six Months Ended June 30, 2017:							
Balance at January 1, 2017	35,048,338	$ 416	$ 130,189	$ (125,825)	$ (90,918)	$ 14,024	$ (72,114)
Stock-based compensation			1,179				1,179
Exercise of stock options	360,211	4	2,521				2,525
Settlement of restricted stock units	397,522	4	(4)				
Acquisition of treasury stock	(1,795,444)				(11,401)		(11,401)
Other comprehensive loss, net						(26,358)	(26,358)
Net income				35,679			35,679
Balance at June 30, 2017	34,010,627	$ 424	$ 133,885	$ (90,146)	$ (102,319)	$ (12,334)	$ (70,490)

The accompanying notes are an integral part of these consolidated financial statements.

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MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	Six Months Ended June 30, 2018	Six Months Ended June 30, 2017
	(In thousands of US dollars)	
Cash flows from operating activities		
Net income (loss)	$ (18,742)	$ 35,679
Adjustments to reconcile net income to net cash used in operating activities		
Depreciation and amortization	15,970	13,531
Provision for severance benefits	9,165	10,776
Amortization of debt issuance costs and original issue discount	1,073	950
Loss (gain) on foreign currency, net	32,369	(35,813)
Restructuring and other gain		(17,010)
Stock-based compensation	2,810	1,179
Other	1,053	220
Changes in operating assets and liabilities		
Accounts receivable, net	5,305	(9,730)
Unbilled accounts receivable	887	
Inventories, net	(16,797)	2,646
Other receivables	(4,508)	2,598
Other current assets	2,253	1,135
Accounts payable	(4,473)	(1,919)
Other accounts payable	(5,229)	(7,790)
Accrued expenses	(1,435)	(10,776)
Deferred revenue	5,413	(265)
Other current liabilities	760	(436)
Other non-current liabilities	1,116	(268)
Payment of severance benefits	(5,754)	(18,082)
Other	516	(107)
Net cash provided by (used in) operating activities	21,752	(33,482)
Cash flows from investing activities		
Proceeds from settlement of hedge collateral	4,863	6,781
Payment of hedge collateral	(7,490)	(10,036)
Proceeds from disposal of plant, property and equipment	13	1,125
Purchase of plant, property and equipment	(11,432)	(10,807)
Payment for property related to water treatment facility arrangement (Note 4)	(4,283)	
Payment for intellectual property registration	(574)	(566)
Collection of guarantee deposits	659	1,400
Payment of guarantee deposits		(41)
Other	(38)	22

Net cash used in investing activities		(18,282)		(12,122)
Cash flows from financing activities				
Proceeds from issuance of senior notes				86,250
Payment of debt issuance costs				(5,902)
Proceeds from exercise of stock options		435		2,525
Acquisition of treasury stock				(11,401)
Proceeds from property related to water treatment facility arrangement (Note 4)		4,283		
Net cash provided by financing activities		4,718		71,472
Effect of exchange rates on cash, cash equivalents and restricted cash		(5,081)		4,049
Net increase in cash, cash equivalents and restricted cash		3,107		29,917
Cash, cash equivalents and restricted cash				
Beginning of the period		128,575		101,606
End of the period	$	131,682	$	131,523
Supplemental cash flow information				
Cash paid for interest	$	9,609	$	7,980
Cash paid for income taxes	$	668	$	790
Non-cash investing activities				
Property, plant and equipment additions in other accounts payable	$	2,582	$	2,092
Non-cash financing activities				
Acquisition of treasury stock to satisfy the tax withholding obligations in connection with equity- based compensation	$	(199)	$	

The accompanying notes are an integral part of these consolidated financial statements.

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MAGNACHIP SEMICONDUCTOR CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(TABULAR DOLLARS IN THOUSANDS, EXCEPT SHARE DATA)

1. Business, Basis of Presentation and Significant Accounting Policies

Business

MagnaChip Semiconductor Corporation (together with its subsidiaries, the Company) is a designer and manufacturer of analog and mixed-signal semiconductor platform solutions for communications, Internet of Things (IoT) applications, consumer, industrial and automotive applications. The Company provides technology platforms for analog, mixed signal, power, high voltage, non-volatile memory and Radio Frequency (RF) applications. The Company s business is comprised of two operating segments: Foundry Services Group and Standard Products Group. The Company s Foundry Services Group provides specialty analog and mixed-signal foundry services mainly for fabless and Integrated Device Manufacturer (IDM) semiconductor companies that primarily serve communications, IoT, consumer, industrial and automotive applications. The Company s Standard Products Group is comprised of two business lines: Display Solutions and Power Solutions. The Company s Display Solutions products provide panel display solutions to major suppliers of large and small rigid and flexible panel displays, and mobile, automotive applications and home appliances. The Company s Power Solutions products include discrete and integrated circuit solutions for power management in communications, consumer and industrial applications.

