

# **Internet Initiative Japan Inc. fiscal year ended March 31, 2008 Consolidated Financial Results**



May 15, 2008

<http://www.iij.ad.jp/en/IR/>

- **Summary of FY2007 Financial Results**

President and CEO Koichi Suzuki

- **Consolidated Financial Results  
for FY2007**

CFO

Akihisa Watai

- **Medium-term target and  
the forecast for FY2008**

President and CEO Koichi Suzuki

- **Reference Materials**

# Summary of FY2007 Financial Results

- **The continued trend in operating income growth, 4 consecutive years of increase in Revenues and operating income**

FY07

· Total Revenues	66.9 billion	(17.1 % YoY)
· Operating Income	4.8 billion	(36.0 % YoY)
· Operating Margin Ratio	7.1 %	(1.0 Points YoY)

- **Revise in FY2007 year-end dividend followed by the growth of operating income**
  - Year end dividend from JPY750 to JPY1,000 (Annual dividend from JPY1,500 to JPY1,750)
  - Targets dividend of JPY2,000 (Annual) for FY2008

- **The strategy to increase recurring revenues, a profit driver bore fruit**

- Recurring Revenues (Connectivity and Value-added Services (“VAS”) and Systems Operation) increased 23.7% YoY
- Recurring Revenues were stronger-than-expected. It will bottom-up the growth in the following years

- **SI : Engagement in large-scaled network and application development projects**

- Completion of a remarkable large-scaled network and application development project in 3Q07, followed by the increase in revenues from Systems Operation and Maintenance in 4Q07.
- A step forward to enhance large-scale SI project

- **Initiated in new business development**

- “IIJ Mobile”, “acTVila”, GDX Japan Inc. (new subsidiary,51.0%), On-Demand Solutions Inc. (new subsidiary,100%), Trust Networks Inc. (new subsidiary,60.2%), IIJ Innovation Institute (plan to establish new subsidiary,100%)
- Initial expenses for new business development was JPY0.3 billion in FY07, which was covered by the growth in income from Core business

# -1. Consolidated Financial Results for FY2007

Unit: JPY billion

	<b>% of Revenues FY07 (07/4 ~ 08/3)</b>	<b>% of Revenues FY06 (06/4 ~ 07/3)</b>	<b>YoY</b>
Total Revenues	<b>66.8</b>	<b>57.1</b>	<b>17.1%</b>
Total Costs	<b>52.9</b>	<b>46.0</b>	<b>15.0%</b>
Gross Margin	<b>14.0</b>	<b>11.1</b>	<b>25.8%</b>
SG&A/R&D	<b>9.2</b>	<b>7.6</b>	<b>21.2%</b>
Operating Income	<b>4.8</b>	<b>3.5</b>	<b>36.0%</b>
Income before Income Tax Benefit	<b>4.4</b>	<b>5.0</b>	<b>13.6</b>
Net Income	<b>5.2</b>	<b>5.4</b>	<b>4.3</b>

Connectivity and VAS and Systems Operation continuously increased, up 17.1% YoY

Weaker-than-expected revenues from Systems Construction in 4Q07 affected by the unanticipated extra support required for the SI project that was completed in 3Q07.

Up 36.0% YoY due to growth in recurring revenues from the increase in service contracts

The Growth in operating income covered the Initial Business Cost of JPY303 million.

Net loss or gain from impairment loss and capital gain from equity securities: JPY 71 million in FY07, JPY1,867 million in FY06.

