SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORP
Form 20-F
June 27, 2008

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 20-F

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2007
Commission file number 1-31994

Semiconductor Manufacturing International Corporation
(Exact name of Registrant as specified in its charter)
(Translation of Registrant s name into English)

Cayman Islands
(Jurisdiction of incorporation or organization)
18 Zhangjiang Road, Pudong New Area, Shanghai, China 201203
(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act.

Title of each class	Name of each exchange on which registered
Ordinary Shares, par value US$0.0004	The Stock Exchange of Hong Kong Limited*
American Depositary Shares	The New York Stock Exchange, Inc.

Securities registered or to be registered pursuant to Section 12(g) of the Act.
None
(Title of Class)
Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.
None
(Title of Class)

Indicate the number of outstanding shares of each of the issuer s classes of capital or ordinary shares as of the close of the period covered by the annual report.

As of December 31, 2007, there were 18,558,919,712 ordinary shares, par value US$0.0004 per share, outstanding, of which 2,818,175,550 ordinary shares were held in the form of 56,363,511 ADSs. Each ADS represents 50 ordinary shares.

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

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934. Yes o No þ

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 þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Securities Exchange Act of 1934 (Check one):

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

Indicate by check mark which financial statement item the registrant has elected to follow. Item 17 o
Item 18 þ

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Securities Exchange Act of 1934). Yes o No þ

* Not for trading, but only in connection with the listing of American Depositary Shares on the New York Stock Exchange, Inc.

Table of Contents

CAUTIONARY STATEMENT FOR PURPOSES OF THE SAFE HARBOR PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

Table of Contents

Table of Contents

CAUTIONARY STATEMENT FOR PURPOSES OF THE SAFE HARBOR PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This annual report may contain, in addition to historical information, forward-looking statements within the meaning of the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. These forward-looking statements are based on SMIC s current assumptions, expectations and projections about future events. SMIC uses words like believe, anticipate, intend, estimate, expect, project and similar expressions to identify forward-looking statements, although not all forward-looking statements contain these words. These forward-looking statements are necessarily estimates reflecting the best judgment of SMIC s senior management and involve significant risks, both known and unknown, uncertainties and other factors that may cause SMIC s actual performance, financial condition or results of operations to be materially different from those suggested by the forward-looking statements including, among others, risks associated with cyclicality and market conditions in the semiconductor industry, intense competition, timely wafer acceptance by SMIC s customers, timely introduction of new technologies, SMIC s ability to ramp new products into volume, supply and demand for semiconductor foundry services, industry overcapacity, shortages in equipment, components and raw materials, availability of manufacturing capacity, orders or judgments from pending litigation, and financial stability in end markets.

Except as required by law, SMIC undertakes no obligation and does not intend to update any forward-looking statement, whether as a result of new information, future events or otherwise.

ADDITIONAL INFORMATION

References in this annual report to:

China or the PRC are to the People s Republic of China, excluding for the purpose of this annual report, Hong Kong, Macau and Taiwan;

HK$ are to Hong Kong dollars;

Rmb are to Renminbi, the legal currency of China;

US$ are to U.S. dollars;

SEHK or Hong Kong Stock Exchange are to The Stock Exchange of Hong Kong Limited;

SEC are to the U.S. Securities and Exchange Commission;

NYSE or New York Stock Exchange are to the New York Stock Exchange, Inc.;

global offering are to the initial public offering of our ADSs and our ordinary shares, which offering was completed on March 18, 2004; and

IPO registration statement are to our registration statement on Form F-1 (File No. 333-112720), as filed with the Securities and Exchange Commission on March 11, 2004, sections of which are incorporated by reference into this annual report.

All references in this annual report to silicon wafer quantities are to 8-inch wafer equivalents, unless otherwise specified. Conversion of quantities of 12-inch wafers to 8-inch wafer equivalents is achieved by multiplying the number of 12-inch wafers by 2.25. When we refer to the capacity of wafer fabrication facilities, we are referring to the installed capacity based on specifications established by the manufacturers of the equipment used in those facilities. References to key process technology nodes, such as 0.35 micron, 0.25 micron, 0.18 micron, 0.15 micron, 0.13 micron, 90 nanometer include the stated resolution of the process technology, as well as intermediate resolutions down to but not including the next key process technology node of finer resolution. For example, when we state 0.25 micron process technology, that also includes 0.22 micron, 0.21 micron, 0.20 micron and 0.19 micron technologies, 0.18 micron process technology also includes 0.17 micron and 0.16 micron technologies; 0.15 micron process

technology

Table of Contents

includes 0.14 micron technology; and 0.13 micron process technology includes 0.11 micron and 0.10 micron technologies.

References to U.S. GAAP mean the generally accepted accounting principles in the United States. Unless otherwise indicated, our financial information presented in this annual report has been prepared in accordance with U.S. GAAP.

All references to our ordinary shares in this annual report gives effect to the 10-for-1 share split we effected in the form of a share dividend immediately prior to the completion of the global offering. All references to price per ordinary share and price per preference share reflect the share split referenced above.

The Glossary of Technical Terms contained in Annex A of this annual report sets forth the description of certain technical terms and definitions used in this annual report.

This annual report contains translations of certain Hong Kong dollar and Renminbi amounts into U.S. dollars at specified rates. All translations from Hong Kong dollars and Renminbi to U.S. dollars were made (unless otherwise indicated) at the noon buying rates in The City of New York for cable transfers in Hong Kong dollars and Renminbi per US$1.00 as certified for customs purposes by the Federal Reserve Bank of New York. Unless otherwise stated, the translations of Hong Kong dollars and Renminbi into U.S. dollars have been made at the noon buying rates in effect on the date of the related transaction. No representation is made that the Hong Kong dollar, Renminbi or U.S. dollar amounts referred to in this offering circular could have been or could be converted into U.S. dollars, Hong Kong dollars or Renminbi, as the case may be, at any particular rate or at all. See Risk Factors Risks Related to Conducting Operations in China Devaluation or appreciation in the value of the Renminbi or restrictions on convertibility of the Renminbi could adversely affect our operating results and Risk Factors Risks Related to Our Financial Condition and Business Exchange rate fluctuations could increase our costs, which could adversely affect our operating results and the value of our ADSs for a discussion of the effects on our company of fluctuating exchange rates.

PART I

Item 1. Identity of Directors, Senior Management and Advisors

Not applicable.

Item 2. Offer Statistics and Expected Timetable

Not applicable.

Item 3. Key Information

Selected Consolidated Financial Data

The summary consolidated financial data presented below as of and for the years ended December 31, 2005, 2006 and 2007 are derived from, and should be read in conjunction with, and are qualified in their entirety by reference to, our audited consolidated financial statements, including the related notes, included elsewhere in this annual report. The selected consolidated financial data as of and for the years ended December 31, 2003 and 2004 is derived from our audited consolidated financial statements not included in this annual report. The summary consolidated financial data presented below has been prepared in accordance with U.S. GAAP.

Table of Contents

	For the year ended December 31,				
	2003	2004	2005	2006	2007
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Statement of Operations Data:					
Sales	$365,824	$974,664	$1,171,319	$1,465,323	$1,549,765
Cost of sales[(1)]	359,779	716,225	1,105,134	1,338,155	1,397,038
Gross profit	6,045	258,439	66,185	127,168	152,727
Operating expenses:					
Research and development	34,913	74,113	78,865	94,171	97,034
General and administrative	29,705	54,038	35,701	47,365	74,490
Selling and marketing	10,711	10,384	17,713	18,231	18,716
Litigation settlement		16,695			
Amortization of acquired intangible assets	3,462	14,368	20,946	24,393	27,071
Income from sale of plant and equipment and other fixed assets				(43,122)	(28,651)
Total operating expenses	78,791	169,598	153,225	141,038	188,659
Income (loss) from operations	(72,746)	88,841	(87,040)	(13,870)	(35,932)
Other income (expenses):					
Interest income	5,616	10,587	11,356	14,916	12,349
Interest expense	(1,425)	(13,698)	(38,784)	(50,926)	(37,936)
Foreign currency exchange gain (loss)	1,523	8,218	(3,355)	(21,912)	11,250
Other, net	888	2,441	4,462	1,821	2,238
Total other income (expense), net	6,602	7,548	(26,322)	(56,101)	(12,100)
Income (loss) before income tax	(66,144)	96,389	(113,362)	(69,971)	(48,032)
Income tax benefit (expense)		(186)	(285)	24,928	29,720
Minority interest			251	(19)	2,856
Loss from equity investment			(1,379)	(4,201)	(4,013)
Net (loss) income before cumulative effect of a change in accounting principle	(66,144)	96,203	(114,775)	(49,263)	(19,468)

Table of Contents

	For the year ended December 31,				
	2003	2004	2005	2006	2007
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Cumulative effect of a change in accounting principle				5,154	
Net (loss) income	(66,144)	96,203	(114,775)	(44,109)	(19,468)
Deemed dividend on preference shares[2]	37,117	18,840			
Income (loss) attributable to holders of ordinary shares	$ (103,261)	$ 77,363	$ (114,775)	$ (44,109)	$ (19,468)
Income (loss) per ordinary share, basic	$ (1.14)	$ 0.01	$ (0.00)	$ (0.00)	$ (0.00)
Income (loss) per ordinary share, diluted	$ (1.14)	$ 0.00	$ (0.00)	$ (0.00)	$ (0.00)
Ordinary shares used in calculating basic income (loss) per ordinary share[3][4]	90,983,200	14,199,163,517	18,184,429,255	18,334,498,923	18,501,940,489
Ordinary shares used in calculating diluted income (loss) per ordinary share[3][4]	90,983,200	17,934,393,066	18,184,429,255	18,334,498,923	18,501,940,489
Income (loss) per ADS, basic[5]		$ 0.27	$ (0.32)	$ (0.12)	$ (0.05)
Income (loss) per ADS, diluted[5]		$ 0.22	$ (0.32)	$ (0.12)	$ (0.05)
ADS used in calculating basic income (loss) per ADS[5]		283,983,270	363,688,585	366,689,978	370,038,810
ADS used in calculating diluted income (loss) per ADS[5]		358,687,861	363,688,585	366,689,978	370,038,810

Table of Contents

	For the year ended December 31,				
	2003	2004	2005	2006	2007
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Other Financial Data:					
Gross margin	1.7%	26.5%	5.7%	8.7%	9.9%
Operating margin	-19.9%	9.1%	-7.4%	-0.9%	-2.3%
Net margin	-18.1%	9.9%	-9.8%	-3.0%	-1.3%
Operating Data:					
Wafers shipped (in 8 equivalents)					
Total	476,451	943,463	1,347,302	1,614,888	1,849,957
ASP[6]	768	1,033	869	907	838

(1) Including amortization of deferred stock compensation for employees directly involved in manufacturing activities.

(2) Deemed dividend represents the difference between the sale and conversion prices of warrants to purchase convertible preference shares we issued and their respective fair market values.

(3) Anti-dilutive preference shares, options and warrants were excluded from the

weighted average ordinary shares outstanding for the diluted per share calculation.

(4) All share information have been adjusted retroactively to reflect the 10-for-1 share split effected upon completion of the global offering of its ordinary shares in March 2004 (the Global Offering).

(5) Fifty ordinary shares equals one ADS.

(6) Total sales/total wafers shipped.

	As of December 31,				
	2003	2004	2005	2006	**2007**
			(in US$ thousands)		
Balance Sheet Data:					
Cash and cash equivalents	$ 445,276	$ 607,173	$ 585,797	$ 363,620	**$ 469,284**
Short-term investments	27,165	20,364	13,796	57,951	**7,638**
Accounts receivable, net of allowances	90,539	169,188	241,334	252,185	**298,388**
Inventories	69,924	144,018	191,238	275,179	**248,310**
Total current assets	680,882	955,418	1,047,465	1,049,666	**1,075,302**
Land use rights, net	41,935	39,198	34,768	38,323	**57,552**
Plant and equipment, net	1,523,564	3,311,925	3,285,631	3,244,401	**3,202,958**
Total assets	2,290,506	4,384,276	4,586,633	4,541,292	**4,708,444**
Total current liabilities	325,430	723,871	896,038	677,362	**930,190**
Total long-term liabilities	479,961	544,462	622,497	817,710	**730,790**
Total liabilities	805,391	1,268,333	1,518,535	1,495,072	**1,660,980**
Minority interest			38,782	38,800	**34,944**

Stockholders equity	$1,485,115	$3,115,942	$ 3,029,316	$3,007,420	**$3,012,519**

	For the year ended December 31,				
	2003	2004	2005	**2**006	**2007**
	(in US$ thousands, except percentages and operating data)				
Cash Flow Data:					
Net income (loss)	$ (66,145)	$ 96,203	$(114,775)	$ (49,263)	$ **(19,468)**
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:					
Depreciation and amortization	233,905	456,961 8	769,472	919,616	**706,277**

Table of Contents

	For the year ended December 31,				
	2003	2004	2005	2006	**2007**
	(in US$ thousands, except percentages and operating data)				
Net cash provided by (used in) operating activities	114,270	518,662	648,105	769,649	**672,465**
Purchases of plant and equipment	(453,097)	(1,838,773)	(872,519)	(882,580)	**(717,171)**
Net cash used in investing activities	(454,498)	(1,826,787)	(859,652)	(917,369)	**(643,344)**
Net cash provided by financing activities	693,497	1,469,764	190,364	(74,440)	**76,637**
Net increase (decrease) in cash and cash equivalents	$ 353,412	$ 161,896	$ (21,376)	$ (222,177)	$ **105,664**
Other Financial Data:					
Gross margin	1.7%	26.5%	5.7%	8.7%	**9.9%**
Operating margin	-19.9%	9.1%	-7.4%	-0.9%	**-2.3%**
Net margin	-18.1%	9.9%	-9.8%	-3.0%	**-1.3%**
Operating Data:					
Wafers shipped (in units):					
Total[(1)]	476,451	943,463	1,347,302	1,614,888	1,849,957

(1) Including logic, DRAM, copper interconnects and all other wafers.

Risk Factors

Risks Related to Our Financial Condition and Business

We may not be able to achieve or maintain a level of profitability, primarily due to our high fixed costs and correspondingly high levels of depreciation expenses.

In 2006 and 2007, our losses from operations totaled $13.9 million and $35.9 million, respectively. We may not be able to achieve or maintain profitability on an annual or quarterly basis, primarily because our business is characterized by high fixed costs relating to equipment purchases, which result in correspondingly high levels of depreciation expenses. We will continue to incur high capital expenditures and depreciation expenses as we equip and ramp up additional fabs, expand our capacity at our existing fabs and construct new fabs. Accordingly, we may not be able to achieve or maintain profitability.

The cyclical nature of the semiconductor industry and periodic overcapacity in the industry make our business and operating results particularly vulnerable to economic downturns.

The semiconductor industry has historically been highly cyclical and, at various times, has experienced significant downturns characterized by fluctuations in end-user demand, reduced demand for integrated circuits, rapid erosion of average selling prices and production overcapacity. Companies in the semiconductor industry have expanded aggressively during periods of increased demand in order to have the capacity needed to meet expected demand in the future. If actual demand does not increase or declines, or if companies in the industry expand too aggressively in light of the actual increase in demand, the industry will generally experience a period in which industry-wide capacity exceeds demand. If industry-wide capacity exceeds demand, our operations would be subject to more intense competition, and our results of operations may suffer because of the resulting pricing pressure and capacity underutilization. Severe pricing pressure could result in the overall foundry industry becoming less profitable, at least for the duration of the downturn, and could prevent us from maintaining our current level of profitability. We expect

that industry cyclicality will continue. In addition, a slowdown in the growth in demand for, or the continued reduction in selling prices of, devices that use semiconductors may decrease the demand for our services and reduce our profit margins. If we cannot take appropriate or effective actions in a timely manner during future downturns, such as reducing our costs to sufficiently offset declines in demand for our services, our business and operating results may be adversely affected.

Table of Contents

Our results of operations may fluctuate from year to year, which may make it difficult to predict our future performance and may result in a decline in the prices of our ordinary shares and ADSs if we fail to meet our expectations or those of the public market analysts and investors in these periods.

Our sales, expenses, and results of operations may fluctuate significantly from year to year due to a number of factors, many of which are outside our control. Our business and operations are subject to a number of factors, including:

- our customers sales outlook, purchasing patterns and inventory adjustments based on general economic conditions or other factors;
- the loss of one or more key customers or the significant reduction or postponement of orders from such customers;
- timing of new technology development and the qualification of this technology by our customers;
- timing of our expansion and development of our facilities;
- our ability to obtain equipment and raw materials; and
- our ability to obtain financing in a timely manner.

Due to the factors noted above and other risks discussed in this section, many of which are beyond our control, you should not rely on year-to-year comparisons to predict our future performance. Unfavorable changes in any of the above factors may adversely affect our business and operating results. In addition, our operating results may be below the expectations of public market analysts and investors in some future periods.

If the recent trend of increasing demand for foundry services reverses or slows down, we may achieve a lower rate of return on investments than anticipated and our business and operating results will be adversely affected.

The demand for foundry services by IDMs, fabless semiconductor companies and systems companies has been increasing in recent years. We have made and are planning to make significant investments in anticipation of the continuation of this trend. A reversal of, or slowdown in, this trend will likely result in a lower rate of return on our investments than anticipated. For example, if IDMs change their strategy and target greater internal production or become dissatisfied with the services of independent foundry service providers, such as our company, they may reduce their outsourcing of wafer fabrication. In addition, in the event of an industry downturn, in order to maintain their equipment s utilization rates, these IDMs may allocate a smaller portion of their fabricating needs to foundry service providers and perform a greater amount of foundry services for system companies and fabless semiconductor companies. If this occurs, our business and operating results will be adversely affected.

If we are unable to maintain high capacity utilization, optimize the technology and product mix of our services or improve our yields, our margins may substantially decline, thereby adversely affecting our operating results.

Our ability to achieve and maintain profitability depends, in part, on our ability to:

- maintain high capacity utilization, which is the actual number of wafers we produce in relation to our capacity;
- optimize our technology and product mix, which is the relative number of wafers fabricated utilizing higher margin technologies as compared to commodity and lower margin technologies; and
- continuously maintain and improve our yield, which is the percentage of usable fabricated devices on a wafer.

Table of Contents

Our capacity utilization affects our operating results because a large percentage of our costs are fixed. In general, more advanced technologies sell for higher prices and higher margins. Therefore, our technology and product mix has a direct impact upon our average selling prices and overall margins. Our yields directly affect our ability to attract and retain customers, as well as the price of our services. If we are unable to maintain high capacity utilization, optimize the technology and product mix of our wafer production and continuously improve our yields, our margins may substantially decline, thereby adversely affecting our operating results.

Our rapid growth has presented significant challenges to our management and administrative systems and resources, and as a result, we may experience difficulties managing our growth, which may adversely affect our business and operating results.

Since our inception in 2000, we have grown rapidly. Our wafer shipment and sales grew from zero in 2000 to 1,849,957 wafers and US$1.5 billion in 2007. During this period, we commenced commercial production at two 8-inch fabs (which includes our Shanghai megafab and Tianjin fab) and one 12-inch fab, and the range of process technologies we offered grew significantly. We are also in the process of ramping up one additional 12-inch fab at our Shanghai site and have already undertaken management contracts to manage the operations of wafer manufacturing facilities in Chengdu and Wuhan, China. In addition, we are preparing to construct one additional 8-inch and one additional 12-inch fab in Shenzhen. At December 31, 2000, we had 122 employees; and at December 31, 2007, we had 10,105 employees. We plan to hire a significant number of additional employees as our fabs in Tianjin, Beijing, and Shanghai increase in production capacity. This expansion, as well as our participation in a joint venture with Toppan Printing Co., Ltd. and an assembly and testing facility in Chengdu, and the management of wafer manufacturing facilities in Chengdu and Wuhan, China, have presented, and continue to present, significant challenges for our management and administrative systems and resources. If we fail to develop and maintain management and administrative systems and resources sufficient to keep pace with our planned growth, we may experience difficulties managing our growth and our business and operating results could be adversely affected.

If we lose one or more of our key personnel without obtaining adequate replacements in a timely manner or if we are unable to retain and recruit skilled personnel, our operations could become disrupted and the growth of our business could be delayed or restricted.

Our success depends on the continued service of our key executive officers, and in particular, Richard Ru Gin Chang, our President and Chief Executive Officer. We do not carry key person insurance on any of our personnel. If we lose the services of any of our key executive officers, it could be very difficult to find, relocate and integrate adequate replacement personnel into our operations, which could seriously harm our operations and the growth of our business.

We will require an increased number of experienced executives, engineers and other skilled employees in the future to implement our growth plans. There is intense competition for the services of these personnel in the semiconductor industry. In addition, we expect demand for skilled and experienced personnel in China to increase in the future as new wafer fabrication facilities and other similar high technology businesses are established there. If we are unable to retain our existing personnel or attract, assimilate and retain new experienced personnel in the future, our operations could become disrupted and the growth of our business could be delayed or restricted.

Our customers generally do not place purchase orders far in advance, which makes it difficult for us to predict our future sales, adjust our production costs and efficiently allocate our capacity on a timely basis and could therefore have an adverse effect on our business and operating results.

Our customers generally do not place purchase orders far in advance of the required shipping dates. In addition, due to the cyclical nature of the semiconductor industry, our customers purchase orders have varied significantly from period to period. As a result, we do not typically operate with any significant backlog, which makes it difficult for us to forecast our sales in future periods. Also, since our cost of sales and operating expenses have high fixed cost components, including depreciation and employee costs, we may be unable to adjust our cost structure in a timely manner to compensate for shortfalls in sales. Our

Table of Contents

current and anticipated customers may not place orders with us in accordance with our expectations or at all. As a result, it may be difficult to plan our capacity, which requires significant lead time to ramp-up and cannot be altered easily. If our capacity does not match our customer demand, we will either be burdened with expensive and unutilized overcapacity or unable to support our customers requirements, both of which could have an adverse effect on our business and results of operations.

Our sales cycles can be long, which could adversely affect our operating results and cause our income stream to be unpredictable.

Our sales cycles, which measure the time between our first contact with a customer and the first shipment of product orders to the customer, vary substantially and can last as long as one year or more, particularly for new technologies. Sales cycles to IDM customers typically take relatively longer since they usually require our engineers to become familiar with the customer s proprietary technology before production can commence. In addition, even after we make the initial product shipments, it may take the customer several more months to reach full production of that product using our foundry services. As a result of these long sales cycles, we may be required to invest substantial time and incur significant expenses in advance of the receipt of any product order and related revenue. Orders ultimately received may not be in accordance with our expectation with respect to product, volume, price or other terms, which could adversely affect our operating results and cause our income stream to be unpredictable.

We must consistently anticipate trends in technology development or else we will be unable to maintain or increase our business and operating margins.

The semiconductor industry is developing rapidly and the related technology is constantly evolving. If we are unable to anticipate the trends in technology development and rapidly develop and implement new and innovative technology that our customers require, we may not be able to produce sufficiently advanced products at competitive prices. As the life cycle for a process technology matures, the average selling price falls. Accordingly, unless we continually upgrade our capability to manufacture any new products that our customers design, our customers may use the services of our competitors instead of ours and the average selling prices of our wafers may fall, which could adversely affect our business and operating margins.

Our sales are dependent upon a small number of customers and any decrease in sales to any of them could adversely affect our results of operations.

We have been dependent on a small number of customers for a substantial portion of our business. For the year ended December 31, 2007, our five largest customers accounted for 60.0% of our total sales. We expect that we will continue to be dependent upon a relatively limited number of customers for a significant portion of our sales. Sales generated from these customers, individually or in the aggregate, may not reach or exceed our expectations or historical levels in any future period. Our sales could be significantly reduced if any of these customers cancels or reduces its orders, significantly changes its product delivery schedule, or demands lower prices, which could have an adverse effect on our results of operations.

Since our operating cash flows will not be sufficient to cover our planned capital expenditures, we will require additional external financing, which may not be available on acceptable terms or at all. Any failure to raise adequate funds in a timely manner could adversely affect our business and operating results.

In 2007, our capital expenditures totaled approximately US$860 million and we currently expect our capital expenditures in 2008 to total approximately US$700 million. These capital expenditures will be used primarily to expand our operations at our mega-fabs in Shanghai and Beijing and fab in Tianjin. In addition, our actual expenditures may exceed our planned expenditures for a variety of reasons, including changes in our business plan, our process technology, market conditions, equipment prices, customer requirements or interest rates. Future acquisitions, mergers, strategic investments, or other developments also may require additional financing. The amount of capital required to meet our growth and development targets is difficult to predict in the highly cyclical and rapidly changing semiconductor industry.

Table of Contents

Our operating cash flows may not be sufficient to meet our capital expenditure requirements in 2008. If our operating cash flows are insufficient, we plan to fund the expected shortfall through bank loans. If necessary, we will also explore other forms of external financing. Our ability to obtain external financing is subject to a variety of uncertainties, including:

- our future financial condition, results of operations and cash flows;
- general market conditions for financing activities of semiconductor companies;
- our future stock price; and
- our future credit rating.

External financing may not be available in a timely manner, on acceptable terms, or at all. Since our capacity expansion is a key component of our overall business strategy, any failure to raise adequate funds could adversely affect our business and operating results.

The construction and equipping of new fabs and the expansion of existing fabs are subject to certain risks that could result in delays or cost overruns, which could require us to expend additional capital and adversely affect our business and operating results.

We plan to continue to expand our business through the development of new fabs. There are a number of events that could delay these expansion projects or increase the costs of building and equipping these or future fabs in accordance with our plans. Such potential events include, but are not limited to:

- shortages and late delivery of building materials and facility equipment;
- delays in the delivery, installation, commissioning and qualification of our manufacturing equipment;
- seasonal factors, such as a long and intensive wet season that limits construction;
- labor disputes;
- design or construction changes with respect to building spaces or equipment layout;
- delays in securing the necessary governmental approvals and land use rights; and
- technological, capacity and other changes to our plans for new fabs necessitated by changes in market conditions.

As a result, our projections relating to capacity, process technology capabilities or technology developments may significantly differ from actual capacity, process technology capabilities or technology developments.

Delays in the construction and equipping or expansion of any of our fabs could result in the loss or delayed receipt of earnings, an increase in financing costs, or the failure to meet profit and earnings projections, any of which could adversely affect our business and operating results.

If we cannot compete successfully in our industry, particularly in China, our results of operations and financial condition will be adversely affected.

The worldwide semiconductor foundry industry is highly competitive. We compete with other foundries, such as TSMC, United Microelectronics Corporation, or UMC, and Chartered Semiconductor Manufacturing Ltd., or Chartered Semiconductor, as well as the foundry services offered by some IDMs, such as IBM. We also compete with smaller semiconductor foundries in China, Korea, Malaysia and other countries. Some of our competitors have greater access to capital and substantially higher capacity, longer or more established relationships with their customers, superior research and development capability, and greater marketing and other resources than we do. As a result, these companies may be able to compete more aggressively over a longer period of time than we can.

Table of Contents

Our competitors have established operations in mainland China in order to compete for the growing domestic market in China. TSMC has commenced commercial production at its fab in China, and UMC has established a relationship with a fab in commercial production in China. We understand that the ability of these fabs to manufacture wafers using certain more advanced technologies is subject to restrictions by the home jurisdiction of TSMC and UMC. Such restrictions could be reduced or lifted at any time, which may lead to increased domestic competition with such competitors and adversely affect our business and operating results.

Our ability to compete successfully depends to some extent upon factors outside of our control, including import and export controls, exchange controls, exchange rate fluctuations, interest rate fluctuations and political developments. If we cannot compete successfully in our industry or are unable to maintain our position as a leading foundry in China, our results of operations and financial condition will be adversely affected.

We may be unable to obtain in a timely manner and at a reasonable cost the equipment necessary for our business and therefore may be unable to achieve our expansion plans or meet our customers orders, which could negatively impact our competitiveness, financial condition and results of operations.

The semiconductor industry is capital-intensive and requires investment in advanced equipment that is available from a limited number of manufacturers. The market for equipment used in semiconductor foundries is characterized, from time to time, by significant demand, limited supply and long delivery cycles. Our business plan depends upon our ability to obtain our required equipment in a timely manner and at acceptable prices. During times of significant demand for the types of equipment we use, lead times for delivery can be as long as one year. Shortages of equipment could result in an increase in equipment prices and longer delivery times. If we are unable to obtain equipment in a timely manner and at a reasonable cost, we may be unable to achieve our expansion plans or meet our customers orders, which could negatively impact our competitiveness, financial condition, and results of operations.

We expect to have an ongoing need to obtain licenses for the proprietary technology of others, which subjects us to the payment of license fees and potential delays in the development and marketing of our products.

While we continue to develop and pursue patent protection for our own technologies, we expect to continue to rely on third party license arrangements to enable us to manufacture certain advanced wafers. As of December 31, 2007, we had been granted two hundred and nine patents worldwide, of which, forty-eight are in Taiwan, thirty five are in the U.S., and one hundred and twenty six are in China, whereas we believe our competitors and other industry participants have been issued numerous patents concerning wafer fabrication in multiple jurisdictions. Our limited patent portfolio may in the future adversely affect our ability to obtain licenses to the proprietary technology of others on favorable license terms due to our inability to offer cross-licensing arrangements. The fees associated with such licenses could adversely affect our financial condition and operating results. They might also render our services less competitive. If for any reason we are unable to license necessary technology on acceptable terms, it may become necessary for us to develop alternative technology internally, which could be costly and delay the marketing and delivery of key products and therefore have an adverse effect on our business and operating results. In addition, we may be unable to independently develop the technology required by our customers on a timely basis or at all, in which case our customers may purchase wafers from our competitors.

We may be subject to claims of intellectual property rights infringement owing to the nature of our industry, our limited patent portfolio and limitations of the indemnification provisions in our technology license agreements. These claims could adversely affect our business and operating results.

There is frequent intellectual property litigation, involving patents, copyrights, trade secrets, mask works and other intellectual property subject matters, in our industry. In some cases, a company can avoid or settle litigation on favorable terms because it possesses patents that can be asserted against the plaintiff. The limited size of our current patent portfolio will not likely place us in such a bargaining position. Moreover, some of our technology license agreements with our major technology partners do not provide for us to be indemnified in the event that the processes we license pursuant to such agreements infringe

Table of Contents

third party intellectual property rights. We could be sued for allegedly infringing one or more patents as to which we will be unable to obtain a license and unable to design around. As a result, we would be foreclosed from manufacturing or selling the products which are dependent upon such technology, which could have a material adverse effect on our business. We may litigate the issues of whether these patents are valid or infringed, but in the event of a loss we could be required to pay substantial monetary damages and be enjoined from further production or sale of such products.

If we breach the terms and conditions of the settlement agreement regarding the patent and trade secret litigation with TSMC, we may be required to accelerate the payment of the then outstanding amounts due under the settlement agreement. If we are unable to successfully defend ourselves within the current ongoing litigation with TSMC, we may be required to pay damages, obtain a license from TSMC, or discontinue sales of certain of our products.

In December 2003, we became the subject of a lawsuit in U.S. federal district court brought by TSMC relating to alleged infringement of five U.S. patents and misappropriation of alleged trade secrets relating to methods for conducting semiconductor fab operations and manufacturing integrated circuits. After the dismissal without prejudice of the trade secret misappropriation claims by the U.S. federal district court on April 21, 2004, TSMC refiled the same claims in California State Superior Court and alleged infringement of an additional 6 patents in the U.S. federal district court lawsuit. In August 2004, TSMC filed a complaint with the U.S. International Trade Commission (ITC) alleging similar trade secret misappropriation claims and asserting 3 new patent infringement claims and simultaneously filed another patent infringement suit in federal district court on the same 3 patents as alleged in the ITC complaint. Prior to the start of the initial lawsuit in the United States, TSMC had instituted a legal proceeding in Taiwan in January 2002 that alleged improper hiring practices and trade secret misappropriation. In the Taiwan proceeding, the Hsinchu District Court in Taiwan issued an ex parte provisional injunction that prohibits our wholly owned subsidiary, Semiconductor Manufacturing International (Shanghai) Corporation, or SMIC Shanghai, and Richard Ru Gin Chang, our president and chief executive officer, from improperly soliciting or hiring certain categories of employees of TSMC or causing such employees to divulge to us, or use, trade secrets of TSMC.

On January 31, 2005, we entered into a settlement agreement with TSMC that provides for the dismissal of all pending legal actions without prejudice between TSMC and our company in U.S. federal district court, California State Superior Court, the ITC and Taiwan District Court. In the settlement agreement, TSMC covenants not to sue us for itemized acts of trade secret misappropriation as alleged in the complaints, although the settlement does not grant a license to use any of TSMC s trade secrets. Furthermore, the parties also entered into a patent cross-license agreement under which each party will license the other party s patent portfolio through December 2010. As a part of the settlement, we also agreed to pay TSMC an aggregate amount of US$175 million, in installments of US$30 million each year for five years and US$25 million in the sixth year.

On August 25, 2006, TSMC filed a lawsuit against the Company and certain subsidiaries (SMIC (Shanghai), SMIC (Beijing) and SMIC (Americas) in the Superior Court of the State of California, County of Alameda for alleged breach of the Settlement Agreement, alleged breach of promissory notes and alleged trade secret misappropriation by the Company. TSMC seeks, among other things, damages, injunctive relief, attorneys fees, and the acceleration of the remaining payments outstanding under the Settlement Agreement.

On September 13, 2006, the Company announced that in addition to filing a response strongly denying the allegations of TSMC in the United States lawsuit, it filed on September 12, 2006, a cross-complaint against TSMC seeking, among other things, damages for TSMC s breach of contract and breach of implied covenant of good faith and fair dealing.

On November 16, 2006, the High Court in Beijing, the People s Republic of China, accepted the filing of a complaint by the Company and its wholly-owned subsidiaries, SMIC (Shanghai) and SMIC (Beijing), regarding the unfair competition arising from the breach of bona fide (i.e. integrity, good faith) principle and commercial defamation by TSMC (PRC Complaint). In the PRC Complaint, the Company is seeking, among other things, an injunction to stop TSMC s infringing acts, public apology from TSMC

Table of Contents

to the Company and compensation from TSMC to the Company, including profits gained by TSMC from their infringing acts.

TSMC filed with the California court in January 2007 a motion seeking to enjoin the PRC action. In February 2007, TSMC filed with the Beijing High Court a jurisdictional objection, challenging the competency of the Beijing High Court s jurisdiction over the PRC action.

In March 2007, the California Court denied TSMC s motion to enjoin the PRC action. TSMC has appealed this ruling to California Court of Appeal. On March 26, 2008, the Court of Appeal, in a written opinion, denied TSMC s appeal. That decision is now final and unappealable.

In July 2007, the Beijing High Court denied TSMC s jurisdictional objection and issued a court order holding that the Beijing High Court shall have proper jurisdiction to try the PRC action. TSMC has appealed this order to the Supreme Court of the People s Republic of China. On January 7, 2008, the Supreme Court heard TSMC s appeal. On May 29, 2008, the Supreme Court denied TSMC s appeal and confirmed the jurisdiction of the Beijing High Court.

On August 14, 2007, the Company filed an amended cross-complaint against TSMC seeking, among other things, damages for TSMC s breach of contract and breach of patent license agreement. TSMC thereafter denied the allegations of the Company s amended cross-complaint and attempted to file additional claims that the Company breached the Settlement Agreement by filing an action in the Beijing High Court. Upon the Company s motion, the California Court struck TSMC s new claims as procedurally improper, but granted TSMC leave to replead its claims.

On August 15-17, 2007, the California Court held a preliminary injunction hearing on TSMC s motion to enjoin use of certain process recipes in certain of the Company s 0.13 micron logic process flows. On September 7, the Court denied TSMC s preliminary injunction motion, thereby leaving unaffected the Company s development and sales. However, the court required the Company to provide 10 days advance notice to TSMC if the Company plans to disclose logic technology to non-SMIC entities under certain circumstances, to allow TSMC to object to the planned disclosure.

On March 11, 2008, TSMC filed an application for a right to attach order in the California Court. By its application, TSMC sought an order securing an amount equal to the remaining balance on the promissory notes issued by the Company in connection with the Settlement Agreement.

In May 2008, TSMC filed a motion in the California Court for summary adjudication against the Company on several of the Company s cross claims. The Company will oppose the motion. A hearing has been set on the motion for July 25, 2008.

On June 23, 2008, the Company filed with California court a cross-complaint against TSMC seeking, among other things, damages for TSMC s unlawful stealing of trade secrets from SMIC to improve its competitive position against SMIC.

On June 25, 2008, the Court issued an order denying TSMC s application for a right to attach order.

If TSMC were to succeed on its claims in the United States, we may be ordered to pay damages for breach of contract and discontinue sales of certain of our products in the United States or elsewhere.

The occurrence of any of these events could have a material adverse effect on our business and operating results and, in any event, the cost of litigation could be substantial.

Table of Contents

If our relationships with our technology partners deteriorate or we are unable to enter into new technology alliances, we may not be able to continue providing our customers with leading edge process technology, which could adversely affect our competitive position and operating results.

Enhancing our process technologies is critical to our ability to provide high quality services for our customers. We intend to continue to advance our process technologies through internal research and development efforts and technology alliances with other companies. Although we have an internal research and development team focused on developing new process technologies, we depend upon our technology partners to advance our portfolio of process technologies. We currently have joint technology development arrangements and technology sharing arrangements with several companies and research institutes. If we are unable to continue our technology alliances with these entities, or maintain on mutually beneficial terms any of our other joint development arrangements, research and development alliances and other similar agreements, or are unable to enter into new technology alliances with other leading developers of semiconductor technology, we may not be able to continue providing our customers with leading edge process technology, which could adversely affect our competitive position and operating results.

Global or regional economic, political and social conditions could adversely affect our business and operating results.

External factors such as potential terrorist attacks, acts of war, financial crises or geopolitical and social turmoil in those parts of the world that serve as markets for our products could significantly adversely affect our business and operating results in ways that cannot presently be predicted. These uncertainties could make it difficult for our customers and us to accurately plan future business activities. More generally, these geopolitical, social and economic conditions could result in increased volatility in worldwide financial markets and economies that could adversely impact our sales. We are not insured for losses and interruptions caused by terrorist acts or acts of war. Therefore, any of these events or circumstances could adversely affect our business and operating results.

Exchange rate fluctuations could increase our costs, which could adversely affect our operating results and the value of our ADSs.