Basis of Presentation

The accompanying unaudited interim consolidated financial statements of the Company have been prepared in accordance with generally accepted accounting principles in the United States of America (US GAAP). These interim consolidated financial statements include normal recurring adjustments and the elimination of all intercompany accounts and transactions which are, in the opinion of management, necessary to provide a fair statement of the Company s financial condition and results of operations for the periods presented. These interim consolidated financial statements are presented in accordance with Accounting Standards Codification 270, *Interim Reporting* and, accordingly, do not include all of the information and note disclosures required by US GAAP for complete financial statements, except for the changes below. The results of operations for the three and six months ended June 30, 2018 are not necessarily indicative of the results to be expected for a full year or for any other periods.

The December 31, 2017 balance sheet data was derived from the Company s audited financial statements, but does not include all disclosures required by US GAAP.

Upon the adoption of Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) (ASU 2014-09) effective on January 1, 2018 (the new revenue standard), the Company has updated its accounting policy for revenue recognition as detailed below. As the Company adopted the new revenue standard using the modified retrospective method, which allows the recognition of the cumulative effect of initially applying the new revenue standard as an adjustment to the Company s equity as of January 1, 2018. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods.

Revenue Recognition

The Company recognizes revenue when it satisfies a performance obligation by transferring control over a product or service to a customer. Revenue is measured based on a consideration specified in a contract with a customer in exchange for such product or service.

The Foundry Services Group of the Company manufactures products based on customers specific product designs. The Company recognizes revenue over time for those foundry products without alternative use where the Company has an enforceable right to payment for the related foundry services completed to date. The revenue recognized over time is in proportion of wafer manufacturing costs incurred relative to total estimated costs at completion to measure the Company s performance to date. However, in certain circumstances, the Company may not have an enforceable right to payment for performed foundry services pursuant to a customer contract or an individual purchase order. In this situation, the Company recognizes revenue when a customer obtains control of the product, which is generally upon product shipment, delivery at the customer s location or upon customer acceptance, depending on the terms of the arrangement.

The Standards Products Group of the Company sells products manufactured based on the Company s design. The Standard Products Group s products are either standardized with an alternative use or the Company does not have an enforceable right to payment for the related manufacturing services completed to date. For those products, revenue is recognized when a customer obtains control of the product, which is generally upon product shipment, delivery at the customer s location or upon customer acceptance, depending on the terms of the arrangement.

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A portion of the Company s sales are made through distributors for which the Company applies the same revenue recognition guidance as described above. The Company defers recognition of revenue when it receives cash from certain customers and distributors for the sale of products prior to obtaining an enforceable right to payment for performance completed to date or control of the product being transferred to the customer.

In accordance with revenue recognition guidance, any tax assessed by a governmental authority that is both imposed on and concurrent with a specific revenue-producing transaction, and that is collected by the Company from a customer, is excluded from revenue and presented in the statement of operations on a net basis.

The Company provides a warranty, under which customers can return defective products. The Company estimates the costs related to those defective product returns and records them as a component of cost of sales.

In addition, the Company offers sales returns (other than those that relate to defective products under warranty), cash discounts for early payments, volume rebate and certain allowances to its customers, including distributors. The Company records reserves for those returns, discounts and allowances as a deduction from sales, based on historical experience and other quantitative and qualitative factors.

Substantially all of the Company s contracts are one year or less in duration. The standard payment terms with customers is generally thirty to sixty days from the time of shipment, product delivery at the customer s location or customer acceptance, depending on the terms of the related arrangement.

Recent Accounting Pronouncements

In February 2018, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2018-02 Income Statement Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income (ASU 2018-02). ASU 2018-02 addresses the accounting issue pertaining to the deferred tax amounts that are stranded in accumulated other comprehensive income as a result of the Tax Cuts and Jobs Act. ASU 2018-02 is effective for interim and annual periods beginning after December 15, 2018 and interim periods within those fiscal years. The Company does not have deferred tax amounts recorded through accumulated other comprehensive income and thus does not expect that the adoption will have an impact on its consolidated financial statements.

In August 2017, the FASB issued Accounting Standards Update No. 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities (ASU 2017-12). ASU 2017-12 provides new guidance about income statement classification and eliminates the requirement to separately measure and report hedge ineffectiveness. The entire change in fair value for qualifying hedge instruments included in the effectiveness will be recorded in other comprehensive income (OCI) and amounts deferred in OCI will be reclassified to earnings in the same income statement line item in which the earnings effect of the hedged item is reported. ASU 2017-12 is effective for interim and annual periods for the Company on January 1, 2019, with early adoption permitted. The Company is currently evaluating the impact of adoption of ASU 2017-12 on its consolidated financial statements.