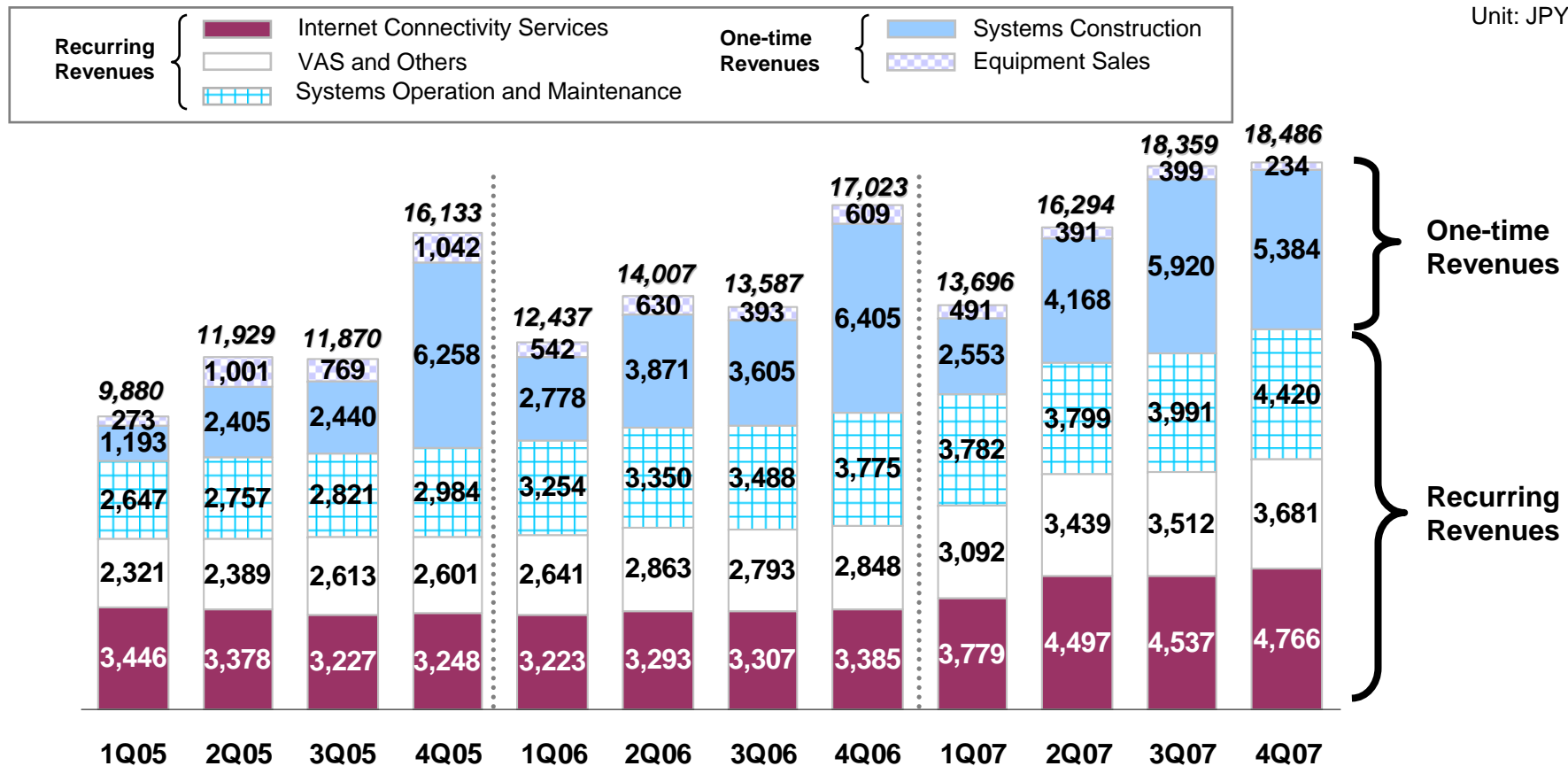
Deferred tax benefit of JPY1,653 million in FY07.