Our financial statements are prepared in U.S. dollars. Our sales are generally denominated in U.S. dollars and our operating expenses and capital expenditures are generally denominated in U.S. dollars, Japanese Yen, Euros and Renminbi. Although we enter into foreign currency forward exchange contracts, we are still affected by fluctuations in exchange rates between the U.S. dollar and each of the Japanese Yen, the Euro and the Renminbi. Any significant fluctuations among these currencies may lead to an increase in our costs, which could adversely affect our operating results. See Risks Related to Conducting Operations in China Devaluation or appreciation in the value of the Renminbi or restrictions on convertibility of the Renminbi could adversely affect our business and operating results for a discussion of risks relating to the Renminbi.

Fluctuations in the exchange rate of the Hong Kong dollar against the U.S. dollar will affect the U.S. dollar value of the ADSs, since our ordinary shares are listed and traded on the Hong Kong Stock Exchange and the price of such shares are denominated in Hong Kong dollars. While the Hong Kong government has continued to pursue a fixed exchange rate policy, with the Hong Kong dollar trading in the range of HK$7.75 to HK$7.85 per US$1.00, we cannot assure you that such policy will be maintained. Exchange rate fluctuations also will affect the amount of U.S. dollars received upon the payment of any cash dividends or other distributions paid in Hong Kong dollars and the Hong Kong dollar proceeds received from any sales of ordinary shares. Therefore, such fluctuations could also adversely affect the value of our ADSs.

If we fail to maintain an effective system of internal control over financial reporting, we may not be able to accurately report our financial results or prevent fraud and, because of the inherent limitation of internal control over financial reporting, material misstatements due to error or fraud may not be prevented or detected on a timely basis.

Table of Contents

We are subject to reporting obligations under the United States securities laws. The Securities and Exchange Commission, or the SEC, as required by Section 404 of the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, adopted rules requiring every public company to include a management report on such company s internal controls over financial reporting in its annual report, which contains management s assessment of the effectiveness of the company s internal controls over financial reporting. In addition, an independent registered public accounting firm must attest to the effectiveness of the company s internal controls over financial reporting. Our management has concluded that our internal controls over our financial reporting as of December 31, 2007 are effective. However, we cannot assure you that in the future we or our independent registered public accounting firm will not identify material weaknesses during the Section 404 of the Sarbanes-Oxley Act audit process or for other reasons. In addition, because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. As a result, if we fail to maintain effective internal controls over financial reporting or should we be unable to prevent or detect material misstatements due to error or fraud on a timely basis, investors could lose confidence in the reliability of our financial statements, which in turn could harm our business and negatively impact the trading price of our securities. Furthermore, we have incurred and expect to continue to incur considerable costs and to use significant management time and other resources in an effort to comply with Section 404 and other requirements of the Sarbanes-Oxley Act.

Table of Contents

Risks Related to Manufacturing

Our manufacturing processes are highly complex, costly and potentially vulnerable to impurities and other disruptions, which could significantly increase our costs and delay product shipments to our customers.

Our manufacturing processes are highly complex, require advanced and costly equipment, demand a high degree of precision and may have to be modified to improve yields and product performance. Dust and other impurities, difficulties in the fabrication process or defects with respect to the equipment or facilities used can lower yields, cause quality control problems, interrupt production or result in losses of products in process. As system complexity has increased and process technology has become more advanced, manufacturing tolerances have been reduced and requirements for precision have become even more demanding. As a result, we may experience production difficulties, which could significantly increase our costs and delay product shipments to our customers.

We may have difficulty in ramping up production, which could cause delays in product deliveries and loss of customers and adversely affect our business and operating results.

As is common in the semiconductor industry, we may experience difficulty in ramping up production at new or existing facilities, such as our Beijing mega-fab and our fab in Tianjin in which we expect to add a significant amount of new equipment. This could be due to a variety of factors, including hiring and training of new personnel, implementing new fabrication processes, recalibrating and requalifying existing processes and the inability to achieve required yield levels.

In the future, we may face construction delays or interruptions, infrastructure failure, or delays in upgrading or expanding existing facilities or changing our process technologies, which may adversely affect our ability to ramp up production in accordance with our plans. Our failure to ramp up our production on a timely basis could cause delays in product deliveries, which may result in the loss of customers and sales. It could also prevent us from recouping our investments in a timely manner or at all, and adversely affect our business and operating results.

We have formed joint ventures that, if not successful, may adversely impact our business and operating results.

In July 2004, we announced an agreement with Toppan Printing Co., Ltd., to establish Toppan SMIC Electronics (Shanghai) Co., Ltd., a joint venture in Shanghai, to manufacture color filters and micro-lenses for CMOS image sensors. In May 2005, we announced an agreement with United Test and Assembly Center Ltd. to establish a joint venture in Chengdu to provide assembly and testing services for memory and logic devices.

The results of the joint ventures may be reflected in our operating results to the extent of our ownership interest, and losses of the joint ventures could adversely impact our operating results. For example, as a result of our ownership of Toppan SMIC Electronics (Shanghai) Co., Ltd., we recorded a loss of US$4.0 million in 2007. Integration of assets and operations being contributed by each partner will involve complex activities that must be completed in a short period of time. The joint ventures are likely to continue to face numerous challenges in commencing their operations and operating successfully. The business of the joint ventures will be subject to operational risks that would normally arise for these types of businesses pertaining to manufacturing, sales, service, marketing, and corporate functions. Competition in the CMOS image sensor market and semiconductor assembly and testing industry will involve challenges from well-established companies with substantial resources and significant market share.

If the joint ventures are not successful or less successful than we anticipate, we may incur higher costs for performing assembly and testing services through our current partners or for manufacturing color filters and micro-lenses, which typically require mature technologies and thus command a lower wafer price and generate lower margins, at our existing fabs. Either result may adversely affect our business and operating results.

Table of Contents

If we are unable to obtain raw materials and spare parts in a timely manner, our production schedules could be delayed and our costs could increase.

We depend on suppliers of raw materials, such as silicon wafers, gases and chemicals, and spare equipment parts, in order to maintain our production processes. To maintain operations, we must obtain from our suppliers sufficient quantities of quality raw materials and spare equipment parts at acceptable prices and in a timely manner. The most important raw material used in our production is silicon in the form of raw wafers. We currently purchase approximately 71.8% of our overall raw wafer requirements from our top three raw wafer suppliers. In addition, a portion of our gas and chemical requirements currently must be sourced from outside China. We may not be able to obtain adequate supplies of raw materials and spare parts in a timely manner and at a reasonable cost. In addition, from time to time, we may need to reject raw materials and parts that do not meet our specifications, resulting in potential delays or declines in output. If the supply of raw materials and necessary spare parts is substantially reduced or if there are significant increases in their prices, we may incur additional costs to acquire sufficient quantities of these parts and materials to maintain our production schedules and commitments to customers.

Our production may be interrupted, limited or delayed if we cannot maintain sufficient sources of fresh water and electricity, which could adversely affect our business and operating results.

The semiconductor fabrication process requires extensive amounts of fresh water and a stable source of electricity. As our production capabilities increase and our business grows, our requirements for these factors will grow substantially. While we have not, to date, experienced any instances of the lack of sufficient supplies of water or material disruptions in the electricity supply to any of our fabs, we may not have access to sufficient supplies of water and electricity to accommodate our planned growth. Droughts, pipeline interruptions, power interruptions, electricity shortages or government intervention, particularly in the form of rationing, are factors that could restrict our access to these utilities in the areas in which our fabs are located. In particular, our fab in Tianjin and our Beijing mega-fab are located in areas that are susceptible to severe water shortages during the summer months. If there is an insufficient supply of fresh water or electricity to satisfy our requirements, we may need to limit or delay our production, which could adversely affect our business and operating results. In addition, a power outage, even of very limited duration, could result in a loss of wafers in production and a deterioration in yield.

Our operations may be delayed or interrupted due to natural disasters which could adversely affect our business and operating results.

We depend on suppliers of raw materials, such as silicon wafers, gases and chemicals, and spare equipment parts, in order to maintain our production processes in addition to requiring extensive amounts of fresh water and a stable source of electricity. The occurrence of natural disasters such as earthquakes may disrupt this required access to goods and services provided by our suppliers as well as access to fresh water and electricity. As a result, our production could be limited or delayed, which could adversely affect our business and operating results.

We are subject to the risk of damage due to fires or explosions because the materials we use in our manufacturing processes are highly flammable. Such damage could temporarily reduce our manufacturing capacity, thereby adversely affecting our business and operating results.

We use highly flammable materials such as silane and hydrogen in our manufacturing processes and are therefore subject to the risk of loss arising from explosions and fires. While we have not, to date, experienced any explosion or fire due to the nature of our raw materials, the risk of explosion and fire associated with these materials cannot be completely eliminated. Although we maintain comprehensive fire insurance and insurance for the loss of property and the loss of profit resulting from business interruption, our insurance coverage may not be sufficient to cover all of our potential losses due to an explosion or fire. If any of our fabs were to be damaged or cease operations as a result of an explosion or fire, it could temporarily reduce our manufacturing capacity, which could adversely affect our business and operating results.

Table of Contents

Our Beijing mega-fab is located in an area that is susceptible to seasonal dust storms, which could create impurities in the production process at these facilities and require us to take additional measures or spend additional capital to further insulate these fabs from dust, thereby adversely affecting our business and operating results.

The location of our Beijing mega-fab makes it susceptible to seasonal dust storms, which could cause dust particles to enter the buildings and affect the production process. Although we are constructing precautionary filtration systems, these may not adequately insulate the Beijing mega-fab against dust contamination. If dust were to affect production in the Beijing mega-fab, we could experience quality control problems, losses of products in process and delays in shipping products to our customers. In addition, we may have to spend additional capital to further insulate the Beijing mega-fab from dust if our current precautionary measures are insufficient. The occurrence of any of these events could adversely affect our business and operating results.

Our operations may be delayed or interrupted and our business could suffer as a result of steps we may be required to take in order to comply with environmental regulations.

We are subject to a variety of Chinese environmental regulations relating to the use, discharge and disposal of toxic or otherwise hazardous materials used in our production processes. Any failure or any claim that we have failed to comply with these regulations could cause delays in our production and capacity expansion and affect our company s public image, either of which could harm our business. In addition, any failure to comply with these regulations could subject us to substantial fines or other liabilities or require us to suspend or adversely modify our operations.

Table of Contents

Risks Related to Conducting Operations in China

Our business is subject to extensive government regulation and benefits from certain government incentives, and changes in these regulations or incentives could adversely affect our business and operating results.

The Chinese government has broad discretion and authority to regulate the technology industry in China. China s government has also implemented policies from time to time to regulate economic expansion in China. The economy of China has been transitioning from a planned economy to a market-oriented economy. Although in recent years the Chinese government has implemented measures emphasizing the utilization of market forces for economic reform, the reduction of state ownership of productive assets, and the establishment of sound corporate governance in business enterprises, a substantial portion of productive assets in China is still owned by the Chinese government. In addition, the Chinese government continues to play a significant role in regulating industrial development. It also exercises significant control over China s economic growth through the allocation of resources, controlling payment of foreign currency-denominated obligations, setting monetary policy, and providing preferential treatment to particular industries or companies. New regulations or the readjustment of previously implemented regulations could require us to change our business plan, increase our costs or limit our ability to sell products and conduct activities in China, which could adversely affect our business and operating results.

In addition, the Chinese government and provincial and local governments have provided, and continue to provide, various incentives to domestic companies in the semiconductor industry, including our company, in order to encourage the development of the industry. Such incentives include tax rebates, reduced tax rates, favorable lending policies, and other measures. Any of these incentives could be reduced or eliminated by governmental authorities at any time. For example, in 2004, the Chinese government announced that by April 1, 2005, the preferential value-added tax policies, which previously entitled certain qualified companies to receive a refund of the amount exceeding 3% of the actual value-added tax burden relating to self-made integrated circuit product sales, would be eliminated. While we have not previously benefited materially from such preferential value-added tax policies, any reduction or elimination of other incentives currently provided to us could adversely affect our business and operating results.

Because our business model depends on growth in the electronics manufacturing supply chain in China, any slowdown in this growth could adversely affect our business and operating results.

Our business is dependent upon the economy and the business environment in China. In particular, our growth strategy is based upon the assumption that demand in China for devices that use semiconductors will continue to grow. Therefore, any slowdown in the growth of consumer demand in China for products that use semiconductors, such as computers, mobile phones or other consumer electronics, could have a serious adverse effect on our business. In addition, our business plan assumes that an increasing number of non-domestic IDMs, fabless semiconductor companies and systems companies will establish operations in China. Any decline in the rate of migration to China of semiconductor design companies or companies that require semiconductors as components for their products could adversely affect our business and operating results.

Limits placed on exports into China could substantially harm our business and operating results.

The growth of our business will depend on the ability of our suppliers to export, and our ability to import, equipment, materials, spare parts, process know-how and other technologies and hardware into China. Any restrictions placed on the import and export of these products and technologies could adversely impact our growth and substantially harm our business. In particular, the United States requires our suppliers and us to obtain licenses to export certain products, equipment, materials, spare parts and technologies from that country. If we or our suppliers are unable to obtain export licenses in a timely manner, our business and operating results could be adversely affected.

In July 1996, thirty-three countries ratified the Wassenaar Arrangement on Export Controls for Conventional Arms and Dual-Use Goods and Technologies, which established a worldwide arrangement to restrict the transfer of conventional arms and dual-use goods and technologies. Under the terms of the

Table of Contents

Wassenaar Arrangement, the participating countries, including the United States, have restricted exports to China of technology, equipment, materials and spare parts that potentially may be used for military purposes in addition to their commercial applications. To the extent that technology, equipment, materials or spare parts used in our manufacturing processes are or become subject to the restrictions of the arrangement, our ability to procure these products and technology could be impaired, which could adversely affect our business and operating results. There could also be a change in the export license regulatory regime in the countries from which we purchase our equipment, materials and spare parts that could delay our ability to obtain export licenses for the equipment, materials, spare parts and technology we require to conduct our business.

Devaluation or appreciation in the value of the Renminbi or restrictions on convertibility of the Renminbi could adversely affect our business and operating results.

The value of the Renminbi is subject to changes in China s governmental policies and to international economic and political developments. Since 1994, the conversion of Renminbi into foreign currencies, including Hong Kong and U.S. dollars, has been based on rates set by the People s Bank of China (PBOC), which are set daily based on the previous day s interbank foreign exchange market rates and current exchange rates on the world financial markets. The Renminbi to U.S. dollar exchange rate experienced significant volatility prior to 1994, including periods of sharp devaluation. On July 21, 2005, the PBOC announced an adjustment of the exchange rate of the U.S. dollar to Renminbi from 1:8.27 to 1:8.11 and modified the system by which the exchange rates are determined. The central parity rate of the U.S. Dollar to Renminbi was set at 7.3046 on December 28, 2007 versus 7.8087 on December 29, 2006 by PBOC. The cumulative appreciation of the Renminbi against the U.S. dollar in 2007 was approximately 6.46%. There remains significant international pressure on the PRC government to adopt an even more flexible currency policy, which could result in a further and more significant appreciation of the Renminbi against the U.S. dollar. As a result, the exchange rate may become volatile and the Renminbi may be devalued again against the U.S. dollar or other currencies, or the Renminbi may be permitted to enter into a full or limited free float, which may result in an appreciation in the value of the Renminbi against the U.S. dollar, any of which could have an adverse affect on our business and operating results.

In the past, financial markets in many Asian countries have experienced severe volatility and, as a result, some Asian currencies have experienced significant devaluation from time to time. The devaluation of some Asian currencies may have the effect of rendering exports from China more expensive and less competitive and therefore place pressure on China s government to devalue the Renminbi. An appreciation in the value of the Renminbi could have a similar effect. Any devaluation of the Renminbi could result in an increase in volatility of Asian currency and capital markets. Future volatility of Asian financial markets could have an adverse impact on our ability to expand our product sales into Asian markets outside of China.

We receive a portion of our sales in Renminbi, which is currently not a freely convertible currency. For the year ended December 31, 2007, approximately 0.89% of our sales were denominated in Renminbi. While we have used these proceeds for the payment of our Renminbi expenses, we may in the future need to convert these sales into foreign currencies to allow us to purchase imported materials and equipment, particularly as we expect the proportion of our sales to China-based companies to increase in the future. Under China s existing foreign exchange regulations, payments of current account items, including profit distributions, interest payments and expenditures from trade may be made in foreign currencies without government approval, except for certain procedural requirements. The Chinese government may, however, at its discretion, restrict access in the future to foreign currencies for current account transactions and prohibit us from converting our Renminbi sales into foreign currencies. If this were to occur, we may not be able to meet our foreign currency payment obligations.

China s entry into the World Trade Organization has resulted in lower Chinese tariff levels, which benefit our competitors from outside China and could adversely affect our business and operating results.

As a result of joining the World Trade Organization, or WTO, China has reduced its average rate of import tariffs to 11.5% in 2003 and will reduce it further by 2010. The import tariff for some information

Table of Contents

technology-related products has been reduced to zero. As a consequence, we expect stronger competition in China from our foreign competitors, particularly in terms of product pricing, which could adversely affect our business and operating results.

China s legal system embodies uncertainties that could adversely affect our business and operating results.

Since 1979, many new laws and regulations covering general economic matters have been promulgated in China. Despite this activity to develop the legal system, China s system of laws is not yet complete. Even where adequate law exists in China, enforcement of existing laws or contracts based on existing law may be uncertain and sporadic, and it may be difficult to obtain swift and equitable enforcement or to obtain enforcement of a judgment by a court of another jurisdiction. The relative inexperience of China s judiciary in many cases creates additional uncertainty as to the outcome of any litigation. In addition, interpretation of statutes and regulations may be subject to government policies reflecting domestic political changes.

Our activities in China will be subject to administrative review and approval by various national and local agencies of China s government. See Item 4 Information on the Company Regulation. Because of the changes occurring in China s legal and regulatory structure, we may not be able to secure the requisite governmental approval for our activities. Failure to obtain the requisite governmental approval for any of our activities could adversely affect our business and operating results.

Our corporate structure may restrict our ability to receive dividends from, and transfer funds to, our Chinese operating subsidiaries, which could restrict our ability to act in response to changing market conditions and reallocate funds from one Chinese subsidiary to another in a timely manner.

We are a Cayman Islands holding company and substantially all of our operations are conducted through our Chinese operating subsidiaries, SMIC Shanghai, Semiconductor Manufacturing International (Beijing) Corporation, or SMIC Beijing, and Semiconductor Manufacturing International (Tianjin) Corporation. The ability of these subsidiaries to distribute dividends and other payments to us may be restricted by factors that include changes in applicable foreign exchange and other laws and regulations. In particular, under Chinese law, these operating subsidiaries may only pay dividends after 10% of their net profit has been set aside as reserve funds, unless such reserves have reached at least 50% of their respective registered capital. In addition, the profit available for distribution from our Chinese operating subsidiaries is determined in accordance with generally accepted accounting principles in China. This calculation may differ from the one performed in accordance with U.S. GAAP. As a result, we may not have sufficient distributions from our Chinese subsidiaries to enable necessary profit distributions to us or any distributions to our shareholders in the future, which calculation would be based upon our financial statements prepared under U.S. GAAP.

Distributions by our Chinese subsidiaries to us other than as dividends may be subject to governmental approval and taxation. Any transfer of funds from our company to our Chinese subsidiaries, either as a shareholder loan or as an increase in registered capital, is subject to registration or approval of Chinese governmental authorities, including the relevant administration of foreign exchange and/or the relevant examining and approval authority. In addition, it is not permitted under Chinese law for our Chinese subsidiaries to directly lend money to each other. Therefore, it is difficult to change our capital expenditure plans once the relevant funds have been remitted from our company to our Chinese subsidiaries. These limitations on the free flow of funds between us and our Chinese subsidiaries could restrict our ability to act in response to changing market conditions and reallocate funds from one Chinese subsidiary to another in a timely manner.

Table of Contents

Risks Related to Ownership of Our Shares and ADSs and Our Trading Markets

Future sales of securities by us or our shareholders may decrease the value of your investment.

Future sales by us or our existing shareholders of substantial amounts of our ordinary shares or ADSs in the public markets could adversely affect market prices prevailing from time to time. In connection with our global offering, we entered into an amended and restated registration rights agreement with Richard Ru Gin Chang and our security holders prior to our global offering. Under the terms of this agreement, every 180-day period, substantially all of our security holders that beneficially own, directly or indirectly and whether individually or as a group with its affiliates, more than 7,500,000 of our ordinary shares immediately prior to the global offering, whom we collectively refer to as our large security holders, may sell 15% of the shares held by such large security holder immediately prior to the completion of the global offering in an annual, demand or incidental offering or without our consent in the open market or in privately negotiated transactions. We refer to the shares sold as released shares and these sales as permitted sales/transfers. The 15% limit for each 180-day period is cumulative, such that if any large security holder does not sell or transfer the 15% released shares from a previous 180-day period, any unsold or non-transferred released shares will roll over and may be sold or transferred at any time in the future, together with all other accumulated released shares from previous periods.

We cannot predict the effect, if any, of a permitted sale or the perception that a permitted sale will occur, on the market price for our ordinary shares or ADSs.

Holders of our ADSs will not have the same voting rights as the holders of our shares and may not receive voting materials in time to be able to exercise their right to vote.

Holders of our ADSs may not be able to exercise voting rights attaching to the shares evidenced by our ADSs on an individual basis. Holders of our ADSs have appointed the depositary or its nominee as their representative to exercise the voting rights attaching to the shares represented by the ADSs. You may not receive voting materials in time to instruct the depositary to vote, and it is possible that you, or persons who hold their ADSs through brokers, dealers or other third parties, will not have the opportunity to exercise a right to vote.

You may not be able to participate in rights offerings and may experience dilution of your holdings as a result.

We may from time to time distribute rights to our shareholders, including rights to acquire our securities. Under the deposit agreement for the ADSs, the depositary will not offer those rights to ADS holders unless both the rights and the underlying securities to be distributed to ADS holders are either registered under the Securities Act or exempt from registration under the Securities Act with respect to all holders of ADSs. We are under no obligation to file a registration statement with respect to any such rights or underlying securities or to endeavor to cause such a registration statement to be declared effective. In addition, we may not be able to take advantage of any exemptions from registration under the Securities Act. Accordingly, holders of our ADSs may be unable to participate in our rights offerings and may experience dilution in their holdings as a result.

The laws of the Cayman Islands and China may not provide our shareholders with benefits provided to shareholders of corporations incorporated in the United States.

Our corporate affairs are governed by our memorandum and articles of association, by the Companies Law (Revised) and the common law of the Cayman Islands. The rights of shareholders to take action against our directors, actions by minority shareholders and the fiduciary responsibilities of our directors to us under Cayman Islands law are to a large extent governed by the common law of the Cayman Islands. The common law in the Cayman Islands is derived in part from comparatively limited judicial precedent in the Cayman Islands and from English common law, the decisions of whose courts are of persuasive authority but are not binding on a court in the Cayman Islands. The rights of our shareholders and the fiduciary responsibilities of our directors under Cayman Islands law are not as clearly established as they would be under statutes or judicial precedents in the United States. In particular, the Cayman Islands have a less developed body of securities laws as compared to the United States. Therefore, our

Table of Contents

public shareholders may have more difficulty protecting their interests in the face of actions by our management, directors or controlling shareholders than would shareholders of a corporation incorporated in a jurisdiction in the United States. In addition, Cayman Islands companies may not have standing to initiate a shareholder derivative action before the federal courts of the United States.

It may be difficult for you to enforce any judgment obtained in the United States against our company, which may limit the remedies otherwise available to our shareholders.

Substantially all of our assets are located outside the United States. Almost all of our current operations are conducted in China. Moreover, a number of our directors and officers are nationals or residents of countries other than the United States. All or a substantial portion of the assets of these persons are located outside the United States. As a result, it may be difficult for you to effect service of process within the United States upon these persons. In addition, there is uncertainty as to whether the courts of the Cayman Islands or China would recognize or enforce judgments of United States courts obtained against us or such persons predicated upon the civil liability provisions of the securities law of the United States or any state thereof, or be competent to hear original actions brought in the Cayman Islands or China, respectively, against us or such persons predicated upon the securities laws of the United States or any state thereof. See Item 4 Information on the Company Business Overview Enforceability of Civil Liabilities

Table of Contents

Item 4. Information on the Company

History and Development of the Company

We were established as an exempted company under the laws of the Cayman Islands on April 3, 2000. Our legal name is Semiconductor Manufacturing International Corporation. Our principal place of business is 18 Zhangjiang Road, Pudong New Area, Shanghai, China 201203, telephone number: (86) 21-5080-2000. Our registered agent is Maples Corporate Services Limited, located at PO Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands. Since our global offering, we have been listed on the New York Stock Exchange under the symbol SMI and the Stock Exchange of Hong Kong under the stock code 0981.

We were founded by Dr. Richard Ru Gin Chang, our Chief Executive Officer and President, who has more than 29 years of experience in the semiconductor industry. In August 2000, we started construction of the first fab in our Shanghai mega-fab. The first fab in the Shanghai mega-fab commenced pilot production in September 2001. That fab and the portion of our second fab in our Shanghai mega-fab which provides aluminum interconnects, commenced commercial production in January 2002. The portion of this second fab which provides copper interconnects and a third fab in our Shanghai mega-fab commenced commercial production in January 2003. All the fabs comprising the Shanghai mega-fab are located in the Zhangjiang High-Tech Park. In January 2004, we completed the acquisition of an 8-inch wafer fab located in the Xiqing Economic Development Area in Tianjin, China, and commenced mass production in May 2004. We commenced construction of our Beijing mega-fab in the Beijing Economic and Technological Development Area in December 2002. The Beijing mega-fab consists of three twelve-inch fabs and commenced commercial production in March 2005. The Beijing mega-fab is China s first 12-inch fab. In January 2008, the Company announced its plan to start a new IC production project in Shenzhen with extensive support from the Shenzhen municipal government. The project is expected to break ground in the first half of 2008.

We have entered into an agreement with Toppan Printing Co., Ltd., to establish Toppan SMIC Electronics (Shanghai) Co., Ltd., to manufacture color filters and micro-lenses for CMOS image sensors and a joint venture agreement with United Test and Assembly Center Ltd. to provide assembly and testing services in Chengdu focusing on memory and logic devices. We have also entered into agreements to manage the operations of wafer manufacturing facilities in Chengdu and Wuhan, China. We maintain customer service and marketing offices in Japan, Europe, and the United States and a representative office in Hong Kong.

The foundry industry requires a significant amount of capital expenditures in order to construct, equip, and ramp up fabs. We incurred capital expenditures of US$903 million, US$912 million, and US$860 million in 2005, 2006 and 2007, respectively, for these purposes. We anticipate that in 2008, we will incur approximately US$700 million of capital expenditures, principally to expand our operations at our mega-fabs in Shanghai and Beijing and fab in Tianjin and new fab in Shenzhen. If our operating cash flows are insufficient, we plan to fund the expected shortfall through bank loans. If necessary, we will also explore other forms of external financing.

Our fabs had an aggregate capacity, as of December 31, 2007, of 185,250 8-inch wafer equivalents per month for wafer fabrication. We anticipate that as of the end of 2008, we will have an aggregate capacity of 193,000 8-inch wafer equivalents per month.

For additional information, see Item 5 Operating and Financial Review and Prospects Factors that Impact Our Results of Operations Substantial Capital Expenditures and Capacity Expansion.

Business Overview

We are one of the leading semiconductor foundries in the world. We operate three 8-inch wafer fabrication facilities in our Shanghai mega-fab located in the Zhangjiang High-Tech Park in Shanghai, China, an 8-inch wafer fab in Tianjin, China and a 12-inch wafer fab in our Beijing mega-fab located in the Beijing Economic and Technological Development Area in Beijing, China. These fabs had an aggregate

Table of Contents

capacity as of December 31, 2007 of 185,250 8-inch wafer equivalents per month for wafer fabrication which positions us as the leading foundry in China. In addition, we have constructed two additional 12-inch fabs for our Beijing mega-fab and have constructed an additional 12-inch fab for our Shanghai mega-fab. We have also entered into agreements to manage the operations of wafer manufacturing facilities in Chengdu and Wuhan, China. We also operate a fab at our Shanghai site which produces solar cells and modules. Due to the unique nature of solar cells and modules, this fab is not considered a part of our Shanghai mega-fab.

We currently provide semiconductor fabrication services using 0.35 micron to 90 nanometer process technology for the following devices:

logic technologies, including standard logic, mixed-signal, RF and high voltage circuits;

memory technologies, including DRAM, SRAM, Flash, and EEPROM; and

specialty technologies, including LCoS, and CIS.

During the first quarter of 2008, the Company took the decision to exit the commodity DRAM business.

In addition to wafer fabrication, our service offerings include a comprehensive portfolio of intellectual property consisting of libraries and circuit design blocks, design support, mask-making, wafer probing, gold/solder bumping and redistribution layer manufacturing. We also work with our partners to provide assembly and testing services.

We have a global and diversified customer base that includes some of the world s leading IDMs and fabless semiconductor companies.

Our Industry

The Semiconductor Industry

Since the invention of the first semiconductor transistor in 1947, integrated circuits have become critical components in an increasingly broad range of electronics applications, including personal computers, wired and wireless communications equipment, televisions, consumer electronics and automotive and industrial control applications. Advancements in semiconductor design techniques and process technologies have allowed for the mass production of increasingly smaller and more powerful semiconductor devices at lower costs. This has resulted in the availability and proliferation of more complex integrated circuits with higher functionality. These integrated circuits may now each contain up to millions of transistors.

The key raw material for a semiconductor foundry is a raw wafer, which is a circular silicon plate. Raw wafers are available in different diameters (e.g., 5-inch, 6-inch, 8-inch or 12-inch) to meet the capabilities of different equipment. A fab capable of manufacturing integrated circuits on an 8-inch raw wafer is commonly described as an 8-inch fab. A raw wafer with a larger diameter has a greater surface area and consequently yields a greater number of integrated circuit dies. One method that foundries attempt to use to maintain their competitiveness is to increase the diameter of the wafers they use in manufacturing, such as the recent trend toward developing 12-inch wafers, each of which has approximately 2.25 times the number of gross dies achievable on an 8-inch wafer. In addition, since 12-inch fabs have been constructed more recently, the equipment used in these fabs permits smaller line-width process technologies to be utilized. However, this equipment is more expensive than equipment for the fabrication of 8-inch wafers as the market for this equipment is less mature with fewer suppliers and the technology involved is more complex.

Table of Contents

Process technologies are the set of specifications and parameters implemented for manufacturing the circuitry on integrated circuits. The transistor circuitry on an integrated circuit typically follows lines that are less than one micron wide (1/1,000,000 of a meter). The line-widths of the circuitry, or the minimum physical dimensions of the transistor gate of integrated circuits in production, is used as a general rule for classifying generations of process technology of integrated circuits. Progress in the advancement of the integrated circuit has been driven by the scaling, or downsizing, of its components, primarily the transistors. By systematically shrinking the size of the transistors, the number of allowable transistors per die increases, and thus the number of dies on a given wafer, has also increased. Our current process technology ranges from 0.35 micron to 90 nanometer.

Importance of Integrated Circuits for China s Domestic Market and China s Emergence as a Global Electronics Manufacturing Center

China has emerged as a global manufacturing center for electronic products that are sold both within China and abroad. In recent years, numerous international companies have established facilities in China for the manufacture of a variety of electronic products, including household appliances, computers, mobile phones, telecommunications equipment, digital consumer products and products with industrial applications. An increasing number of electronic systems manufacturers are relocating production facilities from the United States, Taiwan, Southeast Asia and Mexico to China. China is establishing itself as a favorable manufacturing location due to its well educated labor force, significantly lower costs of operations, large domestic market for semiconductors and cultural similarities and geographical proximity to Japan, Hong Kong, Taiwan, Singapore and Korea, among other factors. Such production growth represents additional potential demand for semiconductors manufactured in China.

Increasing Importance of the Semiconductor Foundry Industry

As the cost of establishing new fabrication capacity has continued to rise, foundries have progressed from simply providing manufacturing capacity to becoming key strategic partners offering research and development capabilities and manufacturing process technologies. There have historically been a limited number of semiconductor foundries in the industry due to the high barriers to entry, which include significant capital commitments, scarcity of qualified engineers and advanced intellectual property and technology requirements. Many IDMs have begun outsourcing their fabrication requirements for complex and high performance semiconductor devices to foundries in order to supplement their own internal capacities and become more cost competitive. In addition, fabless semiconductor companies have shifted from relying on the excess fabrication capacity of IDMs to utilizing independent foundries to meet the majority of their wafer production needs.

Our Fabs

We have implemented a One Mega Fab project to align the capabilities of our Shanghai fabs and of our Beijing fabs by standardizing our equipment and processes. As a mega-fab, a wafer produced at any of our fabs at one location should have statistically the same wafer acceptance test results and wafer yields as a semiconductor wafer produced at any of our other fabs that are producing the same product at that same location. This increases the flexibility of our total capacity and allows us to avoid costs and delays related to additional customer qualifications when we shift production from one fab to another.

The table below sets forth a summary of our current fabs and fabs under construction:

	Shanghai Mega-Fab	**Beijing Mega-Fab**	**Tianjin**
Number and Type of fab	8-inch fabs: three in production 12-inch fab: being equipped	12-inch fabs: two in production, one additional fab being equipped	8-inch fab: one in production
Pilot production commencement	September 2001	July 2004	February 2004

Table of Contents

	Shanghai Mega-Fab	Beijing Mega-Fab	Tianjin
Commercial production commencement	January 2002	March 2005	May 2004
Wafer size	8-inch 12-inch (being equipped)	12-inch	8-inch
Production clean room size	34,610 m^2	23,876 m^2	8,463 m^2

In addition to our Shanghai mega-fab, we have two additional fabs at our Shanghai site. A portion of one facility in Shanghai is being leased to Toppan SMIC Electronics (Shanghai) Co., Ltd., which manufactures color filters and micro-lenses for CMOS image sensors. The other fab in Shanghai manufactures solar cells and modules. Most of the administrative and management functions of our fabs in different locations are centralized at our corporate headquarters in the Zhangjiang High-Tech Park in the Pudong New Area of Shanghai.

Management of Fabs

We also have undertaken agreements relating to wafer manufacturing facilities in Chengdu and Wuhan, China. Under these agreements, we have not owned any equity interest but will manage the operations of the facilities.

Our Services

Wafer Fabrication Services

We currently provide semiconductor fabrication services using 0.35 micron to 90 nanometer technology for the following devices:

logic technologies, including standard logic, mixed-signal, RF and high voltage circuits;

memory technologies, including DRAM, SRAM, Flash, EEPROM and Mask ROM; and

specialty technologies, including LCoS, and CIS.

These semiconductors are used in various computing, communications, consumer and industrial applications, such as computers, mobile telephones, digital televisions, digital cameras, DVD players, entertainment devices, other consumer electronics devices and automotive and industrial applications.

Our Technologies

We manufacture the following types of semiconductors:

Logic Semiconductors. Logic semiconductors process digital data to control the operation of electronic systems. The largest segment of the logic market, standard logic devices, includes microprocessors, microcontrollers, DSPs and graphic chips. Logic semiconductors are used in communications devices, computers and consumer products, with the most advanced logic semiconductors dedicated primarily to computing applications.

Mixed-Signal and RF. Analog/digital semiconductors combine analog and digital devices on a single semiconductor to process both analog signals and digital data. We make 0.35 micron to 0.13 micron mixed-signal and RF semiconductors using the CMOS process. The primary uses of mixed-signal semiconductors are in hard disk drives, wireless communications equipment and network communications equipment, while RF semiconductors are primarily used in communications devices, such as cell phones.

Table of Contents

High Voltage. High voltage semiconductors are semiconductor devices that can drive high voltage electricity to systems that require voltage of between five volts to several hundred volts. Our high voltage technologies provide solutions for display driver integrated circuits, power supplies, power management, telecommunications, automotive electronics and industrial controls.

Memory Semiconductors. Memory semiconductors, which are used in electronic systems to store data and program instructions, are generally classified as either volatile memory, which lose their data content when power supplies are switched off, or non-volatile memory, which retain their data content without the need for a constant power supply. Examples of volatile memory include SRAM and DRAM, and examples of non-volatile memory include electrically erasable programmable read-only memory, or EEPROM, NAND Flash and OTP. Memory semiconductors are used in communications devices, computers and many consumer products.

Specialty Semiconductors.

LCoS. LCoS microdisplays are tiny, high resolution, low power displays designed for high definition televisions, projectors and other products that use or rely on displays. Compared with other display technologies, such as liquid crystal and plasma, LCoS displays have higher resolution and higher fill factor, resulting in superior images, colors and performance. LCoS process technology represents an enhancement of mixed-signal CMOS process technology with the addition of a highly reflective mirror layer.

CIS. CIS devices are sensors that are used in a wide range of camera-related systems, such as digital cameras, digital video cameras, handset cameras, personal computer cameras and surveillance cameras, which integrate image-capturing capabilities onto a chip. CIS is rapidly becoming a cost-effective and low power replacement for competing charged-coupled devices, or CCDs. Since CIS devices are fabricated with CMOS technology, they are easier to produce and more cost-effective than CCDs. By combining camera functions on a chip, from the capture of photos to the output of digital bits, CMOS image sensors reduce the parts required for a digital camera system, which in turn enhances reliability, facilitates miniaturization, and enables on-chip programming. Our CIS process is based on our CIS array technology.

We are one of the leading foundries in the world in terms of the process technologies that we are capable of using in the manufacturing of semiconductors: 53.1% of our wafer sales in 2007 were from products that utilized advanced technology of 0.13 micron and below.