In July 2017, the FASB issued Accounting Standards Update No. 2017-11, Earnings Per Share (Topic 260); Distinguishing Liabilities from Equity (Topic 480); Derivatives and Hedging (Topic 815) (ASU 2017-11), which addresses the complexity of accounting for certain financial instruments with down round features. Down round features are features of certain equity-linked instruments (or embedded features) that result in the strike price being reduced on the basis of the pricing of future equity offerings. Current accounting guidance creates cost and complexity for entities that issue financial instruments (such as warrants and convertible instruments) with down round features that require fair value measurement of the entire instrument or conversion option. For public business entities, the amendments in ASU 2017-11 are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The Company is currently evaluating the impact of adoption of ASU 2017-11 on its consolidated financial statements.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, Leases (Topic 842) (ASU 2016-02) in order to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet for those leases classified as operating leases under US GAAP. ASU 2016-02 requires that a lessee recognizes a liability to make lease payments and a right-of-use asset representing its right to use the underlying asset for the lease term on the balance sheet. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those reporting periods using a modified retrospective approach and early adoption is permitted. In January 2018, the FASB issued Accounting Standards Update No 2018-01, Leases (Topic 842) Land Easement Practical Expedient for Transition to Topic 842 (ASU 2018-01). ASU 2018-01 permits an entity to elect an optional transition practical expedient not to evaluate land easements that exist or expired before the entity s adoption of 2016-02 and that were not accounted for as leases under previous lease guidance. In July 2018, the FASB issued Accounting Standards Update No 2018-10, Codification Improvements to Topic 842 Leases (ASU 2018-10). ASU 2018-10 provides narrow amendments to clarify how to apply certain aspects of the new lease standard. The effective date and transition requirements for ASU 2016-02, ASU 2018-01 and ASU 2018-10 are the same. The Company will adopt this standard on January 1, 2019. The Company is currently evaluating the potential impact of adopting this new guidance. In terms of the Company s evaluation efforts, the Company has assigned internal resources and engaged third party service providers to assist in its evaluation.

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Recently Adopted Accounting Pronouncements

In May 2017, the FASB issued Accounting Standards Update No. 2017-09, Compensation-Stock Compensation (Topic 718): Scope of Modification Accounting (ASU 2017-09). ASU 2017-09 provides clarity and reduces both (i) diversity in practice and (ii) cost and complexity when applying the guidance in Topic 718 to a change to the terms or conditions of a share-based payment award. The amendments in ASU 2017-09 provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. The Company adopted ASU 2017-09 in the first quarter of 2018, and the adoption did not impact the Company s consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230), Restricted Cash (ASU 2016-18). ASU 2016-18 clarifies certain existing principles in ASC 230, including providing additional guidance related to transfers between cash and restricted cash and how entities present, net cash used in operating and net cash used in investing in their statement of cash flows, the cash receipts and cash payments that directly affect the restricted cash accounts. The Company adopted ASU 2016-18 in the first quarter of 2018. As of December 31, 2016, the Company held $18,251 thousand of restricted cash in connection with an arrangement to sell the building that housed the Company s legacy 6-inch fab. This restricted cash was not previously included in the ending cash balance as of December 31, 2016 within the consolidated statements of cash flows. As a result of adopting ASU 2016-18, the consolidated statement of cash flows for the six months ended June 30, 2017 was revised to include such receipt of restricted cash of $18,251 thousand as cash, cash equivalents and restricted cash as of January 1, 2017, resulting in a cash outflow of $1,809 thousand in operating cash flows, a cash outflow of $17,625 thousand in investing cash flows, and an increase of $1,183 thousand in cash, cash equivalents and restricted cash due to the effect of exchange rates, from what was previously reported.

In August 2016, the FASB issued Accounting Standards Update No. 2016-15, Statement of Cash Flows (Topic 230), Classification of Certain Cash Receipts and Cash Payments (ASU 2016-15). ASU 2016-15 reduces the existing diversity in practice in financial reporting across all industries by clarifying certain existing principles in ASC 230, Statement of Cash Flows (ASC 230), including providing additional guidance on how and what an entity should consider in determining the classification of certain cash flows. The Company adopted ASU 2016-15 in the first quarter of 2018, and the adoption of ASU 2016-15 did not impact the Company s consolidated financial statements.

In May 2014, the FASB issued ASU 2014-09. ASU 2014-09 supersedes the revenue recognition requirements in Revenue Recognition (Topic 605) , and requires entities to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. The new guidance allows for the amendments to be applied either retrospectively to each prior reporting period presented (the full retrospective method) or retrospectively as a cumulative-effect adjustment as of the date of adoption (the modified retrospective method). In March 2016, the FASB issued ASU 2016-08, which clarifies the implementation guidance on principal versus agent considerations. In April 2016, the FASB issued ASU 2016-10, which clarifies identifying performance obligations and the licensing implementation guidance. In May 2016, the FASB issued ASU 2016-12, which improves certain aspects of ASC Topic 606 Revenue from Contracts with Customers. In December 2016, the FASB issued ASU 2016-20, which improves certain aspects of ASC Topic 606 Revenue from Contracts with Customers. The effective date and transition requirements for ASU 2016-08, ASU 2016-10, ASU 2016-12 and ASU 2016-20 are the same as the effective date and transition requirements of ASU 2014-09 (collectively, the new revenue standard).