# -2. Revenues



Internet Initiative Japan

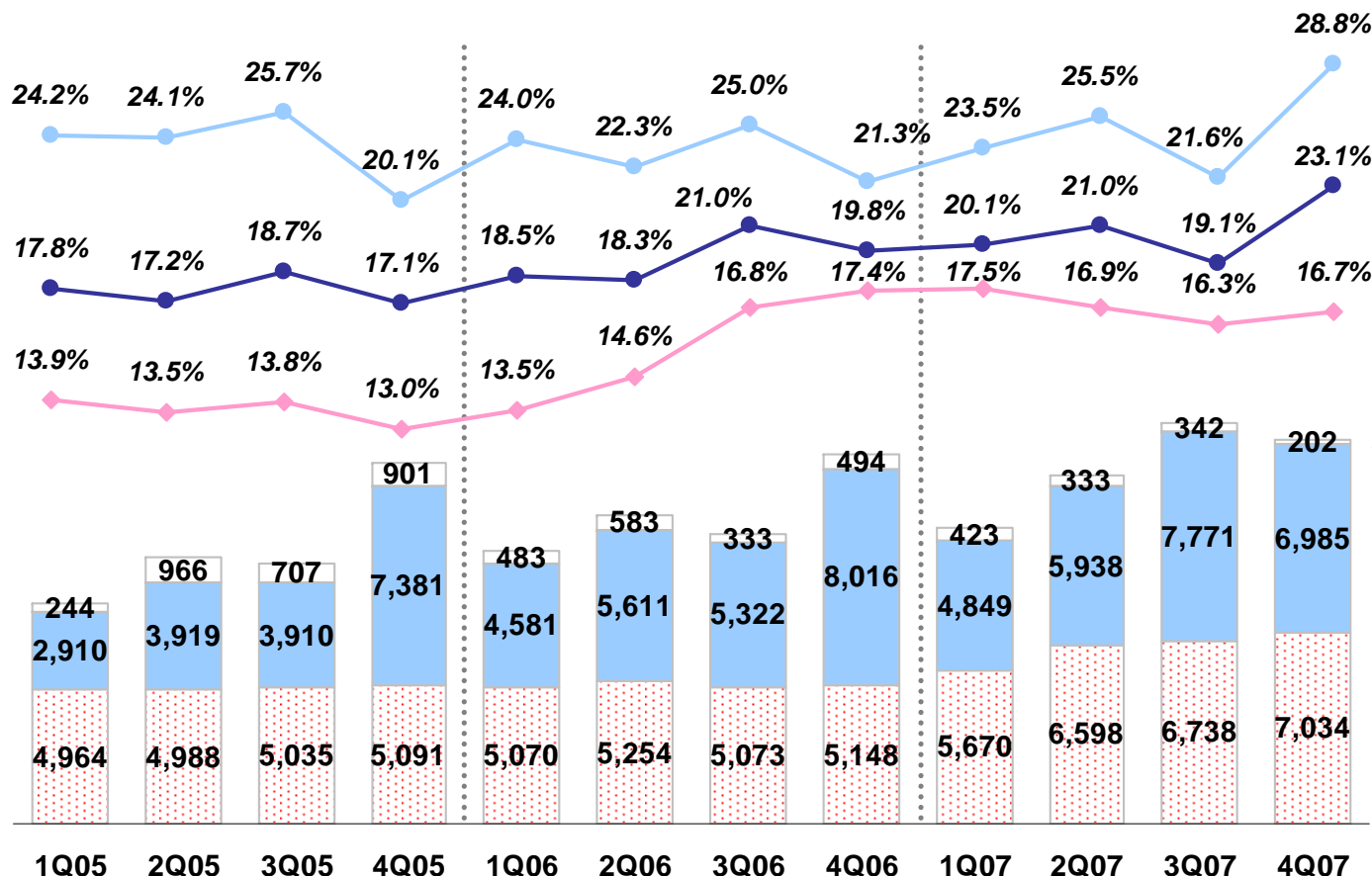
Unit: JPY million



- ◆ Highest revenues in our history: revenues were JPY 66,835 million in FY07, up 17.1% YoY
- ◆ Recurring revenues continuously increased. JPY47,296 million in FY07, up 23.7% YoY.
  - Internet Connectivity Services in 4Q07: Up 40.8% compared to 4Q06, Up 5.1% compared to 3Q07.
  - VAS and Others in 4Q07: Up 29.3% compared to 4Q06, Up 4.8% compared to 3Q07.
  - Systems Operation and Maintenance in 4Q07: Up 17.1% compared to 4Q06, Up 10.8% compared to 3Q07.
- ◆ Systems Construction was JPY18,025 million, up 8.2% YoY due to the remarkably large-scaled SI project in 3Q07.
  - 4Q07 down 16.0% compared to 4Q06, down 9.1% compared to 3Q07 because many of our engineering resources had been engaged in large SI projects during 3Q07.