The following table sets forth the actual and projected range of process technology capabilities of our fabs:

Fab	Month and year of commencement of commercial production of initial fab	Process technology (in microns) 2005	2006	2007	2008
Wafer fabrication:					
Shanghai Mega-fab (8)	January 2002	0.35/0.25/ 0.18/0.15/ 0.13/0.11/0.09	0.35/0.25/ 0.18/0.15/ 0.13/0.11/0.09	0.35/0.25/ 0.18/0.15/ 0.13/0.11/0.09	0.35/0.25/ 0.18/0.15/ 0.13/0.11/0.09
Shanghai fab (12)					0.09/0.065
Beijing Mega-fab (12)	March 2005	0.15/0.13/0.11/	0.15/0.13/0.11/	0.13/0.11/	0.18/0.13/0.09

0.10/0.09	0.10/0.09	0.10/0.09

31

Table of Contents

Fab	Month and year of commencement of commercial production of initial fab	Process technology (in microns) 2005	2006	2007	2008
Tianjin fab (8)	May 2004	0.35/0.18	0.35/0.25/ 0.18/0.15	0.35/0.25/ 0.18/0.15	0.35/0.25/ 0.18/0.15

The following table sets forth a percentage breakdown of wafer sales by process technology for the years ended December 31, 2005, 2006, and 2007 and each of the quarters in the year ended December 31, 2007:

Process Technologies	For the year ended December 31, 2005	2006	For the three months ended March 31, 2007	June 30, 2007	September 30, 2007	December 31, 2007	For the year ended December 31, 2007
			(based on sales in US$)				
0.13 micron and below	40.6%	49.6%	52.5%	55.0%	55.3%	49.7%	53.1%
0.15 micron	5.4%	5.7%	2.9%	1.2%	2.0%	5.5%	2.9%
0.18 micron	42.3%	35.7%	34.1%	30.8%	28.8%	28.3%	30.5%
0.25 micron	3.7%	2.0%	0.7%	0.7%	1.0%	0.5%	0.7%
0.35 micron	8.0%	7.0%	9.8%	12.3%	12.9%	16.0%	12.8%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Manufacturing Capacity

We currently manufacture 8-inch silicon wafers based on proprietary designs provided by our customers or third party designers. Since commencing commercial production, we have the largest 8-inch wafer fabrication capacity among the semiconductor foundries in China. We have the most advanced process technology among foundries in China and were the first fab to use 0.18 micron process technology. In January 2003, we commenced commercial production using 0.13 micron copper interconnects process technology. We are currently one of the few fabs in China to offer 0.13 micron copper interconnects process technology and 90 nanometer wafer fabrication process technology.

The following table sets forth the historical capacity of our wafer fabrication and copper interconnects fabs as December 31, 2007:

Fab	2005	2006	2007
Wafer Fabrication:			
Wafer fabrication capacity as of year-end(1):			
Shanghai mega-fab	89,892	106,000	98,000
Beijing mega-fab	27,368	56,250	65,250
Tianjin fab	15,000	20,000	22,000
Total monthly wafer fabrication capacity as of year-end(1)	132,260	182,250(3)	185,250(3)

Wafer fabrication capacity utilization	89%	90%	94%

Table of Contents

(1) All output and capacity data is provided as 8-inch wafers or 8-inch wafer equivalents per month. Conversion of 12-inch wafers to 8-inch wafer equivalents is achieved by multiplying the number of 12-inch wafers by 2.25.

(2) Reflects wafers fabricated using the copper interconnects line and does not include wafers fabricated using the aluminum interconnects line. As a small number of wafers produced by our aluminum interconnects lines also utilize the copper interconnects capabilities, our reported capacity and output data for our copper interconnects line overlaps to a limited extent with such data for our aluminum interconnects

line.

(3) Megafab structure includes copper interconnects in the total monthly capacity.

As of December 31, 2007, our aggregate wafer fabrication capacity was 185,250 8-inch wafer equivalents per month for wafer fabrication.

A key factor influencing our profit margins is our capacity utilization. Because a high percentage of our cost of sales is of a fixed nature, operations at or near full capacity have a significant positive effect on output and profitability. In 2004 our wafer fabs had an average annual utilization rate of 98%, in 2005, our wafer fabs had an average annual utilization rate of 89%, and in 2006, our wafer fabs had an average annual utilization rate of 89.6%. In 2007 our wafer fabs had an average utilization of 94%. Factors affecting utilization rates include our ability to manage the production facilities and product flows efficiently, the percentage line yield of wafers during the fabrication process, the complexity of the wafer produced, and the actual product mix. In addition, we have manufactured DRAM to fill our production lines when the volume demand of other products does not fully utilize our available capacity. As a result, our utilization rate has historically remained high.

We determine the capacity of a fab based on the capacity ratings given by manufacturers of the equipment used in the fab, adjusted for, among other factors, actual output during uninterrupted trial runs, expected down time due to setup for production runs and approximately one to two days of scheduled annual maintenance, and expected product mix. All of our fabs currently operate 24 hours per day, seven days per week, except during periods of annual maintenance. Employees in our fabs work shifts of 12 hours each day on a two-days-on, two-days-off basis.

We have often used DRAM as the initial product to test the production capabilities at a new fab. This is because DRAM requires higher process accuracy, more precise process control and a higher degree of engineering skills and operational disciplines, and can therefore assist in early identification of any potential process, equipment or fab-related production problems. This DRAM is either manufactured on a foundry basis for our customers or sold by us to the market through our distributors under technology licensing and royalty arrangements. However, the market for DRAM devices has also been more volatile and susceptible to sudden price drops in recent years. We expect that our production of DRAM wafers as a percentage of our overall production will decrease. During the first quarter of 2008, the Company took the decision to exit the commodity DRAM business. For our new wafer fabs, we anticipate using logic products as the initial product to test the wafer fab s production capacity.

Capacity Expansion Plans

We intend to maintain our strategy of expanding capacity and improving our process technology to meet both the capacity requirements and the technological needs of our customers. Our capital expenditures in 2006 were approximately US$912 million and our capital expenditures in 2007 were approximately US$860 million. We currently expect that our capital expenditures in 2008 will be approximately US$700 million, which we plan to fund through our operating cash flows and bank loans. If necessary, we will also explore other forms of external financing. We plan to use this capital primarily to expand our operations at our mega-fabs in Shanghai and Beijing and fab in Tianjin and in Shenzhen. In addition, our actual expenditures may exceed our planned expenditures for a variety of reasons, including changes in our business plan, our process

Table of Contents

technology, market conditions, equipment prices, or customer requirements. We will monitor the global economy, the semiconductor industry, the demands of our customers, and our cash flow from operations to adjust our capital expenditure plans.

We also will seek to participate in strategic partnerships to meet the demands of our customers. For example, in July 2004, we entered into an agreement with Toppan Printing Co., Ltd., to establish Toppan SMIC Electronics (Shanghai) Co., Ltd., a joint venture in Shanghai, for the manufacture of color filters and micro-lenses for CMOS image sensors. These products are increasingly being used in consumer products such as mobile phone cameras, digital cameras and automobile and home security applications. Toppan SMIC Electronics (Shanghai) Co., Ltd. commenced production in December 2005. We hold a 30% equity interest in Toppan SMIC Electronics (Shanghai) Co., Ltd.

Our Integrated Solutions

In addition to wafer fabrication, we provide our customers with a range of complementary services, from circuit design support and mask-making to wafer level probing and testing. This range of services is supported by our network of partners that assist in providing design, probing, final testing, packaging, assembly and distribution services.

The diagram below sets forth our service model and our key points of interaction with our customers:

(1) A portion of this work is outsourced to our service partners.

(2) A portion of these services are outsourced to our service partners.

Design Support Services

Our design support services include providing our customers with access to the fundamental technology files and intellectual property libraries that facilitate customers own integrated circuit design.

Table of Contents

We also offer design reference flows and access to our design center alliance, as well as layout services. In addition, we collaborate with industry leaders in electronic design automation, library and intellectual property services to create a worldwide network of expertise, resources and services that are available to implement and produce a customer s designs. As of December 31, 2007, we employed over 170 engineers devoted solely to design support services.

Libraries

As part of the necessary building blocks for our customers semiconductor designs, we offer libraries of compatible designs for portions of semiconductors, such as standard cells, I/O and selected memory blocks, in addition to technology files. We have a dedicated team of engineers who work with our research and development department to develop, license or acquire from third parties selected key libraries early on in the development of new process technologies so that our customers can quickly design sophisticated integrated circuits that utilize the new process technologies. We also have arrangements with other providers of libraries to provide our customers with access to a broad library portfolio for their designs. In particular, we offer a portfolio of ASIC library and design kits for a wide range of tested and verified circuit applications and design-flow implementation. These include standard cell, I/O and memory compilers in 0.35 micron, 0.25 micron, 0.18 micron, 0.15 micron, 0.13 micron, and 90 nanometer process technologies. They have been developed primarily through our third party alliances, as well as by our internal research and development team, to facilitate easy design reuse and fast integration into the overall design system. We are currently developing additional libraries. Our library partners include ARM, Synopsys, Inc., VeriSilicon, and Virage Logic.

Intellectual Property

Together with the intellectual property developed by our internal design team, our alliances with intellectual property providers enable us to offer foundational designs ranging from 0.35 micron to 0.09 micron and relating to mixed-signal, embedded memory, high-speed interface, digital peripheral device controllers, and embedded processors, among others. We use our own and third party design expertise to realize the functions of these various types of intellectual property. Our intellectual property partners include ARM, MIPS, Virage, Synopsys, and Verisilicon.

Design Reference Flows

Customers implementing designs on our processes can utilize our design reference flows. These flows have been created using design tools developed by our electronic design automation partners, including Cadence Design Systems, Inc., Magma Design Automation, Inc., Mentor Graphics Corporation, and Synopsys, Inc. They include training guides and sample test cases to provide a step-by-step explanation on how the hierarchical design flow works.

Design Center Alliance

If a customer requires assistance in designing its semiconductors, we are able to recommend design partners from among our extensive design services network. This network consists of design companies that we have successfully worked with in the past. In addition, we are also able to offer our own internal design team members to help our clients to complete their designs.

Mask-making Services

Many of our foundry customers utilize our mask-making services.

While most of our mask-making services are for customers that also utilize our wafer fabrication services as part of our overall foundry service, we also produce masks for other domestic and overseas fabs as a separate revenue-generating service. Our mask shop also cooperates with our research and development department to develop new technologies and designs.

Our mask-making facility, which is located in Shanghai, includes a 3,750 square meters clean room with up to class I specifications. At present, our mask shop offers both five-inch by five-inch and six-inch by six-inch reticles. Our facility is capable of producing binary masks, optical proximity correction masks

Table of Contents

and phase shift masks. Our mask facility also offers mask repair services. As of December 31, 2007, we had 172 personnel employed in our mask shop.

We also offer a multi-project wafer service that allows the cost of manufacturing one mask set to be shared among several customers. See Customers and Markets for more details regarding this service.

Intellectual property protection is a key focus of our mask-making services. See " Intellectual Property for more details regarding the intellectual property protection measures we have instituted in our mask facility.

Wafer Probing, Assembly and Testing Services

We have our own probing facilities in Shanghai and Beijing that provide test program development, probe card fabrication, wafer probing, failure analysis, and failure testing. We also outsource these services to our partners for those customers that request them.

Our probing facility in Shanghai occupies a clean room space of 3,000 square meters, and our probing facility in Beijing occupies a clean room space of 1,400 square meters. Both facilities are rated at class 1,000 cleanliness and are equipped with advanced testers, probers and laser repair machines for logic, memory, and mixed-signal products. The probing facility in Beijing supports testing of Beijing s 12-inch wafers and Tianjin s 8-inch wafers. We employ more than 200 personnel to provide these probing services. We have testing equipment for memory, logic and mixed signal applications, including some equipment that has been consigned to our Shanghai facility by our customers. This consigned testing equipment has been specially designed and built by our customers in order to probe their particular products at our facility.

Our facility with United Test and Assembly Center Ltd. is located in Chengdu, China and provides both assembly and testing services for 8-inch and 12-inch wafers. This facility focuses on memory and discrete devices. Our facility in Chengdu occupies a total area of 215,000 square meters. Construction area is 40,668 square meters, including approximately 11,000 square meters of clean room area. We have also established a network of partners that provide additional probing services, as well as assembly and testing services, for our customers that request these additional services. We have relationships with assembly and testing partners, including Amkor Assembly & Test (Shanghai) Co., Ltd. and ST Assembly Test Services Ltd., which have helped to enhance the range of services that we are able to offer our customers.

Customers and Markets

Our customers include IDMs, fabless semiconductor companies and systems companies. The following table sets forth the breakdown of our sales by customer type for 2005, 2006 and 2007:

	For the year ended December 31,					
	2005		2006		2007	
Customer Type	**Sales**	**Percentage**	**Sales**	**Percentage**	**Sales**	**Percentage**
	(in US$ thousands, except percentages)					
Fabless semiconductor companies	$ 515,437	44.0%	601,200	41.0%	720,416	46.5%
Integrated device manufacturers	613,869	52.4%	737,275	50.3%	634,607	40.9%
Systems companies and others	42,013	3.6%	126,848	8.7%	194,742	12.6%
Total	$ 1,171,319	100.0%	1,465,323	100.0%	1,549,765	100.0%

Table of Contents

We categorize our sales geographically based on the headquarter of the customer. The following table sets forth the geographical distribution of our sales and percentage of sales for 2005, 2006 and 2007:

	For the year ended December 31,					
	2005		2006		2007	
Region	Sales	Percentage	Sales	Percentage	Sales	Percentage
	(in US$ thousands, except percentages)					
United States	$ 478,162	40.8%	602,506	41.1%	657,603	42.4%
Europe	316,576	27.0%	440,328	30.0%	328,710	21.2%
Asia Pacific (excluding Japan and Taiwan)(1)	175,846	15.0%	168,608	11.5%	227,973	14.7%
Taiwan	138,154	11.8%	153,058	10.5%	183,114	11.8%
Japan	62,581	5.4%	100,823	6.9%	152,365	9.9%
Total	$ 1,171,319	100.0%	$ 1,465,323	100.0%	$ 1,549,765	100.0%

We have a global and diversified customer base that includes IDMs. IDMs generally provide more stable and longer term purchase contracts, have higher order volumes, and license process technology to us. Although we are not dependent on any single customer, a significant portion of our sales is attributable to a relatively small number of our customers. Our sales could be significantly reduced if any of these customers cancels or reduces its orders, significantly changes its product delivery schedule or demands lower prices.

Our President and Chief Executive Officer, Richard Ru Gin Chang, and his wife together hold shareholding interests of less than 0.1% in one of our five largest customers in 2005, 2006 and 2007, Texas Instruments.

During the first quarter of 2008, the Company took the decision to exit the commodity DRAM business.

The following table sets forth a breakdown of our sales by application type for 2004, 2005 and 2006:

	For the year ended December 31,					
	2005		2006		2007	
Application Type[(1)]	Sales	Percentage	Sales	Percentage	Sales	Percentage
	(in US$ thousands, except percentages)					
Computing	$ 423,163	36.1%	498,135	34.0%	402,262	26.0%
Communications	492,791	42.1%	618,911	42.2%	695,645	44.9%
Consumer	202,153	17.3%	280,873	19.2%	323,230	20.9%
Others	53,212	4.5%	67,404	4.6%	128,628	8.2%
Total	$ 1,171,319	100.0%	$ 1,465,323	100.0%	$ 1,549,765	100.0%

(1) Computing consists of integrated circuits such as hard disk drive controllers, DVD-ROM/CD-ROM driver integrated circuits, graphic processors and other components that are commonly used in personal digital

assistants and desktop and notebook computers and peripherals.

Communications

Table of Contents

consists of integrated circuits used in digital subscriber lines, digital signal processors, wireless LAN, LAN controllers, LCD drivers, handset components and caller ID devices.

Consumer consists of integrated circuits used for DVD players, game consoles, digital cameras, smart cards and toys.

The following table sets forth a breakdown of our sales by service type for 2004, 2005 and 2006:

	For the year ended December 31,					
	2005		2006		2007	
Service Type	Sales	Percentage	Sales	Percentage	Sales	Percentage
	(in US$ thousands, except percentages)					
Fabrication of DRAM wafers	384,587	32.8%	476,970	32.6%	428,355	27.6%
Fabrication of logic wafers[1]	739,296	63.1%	923,411	63.0%	985,776	63.6%
Other[2]	47,436	4.1%	64,942	4.4%	135,634	8.8%
Total	$ 1,171,319	100.0%	$ 1,465,323	100.0%	$ 1,549,765	100.0%

(1) Includes copper interconnects and memory devices whose manufacturing process is similar to that for a logic device.

(2) Includes mask-making and probing, etc.

We have customer service and marketing offices located in California, Milan, Shanghai, and Tokyo and a representative office in Hong Kong. Our Shanghai office serves China and other non-Japan Asian markets, our California office serves the North American market, and our Milan and Tokyo offices serve the European and Japanese markets, respectively. We also sell some products through sales agents in selected markets.

We also provide our customers with the ability to share costs through our multi-project wafer processing shuttle service. This service allows customers to share costs with other customers by processing multiple designs on a single mask set.

We provide our customers with 24-hour online access to necessary information to conduct business with us. From our technical capabilities to a customer s order status, we provide an online solution for our customers. From wafer fabrication, wafer sorting and assembly to final testing and shipping, our data center electronically transfers data, work-in-progress tracking, yield/cycle-time reports, and quality/engineering data to customers.

Our sales cycle, meaning the time between our first contact with a customer in relation to a particular product and our first shipment of that product to the customer, typically lasts between three months to one year, depending on the type of process and product technology involved in the product we are requested to fabricate. Because of the fast-changing technology and functionality in integrated circuit design, foundry customers generally do not place purchase orders far in advance to fabricate a particular type of product. However, we engage in discussions with customers commencing in advance of the placement of purchase orders regarding customers expected fabrication requirements. See Risk Factors Risks Related to Our Financial Condition and Business Our sales cycles can be long, which could adversely affect our operating results and cause our income stream to be unpredictable.

See Item 5 Operating and Financial Review and Prospects Sales for a description of the seasonality of our business.

Research and Development

Our research and development activities are principally directed toward the development and implementation of more advanced and lower cost process technology. We spent US$78.9 million in 2005, US$94.2 million in 2006, and US$97.0 million in 2007 on research and development expenses, which

Table of Contents

represented 6.7%, 6.4%, and 6.3% respectively, of our sales in those respective years. Our research and development costs include non-recurring engineering costs associated with the ramp-up of a new wafer facility. In 2007, we continued to equip the wafer facility in our Beijing mega-fab. These research and development costs are subsequently classified in cost of sales upon commencement of commercial production at that particular wafer facility. We plan to continue to invest significant amounts in research and development in 2008 for our 65 and 45 nanometer manufacturing process.

We employ over 500 research and development personnel. This research and development team includes many experienced semiconductor engineers with advanced degrees from leading universities around the world, as well as top graduates from the leading universities in China. We believe this combination has enabled us to quickly bring our technology in line with the semiconductor industry technology roadmap and ensures that we will have skilled personnel to lead our technology advancement in the future.

Intellectual Property

While we continue to develop and patent our own technologies, we expect to have an ongoing need to obtain licenses for the proprietary technologies of third parties to enable us to manufacture certain advanced wafers for our customers. As of 2007 year-end, we have been granted two hundred and nine patents, and have more than one thousand eight hundred twenty six patent applications pending worldwide. We believe our competitors and other industry participants have numerous patents concerning wafer fabrication and related technologies in multiple countries.

We implement a variety of measures to protect the intellectual property and related interests of our company, customers and technology partners. We require our employees to execute a confidential information and invention assignment agreement relating to non-competition and intellectual property protection issues prior to commencing their employment at our company. Access to customer information is granted to employees strictly on a need-to-know basis both during and after mask tooling.

We have applied for trademarks relating to our corporate logo, English trade name SMIC , and Chinese trade name in the United States, China, Hong Kong and Taiwan. We have been granted registration of trademarks for our corporate logo in China, English trade name in China and Taiwan, and Chinese trade name in Hong Kong, United States and China (except a dispute in China for certain applied product/service category). There can be no assurance that other trademarks registration will be granted.

Competition

We compete internationally and domestically with dedicated foundry service providers, as well as with semiconductor companies that allocate a portion of their fabrication capacity to foundry operations. While the principal elements of competition in the wafer foundry market include technical competence, production speed and cycle time, time-to-market, research and development quality, available capacity, yields, customer service and price, we seek to compete on the basis of process technology capabilities, performance, quality and service, rather than solely on price. The level of competition differs according to the process technology involved.

Our competitors and potential competitors include other pure-play foundries such as TSMC, UMC and Chartered Semiconductor. TSMC has commenced commercial production at its fab in China, and UMC has established a relationship with a fab in commercial production in China. Another group of potential competitors consists of IDMs that have established their own foundry capabilities. These include Fujitsu Limited, Hynix, MagnaChip, IBM, Samsung Electronics Co., Ltd. and Toshiba. IDMs are primarily dedicated to fabricating integrated circuits for the end products of their respective affiliates. See Risk Factors Risks Related to Our Financial Condition and Business If we cannot compete successfully in our industry, particularly in China, our results of operations and financial condition will be adversely affected.

Table of Contents

Quality and Reliability

We have implemented quality assurance measures relating to material quality control, monitoring of our in-line processes and wafer-level reliability control at every stage of our operations from technology development to production. By combining advanced quality assurance procedures and e-commerce technology, we monitor all processes, services and materials in our mask-making, wafer fabrication and probing facilities. These quality assurance measures include inspection of incoming materials, supplier and subcontractor management, manufacturing environmental control and monitoring, in-line defect monitoring, engineering change control, calibration monitoring, chemical analysis and visual inspection. Quality assurance measures also include on-going process and product reliability monitors and failure tracking for early identification of production problems.

We incorporate reliability control in our entire production process and have adopted a system that enables us to track and record wafer-, package- and product-level reliability data throughout the development, qualification and production stages of the relevant process or device. This data enables us to identify problems at an early stage and provide an immediate diagnosis and solution, so as to further reduce our failure rate.

We achieved ISO 9001:2000 certification from the British Standards Institute with zero-defect performance for our Fab 1 in July 2002 and for our Fab 2 and Fab 3B in March 2003. The ISO 9001 quality standards were established by the International Standards Organization, an organization formed by delegates from member countries to establish international quality assurance standards for products and manufacturing processes. International Standards Organization certification is required in connection with sales of industrial products in many countries. To further enhance our quality management system, we obtained TS 16949:2002 certification from the British Standards Institute (BSI) in February 2004. This is an International Standards Organization quality management certification that relates to automobile applications and primarily measures a device s ability to handle extreme changes in temperature. In January 2005, we obtained TL9000 Quality Management System certification from BSI. This is a management certification relating to the telecommunications industry and evaluates research and development, production and installation and maintenance of communication product and services.

Raw Materials

Our fabrication processes use many raw materials, primarily silicon wafers, chemicals, gases, and various types of precious and other metals. Raw material costs constituted 18.9% of our cost of sales in 2005, 18.3% of our cost of sales in 2006 and 21% of our cost of sales in 2007. The three largest components of raw material costs raw wafers, chemicals and gases accounted for approximately 42%, 22% and 11%, respectively, of our raw material costs in 2005, approximately 43%, 21%, and 11%, respectively, of our raw material costs in 2006, and approximately 47%, 20%, and 10%, respectively, of our raw materials in 2007. Most of our raw materials generally are available from several suppliers, but substantially all of our principal materials requirements must currently be sourced from outside China.

The most important raw material used in our production is silicon in the form of raw wafers. In 2007, we purchased approximately 71.8% of our overall raw wafer requirements from our three major raw wafer suppliers. The prices of our principal raw material are not considered to be volatile.

For 2007, our largest and five largest raw materials suppliers accounted for approximately 14.0% and 48.2%, respectively, of our overall raw materials purchases. For 2006, our largest and five largest raw materials suppliers accounted for approximately 14.7% and 46.1%, respectively, of our overall raw materials purchases. For 2005, our largest and five largest raw materials suppliers accounted for approximately 14.0% and 43.5%, respectively, of our overall raw materials purchases. Having made all reasonable inquiry, we are not aware of any director or shareholder (which to the knowledge of our directors own more than 5% of our issued share capital) or their respective associates, which had shareholding interests in any of our five largest suppliers. Most of our materials are imported free of value-added tax and import duties due to concessions granted to our industry in China.

Table of Contents

Electricity and Water

We use substantial amounts of electricity in our manufacturing process. This electricity is sourced from the Pudong Electricity Corporation (for Shanghai), the Beijing Municipal Electricity Department, the Tianjin Municipal Electricity Department, and the PiXian Municipal Electricity Department (for Chengdu). We enjoy a preferential electricity supply for our Shanghai fabs due to our location in the Zhangjiang High-Tech Park. We maintain Uninterrupted Power Supply (UPS) systems and emergency back-up generators to power life safety and critical equipment and systems for emergencies.

The semiconductor manufacturing process uses extensive amounts of fresh water. We source our fresh water for our Shanghai mega-fab from Pudong Vivendi Water Corporation Limited, for our Beijing mega-fab from Beijing Waterworks Group Co. Ltd., for our Tianjin fab from the Tianjin Municipal Water Department, and for our Chengdu facility from the Xipu Water Corporation, Ltd. Because Beijing and Tianjin are subject to potential water shortages in the summer, our fabs in Beijing and Tianjin are equipped with back-up reservoirs. We have taken steps to reduce fresh water consumption in our fabs and capture rainwater for use at our Beijing facilities, and our water recycling systems in each of our fabs allow us to recycle 40% to 70% of the water used during the manufacturing process. The Beijing site is also equipped to use recycled/treated industrial waste water from the Beijing Economic and Technological Development Area for non-critical operations.

Regulation

Integrated circuit industry in China is subject to substantial regulation by the Chinese government. This section sets forth a summary of the most significant Chinese regulations that affect our business in China.

Scope of Regulation

The *Several Policies to Encourage the Development of Software and Integrated Circuit Industry*, or the Integrated Circuit Policies, promulgated by the State Council of The People s Republic of China on June 24, 2000, together with other ancillary laws and regulations, regulate integrated circuit production enterprises, or ICPEs. The State Council issued the Integrated Circuit Policies in order to encourage the development of the software and integrated circuits industry in China. The Integrated Circuit Policies form the basis for a series of laws and regulations that set out in detail the preferential policies relating to ICPEs. Such laws and regulations include:

the *Notice of the Ministry of Finance, the State Administration of Taxation and the General Administration of Customs on Relevant Taxation Policy Encouraging the Further Development of the Software Industry and the Integrated Circuit Industry,* or the Integrated Circuit Notice, jointly issued by the Ministry of Finance, the State Administration of Taxation and the General Administration of Customs on September 22, 2000, as amended by the *Notice of the Ministry of Finance and the State Administration of Taxation on Approval Procedure Concerning Foreign Invested Enterprises Implementing Enterprise Income Tax Policies of the Software and Integrated Circuit Industry*, or the Approval Notice, jointly issued by the Ministry of Finance and the State Administration of Taxation on July 1, 2005;

the *Notice of the Ministry of Finance, the State Administration of Taxation on Taxation Policies Concerning the Tax Policies for Further Encouraging the Development of the Software and the Integrated Circuit Industry*, or the Further Development Taxation Notice, jointly issued by the Ministry of Finance and the State Administration of Taxation on October 10, 2002, as amended by *Notice of the Ministry of Finance, the State Administration of Taxation on Termination of Value-added Tax Refund Policies for Integrated Circuits*, or the Termination Notice, jointly issued by the Ministry of Finance and the State Administration of Taxation on October 25, 2004;

the *Notice of the Ministry of Finance on Taxation Policies Concerning the Import of Self-used Raw Materials and Consumables by Part of Integrated Circuit Production Enterprises*, or the Raw Materials Taxation Notice, issued by the Ministry of Finance on August 24, 2002;

Table of Contents

the *Notice on Taxation Policies Concerning the Import of Construction Materials Specially used for Clean Rooms by Part of the Integrated Circuit Production Enterprises*, or the Construction Materials Taxation Notice, issued by the Ministry of Finance on September 26, 2002;

the *Notice by the Ministry of Finance and the State Administration of Taxation on Increasing Tax Refund Rate for Export of Certain Information Technology(IT) Products*, or the Export Notice, issued by the Ministry of Finance and the State Administration of Taxation on December 10, 2004;

the *Measures for the Accreditation of the Integrated Circuit Enterprise Encouraged by the State (For Trial Implementation)*, or the Accreditation Measures, jointly issued by the National Development and Reform Commission, the Ministry of Information Industry, the State Administration of Taxation and the General Administration of Customs on October 21, 2005; and

the *Interim Measures for the Management of the Special Fund for the Research and Development of the Integrated Circuit Industry,* or the Fund Measures, jointly issued by the Ministry of Finance, the Ministry of Information Industry and the National Development and Reform Commission on March 23, 2005.

Preferential Industrial Policies Relating to ICPEs

ICPEs which are duly accredited in accordance with relevant laws and regulations may qualify for preferential industrial policies. Under the Integrated Circuit Policies, accreditation of ICPEs is determined by the competent examination and approval authorities responsible for integrated circuit projects after consultation with relevant taxation authorities. Under the Accreditation Measures, an integrated circuit enterprise refers to an independent legal entity duly established in the PRC (except for Hong Kong, Macao, and Taiwan) engaging in the fabrication, package, or testing of integrated circuit chips and the production of monocrystalline silicon of six inches or above, excluding the integrated circuit design enterprise. The accreditation of ICPEs is included in the accreditation of the integrated circuit enterprises. Such accreditation is determined by the competent authorities consisting of the National Development and Reform Commission, the Ministry of Information Industry, the State Administration of Taxation and the General Administration of Customs, which jointly designate the China Semiconductor Industrial Association as the accreditation institution. Any enterprise qualified under the requirements set forth in the Accreditation Measures is entitled to apply to the China Semiconductor Association for the Accreditation of the ICPEs. The accreditation of ICPEs is annually reviewed. If the enterprise fails to apply for the annual review in time, it shall be deemed as giving up such accreditation and if the enterprise fails in the annual review, the accreditation will also be canceled.

SMIC Shanghai, SMIC Beijing, and SMIC Tianjin have been accredited as ICPEs and are entitled to the preferential industrial policies described below.

Encouragement of Domestic Investment in ICPEs

Pursuant to the *Interim Provisions on Promoting Industrial Structure Adjustment*, or the Interim Provisions, issued by the State Council on December 2, 2005, and the *Catalogue for the Guidance of Industrial Structure Adjustment*, or the Guidance Catalogue, which is the basis and criteria for implementing the Interim Provisions, issued by the National Development and Reform Commission and all the State Council Institutions on December 2, 2005, the Chinese government encourages (i) the design and fabrication of large scale integrated circuits with a line width of less than 1.2 micron, (ii) the fabrication of the equipment of large scale integrated circuit and (iii) the fabrication of mixed integrated circuits. Under the Interim Provisions, imported equipment that is used for a qualifying domestic investment project and that falls within such project s approved total investment amount is exempt from custom duties and import-linked value-added tax, except for such equipment listed in the *Catalogue of Import Commodities for*

Table of Contents

Domestic Investment Projects Not Entitled to Tax Exemptions, as stipulated by the State Council and amended in 2006.

Encouragement of Foreign Investment in ICPEs

Pursuant to the Integrated Circuit Policies and the *Guideline Catalogue of Foreign Investment Industries* promulgated jointly by the State Development and Reform Commission and the Ministry of Commerce on October 11, 2007, the following foreign investment categories are encouraged:

design of integrated circuits;

fabrication of large scale integrated circuits with a line width of less than 0.18 micron (including 0.18 micron);

fabrication of analog and analog digital integrated circuits with a line width of less than 0.8 micron (including 0.8 micron);

advanced packaging and testing of BGA, PGA, CSP, MCM;

fabrication of mixed integrated circuits.

Foreign investment in such encouraged projects may enjoy preferential treatment as stipulated by the laws and regulations.

Preferential Taxation Policies

Preferential Value-added Tax Policy

Under Article 1 of the Further Development Taxation Notice (October 10, 2002 No. 70 [2002] Cai-Shui), from January 1, 2002 to the end of 2010, the sale of integrated circuits (including monocrystalline silicon chips) is subject to a value-added tax levy of 17%. After the value-added tax is levied, the taxpayer is to be entitled to a refund for the portion exceeding 3% of the actual value-added tax burden. The tax refund was required to be used by the enterprise for the research and development of integrated circuits and to increase production.

Under the Termination Notice (No. 174 [2004] of the Ministry of Finance), as of April 1, 2005, implementation of Article 1 of the Further Development Taxation Notice was terminated.

Under the Export Notice (No. 200 [2004] Cai-Shui), as of November 1, 2004, the tax refund rate for exports of electronic integrated circuits and micro-assemblies is to increase from 13% to 17%.

Preferential Enterprise Income Tax Policies

Under Article 42 of the Integrated Circuit Policies (No. 18 [2000] Guo-Fa) and Article 2(3) of the Integrated Circuit (Notice No. 25 [2000] Cai-Shui*)*, ICPEs whose total investment exceeds Rmb 8,000 million (approximately US$967 million) or whose integrated circuits have a line-width of less than 0.25 micron are entitled to preferential tax treatment similar to that granted for foreign investment in the energy and communications industries. The Income Tax Law of the People s Republic of China for Enterprises with Foreign Investment and Foreign Enterprises, or the Income Tax Law, and the Implementation Rules for the Income Tax Law provide preferential treatment of, exemption from or reduction of foreign enterprise income tax, or FEIT, for enterprises with foreign investment engaged in the energy and communications industries. After approval by the relevant taxation authorities, each of SMIC Shanghai, SMIC Beijing and SMIC Tianjin will become entitled to a full exemption from FEIT for five years starting with the first year of positive accumulated earnings and a 50% reduction for the following five years or five year exemption and five year reduction .

From January 1, 2002 to the end of 2010, investors in ICPEs and integrated circuit packaging enterprises that reinvest their after-income-tax profits from ICPEs for the purpose of increasing the registered capital in the ICPEs, or to establish other ICPEs and integrated circuit packaging enterprises for a

Table of Contents

period of operation of not less than five years, are entitled to a refund of 40% of the total amount of enterprise income tax paid on the reinvested portion. If the investment is withdrawn before the period of operation reaches five years, the amount of enterprise income tax refunded shall be repaid. From January 1, 2002 to the end of 2010, domestic or foreign investors that reinvest their after income-tax profits from sources within China in order to establish ICPEs or integrated circuit package enterprises in China s western regions for a period of operation of not less than five years are entitled to a refund of 80% of total amount of enterprise income tax paid on the reinvested portion. If the investment is withdrawn before the period of operation reaches five years, the amount of enterprise income tax refunded shall be repaid.

On March 16, 2007, the National People s Congress, the PRC legislature, approved and promulgated a new tax law named Enterprise Income Tax Law, On December 6, 2007, the PRC State Council issued the Implementation Regulations of the Enterprise Income Tax Law, both of which became effective on January 1, 2008.The Enterprise Income Tax Law and its Implementation Regulations, or the new EIT law, FIEs and domestic companies are subject to a uniform tax rate of 25%. The new EIT law eliminates or modifies most of the tax exemptions, reductions and preferential treatments available under the previous tax laws and regulations. The State Council issued the Notice of the State Council on the Implementation of the Transitional Preferential Policies in respect of Enterprise Income Tax on December 26, 2007, enterprises that were established before March 16, 2007 and already enjoy preferential tax treatments will (i) in the case of preferential tax rates, continue to enjoy the tax rates which will be gradually increased to the new tax rates within five years from January 1, 2008 or (ii) in the case of preferential tax exemption or reduction for a specified term, continue to enjoy the preferential tax holiday until the expiration of such term. Thus, SMIC Shanghai, SMIC Beijing and SMIC Tianjin could fall into condition (ii) and may be entitled to the five year exemption and five year reduction as subject to the final recognition by the PRC tax authorities. While the EIT Law equalizes the tax rates for FIEs and domestic companies, preferential tax treatment would continue to be given to companies in certain encouraged sectors and to entities classified as high-technology companies supported by the PRC government, whether FIEs or domestic companies. According to the new EIT Law, entities that qualify as high-technology companies especially supported by the PRC government are expected to benefit from a tax rate of 15% as compared to the uniform tax rate of 25%. Implementation Regulations of the Enterprise Income Tax Law, a high-technology enterprise shall have core self-owned intellectual properties and its products shall be within the scope provided by the high-technology field highly supported by the State . However, the high-technology field highly supported by the State has not been issued, so there can be no assurances that SMIC Shanghai, SMIC Beijing, SMIC Tianjin and SMIC Chengdu will continue to qualify as high-technology companies supported by the PRC government in the future, and benefit from such preferential tax rate.

Under the new EIT law, dividends, interests, rent, royalties and gains on transfers of property payable by a foreign-invested enterprise in the PRC to its foreign investor who is a non-resident enterprise will be subject to a 10% withholding tax, unless such non-resident enterprise s jurisdiction of incorporation has a tax treaty with the PRC that provides for a reduced rate of withholding tax. The Cayman Islands, where SMIC is incorporated, does not have such a tax treaty with the PRC. If SMIC is considered a non-resident enterprise, this new 10% withholding tax imposed on SMIC s dividend income received from SMIC Shanghai, SMIC Beijing and SMIC Tianjin would reduce its net income and have an adverse effect on its operating results.

Under the new EIT law, an enterprise established outside the PRC with its de facto management body within the PRC is considered a resident enterprise and will be subject to the enterprise income tax at the rate of 25% on its worldwide income and foreign tax credit may be applicable. The de facto management body is defined as the organizational body that effectively exercises overall management and control over production and business operations, personnel, finance and accounting, and properties of the enterprise. It remains unclear how the PRC tax authorities will interpret such a broad definition. Substantially the majority of management members of SMIC are based in the PRC. If the PRC tax authorities subsequently determine that SMIC should be classified as a resident enterprise, then SMIC s worldwide income will be subject to income tax at a uniform rate of 25%, which may have a material adverse effect on SMIC s financial condition and results of operations. Notwithstanding the foregoing provision, the new EIT law also provides that, if a resident enterprise directly invests in another resident

Table of Contents

enterprise, the dividends received by the investing resident enterprise from the invested enterprise are exempted from income tax, subject to certain conditions. Therefore, if SMIC is classified as a resident enterprise, the dividends received from our PRC subsidiary may be exempted from income tax and the dividends paid to our non-PRC shareholders and gains derived by our non-PRC shareholders from transferring our shares or ADSs may be subject to 10% withholding tax. However, it remains unclear how the PRC tax authorities will interpret the PRC tax resident treatment of an offshore company, like SMIC, having indirect ownership interests in PRC enterprises through intermediary holding vehicles.