Prior to the adoption of the new revenue standard effective on January 1, 2018, the Company had historically recognized revenue when risk and reward of ownership pass to the customer either upon shipment, upon product delivery at the customer s location or upon customer acceptance, depending on the terms of the related arrangement. After the adoption of the new revenue standard effective on January 1, 2018, the Company recognizes revenue over time for those foundry products without alternative use where the Company has an enforceable right to payment for the related foundry services completed to date. As the Company adopted the new revenue standard using the modified retrospective method, it recognized the cumulative effect of initially applying the new revenue standard as an adjustment to the Company s equity as of January 1, 2018, while prior period amounts are not adjusted and continue to be reported under the accounting standards in effect for such periods. The cumulative-effect adjustments increased unbilled accounts receivable by $38,307 thousand and decreased inventories, net by $29,823 thousand, resulting in a net increase of $8,484 thousand in the Company s beginning equity as of January 1, 2018. There was no net income tax impact from those cumulative-effect adjustments due to full allowance on deferred tax assets.

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Of the recorded unbilled accounts receivable of $38,307 thousand as of January 1, 2018, $2,769 thousand and $35,038 thousand were billed to customers upon shipment, upon product delivery or upon customer acceptance, depending on the terms of the related arrangement, during the three and six months ended June 30, 2018, respectively. Of the recorded deferred revenue of $8,335 thousand as of December 31, 2017, $136 thousand and $1,222 thousand were recognized as revenue during the three and six months ended June 30, 2018, respectively.

The impacts of adopting the new revenue standard on the Company s consolidated financial statements for the six months ended June 30, 2018 are as follows (in thousands):

	As of June 30, 2018		
	As Reported	Adjustments	Amounts Without Adoption of Topic 606
	(In thousands of US dollars, except share data)		
Assets			
Current assets			
Unbilled accounts receivable	$ 35,857	$ 35,857	$
Inventories, net	57,456	(26,659)	84,115
Total current assets	350,383	9,198	341,185
Total assets	571,092	9,198	561,894
Liabilities and Stockholders Equity			
Stockholders equity			
Retained earnings (accumulated deficit)	(51,147)	9,607	(60,754)
Accumulated other comprehensive income (loss)	(20,059)	(409)	(19,650)
Total stockholders equity (deficit)	(33,793)	9,198	(42,991)
Total liabilities and stockholders deficit	$ 571,092	$ 9,198	$ 561,894

Unbilled accounts receivable represents the Company s contractual right to consideration for manufacturing work performed on a customer contract or an individual purchase order basis, which has not been invoiced to the customer.

	Three Months Ended June 30, 2018			Six Months Ended June 30, 2018		
	As Reported	As Adjusted	Amounts Without Adoption of Topic 606	As Reported	As Adjusted	Amounts Without Adoption of Topic 606
	(In thousands of US dollars, except share data)					
Net sales	$ 199,685	$ (1,526)	$ 201,211	$ 365,504	$ (887)	$ 366,391
Cost of sales	145,831	(2,070)	147,901	267,069	(2,010)	269,079
Gross profit	53,854	544	53,310	98,435	1,123	97,312

Operating income	13,914	544	13,370	21,293	1,123	20,170
Income (loss) before income tax expenses	(19,984)	544	(20,528)	(16,231)	1,123	(17,354)
Net income (loss)	$ (21,505)	$ 544	$ (22,049)	$ (18,742)	$ 1,123	$ (19,865)
Earnings (loss) per common share						
Basic	$ (0.62)	$ 0.02	$ (0.64)	$ (0.55)	$ 0.03	$ (0.58)
Diluted	$ (0.62)	$ 0.02	$ (0.64)	$ (0.55)	$ 0.03	$ (0.58)

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2. Sales of Accounts Receivable and Receivable Discount Program

The Company has entered into an agreement to sell selected trade accounts receivable to a financial institution from time to time since March 2012. After the sale, the Company does not retain any interest in the receivables and the applicable financial institution collects these accounts receivable directly from the customer. The proceeds from the sales of these accounts receivable totaled $4,733 thousand and $11,345 thousand for the six months ended June 30, 2018 and 2017, respectively, and these sales resulted in pre-tax losses of $5 thousand and $34 thousand for the six months ended June 30, 2018 and 2017, respectively, which are included in selling, general and administrative expenses in the consolidated statements of operations. Net proceeds of this accounts receivable sale program are recognized in the consolidated statements of cash flows as part of operating cash flows.

The Company uses receivable discount programs with certain customers. These discount arrangements allow the Company to accelerate collection of customers receivables.