# -3. Cost of Revenues and Gross Margin Ratio

Unit: JPY million



**SI**  
Personnel related costs, outsourcing costs and purchase etc.

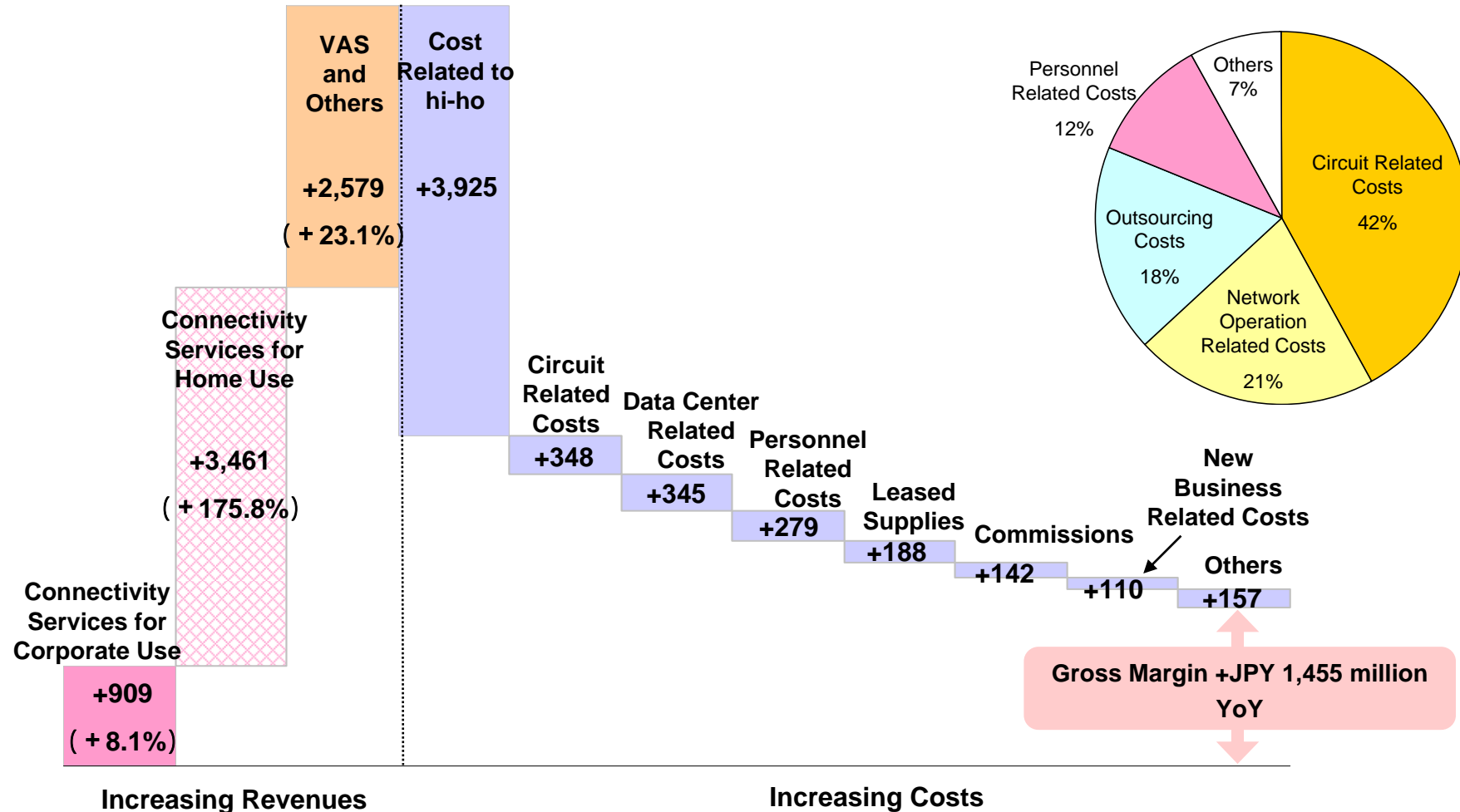
**Connectivity and VAS**  
Network costs such as backbone costs, network equipment costs, network operation costs for such as network operation centers and personnel related costs

- ◆ **Internet Connectivity and VAS:** Cost of Revenues were JPY26,040 million in FY07, up26.7% YoY.  
Gross Margin Ratio was 16.8% in FY07, up 1.2 points YoY.
- ◆ **SI:** Cost of Revenues were JPY25,543 million in FY07, up8.6% YoY.  
Gross Margin Ratio was 24.9% in FY07, up 2.0 points YoY.