Exemption of Customs Duties and Import-related Value-added Tax

Under the Integrated Circuit Policies (No. 18 [2000] Guo-Fa) and the Integrated Circuit Notice (No. 25 [2000] Cai-Shui), ICPEs whose total investment exceeds Rmb 8,000 million or whose integrated circuits have a line-width of less than 0.25 micron are exempt from customs duties and import-related value-added tax for the raw materials and consumables used for production purposes.

Under the Integrated Circuit Notice, integrated circuit technology, production equipment, and equipment and instruments specialized for use in fabricating integrated circuits that are imported by a duly accredited ICPE are, with the exception of commodities listed in the *Catalogue of Imported Commodities for Foreign Investment Projects Not Entitled to Tax Exemptions* and the *Catalogue of Imported Commodities for Domestic Investment Projects Not Entitled to Tax Exemptions* as stipulated by the Ministry of Finance and all the State Council Institutions and Departments and amended in 2006, exempt from customs duties and import-related value-added tax.

Under the Construction Materials Taxation Notice (No. 152 [2002] Cai-Shui), commencing January 1, 2001, the importation of construction materials, auxiliary equipment and spare parts for the production of integrated circuits, specifically for clean rooms (as listed in the annex to the Construction Materials Taxation Notice), by ICPEs whose total investment exceeds Rmb 8,000 million or whose integrated circuits have a linewidth of less than 0.25 micron is exempt from customs duties and import-related value-added tax.

Preferential Policies Encouraging Research and Development

Under the Fund Measures (No. 132 [2005] Cai-Jian), enterprises duly incorporated as independent legal entities in the PRC (except for Hong Kong, Macao, and Taiwan) engaging in the design, fabrication, package or testing of integrated circuits may apply for the special fund designed to support exclusively the research and development of the integrated circuit industry. Such fund is appropriated from central budget and the application of it is subject to the review and approval by the Examination Committee consisting of the members from the Ministry of Finance, the National Development and Reform Commission and the Ministry of Information Industry. The special fund for research and development shall be in a form of gratuitous aid and the amount of such aid to a single research and development activity shall not exceed 50% of the expenditures thereof.

Legal Framework Concerning the Protection of Intellectual Property Relating to Integrated Circuits

China has formulated various laws and regulations on intellectual property protection in respect of integrated circuits including:

the *Patent Law of the People s Republic of China*, adopted at the fourth meeting of the Standing Committee of the Sixth National People s Congress on March 12, 1984, effective April 1, 1985 and amended by the Ninth National People s Congress on August 25, 2000;

the *Paris Convention for the Protection of Industrial Property* of the World Intellectual Property Organization, in which China became a member state as of March 19, 1985;

the *General Principles of the Civil Law of the People s Republic of China* adopted at the fourth session of the Sixth National People s Congress on April 12, 1986, effective January 1, 1987. In

Table of Contents

this legislation, intellectual property rights were defined in China s basic civil law for the first time as the civil rights of citizens and legal persons;

the *Copyright Law of the People s Republic of China*, adopted by the 15th meeting of the Seventh National People s Congress Standing Committee on September 7, 1990, effective June 1, 1991 and amended by the Ninth National People s Congress on October 27, 2000;

the *Regulations for the Protection of the Layout Design of Integrated Circuits*, or the Layout Design Regulations, adopted April 2, 2001 at the thirty-sixth session of the executive meeting of the State Council, effective October 1, 2001; and

the World Intellectual Property Organization s *Washington Treaty on Intellectual Property in Respect of Integrated Circuits*, for which China was among the first signatory states in 1990.

Protection of the Layout Design of Integrated Circuits

Under the Layout Design Regulations, layout design of an integrated circuit refers to a three dimensional configuration in an integrated circuit that has two or more components, with at least one of these being an active component, and part or all of the interconnected circuitry or the three-dimensional configuration prepared for the production of integrated circuits.

Chinese natural persons, legal persons or other organizations that create layout designs are entitled to the proprietary rights in the layout designs in accordance with the Layout Design Regulations. Foreign persons or enterprises that create layout designs and have them first put into commercial use in China are entitled to the proprietary rights in the layout designs in accordance with the Layout Design Regulations. Foreign persons or enterprises that create layout designs and that are from a country that has signed agreements with China regarding the protection of layout designs, or is a party to an international treaty concerning the protection of layout designs to which China is also a party, are entitled to the proprietary rights of the layout designs in accordance with the Layout Design Regulations.

Proprietary Rights in Layout Design of Integrated Circuits

Holders of proprietary rights in a layout design are entitled to the following proprietary rights:

to duplicate the whole protected layout design or any part of the design that is original; and

to make commercial use of the protected layout design, the integrated circuit containing the layout design, or commodities containing the integrated circuit.

Proprietary rights in layout designs become valid after being registered with the administrative department of the State Council responsible for intellectual property. Unregistered layout designs are not protected by the Layout Design Regulations.

The protection period of the proprietary rights in a layout design is ten years, commencing from the date of the application for registration of the layout design or the date that it is put into commercial use anywhere in the world, whichever is earlier. However, regardless of whether or not a layout design is registered, or whether or not it is put into commercial use, it is not protected after 15 years from the time of its creation.

Registration of a Layout Design

The administrative departments of the State Council responsible for intellectual property are responsible for the registration of layout designs and accepting applications for the registration of layout designs. If an application for a layout design registration is not made with the administrative department of the State Council responsible for intellectual property within two years after it has been put into commercial use anywhere in the world, the administrative department of the State Council responsible for

Table of Contents

intellectual property will not register the application. A holder of proprietary rights in a layout design may transfer the proprietary rights or give permission for other parties to use the layout design.

Compulsory Licenses for Exploitation of Patents in Respect of Semiconductor Technology

Under the Patent Law and the Implementing Regulations of the Patent Law, after three years from the date of granting the patent rights, any person or enterprise that has made good faith reasonable proposals to the holder of proprietary rights seeking a license to those rights, but has been unable to obtain such license after an extended period of time, may request the administrative department responsible for patents under the State Council to grant a compulsory license for the relevant patent. However, where a compulsory license involves semiconductor technology, the implementation of a compulsory license is restricted to public and non-commercial uses, or to uses that counteract anti-competitive actions, as determined by judicial or administrative procedures.

PRC Tax for Resident Enterprises

Under China s New EIT Law, we may be classified as a resident enterprise of China. This classification could result in unfavorable tax consequences to us and our non-PRC shareholders. The implementing rules of the New EIT Law define de facto management bodies as management bodies that exercises substantial and overall management and control over the production and operations, personnel, accounting, and properties of the enterprise. Currently no official interpretation or application of this new resident enterprise classification is available, therefore it is unclear how tax authorities will determine tax residency based on the facts of each case.

If the PRC tax authorities determine that our Cayman Islands holding company is a resident enterprise for PRC enterprise income tax purposes, a number of unfavorable PRC tax consequences could follow. First, we may be subject to enterprise income tax at a rate of 25% on our worldwide taxable income as well as PRC enterprise income tax reporting obligations. Second, although under the New EIT Law and its implementing rules dividends income between qualified resident enterprises is exempted income, it is not clear what is considered a qualified resident enterprise under the New EIT Law. Finally, it is possible that future guidance issued with respect to the new resident enterprise classification could result in a situation in which a 10% withholding tax is imposed on dividends we pay to our non-PRC shareholders and with respect to gains derived by our non-PRC shareholders from transferring our shares or ADSs. Similarly, these unfavorable consequences could apply to our other overseas intermediary holding companies if they are classified as a PRC resident enterprises.

Environmental Regulation

Our Chinese subsidiaries are subject to a variety of Chinese environmental laws and regulations promulgated by the central and local governments concerning examination and acceptance of environmental protection measures in construction projects, the use, discharge and disposal of toxic and hazardous materials, the discharge and disposal of waste water, solid waste, and waste gases, control of industrial noise and fire prevention. These laws and regulations set out detailed procedures that must be implemented throughout a project s construction and operation phases. A key document that must be submitted for the approval of a project s construction is an environmental impact assessment report that is reviewed by the relevant environmental protection authorities. Upon completion of construction, and prior to commencement of operations, an additional examination and acceptance by the relevant environmental authority of such projects is also required. Within one month after receiving approval of the environmental impact assessment report, a semiconductor manufacturer is required to apply to and register with the competent environmental authority the types and quantities of liquid, solid and gaseous wastes it plans to discharge, the manner of discharge or disposal, as well as the level of industrial noise and other related factors. If the above wastes and noise are found by the authorities to have been managed within regulatory levels, renewable discharge registrations for the above wastes and noise are then issued for a specified period of time. SMIC Shanghai, SMIC Beijing, SMIC Tianjin, and SMIC Chengdu have all received approval with respect to their relevant environmental impact assessment reports and discharge registrations.

Table of Contents

From time to time during the operation of our Chinese subsidiaries, and also prior to renewal of the necessary discharge registrations, the relevant environmental protection authority will monitor and audit the level of environmental protection compliance of these subsidiaries. Discharge of liquid, solid or gaseous waste over permitted levels may result in imposition of fines, imposition of a time period within which rectification must occur or even suspension of operations.

Enforceability Of Civil Liabilities

We are a Cayman Islands holding company. We are incorporated in the Cayman Islands because of the following benefits associated with being a Cayman Islands corporation:

political and economic stability;

an effective judicial system;

a favorable tax system;

the absence of exchange control or currency restrictions; and

the availability of professional and support services.

However, the Cayman Islands have a less developed body of securities laws as compared to the United States and provides significantly less protection for investors. In addition, Cayman Islands companies may not have standing to sue before the federal courts of the United States. Substantially all of our assets are located outside the United States. In addition, most of our directors and officers are nationals and/or residents of countries other than the United States, and all or a substantial portion of our or such persons assets are located outside the United States. As a result, it may be difficult for a shareholder to effect service of process within the United States upon us or such persons or to enforce against them or against us, judgments obtained in United States courts, including judgments predicated upon the civil liability provisions of the securities laws of the United States or any state thereof.

Maples and Calder, our counsel as to Cayman Islands law, Slaughter and May, our counsel as to Hong Kong law, and Fangda Partners, our counsel as to Chinese law, have advised us that there is uncertainty as to whether the courts of the Cayman Islands, Hong Kong and China, respectively, would:

recognize or enforce judgments of United States courts obtained against us or our directors or officers predicated upon the civil liability provisions of the securities laws of the United States or any state thereof, or

be competent to hear original actions brought in each respective jurisdiction, against us or our directors or officers predicated upon the securities laws of the United States or any state thereof.

Maples and Calder has further advised us that a final and conclusive judgment in the federal or state courts of the United States under which a sum of money is payable, other than a sum payable in respect of taxes, fines, penalties or similar charges, may be subject to enforcement proceedings as a debt in the Courts of the Cayman Islands under the common law doctrine of obligation.

Organizational Structure

We operate primarily through three wholly owned subsidiaries in China. The chart below sets forth our significant operating subsidiaries or affiliates, including their jurisdictions of incorporation and principal activities:

Table of Contents

Name of company	Place and date of incorporation/establishment	Attributable equity interest held	Principal Activity
Garrison Consultants Limited (Garrison)	Samoa April 5, 2000	100%	Provision of consultancy services
Betterway Enterprises Limited (Better Way)	Samoa April 5, 2000	100%	Provision of marketing related services
Semiconductor Manufacturing International (Shanghai) Corporation*	The People s Republic of China (the PRC) December 21, 2000	100%	Manufacturing and trading of semiconductor products
Semiconductor Manufacturing International (Beijing) Corporation*	The PRC July 25, 2002	100%	Manufacturing and trading of semiconductor products
Semiconductor Manufacturing International (Tianjin) Corporation*	The PRC November 3, 2003	100%	Manufacturing and trading of semiconductor products
SMIC Japan Corporation #	Japan October 8, 2002	100%	Provision of marketing related activities
SMIC Europe S.R.L.	Italy July 3, 2003	100%	Provision of marketing related activities
SMIC, Americas	United States of America June 22, 2001	100%	Provision of marketing related activities
Semiconductor Manufacturing International (AT) Corporation	Cayman Islands July 26, 2004	57.3%	Investment holding
Semiconductor Manufacturing International (Chengdu) Corporation (SMICD) *	The PRC August 16, 2004	57.3%	Manufacturing and trading of semiconductor products
		100%	

SMIC Commercial (Shanghai) Limited Company (formerly SMIC Consulting Corporation) *	The PRC September 30, 2003	Operation of a convenience store

Table of Contents

Name of company	Place and date of incorporation/establishment	Attributable equity interest held	Principal Activity
Semiconductor Manufacturing International (Solar Cell) Corporation	Cayman Islands June 30, 2005	100%	Investment holding
SMIC Energy Technology (Shanghai) Corporation#*	The PRC September 9, 2005	100%	Manufacturing and trading of Solar cell related semiconductor products
SMIC Development (Chengdu) Corporation*	The PRC December 29, 2005	100%	Construction, operation, management of SMICD s living quarter, schools and supermarket
Magnificent Tower Limited	British Virgin Islands January 5, 2006	100%	Investment Holding
Semiconductor Manufacturing International (BVI) Corporation (SMIC (BVI))	British Virgin Islands April 26, 2007	100%	Investment Holding
SMIC Solar Cell (HK) Company Limited (SMIC Solar Cell (HK))	Hong Kong October 23, 2007	100%	Investment Holding
SMIC AT (HK) Company Limited (SMIC AT (HK))	Hong Kong October 22, 2007	57.3%	Investment Holding
SMIC Shanghai (HK) Company Limited (SMIC SH (HK))	Hong Kong November 1, 2007	100%	Investment Holding
SMIC Beijing (HK) Company Limited (SMIC BJ (HK))	Hong Kong November 2, 2007	100%	Investment Holding
SMIC Tianjin (HK) Company Limited (SMIC TJ (HK))	Hong Kong November 2, 2007	100%	Investment Holding
SMIC Shanghai (Cayman) Corporation (SMIC SH (Cayman))	Cayman Islands November 8, 2007	100%	Investment Holding
SMIC Beijing (Cayman) Corporation (SMIC BJ (Cayman))	Cayman Islands November 8, 2007	100%	Investment Holding
		100%	

SMIC Tianjin (Cayman) Corporation (SMIC TJ (Cayman))	Cayman Islands November 8, 2007	Investment Holding

* Companies registered as wholly-owned foreign enterprises in the PRC.

\# For identification purposes only

Table of Contents

Property, plant and equipment

Equipment

The quality and level of technology of the equipment used in the semiconductor fabrication process are important because they dictate the limits of the process technology that we use. Advances in process technology cannot be achieved without corresponding advances in equipment technology. The principal pieces of equipment used by us to fabricate semiconductors are scanners, cleaners and track equipment, inspection equipment, etchers, furnaces, wet stations, strippers, implanters, sputterers, CVD equipment, testers and probers. We source substantially all of our equipment from vendors located in the United States, Europe and Japan.

In implementing our capacity expansion and technology advancement plans, we expect to make significant purchases of equipment required for semiconductor fabrication. Some of the equipment is available from a limited number of vendors and/or is manufactured in relatively limited quantities, and in some cases has only recently become commercially available. Our ability to obtain certain kinds of equipment from outside of China may be subject to restrictions. See Risk Factors Risks Related to Conducting Operations in China Limits placed on exports into China could substantially harm our business and operating results.

We maintain our equipment through a combination of in-house maintenance and outside contracting to our equipment vendors. We decide whether to maintain ourselves, or subcontract the maintenance of, a particular piece of equipment based on a variety of factors, including cost, complexity and regularity of the required periodic maintenance and the availability of maintenance personnel in China. Most of our equipment vendors offer maintenance services through technicians based in China.

Property

Our corporate headquarters and our mega-fab in Shanghai occupy 367,895 square meters of land, for which we hold valid land use rights certificates. These fabs currently occupy approximately 45% of this total land area. We also hold valid land use rights for the 240,140 square meters of land that comprise our Beijing site, approximately 75% of which will be occupied by the Beijing mega-fab. In 2005, we received land use rights certificates for 215,733 square meters of land in Tianjin, which is occupied by the Tianjin fab. We own all of the buildings and equipment for our fabs, except for certain customer-owned tooling provided to our Shanghai operations for test production on a consignment basis from our customers.

The following table sets forth the location, size and primary use of our real properties and whether such real properties are owned or leased.

Location	Size (Land/Building) (in square meters)	Primary Use	Owned[1] or Leased (Land/Building)
Zhangjiang High-Tech Park, Pudong New Area, Shanghai	367,895/164,795	Wafer fabrication	owned/owned
Beijing Economic and Technological Development Area	240,140/143,017	Wafer fabrication	owned/owned
Xiqing Economic Development Area, Tianjin	215,733/61,990	Wafer fabrication	owned/owned
Japan	na/55	Marketing activities	na/leased
USA	na/743	Marketing activities	na/leased
Italy	na/280	Marketing activities	na/leased
Hong Kong[2]	na/300	Representative Office	na/owned

(1) With respect to land located in China, ownership refers to holding a valid land use rights certificate. All land within municipal zones in China is owned by the Chinese government. Limited liability companies, joint stock companies, foreign-invested enterprises, privately held companies and individual natural persons must pay fees to be granted rights to use land within municipal zones. Legal

Table of Contents

use of land is evidenced and sanctioned by land use certificates issued by the local municipal administration of land resources. Land use rights granted for industrial purposes are limited to a term of no more than 50 years.

(2) In February 2006, we purchased approximately 300 square meter of property in Hong Kong through our indirect wholly-owned subsidiary, Magnificent Tower Limited, a company incorporated in the British Virgin Islands.

Our right to continued use of the land is subject to our continued compliance with the land use agreement that each of our Chinese subsidiaries has executed. The Chinese government has reserved the right to revoke our land use rights for special eminent domain purposes, in which case the government will compensate us. In addition, pursuant to an amendment to its domestic bank loan agreements, SMIC Beijing and SMIC Tianjin have pledged a portion of its land use right to the lenders. See Item 5 Operating and Financial Review and Prospects Liquidity and Capital Resources.

For a description concerning our capacity, capacity utilization rate and capacity expansion plans, please see Item 5-Operating and Financial Review and Prospects-Factors that Impact our Results of Operations.

Risk Management and Insurance

Our safety management philosophy is based on incident prevention and frequent safety audits. Incident prevention is achieved through:

mandatory staff and vendor safety training;

compliance of equipment and facilities to safety criteria, including the Semiconductor Equipment and Materials International and Chinese National Fire Protection Association standards; and

standard management procedures established by our environmental, health and safety committee.

Regularly scheduled safety audits are performed in accordance with established world standards, and we have been qualified under OHSAS 18001 internal auditing standards as of September 2003.

We have established a risk management committee and an emergency response center to respond to all emergencies. The facility monitoring and control system and security monitoring room located within our emergency response center are where all emergency responses begin. These rooms are equipped with 24-hour safety and security monitoring systems such as closed circuit television, gas monitoring systems, chemical dispensing systems, very early smoke detection apparatus, public announcement systems, and fire alarm systems.

Each department conducts emergency drills on a quarterly basis in accordance with our emergency response plan to address all possible emergency situations that could arise. These emergency scenarios include fires, gas leakages, chemical spills, and power losses.

We maintain insurance with respect to our facilities, equipment, and inventories. The insurance for the fabs and their equipment covers, subject to some limitations, various risks, including industrial accidents and natural disasters, generally up to their respective replacement values and loss due to business interruption. We have not made any significant claims under these insurance policies. Equipment and inventories in transit are also insured.

Environmental Matters

The semiconductor production process generates gaseous chemical wastes, liquid waste, waste water, and other industrial wastes in various stages of the fabrication process. We have installed various types of pollution control equipment for the treatment of gaseous chemical waste and liquid waste and equipment for the recycling of treated water in our fabs. Our operations are subject to regulation and

Table of Contents

periodic monitoring by PRC s State Environmental Protection Bureau, as well as local environmental protection authorities, including those under the Shanghai Pudong Municipal Government, the Beijing Municipal Government, the Tianjin Municipal Government, and the Chengdu Municipal Government, which may in some cases establish stricter standards than those imposed by the State Environmental Protection Bureau. The Chinese national and local environmental laws and regulations impose fees for the discharge of waste substances above prescribed levels, require the payment of fines for serious violations, and authorize the Chinese national and local governments to suspend any facility that fails to comply with orders requiring it to cease or remedy operations causing environmental damage. No such penalties have been imposed on us or any of our subsidiaries for violations of environmental pollution.

We believe our pollution control measures are effective, complying with the requirements applicable to the semiconductor industry in China and comparable to other countries. Waste generated from our operations, including acid waste, alkaline waste, flammable waste, toxic waste, oxidizing waste, and self-igniting waste, are collected and sorted for proper disposal. Furthermore, we have in many cases implemented waste reduction steps beyond the scope of current regulatory requirements.

The ISO14001 standard is a voluntary standard and part of a comprehensive series of standards for environmental management published by the International Standards Organization. The ISO14001standard cover environmental management principles, systems and supporting techniques. Starting in August 2002, all operating fabs have since achieved ISO14001 certification.

Furthermore, by March of 2007, these fabs have been third-party certified to be compliant with the RoHS (Restriction of the use of certain Hazardous Substances in electrical and electronic equipment) Directive of the European Union, which bans the use of various chemicals determined to be harmful to the environment.

Item 4A. Unresolved Staff Comments

Not applicable.

Item 5. Operating and Financial Review and Prospects

Overview

We were founded in April 2000. In 2000 and 2001, our company was in its development stage and did not have any sales. During this period, we established our management structure, acquired land use rights, constructed, equipped and commenced the ramp-up of production at our 8-inch wafer facilities in Shanghai which are referred to as the Shanghai mega-fab, and began our research and development activities. The first fab in the Shanghai mega-fab and the portion of our second fab, commenced commercial production in January 2002. The remaining portion of our second fab and a third fab commenced commercial production in January 2003. In January 2004, we acquired an 8-inch fab in Tianjin, China, which we refer to as our Fab 7, from MCEL, a wholly owned subsidiary of Motorola. The first fab in the Beijing mega-fab commenced commercial production in March of 2005. As of December 31, 2007, we had reached total wafer fabrication capacity of 185,250 8-inch wafer equivalents per month. Our wafers shipped and sales increased from 943,463 wafers and US$974.6 million for 2004 to 1,347,302 wafers and US$1,171.3 million for 2005 to 1,614,888 wafers and US$1,465.3 million for 2006 to 1,849,957 wafers and US$1,549.8 million for 2007.

We manage our business and measure our results of operations based on a single operating segment. We plan to have aggregate monthly wafer fabrication capacity of 162,000 8-inch wafer equivalents by the end of 2008. As we increase our capacity and corresponding wafer production, we benefit from economies of scale. When our capacity utilization is high, these economies of scale enable us to reduce our per wafer production cost and improve our margins. On the other hand, when our capacity utilization rate is low, our unused capacity results in higher per wafer production cost and decreased margins.

Table of Contents

Factors that Impact Our Results of Operations

Cyclicality of the Semiconductor Industry

The semiconductor industry is highly cyclical due mainly to the cyclicality of demand in the markets of the products that use semiconductors. As these markets fluctuate, the semiconductor market also fluctuates. This fluctuation in the semiconductor market is exacerbated by the tendency of semiconductor companies, including foundries, to make capital investments in plant and equipment during periods of high demand since it may require several years to plan, construct and commence operations at a fab. Absent sustained growth in demand, this increase in capacity often leads to overcapacity in the semiconductor market, which in the past has led to a significant underutilization of capacity and a sharp drop in semiconductor prices. The semiconductor industry is generally slow to react to declines in demand due to its capital-intensive nature and the need to make commitments for equipment purchases well in advance of the planned expansion.

Substantial Capital Expenditures

The semiconductor foundry industry is characterized by substantial capital expenditures. This is particularly true for our company as we have recently constructed and equipped fabs and are continuing to construct and equip new fabs. In connection with the construction and ramp-up of our capacity since our inception, we incurred capital expenditures of US$2,000 million, US$903 million, US$912 million, and US$860 in 2004, 2005, 2006, and 2007 respectively. We depreciate our manufacturing machinery and equipment on a straight-line basis over an estimated useful life of five to seven years. We recorded depreciation and amortization of US$457.0 million, US$769.4 million, US$919.6 million, and US$706.3 million in 2004, 2005, 2006, and 2007 respectively.

The semiconductor industry is also characterized by rapid changes in technology, frequently resulting in obsolescence of process technologies and products. As a result, our research and development efforts are essential to our overall success. We spent approximately US$78.9 million in 2005, US$94.1 million in 2006, and US$97.0 million for research and development, which represented 6.7%, 6.4%, and 6.3% respectively, of our sales for 2005, 2006, and 2007. Our research and development costs include non-recurring engineering costs associated with the ramp-up of a new wafer facility. In 2007, we continued to equip our new 12-inch fab at the Shanghai mega-fab. These research and development costs are subsequently classified in cost of sales upon commencement of commercial production at that particular wafer facility.

We currently expect that our capital expenditures in 2008 will reach approximately US$700 million, which we plan to fund through our operating cash flows and bank loans in order to expand our operations. If necessary, we will also explore other forms of external financing. In addition, our actual expenditures may exceed our planned expenditures for a variety of reasons, including changes in our business plan, our process technology, market conditions, equipment prices, or customer requirements. We will monitor the global economy, the semiconductor industry, the demands of our customers, and our cash flow from operations to adjust our capital expenditure plans.

Capacity Expansion

We have expanded, and plan to continue to expand, our capacity through internal growth and acquisitions. An increase in capacity may have a significant effect on our results of operations, both by allowing us to produce and sell more wafers and achieve higher sales, and as a cost component in the form of acquisition costs and depreciation expenses. We plan to have aggregate wafer fabrication capacity of 162,000 8-inch wafer equivalents per month by the end of 2008.

Pricing

We price our foundry services on either a per wafer or a per die basis, taking into account the complexity of the technology, the prevailing market conditions, the order size, the cycle time, the strength

Table of Contents

and history of our relationship with the customer, and our capacity utilization. Since a majority of our costs and expenses are fixed or semi-fixed, fluctuations in the average selling prices of semiconductor wafers have historically had a substantial impact on our margins. The average selling price of the wafers we shipped decreased 7.6% from US$907 per wafer in 2006 to US$838 in 2007, mainly due to lower ASP resulting from DRAM price decline.

Change in Process Mix and Technology Migration

Because the price of wafers processed with different technologies varies significantly, the mix of wafers that we produce is among the primary factors that affect our sales and profitability. The value of a wafer is determined principally by the complexity of the process technology used to fabricate the wafer. In addition, production of devices with higher levels of functionality and greater system-level integration requires more fabrication steps, and these devices generally sell for higher prices.

Prices for wafers of a given level of technology generally decline over the relevant process technology life cycle. As a result, we and our competitors are continuously in the process of developing and acquiring advanced process technologies and migrating our customers to use such technologies to maintain or improve our profit margins. This technology migration requires continuous investment in research and development and technology-related acquisitions, and we expect to continue to spend a substantial amount of capital on upgrading our technologies.

Our initial sales after commencing commercial operations in 2002 consisted mainly of DRAM fabricated and sold on a foundry basis, as well as commodity-type DRAM fabricated using technology licensed from a third party and sold by us to distributors. This commodity-type DRAM was fabricated during our start-up phase in order to test and ramp up our facilities and train our personnel. As our business has grown and our fabs have matured, we have produced proportionately less commodity-type DRAM and more logic products and memory products utilizing more advanced technologies, which generally command a higher margin. During the first quarter of 2008, the Company took the decision to exit the commodity DRAM business.

The following table sets forth a percentage breakdown of wafer sales by process technology for the years ended December 31, 2005, 2006 and 2007 and each of the quarters in the year ended December 31, 2007:

	For the year ended December 31,		For the three months ended				For the year ended
Process Technologies	2005	2006	March 31, 2007	June 30, 2007	September 30, 2007	December 31, 2007	December 31, 2007
			(based on sales in US$)				
0.13 micron and below	40.6%	49.6%	52.5%	55.0%	55.3%	49.7%	53.1%
0.15 micron	5.4%	5.7%	2.9%	1.2%	2.0%	5.5%	2.9%
0.18 micron	42.3%	35.7%	34.1%	30.8%	28.8%	28.3%	30.5%
0.25 micron	3.7%	2.0%	0.7%	0.7%	1.0%	0.5%	0.7%
0.35 micron	8.0%	7.0%	9.8%	12.3%	12.9%	16.0%	12.8%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

The following table sets forth a breakdown of our sales by service type for 2005, 2006 and 2007:

Table of Contents

	For the year ended December 31					
	2005		2006		2007	
Service Type	Sales	Percentage	Sales	Percentage	Sales	Percentage
	(in US$ thousands, except percentages)					
Fabrication of DRAM wafers	$ 384,587	32.8%	$ 476,970	32.6%	428,355	27.6%
Fabrication of logic wafers[1]	739,296	63.1%	923,411	63.0%	985,776	63.6%
Other[2]	47,436	4.1%	64,942	4.4%	135,634	8.8%
Total	$ 1,171,319	100.0%	$ 1,465,323	100.0%	$ 1,549,765	100.0%

(1) Includes copper interconnects and memory devices whose manufacturing process is similar to that for a logic device.

(2) Includes mask-making and probing, etc.

Capacity Utilization Rates

Operations at or near full capacity have a significant positive effect on our profitability because a substantial percentage of our cost of sales is of a fixed nature. In 2005, 2006 and 2007, approximately 60%, 59%, and 47% respectively, of our cost of sales consisted of depreciation expenses, which are fixed costs. If we increase our utilization rates, the number of wafers we fabricate will increase, and therefore our average fixed costs per wafer will decrease. Therefore, our capacity utilization rates have a significant effect on our margins. Our utilization rates have varied from period to period due to capacity ramp-ups and fluctuations in customer orders. Our annual capacity utilization rate was 89% in 2005, 89.6% in 2006, and 94.0% in 2007. Factors affecting utilization rates are the complexity and mix of the wafers produced, overall industry conditions, the level of customer orders, and mechanical failures and other operational disruptions, such as those relating to capacity expansions or relocation of equipment.

Our capacity is determined by us based on the capacity ratings for each piece of equipment, as specified by the manufacturers of such equipment, adjusted for, among other factors, actual output during uninterrupted trial runs, expected down time due to set up for production runs and maintenance, and expected product mix. Because these factors include subjective elements, our measurement of capacity utilization rates may not be comparable to those of our competitors.

Yield Rates

Yield per wafer is the ratio of the number of functional dies on that wafer to the maximum number of dies that can be produced on that wafer. A significant portion of our services, particularly our memory semiconductor wafer fabrication services, is priced on a per die basis.

We continuously upgrade the process technologies that we use. At the beginning of each technology migration, the yield utilizing the new technology is generally lower, sometimes substantially lower, than the yield under the

then-current technology. This is because it requires time to stabilize, optimize and test a new process technology. We do not ship wafers to a customer until we have achieved that customer s minimum yield requirements. Yield is generally improved through the expertise and cooperation of our research and development personnel, process engineers, and equipment suppliers.

Critical Accounting Policies

The methods, estimates and judgments we use in applying our accounting policies have a significant impact on the results we report in our financial statements. Some of our accounting policies require us to make difficult and subjective judgments, often as a result of the need to make estimates of matters that are inherently uncertain. Below we have summarized our accounting policies that we believe are both

Table of Contents

important to the portrayal of our financial results and involve the need to make estimates about the effect of matters that are inherently uncertain. We also have other policies that we consider to be key accounting policies. However, these policies do not meet the definition of critical accounting estimates because they do not generally require us to make estimates or judgments that are difficult or subjective.

Inventory

Inventories are stated at the lower of cost or market. Market represents the net realizable value for finished goods and work-in-progress. For products manufactured pursuant to customer purchase orders, we are not typically exposed to the risk that the selling price will be lower than the inventory carrying value. We also use available manufacturing capacity to produce commodity-type DRAM that we hold in inventory until sold. We are exposed to the risk that the ultimate selling price of such commodity-type DRAM may be less than the inventory carrying value. We estimate the net realizable value for such finished goods and work-in-progress based primarily upon the latest invoice prices and current market conditions. If the market value of a good drops below its carrying value, we record a write-off to cost of sales for the difference between the carrying cost and the market value. As of December 31, 2005, December 31, 2006 and December 31, 2007, the inventory written down as a result of a lower of cost or market was US$13.8 million, US$16.1 million, and US$22.7 million respectively, to reflect a decline in the estimated market value of the inventory we held on that date. We carry out an inventory review at each quarter-end.

Depreciation and Amortization

We operate in a capital-intensive business. We periodically review and assess the estimated useful life of our assets based on expected use by the Company, taking into account effects of obsolescence, demand, and other economic factors. The net book value of our plant and equipment, including land use rights, at December 31, 2007 was US$3,260.5 million. Depreciation of manufacturing buildings and related improvements is provided on a straight-line basis over the estimated useful life of 25 years and commences from the date the facility is ready for its intended use. Depreciation of our manufacturing machinery and equipment, as well as our facility, machinery and equipment, is provided on a straight-line basis over the estimated useful life of 5 to 10 years, commencing from the date that the equipment is placed into productive use. Amortization of land use rights is over the term of the land use right agreement, which ranges from 50 to 70 years. Amortization of intangible assets is computed using the straight-line method over the expected useful life of the assets ranging from 3 to 10 years. The estimated useful life and dates that the equipment is placed into productive use reflects our estimate of the periods that we intend to derive future economic benefits from the use of our plant and equipment and land use rights.

Long-lived Assets

We assess the impairment of long-lived assets when events or changes in circumstances indicate that the carrying value of the assets or the asset grouping may not be recoverable. Factors we consider in deciding when to perform an impairment review include significant under-performance of a manufacturing facility relative to expectations, significant underutilization of specific equipment relative to expectations, significant negative industry or economic trends, and significant changes or planned changes in our use of the assets. Recoverability of assets to be held and used is measured by comparing the carrying amount of the asset grouping to its future undiscounted cash flows. If such assets are considered to be impaired, an impairment charge is recognized for the amount that the carrying value of the asset exceeds its fair value. Assets held for sale are reported at the lower of their carrying amount or fair value less related selling costs.

In order to remain technologically competitive in our industry, we have entered into technology transfer and technology license arrangements with third parties in an attempt to advance our process technologies. The payments made for such technology licenses are recorded as an intangible asset or as a deferred cost and amortized on a straight-line basis over the estimated useful life of the asset. We routinely review the remaining estimated useful lives of these intangible assets and deferred costs. We also evaluate these intangible assets and deferred costs for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable.

Table of Contents

We have continued to construct, acquire, and expand our manufacturing facilities since our inception. We will continue to review impairment factors as described above and, as a result, impairment charges may be necessary in the future as circumstances change.

During the first quarter of 2008, the Company took the decision to exit the commodity DRAM business. The Company considers this an indicator of impairment in regard to the long-lived assets of SMIB in accordance with SFAS 144. The Company is in the process of evaluating whether or not such assets have been impaired. As of December 31, 2007, the carrying value of the total property, plant, and equipment at SMIB amounted to approximately $1.2 billion.

Revenue Recognition

We manufacture semiconductor wafers for our customers based on the customers designs and specifications pursuant to manufacturing agreements and purchase orders. We also sell certain semiconductor standard products to customers. Customers do not have any rights of return except pursuant to warranty provisions, which returns have been minimal. We typically perform tests of our products prior to shipment to identify yield of acceptable products per wafer. Occasionally, product tests performed after shipment identify yields below the level agreed with the customer. In those circumstances, the customer arrangement may provide for a reduction to the price paid or for its costs to ship replacement products. We estimate the amount of sales returns and the cost of replacement products based on the historical trend of returns and warranty replacements relative to sales and any current information regarding specific customer yield issues that may exceed historical trends. We recognize revenue upon shipment and title transfer. We also provide certain services such as mask making and probing and revenue is recognized when our services are completed.

Share-based Compensation Expense

Our share-based employee compensation plans are described in more detail under Share Ownership. We grant stock options to our employees and we record a compensation charge for the excess of the fair value of the stock at the measurement date over the amount an employee must pay to acquire the stock. We amortize share-based compensation using the straight-line method over the vesting periods of the related options, which are generally four years.

We grant stock options to our employees and certain non-employees. Prior to January 1, 2006, we accounted for share-based compensation in accordance with Accounting Principles Board Opinion No. 25, (APB 25), Accounting for Stock Issued to Employees, and related interpretations. We also followed the disclosure requirements of SFAS No. 123, Accounting for Stock-Based Compensation , as amended by SFAS 148, Accounting for Stock-Based Compensation-Transition and Disclosure. As a result, no expense was recognized for options to purchase our ordinary shares that were granted with an exercise price equal to fair market value at the day of the grant prior to January 1, 2006. Effective January 1, 2006, we adopted the provisions of Statement of Financial Accounting Standards No. 123(R), (SFAS 123(R)) Share-Based Payment, which establishes accounting for equity instruments exchanged for services. Under the provisions of SFAS 123(R), share-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as an expense over the employee s requisite service period (generally the vesting period of the equity grant). We elected to adopt the modified prospective transition method as provided by SFAS 123(R) and, accordingly, financial statement amounts for the prior periods presented in this report have not been restated to reflect the fair value method of expensing share-based compensation. As a result of adopting SFAS 123 (R) on January 1, 2006, we recognized a benefit of US$5.2 million as a result of the cumulative effect of a change in accounting principle, in relation to the forfeiture rate applied on the unvested portion of the stock options. Our total actual share-based compensation expense for the year ended December 31, 2007, 2006 and 2005 was US$20.6, US$23.5, and US$25.7 million respectively.

The fair value of options and shares issued pursuant to our option plans at the grant date was estimated using the Black-Scholes option pricing model. This model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option-pricing models require the input of highly subjective assumptions, including the expected stock

Table of Contents

price volatility. We use projected volatility rates, which are based upon historical volatility rates experienced by comparable public companies. Because our employee stock options issued under our 2001 Stock Plan, 2001 Regulation S Stock Plan, 2001 Preference Shares Stock Plan and 2001 Regulation S Preference Shares Stock Plan had characteristics significantly different from those of publicly traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management s opinion, the existing models do not necessarily provide a reliable single measure of the fair value of our stock options.

Inflation

Although there can be no assurance as to the impact in future periods, we believe that, to date, inflation in China has not had a material impact on our results of operations. Inflation in China was approximately 1.8%, 1.5%, and 4.8% in 2005, 2006 and 2007, respectively.