3. Inventories

Inventories as of June 30, 2018 and December 31, 2017 consist of the following (in thousands):

	June 30, 2018	December 31, 2017
Finished goods	$ 10,953	$ 13,737
Semi-finished goods and work-in-process	35,862	53,148
Raw materials	14,502	12,445
Materials in-transit	838	134
Less: inventory reserve	(4,699)	(6,391)
Inventories, net	$ 57,456	$ 73,073

Changes in inventory reserve for the three and six months ended June 30, 2018 and 2017 are as follows (in thousands):

	Three Months Ended June 30, 2018	Six Months Ended June 30, 2018	Three Months Ended June 30, 2017	Six Months Ended June 30, 2017
Beginning balance	$ (4,672)	$ (6,391)	$ (7,966)	$ (7,177)
Change in reserve				
Inventory reserve charged to costs of sales	(1,504)	(2,515)	(1,399)	(2,286)
Sale of previously reserved inventory	898	1,118	2,943	3,445
	(606)	(1,397)	1,544	1,159
Write off	339	2,863	983	1,150
Translation adjustments	240	226	142	(429)
Ending balance	$ (4,699)	$ (4,699)	$ (5,297)	$ (5,297)

Inventory reserve represents the Company s best estimate in value lost due to excessive inventory level, physical deterioration, obsolescence, changes in price levels, or other causes based on individual facts and circumstances. Inventory reserve relates to inventory items including finished goods, semi-finished goods and work-in-process. Write off of this reserve is recognized only when the related inventory has been disposed or scrapped.

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4. Property, Plant and Equipment

Property, plant and equipment as of June 30, 2018 and December 31, 2017 are comprised of the following (in thousands):

	June 30, 2018	December 31, 2017
Buildings and related structures	$ 70,194	$ 69,958
Machinery and equipment	302,207	308,713
Others	45,158	42,497
	417,559	421,168
Less: accumulated depreciation	(235,894)	(231,356)
Land	15,369	16,091
Property, plant and equipment, net	$ 197,034	$ 205,903

Aggregate depreciation expenses totaled $15,562 thousand and $13,233 thousand for the six months ended June 30, 2018 and 2017, respectively.

As of June 29, 2018, the Company s Korean subsidiary entered into an arrangement whereby it acquired a water treatment facility to support its fab in Gumi, Korea from SK Hynix for $4,172 thousand, and sold it for $4,172 thousand to a third party management company that the Company has engaged to run the facility for a 10-year term. This arrangement is accounted for as a financing due to the Company s Korean subsidiary s continuing involvement with the facility. As a result, as of June 30, 2018, the Company recorded the acquisition of water treatment facility of $4,172 thousand as property, plant and equipment, net, and the related liabilities of $553 thousand as other current liabilities and $3,619 thousand as other non-current liabilities, which relates to the financing and service portion of the arrangement.

5. Intangible Assets

Intangible assets as of June 30, 2018 and December 31, 2017 are comprised of the following (in thousands):

	June 30, 2018		
	Gross amount	Accumulated amortization	Net amount
Technology	$ 19,288	$ (19,288)	$
Customer relationships	27,702	(27,702)	
Intellectual property assets	11,180	(7,214)	3,966
Intangible assets, net	$ 58,170	$ (54,204)	$ 3,966

	December 31, 2017		
	Gross amount	Accumulated amortization	Net amount
Technology	$ 20,194	$ (20,194)	$
Customer relationships	29,002	(29,002)	
Intellectual property assets	11,319	(7,258)	4,061
Intangible assets, net	$ 60,515	$ (56,454)	$ 4,061

Aggregate amortization expenses for intangible assets totaled $408 thousand and $298 thousand for the six months ended June 30, 2018 and 2017, respectively.

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6. Accrued Expenses

Accrued expenses as of June 30, 2018 and December 31, 2017 are comprised of the following (in thousands):

	June 30, 2018	December 31, 2017
Payroll, benefits and related taxes, excluding severance benefits	$ 16,378	$ 16,724
Withholding tax attributable to intercompany interest income	19,264	18,138
Interest on senior notes	8,268	8,268
Outside service fees	1,089	1,942
Others	4,507	6,674
Accrued expenses	$ 49,506	$ 51,746

7. Derivative Financial Instruments

The Company s Korean subsidiary from time to time has entered into zero cost collar and forward contracts to hedge the risk of changes in the functional-currency-equivalent cash flows attributable to currency rate changes on U.S. dollar denominated revenues.