# -4. Gross Margin Increase-Connectivity and VAS (YoY)

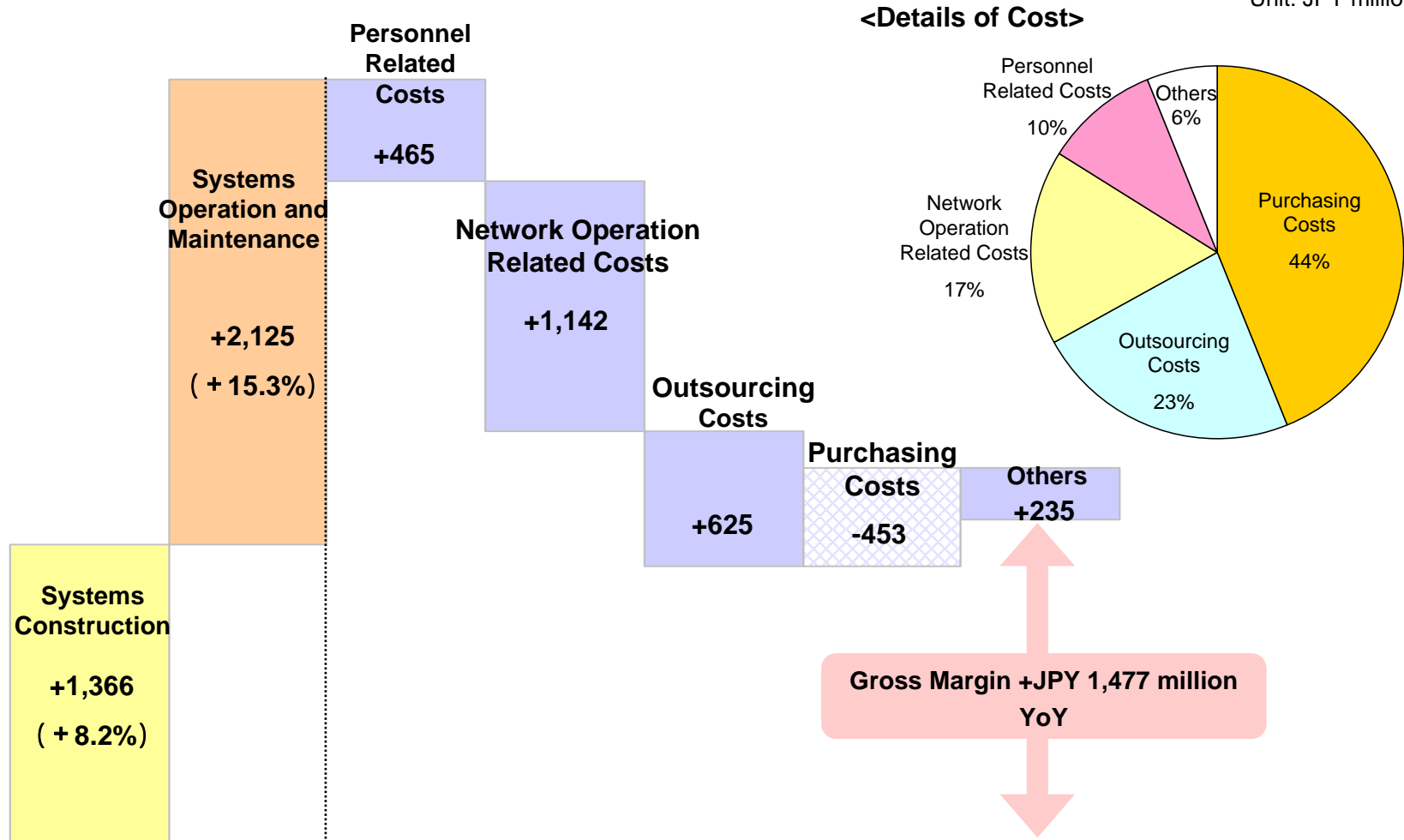
<Details of Cost>

Unit: JPY million



◆ **Gross margin:** JPY 5,263 million (FY07) compared to JPY 3,808 million (FY06) (+JPY 1,455 million, up 38.2%)  
 ◆ **Gross margin ratio:** 16.8% (FY07) compared to 15.6% (FY06) (+1.2 points)