Income Tax

As an exempted company incorporated in the Cayman Islands, we are exempt from Cayman Islands taxation. Our Chinese subsidiaries are subject to taxation pursuant to the Income Tax Law of the PRC Concerning Foreign Investment and Foreign Enterprises and various local income tax laws. Under relevant regulations and after approval by the local Tax Bureau, our Shanghai, Beijing and Tianjin subsidiaries will become entitled to a full exemption from foreign enterprise income tax, or FEIT, for five years starting with the first year of positive accumulated earnings, and a 50% reduction for the following five years. Our Shanghai subsidiary had positive accumulated earnings since the financial year ended December 31, 2004. While as of December 31, 2007, Beijing and Tianjin are still in a cumulative operating loss.

According to PRC tax regulations, the Company s Chengdu subsidiary is entitled to a full exemption from FEIT for two years starting with the first year of positive accumulated earnings and a 50% reduction for the following three years. Up to December 31, 2007, Chengdu subsidiary is still in the process of applying for the tax holiday. As of December 31, 2007, the Chengdu subsidiary is still in a cumulative operating loss.

Our other subsidiaries are subject to their respective jurisdictions income tax laws, including Japan, United States, and Europe. Our income tax obligations to date have been minimal.

We account for income taxes in accordance with SFAS No. 109, Accounting for Income Taxes. SFAS No. 109 requires an asset and liability approach for financial accounting and reporting for income tax purposes. Under the asset and liability method, deferred income taxes are recognized for temporary differences, net operating loss carry-forwards and credits by applying enacted statutory tax rates applicable to future years. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

Effective January 1, 2007, the Company adopted FASB Interpretation No. 48 Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement 109 (FIN 48), which prescribes a more-likely-than-not threshold for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This interpretation also provides guidance on de-recognition of income tax assets and liabilities, classification of current and deferred income tax assets and liabilities, accounting for interest and penalties associated with tax positions, accounting for income taxes in interim periods and income tax disclosures.

On March 16, 2007, the National People s Congress, the PRC legislature, approved and promulgated a new tax law named Enterprise Income Tax Law, On December 6, 2007, the PRC State Council issued the Implementation Regulations of the Enterprise Income Tax Law, both of which became effective on January 1, 2008.The Enterprise Income Tax Law and its Implementation Regulations, or the new EIT law, FIEs and domestic companies are subject to a uniform tax rate of 25%. The new EIT law eliminates or modifies most of the tax exemptions, reductions and preferential treatments available under the previous tax laws and regulations. The State Council issued the Notice of the State Council on the Implementation of the

Table of Contents

Transitional Preferential Policies in respect of Enterprise Income Tax on December 26, 2007, enterprises that were established before March 16, 2007 and already enjoy preferential tax treatments will (i) in the case of preferential tax rates, continue to enjoy the tax rates which will be gradually increased to the new tax rates within five years from January 1, 2008 or (ii) in the case of preferential tax exemption or reduction for a specified term, continue to enjoy the preferential tax holiday until the expiration of such term. Thus, SMIC Shanghai, SMIC Beijing and SMIC Tianjin could fall into condition (ii) and may be entitled to the five year exemption and five year reduction as subject to the final recognition by the PRC tax authorities. While the EIT Law equalizes the tax rates for FIEs and domestic companies, preferential tax treatment would continue to be given to companies in certain encouraged sectors and to entities classified as high-technology companies supported by the PRC government, whether FIEs or domestic companies. According to the new EIT Law, entities that qualify as high-technology companies especially supported by the PRC government are expected to benefit from a tax rate of 15% as compared to the uniform tax rate of 25%. Implementation Regulations of the Enterprise Income Tax Law, a high-technology enterprise shall have core self-owned intellectual properties and its products shall be within the scope provided by the high-technology field highly supported by the State . However, the high-technology field highly supported by the State has not been issued, so there can be no assurances that SMIC Shanghai, SMIC Beijing, SMIC Tianjin and SMIC Chengdu will continue to qualify as high-technology companies supported by the PRC government in the future, and benefit from such preferential tax rate.

Under the new EIT law, dividends, interests, rent, royalties and gains on transfers of property payable by a foreign-invested enterprise in the PRC to its foreign investor who is a non-resident enterprise will be subject to a 10% withholding tax, unless such non-resident enterprise s jurisdiction of incorporation has a tax treaty with the PRC that provides for a reduced rate of withholding tax. The Cayman Islands, where SMIC is incorporated, does not have such a tax treaty with the PRC. If SMIC is considered a non-resident enterprise, this new 10% withholding tax imposed on SMIC s dividend income received from SMIC Shanghai, SMIC Beijing and SMIC Tianjin would reduce its net income and have an adverse effect on its operating results.

Under the new EIT law, an enterprise established outside the PRC with its de facto management body within the PRC is considered a resident enterprise and will be subject to the enterprise income tax at the rate of 25% on its worldwide income and foreign tax credit may be applicable. The de facto management body is defined as the organizational body that effectively exercises overall management and control over production and business operations, personnel, finance and accounting, and properties of the enterprise. It remains unclear how the PRC tax authorities will interpret such a broad definition. Substantially the majority of management members of SMIC are based in the PRC. If the PRC tax authorities subsequently determine that SMIC should be classified as a resident enterprise, then SMIC s worldwide income will be subject to income tax at a uniform rate of 25%, which may have a material adverse effect on SMIC s financial condition and results of operations. Notwithstanding the foregoing provision, the new EIT law also provides that, if a resident enterprise directly invests in another resident enterprise, the dividends received by the investing resident enterprise from the invested enterprise are exempted from income tax, subject to certain conditions. Therefore, if SMIC is classified as a resident enterprise, the dividends received from our PRC subsidiary may be exempted from income tax. However, it remains unclear how the PRC tax authorities will interpret the PRC tax resident treatment of an offshore company, like SMIC, having indirect ownership interests in PRC enterprises through intermediary holding vehicles.

Foreign Currency Fluctuations

Our sales are generally denominated in U.S. dollars and our operating expenses and capital expenditures are generally denominated in U.S. dollars, Japanese Yen, Euros and Renminbi. Accordingly, we are affected by fluctuations in exchange rates between the U.S. dollar and each of the Japanese Yen, the Euro and the Renminbi. See Risk Factors Risks Related to Conducting Operations in China Devaluation or appreciation in the value of the Renminbi or restrictions on convertibility of the Renminbi could adversely affect our operating results and Risk Factors Risks Related to Our Financial Condition and Business Exchange rate fluctuations could increase our costs, which could adversely affect our

Table of Contents

operating results and the value of our ADSs for a discussion of the effects on our company of fluctuating exchange rates and Item 11-Quantative and Qualitative Disclosures About Market Risk-Foreign Exchange Rate Fluctuation Risk for a discussion of our efforts to minimize such risks.

Recent Accounting Pronouncements

As of December 31, 2007, we had not yet adopted the following recently issued accounting pronouncements because they are not yet applicable in part or in total:

In September 2006, the Financial Accounting Standard Board (FASB) issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS 157), which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 applies under most other accounting pronouncements that require or permit fair value measurements and does not require any new fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years, with earlier application encouraged. The provisions of SFAS 157 should be applied prospectively as of the beginning of the fiscal year in which the statement is initially applied, except for a limited form of retrospective application for certain financial instruments. The adoption of SFAS 157 will not have a material impact on the Company s consolidated financial position or results of operations.

In February 2007, the FASB issued Statement No. 159, Fair Value Option for Financial Assets and Financial Liabilities including an amendment of FASB Statement No. 115 (SFAS 159). SFAS 159 permits companies to measure certain financial instruments and certain other items at fair value. The standard requires that unrealized gains and losses on items for which the fair value option has been elected be reported in earnings. SFAS 159 is effective for the Company on January 1, 2008, as earlier adoption was not elected. The Company does not expect the adoption of SFAS 159 to have a material impact on the Company s consolidated financial position or results of operations.

In December 2007, the FASB issued Statement No. 141 (revised 2007) Business Combinations (SFAS 141(R)). SFAS 141(R) retains the fundamental requirements of the original pronouncement requiring that the purchase method be used for all business combinations. SFAS 141(R) defines the acquirer as the entity that obtains control of one or more businesses in the business combination, establishes the acquisition date as the date that the acquirer achieves control and requires the acquirer to recognize the assets acquired, liabilities assumed and any non-controlling interest at their fair values as of the acquisition date. SFAS 141(R) also requires that acquisition-related costs be recognized separately from the acquisition. SFAS 141(R) is applicable to the Company s business combinations, if any, occurring after January 1, 2009. SFAS 141(R) has no impact on previously consummated business combinations. The Company is currently evaluating the impact, if any, of the statement on its consolidated financial statements.

In December 2007, the FASB issued Statement No. 160 Non-controlling Interests in Consolidated Financial Statements , an amendment of ARB 51 (SFAS 160). SFAS 160 requires non-controlling interests in subsidiaries initially to be measured at fair value and classified as a separate component of equity. SFAS 160 also requires that when a parent company acquires control of a subsidiary, it must include 100% of the fair value of all the acquired company s assets and liabilities in its consolidated financial statements. SFAS 160 is effective for us on January 1, 2009. SFAS 160 is to be applied prospectively to business combinations; certain disclosure and presentation requirements are to be applied retrospectively upon adoption. The Company is currently evaluating the impact, if any, of the statement on its consolidated financial statements.

Incentives from the Chinese government

The chart below sets forth a brief summary of the material incentives received by our Chinese subsidiaries from the Chinese government. Our Shanghai, Beijing, and Tianjin subsidiaries are qualified as integrated circuit production enterprises under the Chinese government s *Several Policies to Encourage the Development of Software and Integrated Circuit Industry*. Under these policies, any company that engages in the semiconductor industry in China and has a total investment size in excess of 8,000 million Renminbi

Table of Contents

(approximately US$964 million) and fabricates integrated circuits that have a linewidth of less than 0.25 micron are entitled to the last three benefits listed below. For a more detailed discussion of these incentives, see Item 4 Information on the Company Regulation.

Incentive	SMIC Shanghai	SMIC Beijing	SMIC Tianjin
Preferential Value-added Tax Policies	- 17% VAT rate - 17% tax refund rate for exports reduced to 13% as of January 1, 2004 - 13% tax refund rate for exports increased to 17% as of November 1, 2004	- 17% VAT rate - 17% tax refund rate for exports reduced to 13% as of January 1, 2004 - 13% tax refund rate for exports increased to 17% as of November 1, 2004	- 17% VAT rate - 17% tax refund rate for exports reduced to 13% as of January 1, 2004 - 13% tax refund rate for exports increased to 17% as of November 1, 2004
Preferential Enterprise Income Tax Policies	Five-year full exemption and five-year 50% reduction upon approval from the local tax bureau	Five-year full exemption and five-year 50% reduction upon approval from the local tax bureau	Five-year full exemption and five-year 50% reduction upon approval from the local tax bureau
Preferential Customs Duties and Import-related VAT Policies	Exemption from customs duties and import-related VAT with respect to its imported equipment, spare parts and raw materials	Exemption from customs duties and import-related VAT with respect to its imported equipment, spare parts and raw materials	Exemption from customs duties and import-related VAT with respect to its imported equipment, spare parts and raw materials

Table of Contents

Operating Results

Sales

We generate our sales primarily from fabricating semiconductors. We also derive a relatively small portion of our sales from the mask-making and wafer probing services that we perform for third parties separately from our foundry services.

In 2007, fabless semiconductor companies accounted for 46.4%, IDMs accounted for 41.0% and systems and other companies accounted for 12.5%, respectively, of our sales. Although we are not dependent on any single customer, a significant portion of our net sales is attributable to a relatively small number of our customers. In 2005, 2006, and 2007 our five largest customers accounted for approximately 64.0%, 59.5%, and 60.0% of our sales, respectively.

Cost of sales

Our cost of sales consists principally of:

depreciation and amortization;

overhead, including maintenance of production equipment, indirect materials, including chemicals, gases and various types of precious and other metals, utilities and royalties;

direct materials, which consist of raw wafer costs;

labor, including amortization of deferred stock compensation for employees directly involved in manufacturing activities; and

production support, including facilities, utilities, quality control, automated systems and management functions.

Our depreciation expenses attributable to cost of were US$387.5 million in 2004, US$661.0 million in 2005, US$786.7 million in 2006, and US$658.2 million in 2007.

Operating expenses (incomes)

Our operating expenses (incomes) consist of:

Research and development expenses. Research and development expenses consist primarily of salaries and benefits of research and development personnel, materials costs, depreciation and maintenance on the equipment used in our research and development efforts, and contracted technology development costs.

General and administrative expenses. General and administrative expenses consist primarily of salaries and benefits for our administrative, finance and human resource personnel, commercial insurance, fees for professional services, foreign exchange gains and losses from operating activities and costs incurred in connection with developing production capabilities at new fabs, including facility costs and employee costs. Foreign exchange gains and losses relate primarily to period-end translation adjustments due to exchange rate fluctuations that affect payables and receivables directly related to our operations.

Selling and marketing expenses. Selling and marketing expenses consist primarily of salaries and benefits of personnel engaged in sales and marketing activities, costs of customer wafer samples, other marketing incentives and related marketing expenses.

Amortization of acquired intangible assets. Amortization of acquired intangible assets consist primarily of the cost associated with the purchase of technology, licenses, and patent licenses.

Table of Contents

Income from sale of plant and equipment and other fixed assets. In 2007, the Company sold plant, equipment and other fixed assets with a carrying value of US$35,323,389 for US$63,974,835, which resulted in a gain on disposal of US$28,651,446. The plant and equipment was sold to a government-owned foundry based in Chengdu, Sichuan province, to which SMIC is also contracted to provide management services.

Other income (expenses)

Our other income (expenses) consists of:

interest income, which has been primarily derived from cash equivalents and short-term investments and interest on share purchase receivables;

interest expenses, net of capitalized portions and government interest subsidies, which have been primarily attributable to our bank loans and the imputed interest rate on an outstanding interest-free promissory note; and

other income and expense items, such as those relating to the employee living quarters and school; and

foreign exchange gains and losses relating to financing and investing activities, including forward contracts.

Comparisons of Results of Operations

Consolidated Financial Data

The summary consolidated financial data presented below as of and for the years ended December 31, 2005, 2006 and 2007 are derived from, and should be read in conjunction with, and are qualified in their entirety by reference to, our audited consolidated financial statements, including the related notes, included elsewhere in this annual report. The selected consolidated financial data as of and for the years ended December 31, 2003 and 2004 is derived from our audited consolidated financial statements not included in this annual report. The summary consolidated financial data presented below has been prepared in accordance with U.S. GAAP.

	For the year ended December 31,				
	2003	**2004**	**2005**	**2006**	**2007**
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Statement of Operations Data:					
Sales	$365,824	$974,664	$1,171,319	$1,465,323	$1,549,765
Cost of sales[(1)]	359,779	716,225	1,105,134	1,338,155	1,397,038
Gross profit (loss)	6,045	258,439	66,185	127,168	152,727
Operating expenses:					
Research and development	34,913	74,113	78,865	94,171	97,034
General and administrative	29,705	54,038	35,701	47,365	74,490
Selling and marketing	10,711	10,384	17,713	18,231	18,716

Table of Contents

	For the year ended December 31,				
	2003	**2004**	**2005**	**2006**	**2007**
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Litigation settlement		16,695			
Amortization of acquired intangible assets	3,462	14,368	20,946	24,393	27,071
Income from sale of plant and equipment and other fixed assets				(43,122)	(28,651)
Total operating expenses	78,791	169,598	153,225	141,038	188,659
Income (loss) from operations	(72,746)	88,841	(87,040)	(13,870)	(35,932)
Other income (expenses):					
Interest income	5,616	10,587	11,356	14,916	12,349
Interest expense	(1,425)	(13,698)	(38,784)	(50,926)	(37,936)
Foreign currency exchange gain (loss)	1,523	8,218	(3,355)	(21,912)	11,250
Other, net	888	2,441	4,462	1,821	2,238
Total other income (expense), net	6,602	7,548	(26,322)	(56,101)	(12,100)
Income (loss) before income tax	(66,144)	96,389	(113,362)	(69,971)	(48,032)
Income tax current		(186)	(285)	24,928	29,720
Minority interest			251	(19)	2,856
Loss from equity investment			(1,379)	(4,201)	(4,013)
Net (loss) income before cumulative effect of a change in accounting principle	(66,144)	96,203	(114,775)	(49,263)	(19,468)
Cumulative effect of a change in accounting principle				5,154	
Net (loss) income	(66,144)	96,203	(114,775)	(44,109)	(19,468)

Table of Contents

	For the year ended December 31,				
	2003	**2004**	**2005**	**2006**	**2007**
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Deemed dividend on preference shares[2]	37,117	18,840			
Income (loss) attributable to holders of ordinary shares	$ (103,261)	$ 77,363	$ (114,775)	$ (44,109)	$ (19,468)
Income (loss) per ordinary share, basic	$ (1.14)	$ 0.01	$ (0.00)	$ (0.00)	$ (0.00)
Income (loss) per ordinary share, diluted	$ (1.14)	$ 0.00	$ (0.00)	$ (0.00)	$ (0.00)
Ordinary shares used in calculating basic income (loss) per ordinary share [3][4]	90,983,200	14,199,163,517	18,184,429,255	18,334,498,923	18,501,940,489
Ordinary shares used in calculating diluted income (loss) per ordinary share [3][4]	90,983,200	17,934,393,066	18,184,429,255	18,334,498,923	18,501,940,489
Income (loss) per ADS, basic[5]		$ 0.27	$ (0.32)	$ (0.12)	$ (0.05)
Income (loss) per ADS, diluted [5]		$ 0.22	$ (0.32)	$ (0.12)	$ (0.05)
ADS used in calculating basic income (loss) per ADS[5]		283,983,270	363,688,585	366,689,978	370,038,810
ADS used in calculating diluted income (loss) per ADS[5]		358,687,861	363,688,585	366,689,978	370,038,810
Other Financial Data:					

Table of Contents

	For the year ended December 31,				
	2003	**2004**	**2005**	**2006**	**2007**
	(in US$ thousands, except for per share, per ADS data, percentages, and operating data)				
Gross margin	1.7%	26.5%	5.7%	8.7%	9.9%
Operating margin	-19.9%	9.1%	-7.4%	-0.9%	-2.3%
Net margin	-18.1%	9.9%	-9.8%	-3.0%	-1.3%

Operating Data:

Wafers shipped (in 8 equivalents)

(1) Including amortization of deferred stock compensation for employees directly involved in manufacturing activities.

(2) Deemed dividend represents the difference between the sale and conversion prices of warrants to purchase convertible preference shares we issued and their respective fair market values.

(3) Anti-dilutive preference shares, options and warrants were excluded from the weighted average ordinary shares outstanding for the diluted per

share calculation. For 2002, 2003, 2005, 2006, and 2007 basic income (loss) per share did not differ from diluted loss per share.

(4) All share information has been adjusted retroactively to reflect the 10-for-1 share split effected upon completion of the global offering of our ordinary shares in March 2004 (the Global Offering).

(5) Fifty ordinary shares equals one ADS.

(6) Total sales/total wafers shipped.

Comparisons of the Years Ended December 31, 2005, 2006 and 2007

Year Ended December 31, 2007 Compared to Year Ended December 31, 2006

Sales. Sales increased by 5.8% from US$1,465.3 million for 2006 to US$1,549.8 million for 2007, primarily as a result of the increase in the Company s manufacturing capacity and ability to use such capacity to increase sales. The number of wafers the Company shipped increased by 14.6%, from 1,614,888 8-inch wafer equivalents to 1,849,957 8-inch wafer equivalents, between these two periods. The average selling price of the wafers the Company shipped decreased by 7.6% from US$907 per wafer to US$838 per wafer primarily due to the decline in DRAM average selling price. The percentage of wafer revenues that used 0.13 micron and below process technology increased from 49.6% to 53.1% between these two periods.

Cost of sales and gross profit. Cost of sales increased by 4.4 % from US$1,338.2 million for 2006 to US$1,397.0 million for 2007. This increase was primarily due to the significant increase in wafer shipments as well as subcontracting costs associated with turn-key services. The Company had a gross profit of US$152.7 million for 2007 compared to a gross profit of US$127.2 million in 2006. Gross margins were 9.9 % in 2007 compared to 8.7 % in 2006. The increase in gross margins was primarily due to a decrease in depreciation expenses.

Operating expenses and loss from operations. Operating expenses increased by 33.8% from US$141.0 million for 2006 to US$188.7 million for 2007 primarily due to the combination of a $27.1M increase in general and administrative expenses and a $14.5 million decrease of income received from the sale of plant and equipments, from $43.1 million in 2006 compared to $28.7 million in 2007.

67

Table of Contents

As described in Note 11. Acquired intangible assets, net , the amortization of acquired intangible assets increased from US$24.4 million for 2006 to US$27.1 million for 2007.

Research and development expenses increased by 3.0% from US$94.2 million for 2006 to US$97.0 million for 2007. This increase in research and development expenses resulted primarily from an increase in material and other production related expenses associated with 65nm technology development and the start-up costs associated with the new Shanghai 12-inch project.

General and administrative expenses increased by 57.2% to US$74.5 million for 2007 from US$47.4 million for 2006, primarily due to an increase in personnel related expenses, legal fees and tax related expenses.

Selling and marketing expenses increased by 2.7% from US$18.2 million for 2006 to US$18.7 million for 2007, due to an increase in sales and marketing personnel expenses.

As a result, the Company s loss from operations was US$35.9 million in 2007 compared to loss from operations of US$13.9 million in 2006. Operating margin was negative 2.3% and 0.9%, respectively, for these two years.

Other income (expenses). Other expenses decreased from US$56.1 million in 2006 to US$12.1 million in 2007. This decrease was primarily attributable to the decrease in interest expense from US$51.0 million in 2006 to US$37.9 million in 2007, and the decrease in foreign exchange loss from US$21.9 million in 2006 to a gain of US$11.2 million in 2007.

Net loss. Due to the factors described above, the Company had a net loss of US$19.5 million in 2007 compared to a net loss of US$44.1 million for 2006.

Year Ended December 31, 2006 Compared to Year Ended December 31, 2005

Sales**.** Sales increased by 25.1% from US$1,171.3 million for 2005 to US$1,465.3 million for 2006, primarily as a result of the increase in our manufacturing capacity and ability to use such capacity to increase sales. The number of wafers the Company shipped increased by 19.9%, from 1,347,302 8-inch wafer equivalents to 1,614,888 8-inch wafer equivalents, between these two periods. The average selling price of the wafers we shipped increased by 4.4% from US$869 per wafer to US$907 per wafer. The percentage of wafer revenues that used 0.13 micron and below process technology increased from 40.6% to 49.6% between these two periods.

Cost of sales and gross profit**.** The cost of sales increased by 21.1% from US$1,105.1 million for 2005 to US$1,338.2 million for 2006. This increase was primarily due to the significant increase in sales volume, depreciation expenses as we installed new equipment to increase its capacity, and manufacturing labor expenses due to the increase in headcount. Other factors included an increase in the amount of direct and indirect materials purchased corresponding to the increase in wafers shipped and a product mix shift toward more advanced technology nodes (0.13 micron and below). We had a gross profit of US$127.2 million for 2006 compared to a gross profit of US$66.2 million in 2005. Gross margins were 8.7% in 2006 compared to 5.7% in 2005. The increase in gross margins was primarily due to a higher ASP and a product mix shift toward more advanced technology nodes (0.13 micron and below).

Operating expenses and loss from operations**.** Operating expenses decreased by 8.0% from US$153.2 million for 2005 to US$141.0 million for 2006 primarily due to income from sale of plant and equipments of US$43.1 million in 2006 and the increase of research and development, administrative, and selling and marketing expenses and amortization of acquired intangible assets of US$15.3 million, US$11.7 million, US$0.5 million and US$3.5million respectively.

Research and development expenses increased by 19.4% from US$78.9 million for 2005 to US$94.2 million for 2006. This increase in research and development expenses resulted primarily from an increase

Table of Contents

in depreciation and amortization costs associated with research and development, and 65nm research and development activities.

General and administrative expenses increased by 32.7% to US$47.4 million for 2006 from US$35.7 million for 2005, primarily due to an increase in bad debt of US$3.0 million, tax related expenses of US$2.3 million, and foreign exchange loss of US$3.9 million as compared to a foreign exchange gain of US$5.2 million recorded in 2005.

Selling and marketing expenses increased by 2.9% from US$17.7 million for 2005 to US$18.2 million for 2006, primarily due to an increase in sales and marketing personnel.

Amortization of acquired intangible assets increased by 16.5%.

As a result, the Company s loss from operations was US$13.9 million in 2006 compared to loss from operations of US$87.0 million in 2005. Operating margin was negative 0.9% and 7.4%, respectively, for these two years.

Other income (expenses). Other expenses increased from US$26.3 million in 2005 to US$56.1 million in 2006. This increase was primarily attributable to the increase in interest expense from US$38.8 million in 2005 to US$51.0 million in 2006, and the increase in foreign exchange loss from US$3.4 million in 2005 to US$21.9 million in 2006. This increase of the interest expense was primarily due to the increase in borrowing, the increased costs of borrowing, and losses from interest rate swap contracts.

Net loss. Due to the factors described above, the Company had a net loss of US$44.1 million in 2006 compared to a net loss of US$114.8 million for 2005.

Liquidity and Capital Resources

The following table sets forth a condensed summary of our audited statements of cash flows for the periods indicated:

	For the year ended December 31,		
	2005	**2006**	**2007**
	(in US$ thousands)		
Net cash provided by operating activities:			
Net (loss) before cumulative effect of change in accounting principle	$(114,775)	$ (49,263)	$ (19,468)
Depreciation and amortization	769,472	919,616	706,277
Total	648,105	769,649	672,465
Net cash used in investing activities:			
Purchase of property, plant and equipment	(872,519)	(882,581)	(717,171)
Total	(859,652)	(917,369)	(643,344)
Net cash provided by (used in) financing activities:			
Proceeds from short-term borrowings	394,159	255,004	201,658
Proceeds from long-term debt	253,433	785,345	262,248
Total	190,364	(74,440)	76,637
Net increase (decrease) in cash and cash equivalents	$ (21,376)	$(222,177)	$ 105,664

Table of Contents

We incurred capital expenditures of US$903 million, US$912 million, and US$860 million in 2005, 2006 and 2007, respectively. We have financed our substantial capital expenditure requirements through the proceeds received in our global offering, several rounds of private financing, cash flows from operations, and bank borrowings. Once a fab is in operation at acceptable capacity and yield rates, it can provide significant cash flows. Our cash flows from operations have historically exceeded operating income, reflecting our significant non-cash depreciation expenses. Our operating cash flows may not be sufficient to meet our capital expenditure requirements in 2008. If our operating cash flows are insufficient, we plan to fund the expected shortfall through bank loans. If necessary, we will also explore other forms of external financing.

Any transfer of funds from our company to our Chinese subsidiaries, either as a shareholder loan or as an increase in registered capital, is subject to registration or approval of Chinese governmental authorities, including the relevant administration of foreign exchange and/or the relevant examining and approval authority. In addition, it is not permitted under Chinese law for our Chinese subsidiaries to directly lend money to each other. Therefore, it is difficult to change our capital expenditure plans once the relevant funds have been remitted from our company to our Chinese subsidiaries. These limitations on the free flow of funds between us and our Chinese subsidiaries could restrict our ability to act in response to changing market conditions and reallocate funds from one Chinese subsidiary to another in a timely manner. See Risk Factors Risks Related to Conducting Operations in China Our corporate structure may restrict our ability to receive dividends from, and transfer funds to, our Chinese operating subsidiaries, which could restrict our ability to act in response to changing market conditions and reallocate funds from one Chinese subsidiary to another in a timely manner.

As of December 31, 2007, we had US$469.3 million in cash and cash equivalents. These cash and cash equivalents are held in the form of United States dollars, Japanese Yen, European Euros, and Chinese Renminbi. Our net cash provided by operating activities in 2007 was US$672.5 million, which was primarily due to the loss attributable to holders of ordinary shares of US$19.5 million, a decrease of US$26.9 million in inventories, an increase of US$46.2 million in accounts receivable due to an increase in sales and an increase of US$19.9 million in accounts payable relating to the purchase of materials and inventories, and the add-back of US$706.3 million in depreciation and amortization relating to commercial production.

As of December 31, 2006, we had US$363.6 million in cash and cash equivalents. These cash and cash equivalents are held in the form of United States dollars, Japanese Yen, European Euros, and Chinese Renminbi. Our net cash provided by operating activities in 2006 was US$769.6 million, which was primarily due to the loss attributable to holders of ordinary shares of US$44.1 million, an increase of US$83.9 million in inventories due to the increase in commercial production, an increase of US$10.9 million in accounts receivable due to an increase in sales and an increase of US$24.7 million in accounts payable relating to the purchase of materials and inventories, and the add-back of US$919.6 million in depreciation and amortization relating to commercial production.

Our net cash provided by operating activities in 2005 was US$648.1 million, which was primarily due to the loss attributable to holders of ordinary shares of US$114.8million, an increase of US$47.2 million in inventories due to the increase in commercial production, an increase of US$72.1 million in accounts receivable due to an increase in sales and an increase of US$26.4 million in accounts payable relating to the purchase of materials and inventories, and the add-back of US$769.5 million in depreciation and amortization relating to commercial production.

Our net cash used in investing activities was US$643.3 million in 2007, US$917.4 million in 2006, and US$859.7 million in 2005. This was primarily attributable to purchases of plant and equipment and land use rights for our mega-fabs in Shanghai and Beijing, and Tianjin fab in these periods as well as costs associated with the Shanghai fab construction.

Our net cash used in financing activities in 2007 was US$76.6 million. This was primarily derived from US$201.7 million in proceeds from short-term borrowings, US$262.2 million in proceeds from long-

Table of Contents

term debt, US$165.7 million in the repayment of short-term borrowings, and US$195.6 million in the repayment of long-term debt.

Our net cash used in financing activities in 2006 was US$74.4 million. This was primarily derived from US$255.0 million in proceeds from short-term borrowings, US$785.3 million in proceeds from long-term debt, US$449.5 million in the repayment of short-term borrowings, and US$635.6 million in the repayment of long-term debt.

Our net cash provided by financing activities in 2005 was US$190.4 million. This was primarily derived from US$394.2 million in proceeds from short-term borrowings, US$253.4 million in proceeds from long-term debt, US$219.7 million in the repayment of short-term borrowings, and US$249.2 million in the repayment of long-term debt.

As of December 31, 2007, we had commitments of US$57.1 million for facilities construction obligations for our facility in Chengdu and the Beijing, Tianjin and Shanghai fabs and US$239.6 million to purchase machinery and equipment for the testing facility in Chengdu, and the Beijing, Tianjin and Shanghai fabs.

For additional information, see Item 5 Operating and Financial Review and Prospects Factors that Impact Our Results of Operations Substantial Capital Expenditures and Capacity Expansion.

As of December 31, 2007, our outstanding long-term liabilities primarily consisted of US$957.0 million in secured bank loans, of which US$340.7 million is classified as the current portion of long-term loans. The long-term loans are repayable in installments commencing in June 2007, with the last payment in August 2012.

2001 Loan Facility (SMIC Shanghai). In December 2001, Semiconductor Manufacturing International (Shanghai) Corporation (SMIC Shanghai) entered into a USD denominated long-term debt agreement for US$432.0 million with a syndicate of four Chinese banks. The withdrawal period of the facility was 18 months starting from the loan agreement date. As of December 31, 2004, SMIC Shanghai had fully drawn down on this loan facility. In 2006, the interest rate on the loan ranged from 6.16% to 7.05%. The interest payment is due on a semi-annual basis. The principal amount is repayable starting in March 2005 in five semi-annual installments of US$86.4 million. The interest expense incurred in 2006 and 2005 was US$6.6 million and US$16.5 million, respectively, of which US$0.8 million and US$3.6 million were capitalized as additions to assets under construction in 2006 and 2005, respectively. As of December 31, 2007, 2006 and 2005, this facility was fully repaid.

2004 Loan Facility (SMIC Shanghai). In January 2004, SMIC Shanghai entered into the second phase USD denominated long-term facility arrangement for US$256.5 million with four Chinese banks. As of December 31, 2005, SMIC Shanghai had fully drawn down on this loan facility. In 2006, the interest rate on the loan ranged from 6.16% to 7.05%. The interest payment is due on a semi-annual basis. The principal amount is repayable starting in March 2006 in seven semi-annual installments of US$36.6 million. The interest expense incurred in 2006 and 2005 was US$7.2 million and US$12.5 million, of which US$0.9 million and US$2.7 million were capitalized as additions to assets under construction in 2006 and 2005, respectively. As of December 31, 2006, the borrowing was fully repaid through the Shanghai new USD syndicate loan.

In connection with the second phase long-term facility arrangement, SMIC Shanghai has a RMB denominated line of credit of RMB235,678,000 (approximately US$28.5 million). In 2005, SMIC Shanghai fully utilized this line of credit, which was then repaid in full prior to December 31, 2005. The interest expenses incurred in 2005 was US$0.03 million.

2006 Loan Facility (SMIC Shanghai). In June 2006, SMIC Shanghai entered into a new USD denominated long-term facility arrangement for US$600.0 million with a consortium of international and PRC banks. Of this principal amount, US$393.0 million was used to repay the principal amount

Table of Contents

outstanding under SMIC Shanghai s bank facilities from December 2001 and January 2004. The remaining principal amount will be used to finance future expansion and general corporate requirement for SMIC Shanghai. This facility is secured by the manufacturing equipment located in SMIC Shanghai 8-inch fabs. As of December 31, 2007, SMIC Shanghai had fully drawn down on this loan facility. The principal amount is repayable starting from December 2006 in ten semi-annual installments. As of December 31, 2007, SMIC Shanghai had repaid US$111.1 million according to the repayment schedule and had early repaid US$95.0 million. In 2007, the interest rate on the loan ranged from 5.74% to 6.46%. The interest expense incurred in 2007 and 2006 was US$17.3 and US$13.5 million, of which $3.3 million and $1.6 million were capitalized as additions to assets under construction in 2007 and 2006, respectively.

The total outstanding balance of these long-term facilities is collateralized by certain plant and equipment at the original cost of US$1,883 million as of December 31, 2007.

The following are covenants contained in the long-term loan agreement entered into in June 2006 which SMIC Shanghai is (unless otherwise waived by the lenders to such agreement) required to comply with.

Financial covenants for the Borrower including:

1. Consolidated Tangible Net Worth of no less than US$1,200 million;

2. Consolidated Total Borrowings to Consolidated Tangible Net Worth of:

(a) no more than 60% for periods up to and including 31 December 2008; and

(b) no more than 45% thereafter;

3. Consolidated Total Borrowings to trailing preceding four quarters EBITDA not to exceed 1.50x.

4. Debt Service Coverage Ratio of no less than 1.5x. Debt Service Coverage Ratio means trailing four quarters EBITDA divided by scheduled principal repayments and interest expense for all bank borrowings (including hire purchases, leases and other borrowed monies) for the same period.

Financial covenants for the Guarantor including:

1. Consolidated Tangible Net Worth of no less than US$2,300 million;

2. Consolidated Net Borrowings to Consolidated Tangible Net Worth of:

(a) no more than 50% for period up to and including 30 June 2009;

(b) no more than 40% thereafter.

3. Consolidated Net Borrowings to trailing four quarters EBITDA of:

(a) no more than 1.50x for periods up to and including 30 June 2009;

(b) no more than 1.30x thereafter.

2005 Loan Facility (SMIC Beijing). In May 2005, Semiconductor Manufacturing International (Beijing) Corporation (SMIC Beijing) entered into a five year USD denominated loan facility in the aggregate principal amount of US$600.0 million, with a syndicate of financial institutions based in the PRC. This five-year bank loan will be used to expand the capacity of SMIC Beijing s fabs. The drawdown period of this facility was twelve months from the sign off date of the agreement. As of December 31, 2007, SMIC Beijing had fully drawn-down US$600.0 million on this loan facility. The interest rate on this loan facility in 2007 ranged from 6.38% to 7.00%. The principal amount is repayable starting in December 2007 in six semi-annual installments. As of December 2007, SMIC Beijing had repaid the first installment of US$100 million according to the repayment schedule. The interest expense incurred in 2007 and 2006 was US$42.2 million and US$28.5 million, of which US$2.3 million and US$0.5 million were capitalized as additions to assets under construction in 2007 and 2006, respectively.

Table of Contents

The total outstanding balance of SMIC Beijing USD syndicate loan is collateralized by certain plant and equipment at the original cost of US$1,058.4 million as of December 31, 2007.

Any of the following would constitute an event of default for SMIC Beijing (unless otherwise waived by the lenders to such agreement):

1. [Net profit + depreciation + amortization + financial expenses (increase of accounts receivable and advanced payments + increase of inventory increase in accounts payable and advanced receipts)]/ financial expenses < 1; and

2. (Total liability borrowings from shareholders, including principal and interest)/Total assets > 60% (when SMIC Beijing s capacity is less than 20,000 12-inch wafers per month); and (Total liability borrowings from shareholders, including principal and interest)/Total assets > 50% (when SMIC Beijing s capacity exceeds 20,000 12-inch wafers per month).

2005 Loan Facility (SMIC). On December 15, 2005, we entered into a EUR denominated long-term loan facility agreement in the aggregate principal amount of EUR 85 million (equivalent to approximately US$105 million) with a syndicate of banks and ABN Amro Bank N.V. Commerz Bank (Nederland) N.V. as the leading bank. The drawdown period of the facility ends on the earlier of (i) twenty six months after the execution of the agreement or (ii) the date which the loans have been fully drawn down. Each draw down made under the facility shall be repaid in full by us in ten equal semi-annual installments. SMIC Tianjin had drawn down in 2006 and SMIC Shanghai had drawn down in 2007.

As of December 31, 2007, SMIC Tianjin had drawdown EUR15.1 million and repaid the first four installments with an aggregated amount of EUR 6.0 million. As of December 31, 2007, the remaining balance is EUR 9.1 million, with the US dollar equivalent of US$13.4 million. In 2007, the interest rate on the loan ranged from 3.95% to 5.87%. The interest expense incurred in 2007 and 2006 were US$0.7 and US$0.3 million of which $0.06 million and $0.07 million was capitalized additions to assets under construction in 2007 and 2006, respectively.

The total outstanding balance of the facility is collateralized by SMIC Tianjin s certain plant and equipment at the original cost of EUR 17.8 million as of December 31, 2007.