Details of derivative contracts as of June 30, 2018 are as follows (in thousands):

Date of transaction	Type of derivative	Total notional amount	Month of settlement
June 18, 2018	Zero cost collar	$ 20,000	September 2018 to December 2018
June 18, 2018	Forward	$ 40,000	September 2018 to December 2018
June 27, 2018	Zero cost collar	$ 32,000	September 2018 to June 2019
June 27, 2018	Forward	$ 58,000	September 2018 to June 2019

Details of derivative contracts as of December 31, 2017 are as follows (in thousands):

Date of transaction	Type of derivative	Total notional amount	Month of settlement
June 22, 2017	Zero cost collar	$ 20,000	January 2018 to February 2018
September 28, 2017	Zero cost collar	$ 54,000	January 2018 to June 2018
September 28, 2017	Forward	$ 36,000	January 2018 to June 2018

The zero cost collar and forward contracts qualify as cash flow hedges under ASC 815, Derivatives and Hedging, since at both the inception of the contracts and on an ongoing basis, the hedging relationship was and is expected to be highly effective in achieving offsetting cash flows attributable to the hedged risk during the term of the contracts. The Company is utilizing the hypothetical derivative method to measure the effectiveness by comparing the changes in value of the actual derivative versus the change in fair value of the hypothetical derivative.

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The fair values of the Company s outstanding zero cost collar and forward contracts recorded as assets and liabilities as of June 30, 2018 and December 31, 2017 are as follows (in thousands):

Derivatives designated as hedging instruments:		**June 30, 2018**	**December 31, 2017**
Asset Derivatives:			
Zero cost collars	Other current assets	$	$ 2,827
Forward	Other current assets	$	$ 2,352
Liability Derivatives:			
Zero cost collars	Other current liabilities	$ 684	$
Forward	Other current liabilities	$ 1,911	$

Offsetting of derivative liabilities as of June 30, 2018 is as follows (in thousands):

As of June 30, 2018	**Gross amounts of recognized liabilities**	**Gross amounts offset in the balance sheets**	**Net amounts of liabilities presented in the balance sheets**	**Gross amounts not offset in the balance sheets: Financial instruments**	**Gross amounts not offset in the balance sheets: Cash collateral received/ pledged**	**Net amount**
Liability Derivatives:						
Zero cost collars	$ 684	$	$ 684	$	$	$ 684
Forward	$ 1,911	$	$ 1,911	$	$	$ 1,911

Offsetting of derivative assets as of December 31, 2017 is as follows (in thousands):

As of December 31, 2017	**Gross amounts of recognized assets**	**Gross amounts offset in the balance sheets**	**Net amounts of assets presented in the balance sheets**	**Gross amounts not offset in the balance sheets: Financial instruments**	**Gross amounts not offset in the balance sheets: Cash collateral pledged**	**Net amount**
Asset Derivatives:						
Zero cost collars	$ 2,827	$	$ 2,827	$	$	$ 2,827
Forward	$ 2,352	$	$ 2,352	$	$	$ 2,352

For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of accumulated other comprehensive income (AOCI) and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative, representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness, are recognized in current earnings.

The following table summarizes the impact of derivative instruments on the consolidated statement of operations for the three months ended June 30, 2018 and 2017 (in thousands):

Derivatives in ASC 815	**Location of Gain**	**Location of Loss**

Cash Flow Hedging Relationships	Amount of Gain (Loss) Recognized in AOCI on Derivatives (Effective Portion)		Location of Gain (Loss) Reclassified from AOCI into Statement of Operations (Effective Portion)	Amount of Gain Reclassified from AOCI into Statement of Operations (Effective Portion)		Location of Loss Recognized in Statement of Operations on Derivative (Ineffective Portion)	Amount of Loss Recognized in Statement of Operations on Derivatives (Ineffective Portion)	
	Three Months Ended June 30,			Three Months Ended June 30,			Three Months Ended June 30,	
	2018	2017		2018	2017		2018	2017
Zero cost collars	$ (1,009)	$ (1,620)	Net sales	$ 865	$ 808	Other income (expenses), net	$ (247)	$ (368)
Forwards	$ (861)	$ 26	Net sales	$ 1,170	$	Other income (expenses), net	$ (1,385)	$ (99)
Total	$ (1,870)	$ (1,594)		$ 2,035	$ 808		$ (1,632)	$ (467)

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The following table summarizes the impact of derivative instruments on the consolidated statement of operations for the six months ended June 30, 2018 and 2017 (in thousands):

Derivatives in ASC 815 Cash Flow Hedging Relationships	Amount of Gain Recognized in AOCI on Derivatives (Effective Portion) Six Months Ended June 30, 2018	2017	Location of Gain Reclassified from AOCI into Statement of Operations (Effective Portion)	Amount of Gain Reclassified from AOCI into Statement of Operations (Effective Portion) Six Months Ended June 30, 2018	2017	Location of Gain (Loss) Recognized in Statement of Operations on Derivative (Ineffective Portion)	Amount of Gain (Loss) Recognized in Statement of Operations on Derivatives (Ineffective Portion) Six Months Ended June 30, 2018	2017
Zero cost collars	$ (1,142)	$ 883	Net sales	$ 2,191	$ 1,305	Other income (expenses), net	$ (318)	$ 269
Forwards	$ (795)	$ 26	Net sales	$ 2,450	$	Other income (expenses), net	$ (1,390)	$ (99)
Total	$ (1,937)	$ 909		$ 4,641	$ 1,305		$ (1,708)	$ 170

As of June 30, 2018, the amount expected to be reclassified from accumulated other comprehensive loss into loss within the next twelve months is $1,280 thousand.