# -5. Gross Margin Increase-SI (YoY)



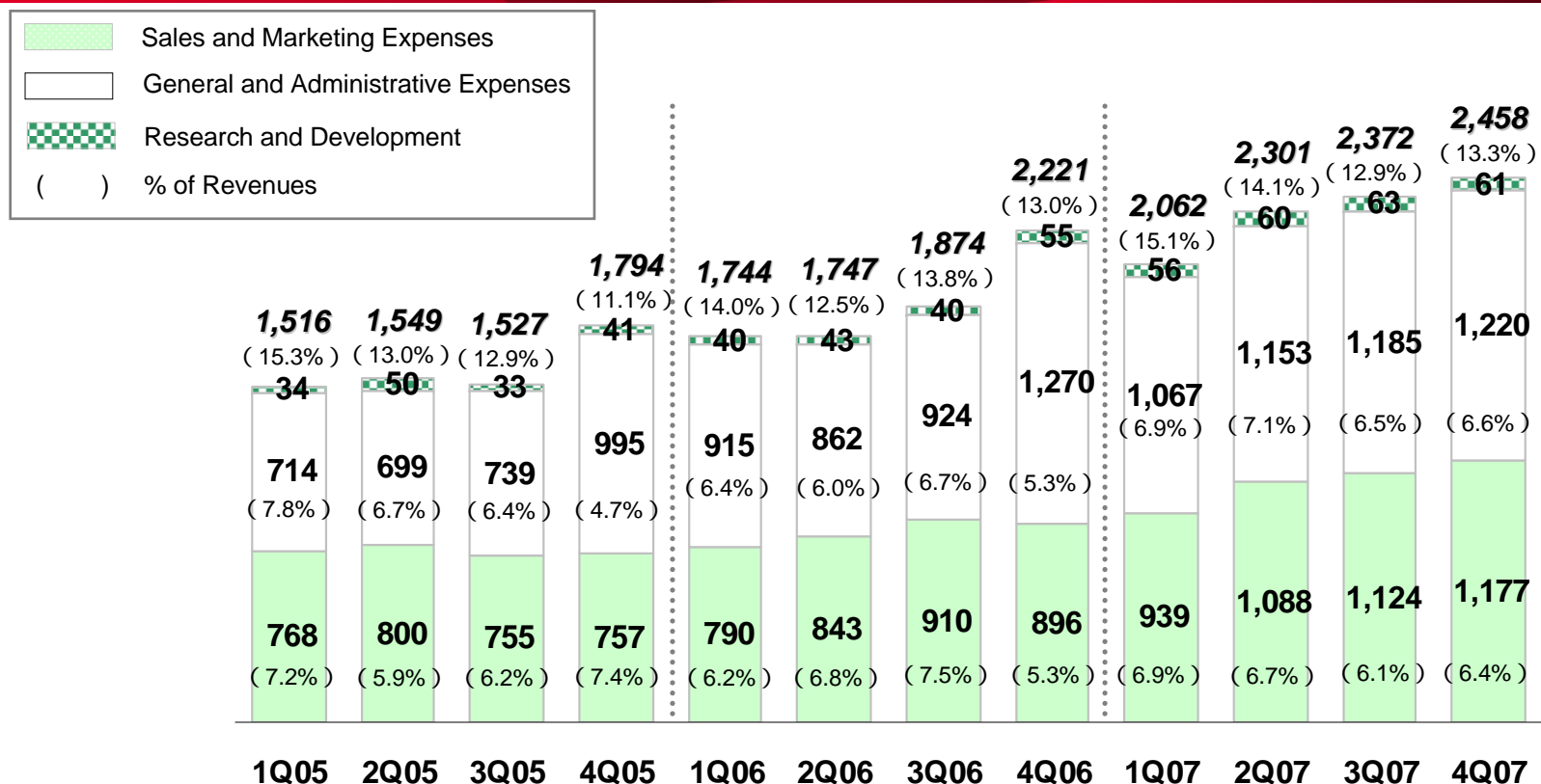
Elements of Increasing Revenues

Elements of Increasing Costs

- ◆ **Gross margin:** JPY 8,475 million (FY07) compared to JPY 6,998 million (FY06) (+JPY 1,477million, up 21.1%)
- ◆ **Gross margin ratio:** 24.9% (FY07) compared to 22.9% (FY06) (+2.0 points)