As of December 31, 2007, SMIC Shanghai had drawdown EUR 28.4 million and repaid the first installment of EUR 2.8 million. As of December 31, 2007, the remaining balance is EUR 25.6 million, with the US dollar equivalent of US$37.7 million. In 2007, the interest rate on the loan ranged from 4.41% to 4.87%. The interest expense incurred in 2007 was US$0.3 million of which $0.06 million was capitalized additions to assets under construction in 2007.

The total outstanding balance of the facility is collateralized by SMIC Shanghai s certain plant and equipment at the original cost of EUR 33.4 million as of December 31, 2007.

2006 Loan Facility (SMIC Tianjin). In May 2006, SMIC Tianjin entered into a loan facility in the aggregate principal amount of US$300.0 million from a consortium of international and Chinese banks. This facility is secured by the manufacturing equipment located in our Tianjin fab, except for the manufacturing equipment purchased using the EUR denominated loan. As of December 31, 2007 SMIC Tianjin had drawn down US$12.0 million from the facility. The remaining amount is available until May 2008. The principal amount is repayable starting from 2010 in six semi-annual installments. In 2007, the interest rate on the loan ranged from 6.03% to 6.58%. The interest expense incurred ended December 31, 2007 was US$0.3 million, of which $0.02 million was capitalized as additions to assets under construction in 2007.

The total outstanding balance of the facility is collateralized by certain plant and equipment with an original cost of $207.0 million as of December 31, 2007.

Table of Contents

Any of the following with respect to SMIC Tianjin would constitute an event of default for SMIC Tianjin (unless otherwise waived by the lenders to such agreement):

1. [Net profit + depreciation + amortization + financial expenses (increase of accounts receivable and advanced payments + increase of inventory increase in accounts payable and advanced receipts)]/ financial expenses < 1; and

2. The ratio of total debt to total assets is more than 60% during the ramp up period of SMIC Tianjin and more than 40% after the facility is at full capacity.

Short-term Credit Agreements. As of December 31, 2007, we had fifteen short-term credit agreements that provided total credit facilities up to US$484.4 million on a revolving credit basis. As of December 31, 2007, we had drawn down US$107.0 million under these credit agreements and US$377.4 million is available for future borrowings. The outstanding borrowings under the credit agreements are unsecured. The interest expense incurred in 2007 was US$4.5 million. The interest rate on the loans ranged from 5.37% to 6.44% in 2007.

We have accepted promissory notes from employees exercising options to purchase either ordinary shares or Series A convertible preference shares under our 2001 employee stock option plans (the Stock Option Plans). At December 31, 2007, 2006, and 2005, we had notes receivable from employees related to the early exercise of employee stock options in the aggregate amount of US$nil, US$nil, and US$nil, respectively. In 2005, we collected $391,375 through the repayment of notes receivable by certain employees and the sale of the notes receivable to a third party bank. The notes are full recourse and are secured by the underlying ordinary shares and preference shares. The notes are due at various dates from year 2007 to 2008 and payable at varying rates from 3.02% to 4.28% per annum.

Please see Item 8 Financial Information Dividends and Dividend Policy on our ability to pay dividends on our ordinary shares.

Please see Item 11 Quantitative and Qualitative Disclosures About Market Risk regarding the risk of loss related to adverse changes in market prices, including foreign currency exchange rates and interest rates of financial instruments.

Research and Development, Patents and Licenses, etc.

Our research and development activities are principally directed toward the development and implementation of more advanced and lower cost process technology. We spent US$78.9 million in 2005, US$94.2 million in 2006, and US$97.0 million in 2007 on research and development expenses, which represented 6.7%, 6.7%, 6.4%, and 6.3%, respectively, of our sales in those respective years. Our research and development costs include non-recurring engineering costs associated with the ramp-up of a new wafer facility. These research and development costs will subsequently be classified in cost of sales upon commencement of commercial production at that particular wafer facility. We plan to continue to invest significant amounts in research and development in 2008.

See Item 4 Information on the Company Research and Development for more details relating to our research and development activities.

Trend Information

See Item 5 Operating and Financial Review and Prospects Factors that Impact Our Results of Operations for a discussion of the most significant recent trends affecting our operations.

Off-Balance Sheet Arrangements

We have not entered into any off-balance sheet transactions.

Table of Contents

Tabular Disclosure of Contractual Obligations

Set forth in the table below are the aggregate amounts, as of December 31, 2007, of our future cash payment obligations under our existing debt arrangements on a consolidated basis:

Contractual obligations	Total	Payments due by period Less than 1 year	1 3 years	3 5 years	After 5 years
			(consolidated) (in US$ thousands)		
Secured Long-Term Debt[1]	1,047,619	391,947	379,468	276,204	
Operating Lease Obligations[2]	4,561	581	267	674	3,039
Purchase Obligations[3]	296,635	296,635			
Other Long-Term Obligations[4]	227,638	104,138	78,900	44,600	
Total Contractual Obligations	$ 1,576,453	$ 793,301	$ 458,635	$ 321,478	$ 3,039

(1) Interest was computed using rates in effect on December 31, 2007 within the range of 4.77% to 5.82%.

(2) Represents our obligations to make lease payments to use the land on which our fabs are located in Shanghai and other office equipment we have leased.

(3) Represents commitments for construction or purchase of semiconductor equipment, and other property or services.

(4) Includes the settlement with

TSMC and the other long-term liabilities relating to certain license agreements.

In April 2008, we entered into an agreement to purchase equipment from Cension for approximately US$150 million. This set of equipment will be used for SMIC s future expansion.

Table of Contents

Item 6. Directors, Senior Management and Employees

Directors and Senior Management

Members of our board of directors are elected by our shareholders. As of June 15, 2008, our board of directors consists of eight directors.

The following table sets forth the names of our directors and executive officers, including our founder, as of June 15, 2008. Our executive officers are appointed by, and serve at the discretion of, our board of directors.

Name	Age	Position
Directors		
Yang Yuan Wang	73	Chairman, Independent Non-executive Director
Richard Ru Gin Chang	60	Founder, President, Chief Executive Officer and Executive Director
Wang Zheng Gang	56	Non-executive Director
Ta-Lin Hsu	65	Independent Non-executive Director
Tsuyoshi Kawanishi	79	Independent Non-executive Director
Henry Shaw	54	Independent Non-executive Director
Lip-Bu Tan	49	Independent Non-executive Director
Jiang Shang Zhou	61	Independent Non-executive Director
Senior Managers		
Morning Wu	51	Acting Chief Financial Officer, Chief Accounting Officer and Qualified Accountant
Marco Mora	49	Chief Operating Officer
James Sung	50	Senior Vice President of Corporate Marketing & Sales Office
Anne Wai Yui Chen	45	Company Secretary, Hong Kong Representative and Compliance Officer

Chairman of the Board, Independent Non-executive Director

Yang Yuan Wang is currently the Chairman and has been a Director since 2001. Professor Wang has more than 41 years of experience related to the semiconductor industry. He is the Chairman of SMIC Shanghai, SMIC Beijing and SMIC Tianjin and is also the Chief Scientist of the Institute of Microelectronics, Peking University, and Academician of Chinese Science Academy. He is a fellow of the Chinese Academy of Sciences, The Institute of Electrical and Electronics Engineers (USA), The Institute of Electrical Engineers (UK) and Chinese Institute of Electronics (China).

Founder, President, Chief Executive Officer and Executive Director

Richard Ru Gin Chang founded our company in April 2000 and is currently President, Chief Executive Officer and Executive Director. Dr. Chang is also a director of SMIC Shanghai, SMIC Beijing, SMIC Tianjin, Semiconductor Manufacturing International (AT) Corporation, SMIC Solar Cell Corporation and Magnificent Tower Limited. Dr. Chang has over 29 years of semiconductor experience in foundry operations, wafer fabrication and research and development. From 1998 to 1999, Dr. Chang was President of Worldwide Semiconductor Manufacturing Corp., or WSMC, after joining the company in 1997. Prior to joining WSMC, Dr. Chang worked for 20 years at Texas Instruments Incorporated, where he helped build and manage the technology development and operations of ten semiconductor fabs and integrated circuit operations in the United States, Japan, Singapore, Italy and Taiwan. Dr. Chang received a PhD in Electrical Engineering from Southern Methodist University and a master s degree in Engineering Science from the State University of New York. Dr. Chang received many awards from 2003 to 2006. In 2007, Dr. Chang

Table of Contents

was recognized as Chinese Semiconductor Manufacturing Character Of The Year for the Year 2007. In 2008, Dr. Chang was given the Industry Outstanding Contribution Award while the company garnered the SEMI China Social Contribution Award and was honored with the 2007 Fab Person of the Year award and as Movers and Shakers of China s semiconductor industry in 2007 by Semiconductor International China.

Non-executive Director

Wang Zheng Gang has been a Director since 2007. Mr. Wang is the chief representative of the Shanghai Representative Office of Shanghai Industrial Holdings Limited and chairman and managing director of SIIC Management (Shanghai) Ltd. He is also the vice chairman of Bright Dairy and Food Co. Ltd. He was the head of Shanghai Dongfeng Rubber No. 2 Factory, Principal of Shanghai Dongfeng Farm, vice chairman and general manager of Shanghai Agricultural Industrial and Commercial Corp. Ltd. and a director and general manager of SIIC Africa Enterprise Ltd. and general manager of the enterprise management department of Shanghai Industrial Investment (Holdings) Co. Ltd. He graduated from the School of Management of Fudan University with a master s degree in Economics and has over 31 years experience in enterprise management.

Independent Non-executive Directors

Ta-Lin Hsu has been a Director since 2001 and is a director of SMIC Beijing. Dr. Hsu is the founder and chairman of H&Q Asia Pacific. Prior to founding H&Q Asia Pacific in 1986, Dr. Hsu was a general partner at Hambrecht & Quist and held the position of senior manager in the Corporate Research Division of IBM. Dr. Hsu has served on the boards of a number of public and private companies, and he currently serves on the board of trustees of the Asia Foundation and as a member of the Council of Foreign Relations. Dr. Hsu received his PhD in Electrical Engineering from the University of California at Berkeley and his undergraduate degree in Physics from National Taiwan University. Dr. Hsu is a member of the Advisory Board of the Haas School of Business at the University of California at Berkeley.

Tsuyoshi Kawanishi has been a Director since 2001 and is also the chairman of SMIC Japan Corporation. Mr. Kawanishi has more than 50 years of experience in the electronics industry with Toshiba Corporation, where he served as, among other positions, senior executive vice president and senior advisor. Mr. Kawanishi currently serves on the board of directors of Asyst Technologies, Inc., FTD Technology Pte. Ltd. and T.C.S. Japan, and acts as an advisor to Accenture Ltd., Kinetic Holdings Corporation and a number of private companies. Mr. Kawanishi is also the chairman of the Society of Semiconductor Industry Seniors in Japan and the Chairman of the SIP Consortium of Japan.

Henry Shaw has been a Director since 2001. Mr. Shaw is currently the senior partner of AsiaVest Partners TCW/YFY Ltd. Prior to joining AsiaVest Partners, Mr. Shaw was a vice president at Transpac Capital Pte. Ltd. and founded and served as chief financial officer of Mosel Vitelic Inc. Mr. Shaw received a master s degree in Business Administration from National Cheng-Chi University in Taiwan.

Lip-Bu Tan has been a Director since 2002 and is a director of SMIC Tianjin. Mr. Tan is the founder and chairman of Walden International, a venture capital firm. Mr. Tan currently serves on the board of directors of Cadence Design Systems, Inc., Creative Technology Ltd., Flextronics International Ltd., MindTree Ltd. and SINA Corporation, as well as a number of private companies. Mr. Tan received a master s degree in Nuclear Engineering from the Massachusetts Institute of Technology and a master s degree in Business Administration from the University of San Francisco.

Jiang Shang Zhou has been a Director since 2006. Mr. Jiang is currently a committee member of Shanghai Committee of Chinese People s Political Consultive Conference, and an officer and director commissioner of Shanghai State Owned Assets Planning and Investment Committee. Mr. Jiang was also the deputy secretary general of Shanghai Government, officer of the Shanghai Chemical Industrial District Leader Team Office, officer of Shanghai International Automobile City Leader Team Office and officer of the Shanghai Fuel Cell Electric Vehicles (863 major project) Leader Team Office. Mr. Jiang received his master s degree from Tsing Hua University in Telecommunications and his doctorate degree from .

Table of Contents

Senior Management

Morning Wu joined our company as Associate Vice President of Finance and Accounting in January 2003 and was appointed as Acting Chief Financial Officer, Chief Accounting Officer and Qualified Accountant of the Company as of March 28, 2005. Ms. Wu has over 27 years of experience in the investment and finance field. Prior to joining us, Ms. Wu held management positions with First Taiwan Securities Inc. and Grand Cathay Securities Co. Ltd. Her responsibilities at these companies included strategic planning, mergers & acquisitions and designing and monitoring risk management systems. She holds a license for Accounting and Auditor with the Senior Civil Service Examination of Taiwan. Ms. Wu obtained a bachelor s degree in Accounting from the National Chengchi University, Taiwan and received a master s degree in Accounting from the National Taiwan University.

Marco Mora joined our company in 2000 as Vice President of Operations and was named the Chief Operating Officer in November 2003. Mr. Mora has more than 22 years of experience in the semiconductor industry. Prior to joining us, Mr. Mora held management positions with STMicroelectronics N.V., Texas Instruments Italia S.p.A, Micron Technology Italia S.p.A and WSMC. Mr. Mora received a master s degree in Physics from the University of Milan.

James Sung joined our company as Fellow in Technology Development in 2001 and was appointed as Vice President of Marketing and Sales in 2002. He is currently Senior Vice President of Corporate Marketing and Sales Office in Semiconductor Manufacturing International (Shanghai) Corporation. Dr. Sung has over 21 years of experience in semiconductor industry. Prior to joining SMIC, Dr. Sung has been employed by Etron Technology (Taiwan) as Vice President of Product Development, Vanguard International Semiconductor (Taiwan) as Senior Director of Technology Development and Director of quality reliability assurance, and AT&T Bell Laboratories in Murray Hill, Holmdel, Allentown as CMOS/BiCMOS principle technology researcher for high performance networking applications. Dr. Sung was co-recipient of ISCC Beatrice award in 1994 and an honorable member of Phi-Tau-Phi in 1981. He holds over 60 semiconductor patents. Dr. Sung obtained a bachelor degree and a master degree in Electronic Engineering from National Chiao-Tung University (Taiwan) respectively, and doctorate degree in Electronic Engineering from Princeton University.

Company Secretary

Anne Wai Yui Chen joined our company in 2001 and is our Hong Kong Representative, Company Secretary and Compliance Officer. Ms. Chen is admitted as a solicitor in Hong Kong, England and Wales and Australia and was admitted as an advocate and solicitor in Singapore. She had served as a deputy adjudicator of the Small Claims Tribunal in Hong Kong in 1999 and had served as the president from 2000 to 2002 and is currently a council member of the Hong Kong Federation of Women Lawyers. Prior to joining us in 2001, she had been a practicing solicitor in Hong Kong since 1987.

No shareholder has a contractual right to designate a person to be elected to our board of directors.

There are no family relationships among any of our directors and executive officers, including our founder.

Director and Executive Compensation

The aggregate cash compensation that we paid to all of our executive officers as of December 31, 2007 for services rendered to us and our subsidiaries during 2007 was approximately US$856,169. Of this amount, we paid our president and chief executive officer US$195,395 in salary, discretionary bonuses, housing allowances, other allowances and benefits in kind in 2007. We currently do not provide cash compensation to directors that are not employees. Pursuant to an incentive program involving the offering for sale of housing constructed by us to all our directors, employees and certain service providers, we sold one property to each of our five highest paid employees, including our president and chief executive officer, at the same price at which other properties of the same type have been sold by us to other employees under the program. We do not provide pension, retirement or similar benefits to our executive officers and directors except statutorily required.

Table of Contents

We granted options to purchase an aggregate of 17,400,000 ordinary shares under our 2001 Regulation S Stock Plan, under our 2001 Regulation S Preference Shares Stock Plan to certain of our directors and executive officers. No options have been granted under our 2001 Stock Plan or 2001 Preference Shares Stock Plan to our directors or executive officers. Both our 2001 Regulation S Stock Plan and 2001 Regulation S Preference Shares Stock Plan are described below in Share Ownership. The exercise prices of the options granted to our directors and executive officers to purchase ordinary shares range from US$0.01 to US$0.25. The expiration dates of the options range from September 2011 to February 2014.

As of December 31, 2007, we have granted options to purchase an aggregate of 4,300,000 ordinary shares under our 2004 Stock Option Plan, and awarded an aggregate of 7,456,830 restricted share units under our 2004 Equity Incentive Plan to certain of our directors and executive officers. Both our 2004 Stock Option Plan and the 2004 Equity Incentive Plan are described below. The exercise price of the options granted to our executive officers to purchase ordinary shares under the 2004 Stock Option Plan range from US$0.13 to US$0.15 per share. The expiration dates of the options range from November 10, 2009 to September 29, 2016.

On November 10, 2004, our board of directors issued each independent non-executive and non-executive director as of such date, an option to purchase 500,000 ordinary shares at a price per ordinary share of USD$0.22. These options were fully vested on March 19, 2005 and will expire on November 9, 2009. Lai Xing Cai, who resigned as a non-executive director on February 6, 2006, declined this option. As of December 31, 2007, no director has exercised such options. The option granted to Mr. Yen-Pong Jou (who retired as an independent non-executive director at the annual general meeting held on May 30, 2006) lapsed and was cancelled on September 27, 2006.

In 2005, the Board did not grant options or restricted share units to any non-executive director or independent non-executive director as compensation for their service on the Board. On May 11, 2005, the compensation committee issued to Richard Ru Gin Chang an option to purchase 15,000,000 ordinary shares and an award of 2,000,000 restricted share units. The exercise price per ordinary share underlying the option is US$0.196. The option and the award of restricted share units will expire on May 11, 2015. As of December 31, 2007, none of these options have been exercised, and 75% of the RSUs have vested.

On September 29, 2006, the Board granted to each director an option to purchase 500,000 ordinary shares at a price per ordinary share of US$0.132. These options were vested as to 50% on each of May 30, 2007 and May 30, 2008 respectively and such options will expire on the earlier of September 29, 2016 or 120 days after termination of the director s service to the Board. As of December 31, 2007, these options have not been exercised. Fang Yao (who resigned as a non-executive director on August 30, 2007) and Jiang Shang Zhou have declined such options.

On September 29, 2006, the Board granted to Dr. Albert Y. C. Yu 500,000 restricted share units. Shares under the restricted share units, 50% of such restricted share units were vested on each of May 30, 2007 and May 30, 2008 respectively. On June 3, 2008, 500,000 ordinary shares were issued to Dr. Albert Yu pursuant to the vesting of such restricted share units.

In 2007, the Board did not grant options or restricted share units to any director as compensation for their service on the Board.

Table of Contents

On April 25, 2004, the compensation committee approved a profit-sharing plan for the benefit of our employees, including our executive officers. Under our profit-sharing plan, a participant who is an employee of the company at the end of a fiscal quarter will be eligible to receive a percentage of our profits for that quarter. No compensation was received by our executive officers in 2005, 2006 and 2007 as a result of their participation in this plan.

Board Practices

Board of Directors

As of December 31, 2007, our board of directors consisted of nine directors. Directors may be elected to hold office until the expiration of their respective terms upon a resolution passed at a duly convened shareholders meeting by holders of a majority of our outstanding shares being entitled to vote in person or by proxy at such meeting. Our board is divided into three classes with no more than one class eligible for re-election at any annual shareholders meeting.

The Class I directors were elected for a term of three years beginning from June 2, 2008, which is the date of the 2008 annual general meeting of our shareholders. The Class II directors were elected for a term of three years beginning from May 30, 2006, the date of the 2006 annual general meeting our shareholders (the 2006 AGM). The Class III directors were elected for a term of three years beginning from May 23, 2007, which is the date of the 2007 annual general meeting of our shareholders.

The following table sets forth the names and classes of our current directors:

Class I	Class II	Class III
Richard Ru Gin Chang	Ta-Lin Hsu	Tsuyoshi Kawanishi
Henry Shaw	Lip-Bu Tan	Yang Yuan Wang
	Jiang Shang Zhou	Wang Zheng Gang

Dr. Albert Y. C. Yu retired as a Class I independent non-executive director of the Company at our annual general meeting held on June 2, 2008 and did not offer himself for re-election.

None of our directors has any service contract with our company.

Committees of Our Board of Directors

Our board of directors has an audit committee and a compensation committee. The composition and responsibilities of these committees are described below.

Audit Committee. As of December 31, 2007, the members of the audit committee were Henry Shaw (co-chairman of audit committee), Lip-Bu Tan (co-chairman of audit committee) and Yang Yuan Wang. None of the members of the audit committee has been an executive officer or employee of the company or any of its subsidiaries. See Related Party Transactions for a description of transactions between us and the members of the audit committee. In addition to acting as audit committee member of the company, Mr. Lip-Bu Tan currently also serves on the audit committee of two other publicly traded companies, namely SINA Corporation and Flextronics International Ltd. In general and in accordance with section 303A.07(a) of the Listed Company Manual of the New York Stock Exchange, the Board considered and determined that such simultaneous service would not impair the ability of Mr. Tan to effectively serve on our audit committee.

The responsibilities of the audit committee include, among other things:

- making recommendations to the board of directors concerning the appointment, reappointment, retention, evaluation, oversight and termination of compensating and overseeing the work of our independent auditor, including reviewing the experience, qualifications and performance of the

Table of Contents

senior members of the independent auditor team, and pre-approving all non-audit services to be provided by our independent auditor;

approving the remuneration and terms of engagement of our independent auditor;

reviewing reports from our independent auditor regarding its internal quality-control procedures and any material issues raised in the most recent review or investigation of such procedures and regarding all relationships between us and the independent auditor;

pre-approving the hiring of any employee or former employee of our independent auditor who was a member of the audit team during the preceding two years;

reviewing our annual and interim financial statements, earnings releases, critical accounting policies and practices used to prepare financial statements, alternative treatments of financial information, the effectiveness of our disclosure controls and procedures and important trends and developments in financial reporting practices and requirements;

reviewing the planning and staffing of internal audits, the organization, responsibilities, plans, results, budget and staffing of our internal audit department and the quality and effectiveness of our internal controls;

reviewing our risk assessment and management policies;

reviewing any legal matters that may have a material impact and the adequacy and effectiveness of our legal and regulatory compliance procedures;

establishing procedures for the treatment of complaints received by us regarding accounting, internal accounting controls, auditing matters, potential violations of law and questionable accounting or auditing matters; and

obtaining and reviewing reports from management, our internal auditor and our independent auditor regarding compliance with applicable legal and regulatory requirements.

During 2007, the audit committee reviewed:

the financial reports for the year ended December 31, 2006 and the six month period ended June 30, 2007;

the quarterly earnings releases and any updates thereto;

the report and management letter submitted by our outside auditors summarizing the findings of and recommendations from their audit of our financial reports;

our budget for 2007;

the findings and recommendations of our outside consultants regarding our compliance with the requirements of the Sarbanes-Oxley Act of 2002 (the Sarbanes-Oxley Act);

the effectiveness of our internal control structure in operations and financial reporting integrity and compliance with applicable laws and regulations in collaboration with the Internal Audit Department and reported to the Board;

the findings of our risk management committee which assesses risks relating to the company and those of the compliance office, which monitors our compliance with the corporate governance code and insider trading policy;

the audit fees and other non-audit fees such as fees relating to transfer pricing, Sarbanes-Oxley Section 404 compliance testing, for our outside auditors; and

our outside auditors engagement letters

The audit committee reports its work, findings, and recommendations to the board of directors during each quarterly board meeting.

The audit committee meets in person at least on a quarterly basis and on such other occasions as may be required to discuss and vote upon significant issues affecting the audit policy of the company. The regular meeting schedule for a year is planned in the preceding year. The Company s Secretary assists the co-chairmen of the audit committee in preparing the agenda for meetings and assists the audit committee in complying with relevant rules and regulations. The relevant papers for the audit committee meetings are dispatched to audit committee members in accordance with applicable rules and regulations governing the company. Members of the audit committee may include matters for discussion in the agenda if the need arises. Upon the conclusion of the audit committee meeting, minutes are circulated to the members of the

Table of Contents

audit committee for their comment and review prior to their approval of the minutes at the following or the subsequent audit committee meeting.

At each quarterly audit committee meeting, the audit committee reviews with the acting chief financial officer and our outside auditors, the financial statements for the financial period and the financial and accounting principles, policies and controls of the company and its subsidiaries. In particular, the Committee discusses (i) the changes in accounting policies and practices, if any; (ii) the going concern assumptions, (iii) compliance with accounting standards and applicable rules and other legal requirements in relation to financial reporting and (iv) our internal controls relating to financial reporting. Upon the recommendation of the audit committee, the Board will approve the financial statements.

Compensation Committee. As of December 31, 2007, the members of our compensation committee were Ta-Lin Hsu (chairman of compensation committee), Tsuyoshi Kawanishi and Lip-Bu Tan. None of these members of the compensation committee has been an executive officer or employee of the company or any of its subsidiaries. See Related Party Transactions for a description of transactions between us and the members of the compensation committee.

The responsibilities of the compensation committee include, among other things:

- approving and overseeing the total compensation package for our executive officers and any other officer, evaluating the performance of and determining and approving the compensation to be paid to our chief executive officer and reviewing the results of our chief executive officer s evaluation of the performance of our other executive officers;
- reviewing and making recommendations to our board of directors with respect to director compensation, including equity-based compensation;
- administering and periodically reviewing and making recommendations to the board of directors regarding the long-term incentive compensation or equity plans made available to the directors, employees and consultants;
- reviewing and making recommendations to the board of directors regarding executive compensation philosophy, strategy and principles and reviewing new and existing employment, consulting, retirement and severance agreements proposed for the company s executive officers; and
- ensuring appropriate oversight of our human resources policies and reviewing strategies established to fulfill our ethical, legal and human resources responsibilities.

In 2007, the compensation committee reviewed the total compensation package for Richard Ru Gin Chang, who is our president and chief executive officer and an executive director and awarded Richard Ru Gin Chang an annual salary of US$157,477. In 2006, the compensation committee reviewed and approved the total compensation package for Richard Ru Gin Chang. Based on the compensation committee s review of our corporate goals for 2006 and comparable total compensation packages for presidents and chief executive officers of other publicly-listed companies in the same or a similar industry, the compensation committee awarded Richard Ru Gin Chang an annual salary of US$155,076. In 2006, the compensation committee granted Dr. Chang the option to purchase five hundred thousand (500,000) ordinary shares under the 2004 Stock Option Plan. As of December 31, 2007, the option has not been exercised.

In 2005, the compensation committee granted Dr. Chang the option to purchase fifteen million (15,000,000) ordinary shares under the 2004 Stock Option Plan and an award of two million (2,000,000) restricted share units. As of December 31, 2007, the option has not been exercised and 75% of such RSUs have vested.

Table of Contents

On September 29, 2006, the Board granted to each director an option to purchase 500,000 ordinary shares at a price per ordinary share of US$0.132. 50% of these options were vested on each of May 30, 2007 and May 30, 2008. These options will expire on the earlier of September 29, 2016 or 120 days after termination of the director s service to the Board. Mr. Fang Yao (who resigned as Non-executive Director on August 30, 2007) and Mr. Jiang Shang Zhou have declined such option.

On September 29, 2006, the Board granted to Dr. Albert Y. C. Yu 500,000 Restricted Share Units. 50% of such restricted share units automatically vested on each of May 30, 2007 and May 30, 2008. On June 3, 2008, 500,000 ordinary shares were issued to Dr. Yu pursuant to the vesting of such restricted share units.

On November 10, 2004, the board of directors granted to each non-executive director and independent non-executive director, an option to purchase 500,000 ordinary shares at a price per ordinary share of US$0.22. These options were fully vested on March 19, 2005 and will expire on November 9, 2009. Lai Xing Cai (who resigned as an non-executive director on February 6, 2006) has declined such option. As of December 31, 2007, no director has exercised such options. The option granted to Mr. Yen-Pong Jou (who retired as an independent non-executive director at the annual general meeting held on May 30, 2006) lapsed and was cancelled on September 27, 2006.

In addition to reviewing the remuneration of the non-executive directors and the members of our management, the compensation committee reviewed and approved the granting of stock options and restricted share units pursuant to the terms of the Option Plans in 2007. The compensation committee also reviewed and approved on at least a quarterly basis any exception to the compensation guidelines and leave of absence policy of the Company.

The compensation committee reports its work, findings and recommendations to the board of directors during each quarterly board meeting.

The compensation committee meets in person at least on a quarterly basis and on such other occasions as may be required to discuss and vote upon significant issues affecting our compensation policy. The regular meeting schedule for a year is planned in the preceding year. The Company s Secretary assists the chairman of the compensation committee in preparing the agenda for meetings and assists the compensation committee in complying with relevant rules and regulations. The relevant papers for the compensation committee meeting are distributed to compensation committee members in accordance with relevant rules and regulations applicable to us. Members of the compensation committee may include matters for discussion in the agenda if the need arises. Upon the conclusion of the compensation committee meeting, minutes are circulated to the members of the compensation committee for their comment and review prior to their approval of the minutes at the following or a subsequent compensation committee meeting.

Corporate Governance Practices

Companies listed on the New York Stock Exchange must comply with certain corporate governance standards under Section 303A of the New York Stock Exchange Listed Company Manual. However, foreign private issuers, such as us are permitted to follow home country practices in lieu of the provisions of Section 303A, except that such companies are required to comply with the rules relating to the audit committee. Please refer to the following website at http:/www.smics.com/website/enVersion/IR/corporateGovernance.htm for a summary of the significant differences between our corporate governance practices and those required of U.S. companies under New York Stock Exchange listing standards.

Employees

The following table sets forth, as of the dates indicated, the number of our employees serving in the capacities indicated:

Table of Contents

	As of December 31,		
Function	**2005**	**2006**	**2007**
Managers	679	871	916
Professionals[1]	3,648	3,790	4,096
Technicians	4,127	4,804	5,188
Clerical staff	642	583	309
Total[2]	9,096	10,048	10,509

(1) Professionals include engineers, lawyers, accountants and other personnel with specialized qualifications, excluding managers.

(2) Includes 283, 275, and 276 temporary and part-time employees in 2005, 2006 and 2007, respectively.

The following table sets forth, as of the dates indicated, a breakdown of the number of our employees by geographic location:

	As of December 31,		
Location of Facility	**2005**	**2006**	**2007**
Shanghai	6,232	6,400	6,300
Beijing	1,534	1,827	1,942
Tianjin	1,034	1,073	1,205
Chengdu	261	715	1,023
United States	18	16	18
Europe	7	7	8
Japan	6	7	9
Hong Kong	4	3	4
Total	9,096	10,048	10,509

Our employees are not covered by any collective bargaining agreements.

Share Ownership

The table below sets forth the ordinary shares beneficially owned by each of our directors and options to purchase ordinary shares as of December 31, 2007:

Name of Director	Current Shareholding	Options to Purchase Ordinary Shares Number of Options	Exercise Price	Awards of Restricted Share Units
Richard Ru Gin Chang	78,069,550(1)(2)	15,600,000	US$0.132-US$0.31	500,000
Ta-Lin Hsu	15,300,010(3)	1,000,000	US$0.132-US$0.22	
Tsuyoshi Kawanishi	0	2,500,000	US$ 0.05 US$0.22	
Henry Shaw	0	1,000,000	US$0.132-US$0.22	
Lip-Bu Tan	0	1,000,000	US$0.132-US$0.22	
Yang Yuan Wang	0	1,000,000	US$0.132-US$0.22	
Jiang Shang Zhou	0	0		
Albert Y. C. Yu	1,350,000	500,000	US$ 0.132	500,000
Wang Zheng Gang	0	0		

Notes:

1. Pursuant to a Charitable Pledge Agreement dated December 1, 2003, Richard Ru Gin Chang and his spouse, Scarlett K. Chang (collectively, the Donors) have pledged to transfer 10,000,000 of such ordinary shares as a charitable gift to The Richard and Scarlett Chang Family Foundation, a Delaware nonprofit nonstock corporation organized exclusively for religious, charitable, scientific, literary and education purposes within the meaning of

Section 501(c)(3) of the US Internal Revenue Code of 1986, as amended, such transfer to be

Table of Contents

made in full at or prior to the death of the surviving Donor. In addition, 2,639,550 of such ordinary shares are jointly held by Richard Ru Gin Chang and his spouse, Scarlett K. Chang.

2. 20,000,000 of the ordinary shares held as a corporate interest. These ordinary shares are held by Jade Capital Company, LLC, a Delaware limited liability company (the LLC), of which Richard Ru Gin Chang and his spouse, Scarlett K. Chang (collectively, the Members), are the sole members. It is the current intent of the Members that all or a portion of the net income of the LLC be used for philanthropic purposes, including but not limited to contributions to charitable

organizations that are tax-exempt under Section 501(c)(3) of the US Internal Revenue Code of 1986, as amended.

3. Ta-Lin Hsu has a controlling interest in AP3 Co-Investment Partners, LDC, which holds 15,300,010 ordinary shares.

The share holdings set forth above excludes shares beneficially owned by entities affiliated with our directors. Each of our directors disclaims beneficial ownership of the shares beneficially owned by such affiliated entity, except to the extent of such director s pecuniary interest therein as disclosed above.

On July 11, 2002, the compensation committee issued Mr. Kawanishi an option to purchase 500,000 ordinary shares pursuant to the terms of the 2001 Stock Option Plan. This option will expire on July 11, 2012. On January 15, 2004, the board issued him an option to purchase 1,000,000 ordinary shares pursuant to the terms of the 2001 Stock Option Plan. This option will expire on January 15, 2014. The exercise prices of the options are US$0.05 and US$0.10, respectively.

On November 10, 2004, the Board granted to each independent non-executive director and non-executive director as of such date, an option to purchase 500,000 ordinary shares at a price per ordinary share of US$0.22. These options vested on March 19, 2005 and will expire on November 10, 2009. Lai Xing Cai (who resigned as non-executive director on February 6, 2006) has declined this option. As of December 31, 2007, no director has exercised such options. The option granted to Mr. Yen-Pong Jou (who retired as an independent non-executive director at the 2006 AGM) lapsed and cancelled on September 27, 2006.

On April 7, 2004, the compensation committee issued to Richard Ru Gin Chang an option to purchase 100,000 ordinary shares. The exercise price per ordinary share underlying the option was US$0.31. The option will expire on April 7, 2014. On May 11, 2005, the compensation committee issued to Richard Ru Gin Chang an option to purchase 15,000,000 ordinary shares and an award of 2,000,000 restricted share units. The exercise price per ordinary share underlying the option is US$0.196. The option and the award of restricted share units will expire on May 11, 2015. As of December 31, 2007, none of these options have been exercised and 75% of such RSUs have vested.

On September 29, 2006, the Board granted to each director an option to purchase 500,000 ordinary shares at a price per ordinary share of US$0.132. These options were vested as to 50% on each of May 30, 2007 and May 30, 2008 respectively and will expire on the earlier of September 29, 2016 or 120 days after termination of the director s service to the Board. As of December 31, 2007, these options have not been exercised. Fang Yao (who resigned as non-executive director on August 30, 2007) and Jiang Shang Zhou have declined such options.

On September 29, 2006, the Board granted to Dr. Albert Y. C. Yu 500,000 restricted share units. Shares under the restricted share units automatically vested as to 50% on each of May 30, 2007 and May 30, 2008 respectively. On June 3, 2008, 500,000 ordinary shares were issued to Dr. Yu pursuant to vesting of such restricted share units. In 2007, the Board did not grant options or restricted share units to any director as compensation for their service on the Board.

The compensation committee has issued each of our executive officers options to purchase ordinary shares pursuant to our 2001 Regulation S Stock Option Plan, 2001 Regulation S Preference Shares Stock Plan and the 2004 Stock Option Plan and restricted share units that represent rights to receive ordinary

85

Table of Contents

shares pursuant to our 2004 Equity Incentive Plan. The exercise price of the options range from US$0.01 to US$0.35. The options expire between November 10, 2009 and September 29, 2016. The restricted share units expire between July 26, 2015 and September 29, 2016. The majority of the options and restricted share units are subject to a four-year vesting period. Each executive officer owns less than 1% of the total outstanding shares of the company.

2001 Stock Plan and 2001 Regulation S Stock Plan

On March 28, 2001, our board of directors and shareholders adopted our 2001 Stock Plan and our 2001 Regulation S Stock Plan. Under these plans, our directors, employees and consultants are eligible to acquire ordinary shares pursuant to options. At the time of adoption, 250,000,000 post-split ordinary shares were reserved for issuance under the 2001 Stock Plan and 470,000,000 post-split ordinary shares were reserved for issuance under the 2001 Regulation S Stock Plan. On August 27, 2003, our shareholders approved an increase in the number of authorized shares reserved under the plans of 3,438,900 post-split ordinary shares, increasing the total number of authorized shares reserved under the plans to 723,438,900 post-split ordinary shares. On August 27, 2003, September 22, 2003 and December 4, 2003, our shareholders approved additional increases in the number of shares reserved under our 2001 Regulation S Stock Plan of up to 325,000,000, 21,499,990 and 235,089,480 post-split ordinary shares, respectively, which amounts were to be adjusted from time to time to equal 10% of the post-split ordinary shares issuable upon the conversion of all Series C convertible preference shares and Series D convertible preference shares then outstanding. As of December 31, 2007, there were 998,675,840 post-split ordinary shares authorized for issuance under the plans, 331,386,245 post-split ordinary shares subject to outstanding options under the plans and 376,137,074 post-split ordinary shares outstanding from the exercise of options granted under the plans. These plans terminate on December 4, 2013 but may be terminated earlier by our board of directors.

Stock options granted under the 2001 Stock Plan may be incentive stock options, or ISOs, which are intended to qualify for favorable U.S. federal income tax treatment under the provisions of Section 422 of the U.S. Internal Revenue Code of 1986, as amended, or U.S. Internal Revenue Code, or non-qualified stock options, or NSOs, which do not so qualify. Stock options granted under the 2001 Regulation S Stock Plan are NSOs. The aggregate fair market value of the ordinary shares represented by any given optionee s ISOs that become exercisable in any calendar year may not exceed US$100,000. Stock options in excess of this limit are treated as NSOs.