The Company set aside $10,100 thousand and $7,600 thousand of cash deposits to the counterparty, Nomura Financial Investment (Korea) Co., Ltd. (NFIK) as required for the zero cost collar and forward contracts outstanding as of June 30, 2018 and December 31, 2017, respectively. These cash deposits are recorded as hedge collateral on the consolidated balance sheets.

The Company is required to deposit additional cash collateral with NFIK for any exposure in excess of $500 thousand and no such cash collateral was required as of June 30, 2018 and December 31, 2017, respectively. These outstanding zero cost collar and forward contracts are subject to termination if the sum of qualified and unrestricted cash and cash equivalents held by the Company is less than $30,000 thousand on the last day of a fiscal quarter.

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8. Fair Value Measurements

Fair Value of Financial Instruments

As of June 30, 2018, the following table represents the Company s liabilities measured at fair value on a recurring basis and the basis for that measurement (in thousands):

	Carrying Value June 30, 2018	Fair Value Measurement June 30, 2018	Quoted Prices in Active Markets for Identical Asset (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Liabilities:					
Derivative liabilities (other current liabilities)	$ 2,595	$ 2,595		$ 2,595	

As of December 31, 2017, the following table represents the Company s assets measured at fair value on a recurring basis and the basis for that measurement (in thousands):

	Carrying Value December 31, 2017	Fair Value Measurement December 31, 2017	Quoted Prices in Active Markets for Identical Asset (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:					
Derivative assets (other current assets)	$ 5,179	$ 5,179		$ 5,179	

Items not reflected in the table above include cash equivalents, restricted cash, accounts receivable, other receivables, accounts payable, and other accounts payable, fair value of which approximate carrying values due to the short-term nature of these instruments. The fair value of assets and liabilities whose carrying value approximates fair value is determined using Level 2 inputs.

Fair Value of Long-term Borrowings

	June 30, 2018		December 31, 2017	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	(In thousands of US dollars)			
Long-term Borrowings:				
5.0% Exchangeable Senior Notes due March 2021 (Level 2)	$ 82,249	$ 131,100	$ 81,576	$ 127,617
6.625% Senior Notes due July 2021 (Level 2)	$ 222,240	$ 218,700	$ 221,840	$ 224,719

On January 17, 2017, the Company s wholly-owned subsidiary, MagnaChip Semiconductor S.A., closed an offering (the Exchangeable Notes Offering) of 5.0% Exchangeable Senior Notes due March 1, 2021 (the Exchangeable Notes) of $86,250 thousand, which represents the principal amount, excluding $5,902 thousand of debt issuance costs. The Company estimates the fair value of the Exchangeable Notes using the market approach, which utilizes quoted market prices that fall under Level 2. For further description of the Exchangeable Notes, see Note 9, Long-term Borrowings .

On July 18, 2013, the Company issued 6.625% senior notes due July 15, 2021 (the 2021 Notes) of $225.0 million, which represents the principal amount, excluding $1.1 million of original issue discount and $5.0 million of debt issuance costs. The Company estimates the fair value of the 2021 Notes using the market approach, which utilizes quoted market prices that fall under Level 2. For further description of the 2021 Notes, see Note 9, Long-term Borrowings .

Fair Values Measured on a Non-recurring Basis

The Company s non-financial assets, such as property, plant and equipment, and intangible assets are recorded at fair value upon acquisition and are remeasured at fair value only if an impairment charge is recognized. As of June 30, 2018 and 2017, the Company did not have any assets or liabilities measured at fair value on a non-recurring basis.

9. Long-Term Borrowings

Long-term borrowings as of June 30, 2018 and December 31, 2017 are as follows (in thousands):

	June 30, 2018	December 31, 2017
5.0% Exchangeable Senior Notes due March 2021	$ 86,250	$ 86,250
6.625% Senior Notes due July 2021	$ 225,000	$ 225,000
Less: unamortized discount and debt issuance costs	(6,761)	(7,834)
Long-term borrowings, net of unamortized discount and debt issuance costs	$ 304,489	$ 303,416

5.0% Exchangeable Senior Notes

On January 17, 2017, MagnaChip Semiconductor S.A. closed the Exchangeable Notes Offering of $86,250 thousand aggregate principal amount of 5.0% Exchangeable Notes. Interest on the Exchangeable Notes accrues at a rate of 5.0% per annum, payable semi-annually on March 1 and September 1 of each year, beginning on March 1, 2017. The Exchangeable Notes will mature on March 1, 2021, unless earlier repurchased or converted. Holders may convert their notes at their option at any time prior to the close of business on the business day immediately preceding the stated maturity date.