# -6. SG&A Expenses/R&D



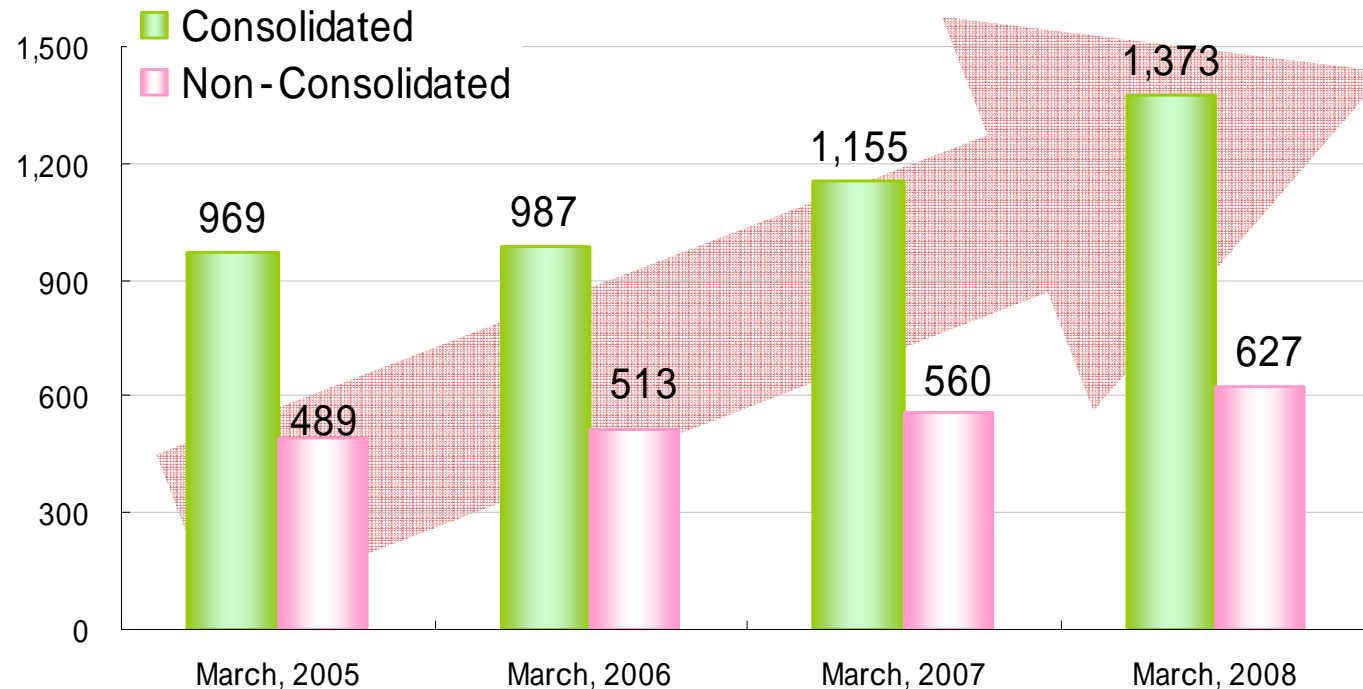
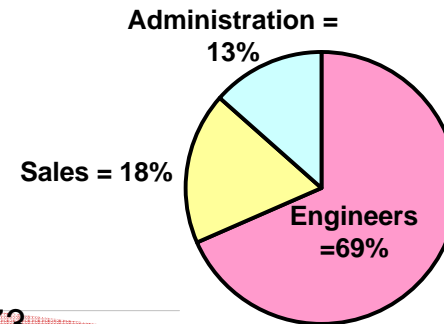
- ◆ **SG&A expenses : % of revenues in FY07 was 13.8% (up 21.2% YoY), in 4Q07 was 13.3%(up 3.6% QoQ).**
- ◆ **Sales and marketing expenses : % of revenues in FY07 was 6.5%, in 4Q07 (3 months) was 6.4%.**
  - JPY 4,329 million in FY07, up 25.9% YoY mainly due to hi-ho's sales expenses of JPY 424 million (10 months) and an increase in personnel related and advertising expenses.
- ◆ **General and administrative expenses : % of revenues in FY07 was 6.9%, in 4Q07 (3 months) was 6.6%.**
  - JPY 4,624 million in FY07, up 16.5% YoY mainly due to an increase in personnel related expenses and increase in rent due to increase in office space affected by business growth.
- ◆ **Research and development expenses : JPY240 million in FY07, up 35.6% YoY.**