The board of directors, the compensation committee, and the non-executive option grant committee administer the 2001 Stock Plan and 2001 Regulation S Stock Plan. The compensation committee selected the eligible persons above a certain compensation grade to whom options were granted and determined the grant date, amounts, exercise prices, vesting periods and other relevant terms of the stock options, including whether the options will be ISOs or NSOs. The non-executive option grant committee selected the eligible persons below a certain compensation grade to whom options were granted and determined the grant date, amounts, exercise prices, vesting periods and other relevant terms of stock options within parameters established by the compensation committee and subject to compensation committee ratification. The exercise price of ISOs granted under the 2001 Stock Plan and NSOs granted to residents of California under the 2001 Stock Plan may not be less than 100% and 85%, respectively, of the fair market value of our ordinary shares on the grant date. The exercise price of NSOs not granted to residents of California under either our 2001 Stock Plan or our 2001 Regulation S Stock Plan can be determined by the board of directors, the compensation committee or the non-executive option grant committee in their discretion.

Stock options granted under the 2001 Stock Plan and 2001 Regulation S Stock Plan may be exercised at any time after they vest, and, in certain instances, prior to vesting. Shares purchased when an option is exercised prior to vesting are subject to our right of repurchase to the extent unvested in the event of the termination of service of the optionee. In the event of the termination of service of an optionee, the unvested portion of a stock option is forfeited and the vested portion terminates six months after a termination of service due to the death or permanent disability of the optionee or 30 days after termination of service for any other reason or such longer periods as may be provided for in option agreements with our optionees. Stock options are generally not transferable during the life of the optionee.

Table of Contents

In the event of a change of control (as defined in the plans) or a merger of our company, each outstanding stock option may be assumed or an equivalent stock option or right may be substituted by the successor corporation. In the event that no such substitution or assumption occurs, the outstanding stock options will automatically vest and become exercisable for a period of 15 days, after which the stock options will terminate.

We have not issued stock options under the 2001 Stock Plan or the 2001 Regulation S Stock Plan since the completion of the global offering.

2001 Preference Shares Stock Plan and 2001 Regulation S Preference Shares Stock Plan

On April 12, 2001, our board of directors and shareholders adopted our 2001 Preference Shares Stock Plan and our 2001 Regulation S Preference Shares Stock Plan. Under these plans, our directors, employees and consultants were eligible to acquire Series A convertible preference shares prior to the completion of the global offering and ordinary shares upon or following the completion of the global offering, pursuant to options. At the time of adoption, 16,000,000 Series A preference shares and ten times that number of ordinary shares (on a post-split basis) were reserved for issuance under the 2001 Preference Shares Stock Plan, and 20,000,360 Series A convertible preference shares and ten times that number of ordinary shares (on a post-split basis) were reserved for issuance under the 2001 Regulation S Preference Shares Stock Plan. On August 19, 2002, our shareholders approved an increase in the number of shares issuable under the plans of 18,000,180 Series A convertible preference shares, increasing the total number of authorized shares reserved under the plans to 54,000,540 Series A convertible preference shares. On August 27, 2003, our shareholders approved a net decrease in the number of shares issuable under the plans of 343,890 Series A convertible preference shares, decreasing the total number of authorized shares reserved under the plans to 53,656,650 Series A convertible preference shares. Upon the conversion of our preference shares into ordinary shares in connection with the global offering, options granted under the 2001 Preference Shares Stock Plan and the 2001 Regulation S Preference Shares Stock Plan converted into options to purchase ordinary shares. As of December 31, 2007, there were 55,923,000 ordinary shares subject to outstanding options under the plans, and there were 400,747,130 ordinary shares outstanding from the exercise of options granted under the plans. Our board of directors has elected not to grant any further options under these plans.

Stock options granted under the 2001 Preference Shares Stock Plan may be ISOs or NSOs. Stock options granted under the 2001 Regulation S Preference Shares Stock Plan are NSOs. The aggregate fair market value of the shares represented by any given optionee s ISOs that become exercisable in any calendar year may not exceed US$100,000. Stock options in excess of this limit are treated as NSOs.

The board of directors, the compensation committee and the non-executive option grant committee administer the 2001 Preference Shares Stock Plan and 2001 Regulation S Preference Shares Stock Plan. The compensation committee selected the eligible persons above a certain compensation grade to whom options were granted and determined the grant date, amounts, exercise prices, vesting periods and other relevant terms of the stock options, including whether the options will be ISOs or NSOs. The non-executive option grant committee selected the eligible persons below a certain compensation grade to whom options were granted and determined the grant date, amounts, exercise prices, vesting periods and other relevant terms of stock options within parameters established by the compensation committee and subject to compensation committee ratification. The exercise price of ISOs granted under the 2001 Preference Shares Stock Plan and NSOs granted to residents of California under the 2001 Preference Shares Stock Plan may not be less than 100% and 85%, respectively, of the fair market value of our Series A convertible preference shares on the grant date. The exercise price of NSOs not granted to California residents under either our 2001 Preference Shares Stock Plan or our 2001 Regulation S Preference Shares Stock Plan can be determined by the board of directors, the compensation committee or the non-executive option grant committee in their discretion.

Stock options granted under the 2001 Preference Shares Stock Plan and 2001 Regulation S Preference Shares Stock Plan may be exercised at any time after they vest, and, in certain instances, prior to vesting. Shares purchased when an option is exercised prior to vesting are subject to our right of repurchase to the extent unvested in the event of the termination of service of the optionee. In the event of the

Table of Contents

termination of service of an optionee, the unvested portion of a stock option is forfeited and the vested portion terminates six months after a termination of service due to the death or permanent disability of the optionee or 30 days after termination of service for any other reason or such longer periods as may be provided for in option agreements with our optionees. Stock options are generally not transferable during the life of the optionee.

In the event of a change of control (as defined in the plans) or a merger of our company, each outstanding stock option may be assumed or an equivalent stock option or right may be substituted by the successor corporation. In the event that no such substitution or assumption occurs, the outstanding stock options will automatically vest and become exercisable for a period of 15 days, after which the stock options will terminate.

We have not issued stock options under the 2001 Preference Shares Stock Plan or the 2001 Regulation S Preference Shares Stock Plan since the completion of the global offering.

2004 Global Equity Incentive Compensation Program

Our board of directors adopted our 2004 Stock Option Plan, our 2004 Employee Stock Purchase Plan, and our 2004 Equity Incentive Plan on January 16, 2004. Our shareholders approved our 2004 Stock Option Plan and 2004 Employee Stock Purchase Plan on February 16, 2004 and our 2004 Equity Incentive Plan on March 10, 2004.

The purpose of these plans is to allow our employees, directors and service providers the opportunity to share in the growth and profitability of our company following the global offering and to provide a non-cash means of incentivizing and retaining these individuals. An aggregate maximum of 1,317,000,000 ordinary shares were reserved for issuance under the 2004 Stock Option Plan and the 2004 Employee Stock Purchase Plan, to be allocated between the plans at the discretion of our board of directors and compensation committee. In no event may a stock option or a purchase right be granted under the 2004 Stock Option Plan or the 2004 Employee Stock Purchase Plan, respectively, if such grant would result in the total aggregate number of ordinary shares subject to all then outstanding stock options or purchase rights granted by us pursuant to the 2004 Stock Option Plan, the 2004 Employee Stock Purchase Plan or any other of our plans or schemes exceeding 30% of the issued and outstanding ordinary shares in issuance from time to time.

A maximum of 2.5% of the ordinary shares that were issued and outstanding immediately following the closing of the global offering, or 455,409,330 ordinary shares, were reserved for issuance under the 2004 Equity Incentive Plan. The number of ordinary shares or ADSs issued upon the settlement of a stock appreciation right that is granted in connection with a stock option granted under the 2004 Stock Option Plan will reduce the plan limit under the 2004 Equity Incentive Plan.

2004 Stock Option Plan. Under the 2004 Stock Option Plan, employees and service providers are eligible to acquire ordinary shares or ADSs pursuant to stock options. The 2004 Stock Option Plan also provides for grants of stock options to non-employee directors at our board of directors discretion.

The 2004 Stock Option Plan will terminate on the tenth anniversary of the date of shareholder approval but may be terminated earlier by our board of directors. The 2004 Stock Option Plan provides for the grant of incentive stock options (ISOs) and non-qualified stock options (NSOs). Any awards of director stock options to non-employee directors are NSOs. The aggregate fair market value of the ordinary shares represented by any given optionee s ISOs that become exercisable in any calendar year may not exceed US$100,000. Stock options in excess of this limit are treated as NSOs.

The compensation committee and the non-executive option grant committee administer the 2004 Stock Option Plan. The compensation committee issues grants of stock options to our executive officers and determines the grant date, number of underlying ordinary shares or ADSs, exercise prices, vesting periods and other relevant terms of the stock options, including whether the stock options will be ISOs or NSOs, except that ISOs may be granted only to employees and director stock options may be granted only

Table of Contents

to non-employee directors. The non-executive option grant committee issues grants to all employees other than our executive officers and determines the grant date, amounts, exercise prices, vesting periods and other relevant terms of stock options within parameters established by the compensation committee and subject to compensation committee ratification. The exercise price of a stock option granted under the 2004 Stock Option Plan shall be no less than the higher of (i) the closing price of an ordinary share on the Hong Kong Stock Exchange (or, in the case of an ADS, of an ADS on the New York Stock Exchange) and (ii) the average closing price of an ordinary share on the Hong Kong Stock Exchange (or, in the case of an ADS, of an ADS on the New York Stock Exchange) for the five business days immediately preceding the date of grant. The compensation committee determines the effect of a termination of employment on a stock option awarded under the 2004 Stock Option Plan except that if employment is terminated for cause, as defined in the plan, all unexercised stock options of an optionee are forfeited. Our board of directors exercises all authority and responsibility with respect to any stock options granted to non-employee directors. Stock options are generally not transferable during the life of the optionee.

The compensation committee will specify the effect that a merger or change in control (as defined in the 2004 Stock Option Plan) will have on grants of stock options, which may include the acceleration of vesting of stock options prior to the date of the change of control.

As of December 31, 2007, options to purchase an aggregate of 861,729,000 ordinary shares in our company had been issued to employees, directors, and other service providers of our company under the 2004 Stock Option Plan. During the year ended 2007, we issued 183,510 ordinary shares upon the exercise of options under the 2004 Stock Option Plan.

2004 Equity Incentive Plan. Under the 2004 Equity Incentive Plan, our employees, officers and service providers are eligible to acquire equity-based awards other than stock options. The 2004 Equity Incentive Plan will terminate on the tenth anniversary of the date of shareholder approval but may be terminated earlier by our board of directors.

The compensation committee and the non-executive option grant committee administer the 2004 Equity Incentive Plan. The compensation committee issues awards to our executive officers and determines the type of award, grant date, amounts, vesting periods and other relevant terms of the awards. The non-executive option grant committee issues awards to our executive officers and determines the type of award, grant date, amounts, vesting periods and other relevant terms of the awards within parameters established by the compensation committee and subject to compensation committee ratification.

As of December 31, 2007, awards to receive an aggregate of up to 297,188,148 ordinary shares in our company pursuant to grants of restricted share units had been issued to employees and other service providers of our company under the 2004 Equity Incentive Plan. During the year ended 2007, we issued 43,253,907 ordinary shares upon the vesting of restricted share units under the 2004 Equity Incentive Plan.

Stock Appreciation Rights. Under the 2004 Equity Incentive Plan, the compensation committee and the non-executive option grant committee may grant stock appreciation rights independent of or in connection with a stock option granted under the 2004 Stock Option Plan. Generally, each stock appreciation right will entitle a participant upon settlement to an amount equal to (1) the excess of (A) the market value on the exercise date of one ordinary share or ADS, divided by (B) the exercise price, multiplied by (2) the number of ordinary shares or ADSs covered by the stock appreciation right. Payment will be made in ordinary shares or ADSs or in cash, or partly in ordinary shares or ADSs and partly in cash, all as determined by the compensation committee and the non-executive option grant committee.

Other Equity-Based Awards. Under the 2004 Equity Incentive Plan, the compensation committee and the non-executive option grant committee may grant awards of restricted shares, restricted share units, dividend equivalents, deferred shares and other awards that are valued in whole or in part by reference to, or are otherwise based on the fair market value of, ordinary shares. The other share-based awards are subject to the terms and conditions established by the compensation committee and the non-executive option grant committee. The compensation committee will specify the effect that a merger or change in control will have on grants of stock options, which may include acceleration of vesting of stock options prior to the date of the change of control.

Table of Contents

2004 Employee Stock Purchase Plan. The 2004 Employee Stock Purchase Plan is intended to qualify for favorable federal income tax treatment under the provisions of Section 423 of the U.S. Internal Revenue Code. Under the 2004 Employee Stock Purchase Plan, all employees of our participating subsidiaries are eligible (subject to limited exceptions set forth in the U.S. Internal Revenue Code) to elect through payroll deductions to purchase ADSs at a discount. The 2004 Employee Stock Purchase Plan will terminate on the tenth anniversary of the date of shareholder approval but may be terminated earlier by our board of directors. The compensation committee administers the 2004 Employee Stock Purchase Plan. The compensation committee may delegate some or all of its authority (with certain restrictions) under the 2004 Employee Stock Purchase Plan to one or more of its members or one or more of our officers.

The 2004 Employee Stock Purchase Plan will be implemented by a series of offering periods. The compensation committee will determine the starting and ending dates of each offering period, but no offering period can be shorter than 6 months or longer than 27 months.

An eligible employee may elect to participate in the 2004 Employee Stock Purchase Plan for any offering period by filing the enrollment documents with the appropriate human resources group. A participant will elect to have payroll deductions made on each payday during the offering period in a dollar amount specified in the employee s enrollment documents. These deductions will be placed into an account on behalf of a participant.

The compensation committee will determine the maximum amount that any employee may contribute to his or her account under the 2004 Employee Stock Purchase Plan during any calendar year. A participant may not accrue share purchase rights at a rate that exceeds US$25,000, based on the fair market value of the plan shares or such lower amount as the compensation committee may determine for each calendar year in which the share purchase right is outstanding.

A participant may terminate participation in the 2004 Employee Stock Purchase Plan and withdraw from an offering by submitting a withdrawal notice and receiving all of his or her accumulated payroll deductions from that offering. Upon withdrawal, the participant s right to purchase ADSs for the current offering period will be terminated, and the participant can no longer participate in the current offering.

On the last day of the offering period, a participant s accumulated contributions are used to purchase ADSs at a price equal to the lesser of 85% of the fair market value of such ADSs on the date the offering period commenced or 85% of the fair market value of such ADSs on the date the offering period concluded. The ADSs are then deposited to an account established in the participant s name with a broker designated by us.

If a participant s employment terminates prior to the end of an offering period for any reason (subject to the limited exception set forth below), we will pay to the participant his or her account balance and the participant s right to purchase ADSs under the 2004 Employee Stock Purchase Plan will automatically terminate. If a participant s employment terminates less than three months prior to the end of the offering period for certain non-cause triggers, the participant will continue to participate in the 2004 Employee Stock Purchase Plan for the offering period then in progress, except that the participant s contributions will cease with the contribution made from such participant s final paycheck.

As of December 31, 2007, no ADSs had been issued pursuant to the 2004 Employee Stock Purchase Plan.

Table of Contents

Item 7. Major Shareholders

Major Shareholders

The following table sets forth information regarding the beneficial ownership as of December 31, 2007 of our ordinary shares, by each shareholder who is known by us to beneficially own 5% or more of our outstanding shares as of such date.

Name of Shareholder	Number of Shares Held	Percentage Held
Shanghai Industrial Investment (Holdings) Company Limited (SIIC)	208,002,000 (long position)(1)	1.12% (long position)
	1,814,991,340 (long position)(2)	9.78% (long position)
	7,272,563 (long position)(3)	0.04% (long position)
Total:	2,030,265,903 (long position)	10.94% (long position)

Notes:

(1) All such ordinary shares are held by SIIC Treasury (B.V.I.) Limited which is a wholly-owned subsidiary of SIIC.

(2) All such ordinary shares are held by S.I. Technology Production Holdings Limited (SITPHL) which is a wholly-owned subsidiary of Shanghai Industrial Holdings Limited (SIHL). SIHL is an indirect non-wholly owned subsidiary of SIIC which are holding SIHL s

shares through its wholly-owned subsidiaries namely, SIIC CM Development Limited, SIIC Capital (B.V.I.) Limited and Shanghai Investment Holdings Limited, which together are entitled to exercise or control the exercise of more than one-third of the voting power at the general meetings of SIHL. By virtue of the SFO, SIIC and its subsidiaries namely, Shanghai Investment Holdings Limited and Shanghai Industrial Investment Treasury Company Limited are deemed to be interested in the 1,814,991,340 Shares held by SITPHL. The Company s Director as of December 31, 2007, Wang Zheng Gang, is the Chief Representative

of the Shanghai Representative Office of SIHL and chairman and managing director of SIIC Management (Shanghai) Limited. It is the Company s understanding that voting and investment control over the ordinary shares beneficially owned by SIHL are maintained by the board of directors of SIHL.

(3) All such ordinary shares are held by SIHL Treasury Limited which is a wholly-owned subsidiary of SIHL.

Each ordinary share is entitled to one vote on all matters upon which the ordinary shares are entitled to vote, including the election of directors. No shareholder has voting rights that are different from those of other shareholders.

As of December 31, 2007, 18,558,919,712 ordinary shares (inclusive of 56,363,511 ADS shares) of our company were outstanding. Of these ordinary shares, 2,818,175,550 shares were registered in the name of J.P. Morgan Chase Bank, the depositary under the deposit agreement. J.P. Morgan has advised us that, as of December 31, 2007, these 56,363,511ADSs, representing 2,818,175,550 ordinary shares, were held of record by 7 U.S. persons. We have no further information as to shares held or beneficially owned by U.S. persons. Each ADS represents 50 ordinary shares.

We do not believe that we are directly or indirectly owned or controlled by another corporation, by any foreign government or by any other natural or legal person severally or jointly.

Table of Contents

Related Party Transactions

The following disclosure is for the purpose of fulfilling disclosure requirements pursuant to the Rules Governing the Listing of Securities on the HKSE (the HK Listing Rules) and the rules and regulations promulgated pursuant to the U.S. Securities and Exchange Act of 1934, as amended, only, and may contain disclosure of related party transactions not required to be disclosed in our financial statements under U.S. GAAP. This section is not applicable under U.S. GAAP since it is not related to financial data.

Indemnification Agreements

Article 156 of our Articles of Association provides (amongst others) that we may indemnify any person who is made a party to any action, suit or proceeding by reason of the fact that the person is or was a our director, officer, employee or agent, or is or was serving at our request as our director, officer, employee or agent at another entity, subject to certain limitations and applicable conditions.

We recognize the substantial increase in corporate litigation in general, subjecting directors, officers, employees, agents and fiduciaries to expensive litigation risks. We desire to attract and retain the services of highly qualified individuals to serve the company and, in part, in order to induce such individuals to continue to provide services to the company, we wish to provide for the indemnification and advancing of expenses of its directors as permitted by law and HK Listing Rules.

Original Indemnification Agreements. On or around March 18, 2004, upon completion of the global offering, we entered into identical indemnification agreements with each director whose appointment as director took effect immediately upon the global offering (the Global Offering Directors), whereby we agreed to indemnify the Global Offering Directors in respect of liability arising from their capacity as our directors (collectively, the Original Indemnification Agreements). Pursuant to the Original Indemnification Agreements, we were obligated to indemnify each Global Offering Director, to the fullest extent permitted by law, against all costs, charges, expenses, liabilities, losses and obligations incurred in connection with any threatened, pending or completed action, suit, proceeding or alternative dispute resolution mechanism, or any hearing, inquiry or investigation which might lead to any of the foregoing (an Applicable Claim) by reason of or arising out of any event or occurrence relating to the fact that he is or was a director, or any of its subsidiaries, or is or was serving at our request at another corporation or enterprise, or by reason of any activity or inactivity while serving in such capacity (an Indemnifiable Event). Our obligation to indemnify our Global Offering Directors pursuant to the Original Indemnification Agreements was subject to certain exceptions and limitations set out therein.

New Indemnification Agreements. At the 2005 annual general meeting of our shareholders held on May 6, 2005, our shareholders, other than the directors, chief executive officer of the company and their respective Associates (as defined in the HK Listing Rules) approved an amendment to the form of the Original Indemnification Agreements (the New Indemnification Agreement). The New Indemnification Agreement reflects the new requirements under Rules 14A.35 of the HK Listing Rules to set a term of no longer than three years and a maximum aggregate annual value for each connected transaction (as defined under the HK Listing Rules). The New Indemnification Agreements superseded the Original Indemnification Agreements which we had previously entered into with any existing directors. The terms of the New Indemnification Agreements are the same as the Original Indemnification Agreements, except that the New Indemnification Agreements are subject to a term of three years and an annual cap (as described below).

The annual cap in relation to the New Indemnification Agreements will not exceed a maximum aggregate annual value as disclosed in our previous announcement (the Current Limit).

The New Indemnification Agreement became effective upon execution by each director. The New Indemnification Agreements will continue in effect with respect to Applicable Claims relating to Indemnifiable Events regardless of whether the relevant director continues to serve as our director or to serve at any other enterprise at our request.

Table of Contents

For the year ended December 31, 2007, no payment was made to any director under the Original Indemnification Agreements or the New Indemnification Agreements. The term of the New Indemnification Agreements expired on June 2, 2008 (which is the date of our 2008 annual general meeting) and we intend to enter into a services contract containing indemnification provisions with each of our directors.

Item 8. Financial Information

Consolidated Statements and Other Financial Information

Please see Item 18. Financial Statements.

See Item 4 Information on the Company Business Overview Customers and Markets regarding the percentage of our sales which are exported from China.

Litigation

As is the case with many companies in the semiconductor industry, we have received from time to time communications from third parties asserting that our technologies, fabrication processes, design of the semiconductors made by us or use by our customers of semiconductors made by us may infringe upon patents or other intellectual property rights of others. Irrespective of the validity of such claims, we could incur significant costs in the defense thereof or could suffer adverse effects on our operations.

In December 2003, we became the subject of a lawsuit in U.S. federal district court brought by TSMC relating to alleged infringement of five U.S. patents and misappropriation of alleged technical and operational trade secrets relating to methods for conducting semiconductor fab operations and manufacturing integrated circuits. After the dismissal without prejudice of the trade secret misappropriation claims by the U.S. federal district court on April 21, 2004, TSMC refiled the same claims in California State Superior Court and claimed alleged infringement of an additional 6 patents in the U.S. federal district court lawsuit. In August 2004, TSMC filed a complaint with the ITC alleging similar trade secret misappropriation claims and asserting 3 new patent infringement claims and simultaneously filed another patent infringement suit in federal district court on the same 3 patents as alleged in the ITC complaint. Prior to the start of the initial lawsuit in the United States, TSMC had instituted a legal proceeding in Taiwan in January 2002 that alleged improper hiring practices and trade secret misappropriation. In the Taiwan proceeding, the Hsinchu District Court in Taiwan issued an ex parte provisional injunction that prohibits our wholly owned subsidiary, Semiconductor Manufacturing International (Shanghai) Corporation, or SMIC Shanghai, from improperly soliciting or hiring certain categories of employees of TSMC or causing such employees to divulge to us, or use, trade secrets of TSMC. According to TSMC s initial complaint filed in the United States, the Taiwan provisional injunction has no territorial effect outside of Taiwan. The provisional injunction may be challenged by us at any time, but we have thus far seen no cause for challenging that ruling, and to date the provisional injunction has not adversely affected our operations.

On January 31, 2005, we entered into a settlement agreement with TSMC that provides for the dismissal of all pending legal actions without prejudice between TSMC and our company in U.S. federal district court, California State Superior Court, the ITC and Taiwan District Court. In the settlement agreement, TSMC covenants not to sue the company for itemized acts of trade secret misappropriation as alleged in the complaints, although the settlement does not grant a license to use any of TSMC s trade secrets. Furthermore, the parties also entered into a patent cross-license agreement under which each party will license the other party s patent portfolio through December 2010. As a part of the settlement, we also agreed to pay TSMC an aggregate amount of US$175 million, in installments of US$30 million each year for five years and US$25 million in the sixth year.

The patent cross-license agreement and settlement agreement are terminable upon a specified breach of the settlement agreement by SMIC. Any such breach may result in the filing of a lawsuit relating to such breach, recommencement or re-filing of the legal proceedings and acceleration of the outstanding monetary payment obligations under the settlement agreement.

Table of Contents

On August 25, 2006, TSMC filed a lawsuit against the Company and certain subsidiaries (SMIC (Shanghai), SMIC (Beijing) and SMIC (Americas)) in the Superior Court of the State of California, County of Alameda for alleged breach of the Settlement Agreement, alleged breach of promissory notes and alleged trade secret misappropriation by the Company. TSMC seeks, among other things, damages, injunctive relief, attorneys fees, and the acceleration of the remaining payments outstanding under the Settlement Agreement.

In the present litigation, TSMC alleges that the Company has incorporated TSMC trade secrets in the manufacture of the Company s 0.13 micron or smaller process products. TSMC further alleges that as a result of this claimed breach, TSMC s patent license is terminated and the covenant not to sue is no longer in effect with respect to the Company s larger process products.

The Company has vigorously denied all allegations of misappropriation. The Court has made no finding that TSMC s claims are valid, nor has it set a trial date.

On September 13, 2006, the Company announced that in addition to filing a response strongly denying the allegations of TSMC in the United States lawsuit, it filed on September 12, 2006, a cross-complaint against TSMC seeking, among other things, damages for TSMC s breach of contract and breach of implied covenant of good faith and fair dealing.

On November 16, 2006, the High Court in Beijing, the People s Republic of China, accepted the filing of a complaint by the Company and its wholly-owned subsidiaries, SMIC (Shanghai) and SMIC (Beijing), regarding the unfair competition arising from the breach of bona fide (i.e. integrity, good faith) principle and commercial defamation by TSMC (PRC Complaint). In the PRC Complaint, the Company is seeking, among other things, an injunction to stop TSMC s infringing acts, public apology from TSMC to the Company and compensation from TSMC to the Company, including profits gained by TSMC from their infringing acts.

TSMC filed with the California court in January 2007 a motion seeking to enjoin the PRC action. In February 2007, TSMC filed with the Beijing High Court a jurisdictional objection, challenging the competency of the Beijing High Court s jurisdiction over the PRC action.

In March 2007, the California Court denied TSMC s motion to enjoin the PRC action. TSMC has appealed this ruling to California Court of Appeal. On March 26, 2008, the Court of Appeal, in a written opinion, denied TSMC s appeal. That decision is now final and unappealable.

In July 2007, the Beijing High Court denied TSMC s jurisdictional objection and issued a court order holding that the Beijing High Court shall have proper jurisdiction to try the PRC action. TSMC has appealed this order to the Supreme Court of the People s Republic of China. On January 7, 2008, the Supreme Court heard TSMC s appeal. On May 29, 2008, the Supreme Court denied TSMC s appeal and confirmed the jurisdiction of the Beijing High Court.

On August 14, 2007, the Company filed an amended cross-complaint against TSMC seeking, among other things, damages for TSMC s breach of contract and breach of patent license agreement. TSMC thereafter denied the allegations of the Company s amended cross-complaint and attempted to file additional claims that the Company breached the Settlement Agreement by filing an action in the Beijing High Court. Upon the Company s motion, the California Court struck TSMC s new claims as procedurally improper, but granted TSMC leave to replead its claims.

On August 15-17, 2007, the California Court held a preliminary injunction hearing on TSMC s motion to enjoin use of certain process recipes in certain of the Company s 0.13 micron logic process flows. On September 7, the Court denied TSMC s preliminary injunction motion, thereby leaving unaffected the Company s development and sales. However, the court required the Company to provide 10 days advance

Table of Contents

notice to TSMC if the Company plans to disclose logic technology to non-SMIC entities under certain circumstances, to allow TSMC to object to the planned disclosure.

On March 11, 2008, TSMC filed an application for a right to attach order in the California Court. By its application, TSMC sought an order securing an amount equal to the remaining balance on the promissory notes issued by the Company in connection with the Settlement Agreement.

In May 2008, TSMC filed a motion in the California Court for summary adjudication against the Company on several of the Company s cross claims. The Company will oppose the motion. A hearing has been set on the motion for July 25, 2008.

On June 23, 2008, the Company filed with California court a cross-complaint against TSMC seeking, among other things, damages for TSMC s unlawful stealing of trade secrets from SMIC to improve its competitive position against SMIC.

On June 25, 2008, the Court issued an order denying TSMC s application for a right to attach order.

In addition to the litigation matters described above, we are occasionally involved in routine litigation matters that are common for our industry, none of which we believe has been or is material.

Dividends and Dividend Policy

Since our inception, we have not declared or paid any cash dividends on our ordinary shares. We intend to retain any earnings for use in our business and do not currently intend to pay cash dividends on our ordinary shares. Dividends, if any, on the outstanding shares will be declared by and subject to the discretion of our board of directors and must be approved at our annual general meeting of shareholders. The timing, amount and form of future dividends, if any, will also depend, among other things, on:

our results of operations and cash flow;

our future prospects;

our capital requirements and surplus;

our financial condition;

general business conditions;

contractual restrictions on the payment of dividends by us to our shareholders or by our subsidiaries to us; and

other factors deemed relevant by our board of directors.

Our ability to pay cash dividends will also depend upon the amount of distributions, if any, received by us from our wholly owned Chinese operating subsidiaries. Under the applicable requirements of Chinese Company Law, our Chinese subsidiaries may only distribute dividends after they have made allowances for:

recovery of losses, if any;

allocation to the statutory common reserve funds;

allocation to staff and workers bonus and welfare funds; and

allocation to a discretionary common reserve fund if approved by our shareholders.

More specifically, these operating subsidiaries may only pay dividends after 10% of their net profit has been set aside as statutory common reserves and a discretionary percentage of their net profit has been set aside for the staff and workers bonus and welfare funds. These operating subsidiaries are not required

Table of Contents

to set aside any of their net profit as statutory common reserves if such reserves are at least 50% of their respective registered capital. Furthermore, if they record no net income for a year, they generally may not distribute dividends for that year.

Significant Changes

Please see the section entitled Litigation above.

Table of Contents

Item 9. The Offer and Listing

Our ordinary shares are principally traded on the Stock Exchange of Hong Kong under the symbol 981.HK. Our ordinary shares began trading on the Stock Exchange of Hong Kong on March 18, 2004. Our American Depositary Shares, which began trading on the New York Stock Exchange on March 17, 2004, are traded under the symbol SMI.

The table below sets forth the high and low closing prices on the Stock Exchange of Hong Kong and the New York Stock Exchange for the ordinary shares represented by the ADSs, since the completion of the global offering and for the first six months of 2008.

	Stock Exchange of Hong Kong Closing price per ordinary share		New York Stock Exchange[1] Closing price per ADS	
	High Price	Low Price	High Price	Low Price
2004				
March 17 March 31	HK$2.47*	HK$2.12	US$15.50	US$13.59
Second Quarter	HK$2.45	HK$1.60	US$15.60*	US$10.47
Third Quarter	HK$1.68	HK$1.48*	US$10.84	US$9.42*
Fourth Quarter	HK$1.94	HK$1.59	US$12.40	US$10.14
2005				
First Quarter	HK$1.75*	HK$1.48	US$11.14	US$9.35
Second Quarter	HK$1.71	HK$1.48	US$10.93	US$9.52
Third Quarter	HK$1.75*	HK$1.21	US$11.33*	US$7.83
Fourth Quarter	HK$1.33	HK$1.00*	US$8.46	US$6.68*
2006				
First Quarter	HK$1.29*	HK$1.02	US$8.38*	US$6.73
Second Quarter	HK$1.21	HK$1.00	US$7.82	US$6.36
Third Quarter	HK$1.07	HK$0.97	US$6.88	US$6.30
Fourth Quarter	HK$1.03	HK$0.87*	US$6.46	US$5.48*
2007				
First Quarter	HK$1.24*	HK$0.87	US$8.30*	US$5.87
Second Quarter	HK$1.24	HK$1.04	US$7.68	US$6.69
Third Quarter	HK$1.18	HK$0.81	US$7.50	US$5.30
Fourth Quarter	HK$1.11	HK$0.71*	US$6.72	US$4.57*
2008				
January	HK$0.82	HK$0.61	US$5.15	US$3.95
February	HK$0.68	HK$0.61	US$4.30	US$3.97
March	HK$0.63	HK$0.41	US$4.13	US$2.75
April	HK$0.73	HK$0.48	US$4.24	US$3.07
May	HK$0.69	HK$0.48	US$4.36	US$3.31
June (through June 15)	HK$0.55	HK$0.48	US$3.53	US$3.09

(1) Each ADS represents 50 ordinary shares.

* Indicates high and low prices for the fiscal year.

** Indicates high and low prices for the fiscal quarter.

Table of Contents

Item 10. Additional Information

Memorandum and Articles of Association

The section entitled Description of Share Capital in our IPO registration statement is incorporated by reference into this annual report.

The sections entitled Item 10-Additional Information-Memorandum and Articles of Association in our annual report on Form 20-F for the fiscal year ended December 31, 2004, filed with the SEC on June 26, 2005 and in our annual report on Form 20-F for the fiscal year ended December 31, 2005, filed with the SEC on June 26, 2006 are incorporated by reference into this annual report. In addition, at the annual general meeting of our shareholders held on June 2, 2008, our shareholders agreed to amend our Articles of Association to provide that a member of our board of directors may be removed by Ordinary Resolution.

Material Contracts

We provide management services to Cension Semiconductor Manufacturing Corporation (Cension) and Wuhan Xinxin Semiconductor Manufacturing Corporation, which are government-owned foundries. Management service revenues under these arrangements for 2007, 2006 and 2005 were $42,000,000, $4,151,238 and $200,000, respectively.

In 2007, we sold plant, equipment and other fixed assets with a carrying value of $19,530,909 for $42,300,258 to Cension, which resulted in a gain on sale of $22,769,349. In 2006, we sold plant, equipment and other fixed assets with a carrying value of $19,411,553 for $61,182,652 to Cension, which resulted in a gain on sale of $41,771,099.

On April 10, 2007, Cension entered into an Asset Purchase Agreement (the Agreement) with Elpida Memory, Inc. (Elpida), a Japan based memory chip manufacturer, for the purchase of Elpida s 200mm wafer processing equipment currently located in Hiroshima, Japan for the total price of approximately $320 million.

As part of the Agreement, we provided a corporate guarantee for a maximum guarantee liability of $163.2 million on behalf of Cension in favour of Elpida. Our guarantee liability will terminate upon full payment of the purchase price by Cension to Elpida. In return for providing the above corporate guarantee, we received a guarantee fee from Cension based on 1.5% of the guarantee amount, or $2.4 million. Some 200mm wafer processing equipment purchased under the Agreement, with the total amount of $160 million, was held as collateral under the guarantee. As of December 31, 2007, the carrying amount of the liability related to the guarantee was approximately $2.4 million, which was presented in other current liabilities.

Of the $320 million of processing equipment (Equipment), a portion remained in Hiroshima and continues to be operated by Elpida. We are entitled to the net profit (loss) associated with the ongoing operations of this equipment, net of a guaranteed fixed share of revenue for Elpida, during the transitional period when the equipment acquired by Cension is relocated from Hiroshima to Chengdu.

On August 30, 2007, Cension negotiated with Elpida and subsequently reduced the purchase price to US$309.5 million.

In April 2008, we entered into an agreement with Cension to purchase roughly half of the Equipment from Cension for approximately US$150 million. This set of equipment will be used for SMIC s future expansion.

SMIC Shanghai and SMIC Tianjin have entered into long-term loan facilities in 2006 (See Item 5 Liquidity and Capital Resources on page 55).

Please also see the section entitled Litigation above regarding the settlement agreement into which we entered with TSMC.

Table of Contents

Exchange Controls

We receive a portion of our sales in Renminbi, which is currently not a freely convertible currency. Approximately 5.8% of our sales for the year ended December 31, 2005, approximately 2.3% of our sales for the year ended December 31, 2006, and approximately 0.9% of our sales for the year ended December, 31, 2007 were denominated in Renminbi. While we have used these proceeds for the payment of our Renminbi expenses, we may in the future need to convert these sales into foreign currencies to allow us to purchase imported materials and equipment, particularly as we expect the proportion of our sales to China-based companies to increase in the future. Under China s existing foreign exchange regulations, payments of current account items, including profit distributions, interest payments and expenditures from trade may be made in foreign currencies without government approval, except for certain procedural requirements. The Chinese government may, however, at its discretion, restrict access in the future to foreign currencies for current account transactions and prohibit us from converting our Renminbi sales into foreign currencies.

Taxation

The following discussion of the material U.S. federal income and Cayman Islands tax consequences of an investment in our ADSs or ordinary shares is based upon laws and relevant interpretations thereof in effect as of the date of this prospectus, all of which are subject to change, possibly with retroactive effect. This discussion does not deal with all possible tax consequences relating to an investment in our ADSs or ordinary shares, such as the tax consequences under U.S. state, local and non-U.S. tax laws.

United States Federal Income Taxation

Except where noted, this summary deals only with the ownership and disposition of the ADSs and ordinary shares that are held as capital assets by U.S. Holders. This summary does not represent a detailed description of the U.S. federal income tax consequences applicable to U.S. Holders that are subject to special treatment under the U.S. federal income tax laws, including:

banks;

dealers in securities or currencies;

financial institutions;

real estate investment trusts;

insurance companies;

tax-exempt organizations;

persons holding ADSs or ordinary shares as part of a hedging, integrated or conversion transaction, constructive sale or straddle;

traders in securities that have elected the mark-to-market method of accounting;

persons liable for the alternative minimum tax;

persons who have ceased to be U.S. citizens or to be taxed as resident aliens;

persons who own or are deemed to own more than 10% of our voting shares; or

U.S. persons whose functional currency is not the U.S. dollar.

This summary is based in part on representations by the depositary and assumes that each obligation under the deposit agreement and any related agreement will be performed in accordance with its terms. Furthermore, the

discussion below is based upon the provisions of the Internal Revenue Code of 1986, as amended, or the Code, and U.S. Treasury regulations, rulings and judicial decisions thereunder as of the

Table of Contents

date hereof, and such authorities may be replaced, revoked or modified, possibly on a retroactive basis, so as to result in U.S. federal income tax consequences different from those discussed below.