The Company used a portion of the net proceeds from the issuance to repurchase 1,795,444 shares of common stock under its stock repurchase program at an aggregate cost of $11,401 thousand.

Upon conversion, the Company will deliver for each $1,000 principal amount of converted notes a number of shares equally to the exchange rate, which will initially be 121.1387 shares of common stock per $1 thousand principal amount of Exchangeable Notes, equivalent to an initial exchange price of approximately $8.26 per share of common stock. The exchange rate will be subject to adjustment in some circumstances, but will not be adjusted for any accrued and unpaid interest. In addition, if a make-whole fundamental change (as defined in the Exchangeable Notes indenture (the Exchangeable Notes Indenture)) occurs prior to the stated maturity date, the Company will increase the exchange rate for a holder who elects to convert its notes in connection with such make-whole fundamental change in certain circumstances. MagnaChip Semiconductor S.A. may also, under certain circumstances, be required to pay additional amounts to holders of Exchangeable Notes if withholding or deduction is required in a relevant tax jurisdiction.

If the Company undergoes a fundamental change, subject to certain conditions, holders may require the Company to repurchase for cash all or part of their notes at a purchase price equal to 100% of the principal amount of the notes to be repurchased, plus accrued and unpaid interest to, but excluding, the fundamental change purchase date. In addition, upon certain events of default described in the Exchangeable Notes Indenture, the trustee or holders of at least 25% principal amount of the Exchangeable Notes may declare 100% of the then outstanding Exchangeable Notes due and payable in full, together with all accrued and unpaid interest thereon. Payment of principal on the Exchangeable Notes may also accelerate and become automatically due and payable upon certain events of default involving bankruptcy or insolvency proceedings involving the Company, MagnaChip Semiconductor S.A. and their significant subsidiaries. The Exchangeable Notes are not redeemable at the option of MagnaChip Semiconductor S.A. prior to the maturity date.

The Exchangeable Notes Indenture contains covenants that limit the ability of the Company, MagnaChip Semiconductor S.A. and the Company s other restricted subsidiaries to: (i) declare or pay any dividend or make any payment or distribution on account of or purchase or redeem the Company s capital stock or equity interests of the restricted subsidiaries; (ii) make any principal payment on, or redeem or repurchase, prior to any scheduled repayment or maturity, any subordinated indebtedness; (iii) make certain investments; (iv) incur additional indebtedness and issue certain types of capital stock; (v) create or incur any lien (except for permitted liens) that secures obligations under any indebtedness; (vi) merge with or into or sell all or substantially all of the Company s assets to other companies; (vii) enter into certain types of transactions with affiliates; (viii) guarantee the payment of any indebtedness; and (ix) designate unrestricted subsidiaries.

These covenants are subject to a number of exceptions and qualifications. Certain of these restrictive covenants will terminate if the Exchangeable Notes are rated investment grade at any time.

The Company incurred debt issuance costs of $5,902 thousand related to the issuance of the Exchangeable Notes. The debt issuance costs are recorded as a direct deduction from the long-term borrowings in the consolidated balance sheets and amortized to interest expense using the effective interest method over the term of the Exchangeable Notes. Interest expense related to the Exchangeable Notes for the three and six months ended June 30, 2018 were $1,418 thousand and $2,829 thousand, respectively. Interest expense related to the Exchangeable Notes for the three and six months ended June 30, 2017 were $1,395 thousand and $2,542 thousand, respectively.

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6.625% Senior Notes

On July 18, 2013, the Company issued a $225,000,000 aggregate principal amount of the 2021 Notes at a price of 99.5%. Interest on the 2021 Notes accrues at a rate of 6.625% per annum, payable semi-annually on January 15 and July 15 of each year, beginning on January 15, 2014.

The Company can optionally redeem all or a part of the 2021 Notes according to the following schedule: on or after July 15, 2017, the Company may on any one or more occasions redeem all or a part of the 2021 Notes, at a redemption price equal to 101.656% and 100% of the principal amount of the notes redeemed on or after July 15, 2018 and 2019, respectively, plus accrued and unpaid interest and special interest, if any, on the notes redeemed, to the applicable date of redemption.

The Indenture relating to the 2021 Notes contains covenants that limit the ability of the Company and its restricted subsidiaries to: (i) declare or pay any dividend or make any payment or distribution on account of or purchase or redeem the Company s capital stock or equity interests of the restricted subsidiaries; (ii) make any principal payment on, or redeem or repurchase, prior to any scheduled repayment or maturity, any subordinated indebtedness; (iii) make certain investments; (iv) incur additional indebtedness and issue certain types of capital stock; (v) create or incur any lien (except for permitted liens) that secures obligations under any indebtedness; (vi) merge with or into or sell all or substantially all of the Company s assets to other companies; (vii