A U.S. Holder that holds ADSs or ordinary shares is urged to consult its own tax advisor concerning the U.S. federal income tax consequences as well as any consequences arising under the laws of any other taxing jurisdiction (including any U.S. state or locality) or any aspect of U.S. federal gift or estate law in light of the particular circumstances of the U.S. Holder.

A U.S. Holder is a beneficial owner of ADSs or ordinary shares that is a U.S. person. A U.S. person is:

- a citizen or resident of the United States;
- a corporation or other entity taxable as a corporation created or organized in or under the laws of the United States, any state thereof, or the District of Columbia;
- an estate the income of which is subject to U.S. federal income taxation, regardless of its source; or
- a trust if it is subject to the primary supervision of a court within the United States and one or more U.S. persons have the authority to control all substantial decisions of the trust or has a valid election in effect under applicable U.S. Treasury regulations to be treated as a U.S. person.

If a partnership holds ADSs or ordinary shares, the tax treatment of a partner will generally depend on the status of the partner and the activities of the partnership. A U.S. Holder that is a partner of a partnership holding ADSs or ordinary shares is urged to consult its own tax advisors.

ADSs or Ordinary Shares. In general, for U.S. federal income tax purposes, a U.S. Holder of ADSs will be treated as the owner of the underlying ordinary shares that are represented by such ADSs. Deposits and withdrawals of ordinary shares in exchange for ADSs will not be subject to U.S. federal income taxation.

Distributions on ADSs or Ordinary Shares. Subject to the discussion under Passive Foreign Investment Company Rules below, the gross amount of the cash distributions on the ADSs or ordinary shares will be taxable to a U.S. Holder as dividends to the extent of our current and accumulated earnings and profits, as determined under U.S. federal income tax principles. Subject to certain limitations, dividends paid to noncorporate U.S. Holders, including individuals, may be eligible for a reduced rate of taxation if we are deemed to be a qualified foreign corporation for U.S. federal income tax purposes. A qualified foreign corporation includes:

- a foreign corporation that is eligible for the benefits of a comprehensive income tax treaty with the United States that includes an exchange of information program; and
- a foreign corporation if its stock with respect to which a dividend is paid or its ADSs backed by such stock are readily tradable on an established securities market within the United States,

but does not include an otherwise qualified corporation that is a passive foreign investment company. We believe that we will be a qualified foreign corporation for so long as we are not a passive foreign investment company and the ordinary shares or ADSs are considered to be readily tradable on an established securities market within the United States. A U.S. Holder that exchanges its ADSs for ordinary shares may not be eligible for the reduced rate of taxation on dividends if the ordinary shares are not readily tradable on an established securities market within the United States. Our status as a qualified foreign corporation, however, may change.

Dividends will be includable in a U.S. Holder s gross income on the date actually or constructively received by such U.S. Holder, in the case of ordinary shares, or by the depositary, in the case of ADSs. These dividends will not be eligible for the dividends-received deduction generally allowed to U.S. corporations in respect of dividends received from other U.S. corporations.

Table of Contents

To the extent that the amount of any cash distribution exceeds our current and accumulated earnings and profits, the distribution will first be treated as a tax-free return of capital, causing a reduction in the adjusted basis of the ADSs or ordinary shares (thereby increasing the amount of gain, or decreasing the amount of loss, a U.S. Holder would recognize on a subsequent disposition of the ADSs or ordinary shares), and the balance in excess of adjusted basis will be subject to tax as capital gain.

To the extent we pay dividends on the ADSs or the ordinary shares in Hong Kong dollars, the U.S. dollar value of such dividends should be calculated by reference to the exchange rate prevailing on the date of actual or constructive receipt of the dividend, regardless of whether the Hong Kong dollars are converted into U.S. dollars at that time. If Hong Kong dollars are converted into U.S. dollars on the date of actual or constructive receipt of such dividends, the tax basis of the U.S. holder in such Hong Kong dollars will be equal to their U.S. dollar value on that date and, as a result, the U.S. Holder generally should not be required to recognize any foreign currency exchange gain or loss. Any gain or loss recognized on a subsequent conversion or other disposition of the Hong Kong dollars generally will be treated as U.S. source ordinary income or loss.

It is possible that distributions of ADSs or ordinary shares that are received as part of a pro rata distribution to all of our ordinary shareholders may not be subject to U.S. federal income tax. The basis of the new ADSs or ordinary shares so received will be determined by allocating a U.S. Holder s basis in the old ADSs or ordinary shares between the old ADSs or ordinary shares and the new ADSs or ordinary shares received, based on their relative fair market values on the date of distribution.

Dividends paid on the ADSs or ordinary shares will be income from sources outside of the United States and for tax years beginning before January 1, 2007, generally will constitute passive income or, in the case of certain U.S. Holders, financial services income and for tax years beginning after December 31, 2006, generally will constitute passive category income or, in the case of certain U.S. Holders, general category income for U.S. foreign tax credit limitation purposes.

Sale, Exchange or Other Disposition of ADSs or Ordinary Shares. Subject to the discussion under Passive Foreign Investment Company Rules below, upon the sale, exchange or other disposition of ADSs or ordinary shares, a U.S. Holder generally will recognize capital gain or loss equal to the difference between the amount realized upon the sale, exchange or other disposition and the adjusted tax basis of the U.S. Holder in the ADSs or ordinary shares. A U.S. Holder s tax basis in an ADS or an ordinary share will be, in general, the price it paid for that ADS or ordinary share. The capital gain or loss generally will be long-term capital gain or loss if, at the time of sale, exchange or other disposition, the U.S. Holder has held the ADS or ordinary share for more than one year. Net long-term capital gains of noncorporate U.S. Holders, including individuals, are eligible for reduced rates of taxation. The deductibility of capital loss is subject to limitations. Any gain or loss that a U.S. Holder recognizes generally will be treated as gain or loss from sources within the United States for U.S. foreign tax credit limitation purposes.

Passive Foreign Investment Company Rules. We believe that we were not a passive foreign investment company for 2007. Based on the projected composition of our income, the timing of our anticipated capital expenditures and valuation of our assets, we do not expect to be a passive foreign investment company for 2008 and do not expect to become one in the future, although this may change.

In general, we will be deemed to be a passive foreign investment company for any taxable year in which either (i) at least 75% of our gross income is passive income or (ii) at least 50% of the value (determined on the basis of a quarterly average) of our assets is attributable to assets that produce or are held for the production of passive income. For this purpose, passive income generally includes dividends, interest, royalties, rents (other than rents and royalties derived in the active conduct of a trade or business and not derived from a related person), annuities and gains from assets that produce passive income.

If we are a PFIC in any taxable year, unless a mark-to-market election described below is made, U.S. Holders will generally be subject to additional taxes and interest charges on certain excess distribution we make and on any gain realized on the disposition or deemed disposition of ADSs or ordinary shares regardless of whether we continue to be a PFIC in the year of the excess distribution or disposition. Distributions in respect of a U.S. Holder s ADSs or ordinary shares during the taxable year will

Table of Contents

generally constitute excess distributions if, in the aggregate, they exceed 125% of the average amount of distributions in respect of the U.S. Holder s ADSs or ordinary shares over the three preceding taxable years or, if shorter, the portion of the U.S. Holder s holding period before such taxable year.

To compute the tax on excess distributions or any gain, (i) the excess distribution or the gain will be allocated ratably to each day in the holding period; (ii) the amount allocated to the current year and any tax year before we became a PFIC will be taxed as ordinary income in the current year; (iii) the amount allocated to other taxable years will be taxable at the highest applicable marginal rate in effect for that year; and (iv) an interest charge at the rate for underpayment of taxes will be imposed with respect to any portion of the excess distribution or gain described under (iii) above that is allocated to such other taxable years. In addition, if we are PFIC, no distribution will qualify for taxation at the preferential rate for non-corporate holders discussed in Distributions on ADSs or Ordinary Shares above.

If we are a PFIC in any year in which our ADSs or ordinary shares are marketable , a U.S. Holder will be able to avoid the excess distribution rules described above if such U.S. Holder makes a timely mark-to-market election with respect to its ADSs or ordinary shares. The ADSs or ordinary shares will be marketable as long as they remain regularly traded on a national securities exchange, such as the New York Stock Exchange or the Hong Kong Stock Exchange. If this election is made in a timely fashion, the U.S. Holder will generally recognize as ordinary income or ordinary loss the difference between the fair market value of the ADSs or ordinary shares on the last day of any taxable year and the U.S. Holder s adjusted tax basis in the ADSs or ordinary shares. Any ordinary income resulting from this election will generally be taxed at ordinary income rates. Any ordinary losses will be deductible only to the extent of the net amount of previously included income as a result of the mark-to-market election, if any. The U.S. Holder s adjusted tax basis in the ADSs or ordinary shares will be adjusted to reflect any such income or loss.

Alternatively, the excess distribution rules described above may generally be avoided by electing to treat us as a Qualified Electing Fund, or QEF, under Section 1295 of the Internal Revenue Code of 1986, as amended. A QEF election is available only if the U.S. Holder receives an annual information statement from the PFIC setting forth its ordinary earnings and net capital gains, as calculated for U.S. federal income tax purposes. We will not provide our U.S. Holders with the information statement necessary to make a QEF election. Accordingly, U.S. Holders will not be able to make or maintain such an election.

A U.S. Holder is urged to consult its own tax advisors concerning the availability of making a mark-to-market election or a qualified electing fund election and the U.S. federal income tax consequences of holding the ADSs or ordinary shares if we are deemed to be a passive foreign investment company in any taxable year.

Information Reporting and Backup Withholding. In general, unless a U.S. Holder belongs to a category of certain exempt recipients (such as corporations), information reporting requirements will apply to distributions on ADSs or ordinary shares made within the United States and to the proceeds of sales of ADSs or ordinary shares that are effected through the U.S. office of a broker or the non-U.S. office of a broker that has certain connections with the United States. Backup withholding currently imposed at a rate of 28% may apply to these payments if a U.S. Holder fails to provide a correct taxpayer identification number or certification of exempt status, fails to report in full dividend and interest income or, in certain circumstances, fails to comply with applicable certification requirements.

Any amounts withheld under the backup withholding rules may generally be allowed as a refund or a credit against a U.S. Holder s U.S. federal income tax, provided the U.S. Holder furnishes the required information to the Internal Revenue Service in a timely manner.

Cayman Islands Taxation

The following summary constitutes the opinion of Maples and Calder as to the material Cayman Islands tax consequences of acquiring, owning, and transferring our ADSs and ordinary shares.

Table of Contents

The Cayman Islands currently levy no taxes on individuals or corporations based upon profits, income, gains or appreciation and there is no taxation in the nature of inheritance tax or estate duty. You will not be subject to Cayman Islands taxation on payments of dividends or upon the repurchase by us of your ADSs or ordinary shares. In addition, you will not be subject to withholding tax on payments of dividends or distributions, including upon a return of capital, nor will gains derived from the disposal of ADSs or ordinary shares be subject to Cayman Islands income or corporation tax.

No Cayman Islands stamp duty will be payable by you in respect of the issue or transfer of ADSs or ordinary shares. However, an instrument transferring title to an ADS, if brought to or executed in the Cayman Islands, would be subject to Cayman Islands stamp duty. The Cayman Islands are not party to any double taxation treaties. There are no exchange control regulations or currency restrictions in the Cayman Islands.

We were incorporated under the laws of the Cayman Islands as an exempted company and, as such, obtained an undertaking in April 2000 from the Governor in Council of the Cayman Islands substantially that, for a period of twenty years from the date of such undertaking, no law which is enacted in the Cayman Islands imposing any tax to be levied on profit or income or gains or appreciation shall apply to us and no such tax and no tax in the nature of estate duty or inheritance tax will be payable, either directly or by way of withholding, on our ADSs or ordinary shares.

Documents on Display

We are subject to the information requirements of the Securities Exchange Act of 1934, as amended. In accordance with these requirements, we file reports and other information with the Securities and Exchange Commission. These materials, including this annual report and the exhibits thereto, may be inspected and copied at the Commission s Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. The public may obtain information on the operation of the Commission s Public Reference Room by calling the Commission in the United States at 1-800-SEC-0330. The Commission also maintains a website at http://www.sec.gov that contains reports, proxy statements and other information regarding registrants that file electronically with the Commission. In addition, material filed by us can be inspected at the offices of the New York Stock Exchange at 20 Broad Street, New York, New York 10005.

Table of Contents

Item 11. Quantitative and Qualitative Disclosures About Market Risk

Market risk is the risk of loss related to adverse changes in market prices, including foreign currency exchange rates and interest rates of financial instruments. We are exposed to these risks in the ordinary course of our business. Our exposure to financial risks derives primarily from changes in interest rates and foreign currency exchange rates. To mitigate some of these risks, we utilize spot, forward, and derivative financial instruments. We do not engage in any speculative activities.

Foreign Exchange Rate Fluctuation Risk

Our revenue, expense, and capital purchasing activities are primarily transacted in U.S. dollars. However, since we have operations consisting of manufacturing, sales activities and capital purchasing outside of the U.S., we enter into transactions in other currencies. We are primarily exposed to changes in exchange rate for the Euro, Japanese Yen, and Rmb.

To minimize these risks, we purchase foreign-currency forward exchange contracts with contract terms normally lasting less than six months to protect against the adverse effect that exchange rate fluctuations may have on foreign-currency denominated activities. These forward exchange contracts are principally denominated in Rmb, Japanese Yen or Euros, and do not qualify for hedge accounting in accordance with SFAS No. 133. As of December 31, 2007, we had outstanding foreign currency forward exchange contracts with notional amounts of US$0.4 million. As of December 31, 2007, the fair value of foreign currency forward exchange contracts was approximately a gain of US$0.5 million, which is recorded in other income and other current assets. We had US$0.4 million of foreign currency exchange contracts outstanding as of December 31, 2007.

We do not enter into foreign currency exchange contracts for speculative purposes. See Risk Factors Risks Related to Our Financial Condition and Business Exchange rate fluctuations could increase our costs, which could adversely affect our operating results and the value of our ADSs and Risks Related to Conducting Operations in China Devaluation or appreciation in the value of the Renminbi or restrictions on convertibility of the Renminbi could adversely affect our business and operating results.

	As of December 31, 2007 Expected maturity date (in US$ thousands)	
	2007	**Fair Value**
Forward Exchange Agreement		
(Receive JPY/Pay US$)		
Contract Amount	404.1	530.4
Total Contract Amount	404.1	530.4

Table of Contents

Cross Currency Swap Fluctuation Risk

On December 15, 2005, the Company entered into a long-term loan facility agreement in the aggregate principal amount of EUR 85 million. The company is primarily exposed to changes in the exchange rate for the Euro. To minimize the risk, the company entered into cross currency swap contracts with a contract term fully matching the repayment schedule of the long-term loan to protect against the adverse effect of exchange rate fluctuations arising from foreign-currency denominated loans. The cross currency swap contract does not qualify for hedge accounting in accordance with SFAS No. 133. As of December 31, 2007, the Company had outstanding cross currency swap contracts with notional amounts of US$51.1 million. Notional amounts are stated in the U.S. dollar equivalents at spot exchange rates as of the respective dates. As of December 31, 2007, the fair value of cross currency swap contracts was approximately a gain of US$1.0 million, which is recorded in other income and other current assets. We had US$51.1 million of cross currency swap contracts outstanding as of December 31, 2007, all of which will mature in 2012.

Interest Rate Risk

Our exposure to interest rate risks relates primarily to our long-term debt obligations, which we generally assume to fund capital expenditures and working capital requirements. The table below presents annual principal amounts due and related weighted average implied forward interest rates by year of maturity for our debt obligations outstanding as of December 31, 2007. Our long-term debt obligations are all subject to variable interest rates. The interest rates on our U.S. dollar-denominated loans are linked to the LIBOR rate, while our EUR-denominated loans have interest rates linked to the EURIBOR rates. As a result, the interest rates on our loans are subject to fluctuations in the underlying interest rates to which they are linked.

	As of December 31,				
	2008	**2009**	**2010**	**2011**	**2012**
			(Forecast)		
			(in US$ thousands, except percentages)		
US$ denominated					
Average balance	578,070	239,860	39,050	4,000	
Average interest rate	5.82%	5.30%	5.08%	5.05%	
Weighted average forward interest rate	5.82%	5.30%	5.08%	5.05%	
EUR denominated	38,225	25,392	12,559	4,186	
Average balance					
Average interest rate	5.08%	4.09%	4.74%	4.73%	
Weighted average forward interest rate	5.78%	5.27%	5.03%	4.95%	

Table of Contents

Item 12. Description of Securities Other Than Equity Securities

Not applicable.

PART II

Item 13. Defaults, Dividend Arrearages, and Delinquencies

None.

Item 14. Material Modifications to the Rights of Security Holders and Use of Proceeds

On March 17 and 18, 2004, we received an aggregate of US$1,017 million from our initial public offering of our ADSs on the New York Stock Exchange and our ordinary shares on the Hong Kong Stock Exchange, respectively. The following use of proceeds information relates to our registration statement on Form F-1 (File No. 333- 112720), filed by us in connection with our initial public offering. As of December 31, 2007, all of the proceeds from the global offering had been used to construct, equip, or increase capacity at our fabs.

Item 15. Controls and Procedures

Disclosure Controls and Procedures

Our Chief Executive Officer and our Acting Chief Financial and Accounting Officer have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934). They have concluded that as of December 31, 2007, our disclosure controls and procedures were adequate and effective to ensure that material information relating to us and our consolidated subsidiaries was made known to them by others within our company and our consolidated subsidiaries.

Management s Annual Report on Internal Control over Financial Report

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended, for our company. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements in accordance with generally accepted accounting principles and includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of a company s assets, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with generally accepted accounting principles, and that a company s receipts and expenditures are being made only in accordance with authorizations of a company s management and directors, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of a company s assets that could have a material effect on the consolidated financial statements.

Because of its inherent limitations, a system of internal control over financial reporting can provide only reasonable assurance with respect to consolidated financial statement preparation and presentation and may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

As required by Section 404 of the Sarbanes-Oxley Act of 2002 and related rules as promulgated by the Securities and Exchange Commission, management assessed the effectiveness of the internal control over financial reporting as of December 31, 2007 using criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Table of Contents

Based on this assessment, management concluded that the our internal control over financial reporting was effective as of December 31, 2007 based on the criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Attestation Report of the Registered Public Accounting Firm

The effectiveness of internal control over financial reporting as of December 31, 2007 has been audited by our independent registered public accounting firm, Deloitte Touche Tohmatsu as stated in their report (See F-2).

Changes In Internal Control Over Financial Reporting

In 2007 there were no changes in our internal control over financial reporting that materially affected, or are reasonably likely to materially affect our internal control over financial reporting.

Item 16A. Audit Committee Financial Expert

Our board has determined that Mr. Henry Shaw and Mr. Lip-Bu Tan are audit committee financial experts as defined under the applicable rules of the SEC issued pursuant to Section 407 of the Sarbanes-Oxley Act of 2002. Each of Mr. Shaw and Mr. Tan are independent as such term is defined under Section 303A.02 of the New York Stock Exchange Listed Company Manual.

Item 16B. Code of Ethics

We have adopted a Code of Business Conduct and Ethics which is applicable to all of our employees, including our Chief Executive Officer, Acting Chief Financial and Accounting Officer, and any other persons performing similar functions.

Our Code of Business Conduct and Ethics is available, free of charge, to any person who sends a request for a paper copy to us at Semiconductor Manufacturing International Corporation, 18 Zhangjiang Road, Pudong New Area, Shanghai, China 201203, Attention: Investor Relations.

Item 16C. Principal Accountant Fees and Services

The following table sets forth the aggregate audit fees, audit-related fees, tax fees and all other fees we paid or incurred for audit services, audit-related services, tax services and other services rendered by our principal accountants during the fiscal years ended December 31, 2006 and December 31, 2007.

	2006	**2007**
Audit Fees	US$ 1,460,000	US$ 1,533,000
Audit-Related Fees	US$	US$ 152,358
Tax Fees	US$ 33,789	US$ 12,935
Total	US$ 1,493,789	US$ 1,698,293

Audit fees consist of the standard work associated with U.S. GAAP and statutory audits of our annual financial statements including the review of our quarterly financial results and filings with the Securities and Exchange Commission, Hong Kong Stock Exchange and other regulators.

Audit-related fees include services relating to our compliance with the requirements of the Sarbanes-Oxley Act and services relating to our resolution of SEC related comments.

Tax services include tax compliance, tax advice, tax planning and transfer pricing with respect to the various regulations to which we are subject.

Table of Contents

The audit committee has approved all audit-related services performed by Deloitte Touche Tohmatsu, 35/F, One Pacific Place, 88, Queensway, Hong Kong. The audit committee has also approved and will continue to consider, on a case-by-case basis, all non-audit services. Accordingly, the charter of the audit committee does not contain any pre-approval policies and procedures. According to the charter of our audit committee, before our principal accountants are engaged by us to render audit or non-audit services, the engagement, including the nature and scope of the work to be performed and the associated fees, must be approved by our audit committee.

Item 16D. Exemptions from the Listing Standards of Audit Committees

Not applicable.

Item 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchasers

The following table sets for the number of ordinary shares we repurchased from our employees, directors and service providers in 2007 pursuant to the terms of our 2001 Stock Plan, 2001 Preference Shares Stock Plan, 2001 Regulation S Stock Plan and 2001 Regulation S Preference Shares Stock Plan. Pursuant to the terms of these plans, recipients of stock options to purchase our ordinary shares are entitled to early exercise their options, subject to the Company s right of repurchase. When employees, directors, or service providers who have early exercised their options terminate their employment with the Company, the Company may repurchase the unvested shares subject to the option, at a price which is the lower of the exercise price of the option and the fair market value of our ordinary shares as of the date of repurchase. Other than repurchases pursuant to our employee stock option plans, the Company has not repurchased any of its outstanding capital stock.

Period	Total Number of Shares Repurchased	Average Price Paid per Share
December	292,500	US $0.13
TOTAL	292,500	

PART III

Item 17. Financial Statements

We have elected to provide the financial statements and related information specified in Item 18 in lieu of Item 17.

Item 18. Financial Statements

See pages F-1 to F-75.

Item 19. Exhibits

Exhibit 1.1	Eleventh Amended and Restated Articles of Association, as adopted at the Registrant s annual general meeting of shareholders on June 2, 2008
Exhibit 4.1	Asset Purchase Agreement dated September 23, 2003 among Semiconductor Manufacturing International Corporation, Motorola, Inc. and Motorola (China) Electronics Limited**
Exhibit 4.2	Sixth Amended and Restated Registration Rights Agreement dated February 23, 2003 among Semiconductor Manufacturing International Corporation and the shareholders listed therein***

Table of Contents

Exhibit 4.3	Settlement Agreement dated January 31, 2005 by and between Semiconductor Manufacturing International Corporation and Taiwan Semiconductor Manufacturing Corporation, Ltd., including Patent License Agreement *
Exhibit 4.4	English language summary of Chinese language Syndicate Loan Agreement dated May 26, 2005, between Semiconductor Manufacturing International (Beijing) Corporation, Semiconductor Manufacturing International Corporation, as guarantor, and China Development Bank, China Construction Bank, Bank of China, Agricultural Bank of China, China Merchants Bank, HuaXia Bank, China Mingsheng Bank, Bank of Communications, Bank of Beijing, Industrial and Commercial Bank of China (Asia) and CITIC Ka Wah Bank*
Exhibit 4.5	Form of Indemnification Agreement, as adopted at the Registrant s annual general meeting of shareholders on May 6, 2005*
Exhibit 4.6	English language summary of Chinese language Syndicate Loan Agreement dated May 31, 2006, between Semiconductor Manufacturing International (Tianjin) Corporation, Semiconductor Manufacturing International Corporation, as guarantor, and China Construction Bank, China Minsheng Bank, China Development Bank, Industrial and Commercial Bank of China, Agricultural Bank of China, Bank of China, China Merchants Bank, China Bo Hai Bank, Bank of Communications and Bangkok Bank. ****
Exhibit 4.7	English language summary of Chinese language Syndicate Loan Agreement dated June 8, 2006, between Semiconductor Manufacturing International (Shanghai) Corporation, Semiconductor Manufacturing International Corporation, as guarantor, and ABN AMRO Bank N.V., Bank of China (Hong Kong) Limited, Bank of Communications, The Bank of Tokyo-Mitsubishi UFJ, Ltd., China Construction Bank, DBS Bank Ltd., Fubon Bank (Hong Kong) Limited, Industrial and Commercial Ban k of China and Shanghai Pudong Development Bank.****
Exhibit 8.1	List of Subsidiaries
Exhibit 12.1	Certification of CEO under Section 302 of the U.S. Sarbanes-Oxley Act of 2002
Exhibit 12.2	Certification of Acting CFO under Section 302 of the U.S. Sarbanes-Oxley Act of 2002
Exhibit 13.1	Certification of CEO and Acting CFO under Section 906 of the U.S. Sarbanes-Oxley Act of 2002
Exhibit 99.1	Consent of Deloitte Touche Tohmatsu

* Previously filed as an exhibit to the Registrant s Annual Report on Form 20F for the fiscal year ended December 31, 2004, filed

June 28, 2005.

** Previously filed as an exhibit to the Registrant s Form F-1dated February 11, 2004.

*** Previously filed as an exhibit to the Registrant s Form F-1/A dated February 25, 2004.

**** Previously filed as an exhibit to the Registrant s Annual Report on Form 20F for the fiscal year ended December 31, 2005, filed June 28, 2006.

Table of Contents

SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION

Date: June 27, 2008

By: /s/ Richard Ru Gin Chang
Name: Richard Ru Gin Chang
Title: President and Chief Executive Officer

Table of Contents

Annex A
GLOSSARY OF TECHNICAL TERMS

ASIC	Application Specific Integrated Circuit. A proprietary integrated circuit designed and manufactured to meet a customer s specific functional requirements.
Cell	A primary unit that normally repeats many times in an integrated circuit. Cells represent individual functional design units or circuits that may be reused as blocks in designs. For example, a memory cell represents a storage unit in a memory array.
CIS	CMOS Image Sensor. CIS can be used in applications such as still and video cameras and embedded cameras in mobile telephones. It is a fast growing imaging sensor technology. The fabrication of CIS is fully compatible with the mainstream CMOS process, which enables system-on-chip capability, low power consumption and low cost of fabrication.
Clean room	Area within a fab in which the wafer fabrication takes place. The classification of a clean room relates to the maximum number of particles of contaminants per cubic foot within that room. For example, a class 100 clean room contains less than 100 particles of contaminants per cubic foot.
CMOS	Complementary Metal Oxide Silicon. A fabrication process that incorporates n-channel and p-channel CMOS transistors within the same silicon substrate. Currently, this is the most commonly used integrated circuit fabrication process technology and is one of the latest fabrication techniques to use metal oxide semiconductor transistors.
CVD	Chemical Vapor Deposition. A process in which gaseous chemicals react on a heated wafer surface to form solid film.
Die	One individual chip cut from a wafer before being packaged.
Dielectric material	A type of non-conducting material used for isolation purposes between conductors, such as metals.
DRAM	Dynamic Random Access Memory. A device that temporarily stores digital information but requires regular refreshing to ensure data is not lost.
DSP	Digital Signal Processor. A type of integrated circuit that processes and manipulates digital information after it has been converted from an analog source.
EEPROM	Electrically Erasable Programmable Read-Only Memory. An integrated circuit that can be electrically erased and electrically programmed with user-defined information.
EPROM	Erasable Programmable Read-Only Memory. A form of PROM that is programmable electrically yet erasable using ultraviolet light.
FCRAM	Fast Cycle Random Access Memory. A proprietary form of RAM developed by Fujitsu Limited.
Fill factor	The percentage of LCOS metal surface area used for light reflection as compared to the total surface area. The higher the fill factor, the more light will be reflected from a given surface area.

Flash memory	A type of non-volatile memory where data is erased in blocks. The name flash is derived from the rapid block erase operation. Flash memory requires only one transistor per memory cell versus two transistors per memory cell for EEPROMs, making flash memory less expensive to produce. Flash memory is the most popular form of non-volatile semiconductor memory currently available.
Gold Bumping	The fabrication process of forming gold bump termination electrodes on a finished wafer.

Table of Contents

High voltage semiconductor	High voltage semiconductors are semiconductor devices that can drive relatively high voltage potential to systems that require higher voltage of between five volts to several hundred volts.
IDM	Integrated Device Manufacturer.
Integrated circuit	An electronic circuit where all the elements of the circuit are integrated together on a single semiconductor substrate.

Table of Contents

Interconnect	Conductive materials such as aluminum, doped polysilicon or copper that form the wiring circuitry to carry electrical signals to different parts of the chip.
I/O	Inputs/Outputs.
LCOS	Liquid Crystal On Silicon. A type of micro-display technology.
Logic device	A device that contains digital integrated circuits that perform a function rather than store information.
Low leakage	Characteristic of a transistor that has a low amount of current leakage. Low leakage allows for power-saving. Low leakage semiconductors are primarily used in applications such as cellular telephones, calculators and automotive applications.
Mask	A glass plate with a pattern of transparent and opaque areas used to create patterns on wafers. Mask is commonly used to refer to a plate that has a pattern large enough to pattern a whole wafer at one time, as compared to a reticle, where a glass plate can contain the pattern for one or more dies but is not large enough to transfer a wafer-sized pattern all at once.
Mask ROM	A type of non-volatile memory that is programmed during fabrication (mask-defined) and the data can be read but not erased.
Memory	A device that can store information for later retrieval.
Micro-display	A small display that is of such high resolution that it is only practically viewed or projected with lenses or mirrors. A micro-display is typically magnified by optics to enlarge the image viewed by the user. For example, a miniature display smaller than one inch in size may be magnified to provide a 12-inch to 60-inch viewing area.
Micron	A term for micrometer, which is a unit of linear measure that equals one one-millionth (1/1,000,000) of a meter. There are 25.4 microns in one one-thousandth of an inch.
Mixed-signal	The combination of analog and digital circuitry in a single semiconductor.
MOS	Metal Oxide Semiconductor. A type of semiconductor device fabricated with a conducting layer and a semiconducting layer separated by an insulating layer.
NAND Flash	A type of flash memory commonly used for mass storage applications such as MP3 players and digital cameras.
Nanometer	A term for micrometer, which is a unit of linear measure that equals one thousandth (1/1,000) of a micron.
Non-volatile memory	Memory products that maintain their content when the power supply is switched off.
OTP	One-time programmable memory used for program and data storage, usually used in applications that require only a one-time data change.

PROM	Programmable Read-Only Memory. Memory that can be reprogrammed once after manufacturing.
RAM	Random Access Memory. Memory devices where any memory cell in a large memory array may be accessed in any order at random.
Redistribution Layer Manufacturing	The manufacturing process of fabricating additional dielectric and copper interconnect layers to redistribute the pads to new locations on a finished wafer.
Reticle	See Mask above.
RF	Radio Frequency. Radio frequency semiconductors are primarily used in communications devices such as cell phones.

Table of Contents

ROM	Read-Only Memory. See Mask ROM above.
Scanner	An aligner that scans light through a slit across a mask to produce an image on a wafer.
Semiconductor	An element with an electrical resistivity within the range of an insulator and a conductor. A semiconductor can conduct or block the flow of electric current depending on the direction and magnitude of applied electrical biases.
Solder bumping	The fabrication processes of forming solder bump termination electrodes, which are elevated metal structures, or lead free bump termination electrodes.
SRAM	Static Random Access Memory. A type of volatile memory product that is used in electronic systems to store data and program instructions. Unlike the more common DRAM, it does not need to be refreshed.
Stepper	A machine used in the photolithography process in making wafers. With a stepper, a small portion of the wafer is aligned with the mask upon which the circuitry design is laid out and is then exposed to strong light. The machine then steps to the next area, repeating the process until the entire wafer has been done. Exposing only a small area of a wafer at a time allows the light to be focused more strongly, which gives better resolution of the circuitry design.
System-on-chip	A chip that incorporates functions usually performed by several different devices and therefore generally offers better performance and lower cost.
Systems companies	Companies that design and manufacture complete end market products or systems for sale to the market.
Transistor	An individual circuit that can amplify or switch electric current. This is the building block of all integrated circuits.
Volatile memory	Memory products that lose their content when the power supply is switched off.
Wafer	A thin, round, flat piece of silicon that is the base of most integrated circuits.

SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPORATION
Report of Independent Registered Public Accounting Firm and Consolidated Financial Statements for the years ended December 31, 2007, 2006, and 2005

INDEX TO FINANCIAL STATEMENTS

Table of Contents

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of Semiconductor Manufacturing International Corporation:

We have audited the accompanying consolidated balance sheets of Semiconductor Manufacturing International Corporation and its subsidiaries (the Company) as of December 31, 2007, 2006, and 2005 and the related consolidated statements of operations, stockholders equity and comprehensive income (loss), and cash flows for each of the three years in the period ended December 31, 2007. Our audits also included the financial statement schedule included in Schedule I. We also have audited the Company s internal control over financial reporting as of December 31, 2007, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company s management is responsible for these financial statements and financial statement schedule, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, including in the accompanying Management s Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule and an opinion on the Company s internal control over financial reporting based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audit of financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control-based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed by, or under the supervision of the company s principal executive and principal financial officers, or persons performing similar functions, and effected by the company s board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with the authorization of Management and Directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Semiconductor Manufacturing International Corporation and subsidiaries as of December 31, 2007, 2006 and 2005 and the results of its operations and their cash flows for each of the three years in the period ended December 31, 2007, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly, in all material respects, the information set forth therein. Also in our opinion, the Company maintained , in all material aspects, effective internal control over financial

reporting as of December 31, 2007, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

As discussed in Note 2(r) to the consolidated financial statements, effective January 1, 2007, the Company adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109 . Also, as discussed in Note 2(u) to the consolidated financial statements, effective January 1, 2006, the Company changed its method of accounting for share-based compensation to conform to Statement of Financial Accounting Standard No. 123(R), Share-Based Payment .

Deloitte Touche Tohmatsu

Certified Public Accountants

Hong Kong

April 25, 2008, except for Schedule I, as to which the date is June 18, 2008

Table of Contents

Semiconductor Manufacturing International Corporation
CONSOLIDATED BALANCE SHEET
(In US dollars except shares data)

	NOTES	December 31, 2007	2006	2005
ASSETS				
Current assets:				
Cash and cash equivalents		$ 469,284,013	$ 363,619,731	$ 585,796,887
Short-term investments	5	7,637,870	57,950,603	13,795,859
Accounts receivable, net of allowances of 4,492,090 ,, $4,048,845 and $1,091,340 at December 31, 2007, 2006 and 2005 respectively	4	298,387,652	252,184,975	241,333,914
Inventories	7	248,309,765	275,178,952	191,237,636
Prepaid expense and other current assets		31,237,755	20,766,945	9,810,591
Receivable for sale of manufacturing equipment		17,321,000	70,544,560	5,490,000
Assets held for sale	8	3,123,567	9,420,729	
Total current assets		1,075,301,622	1,049,666,495	1,047,464,887
Land use rights, net	9	57,551,991	38,323,333	34,767,518
Plant and equipment, net	10	3,202,957,665	3,244,400,822	3,285,631,131
Acquired intangible assets, net	11	232,195,132	71,692,498	80,667,737
Deferred cost, net	24	70,637,275	94,183,034	117,728,792
Equity investment	12	9,896,398	13,619,643	17,820,890
Other long-term prepayments		2,988,404	4,119,433	2,552,407
Deferred tax assets	17	56,915,172	25,286,900	
TOTAL ASSETS		$ 4,708,443,659	$ 4,541,292,158	$ 4,586,633,362
LIABILITIES AND STOCKHOLDERS EQUITY				
Current liabilities:				
Accounts payable	13	$ 301,992,739	$ 309,129,199	$ 262,318,432
Accrued expenses and other current liabilities		150,109,963	97,121,231	92,916,030
Short-term borrowings	15	107,000,000	71,000,000	265,481,082
Current portion of promissory note	14	29,242,000	29,242,001	29,242,001
Current portion of long-term debt	15	340,692,788	170,796,968	246,080,580
Income tax payable		1,152,630	72,417	
Total current liabilities		930,190,120	677,361,816	896,038,125

Long-term liabilities:				
Promissory notes	14	51,057,163	77,601,657	103,254,436
Long-term debt	15	616,294,743	719,570,905	494,556,385
Long-term payables relating to license agreements	16	62,833,433	16,992,950	24,686,398
Other long term liabilities			3,333,333	
Deferred tax liabilities	17	604,770	210,913	
Total long-term liabilities		730,790,109	817,709,758	622,497,219
Total liabilities		1,660,980,229	1,495,071,574	1,518,535,344
Commitments	21			
Minority interest		34,944,408	38,800,666	38,781,863
Stockholders equity:				
Ordinary shares, $0.0004 par value, 50,000,000,000 shares authorized ;18,558,919,712, 18,432,756,463 and 18,301,680,867 shares issued and outstanding at December 31, 2007, 2006 and 2005, respectively		7,423,568	7,373,103	7,320,673
Additional paid-in capital		3,313,375,972	3,288,765,465	3,291,439,835
Accumulated other comprehensive (loss) income		(1,881)	91,840	138,978
Deferred share-based compensation				(24,881,919)
Accumulated deficit		(308,278,637)	(288,810,490)	(244,701,412)
Total stockholders equity		3,012,519,022	3,007,419,918	3,029,316,155
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY		$ 4,708,443,659	$ 4,541,292,158	$ 4,586,633,362

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

Table of Contents

Semiconductor Manufacturing International Corporation
CONSOLIDATED STATEMENTS OF OPERATIONS
(In US dollars, except share data)

	NOTES	Year ended December 31,		
		2007	2006	2005
Sales	23	$ 1,549,765,288	$ 1,465,322,867	$ 1,171,318,735
Cost of sales		1,397,037,881	1,338,155,004	1,105,133,544
Gross profit		152,727,407	127,167,863	66,185,191
Operating expenses (income):				
Research and development		97,034,208	94,170,750	78,865,306
General and administrative		74,489,877	47,364,533	35,700,768
Selling and marketing		18,715,961	18,231,048 &nbs	