# -7. Number of Employees

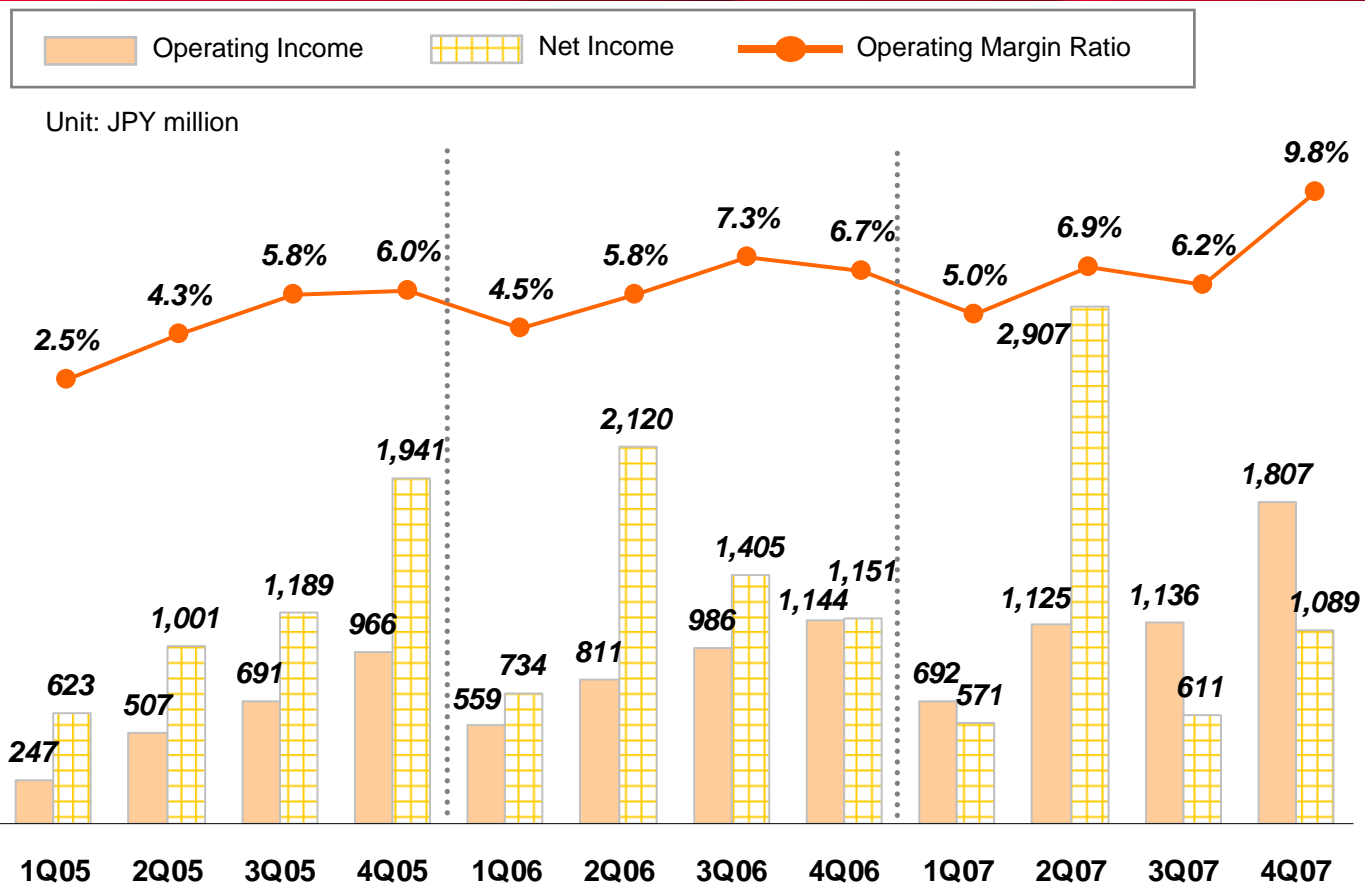
The number of employees increased by 218 in FY07 from FY06.  
(of the above, the number of new graduates were 83)

IIJ will employ at the same level along with the growth.

< Number of Employees per Sector >



# -8. Operating and Net Income



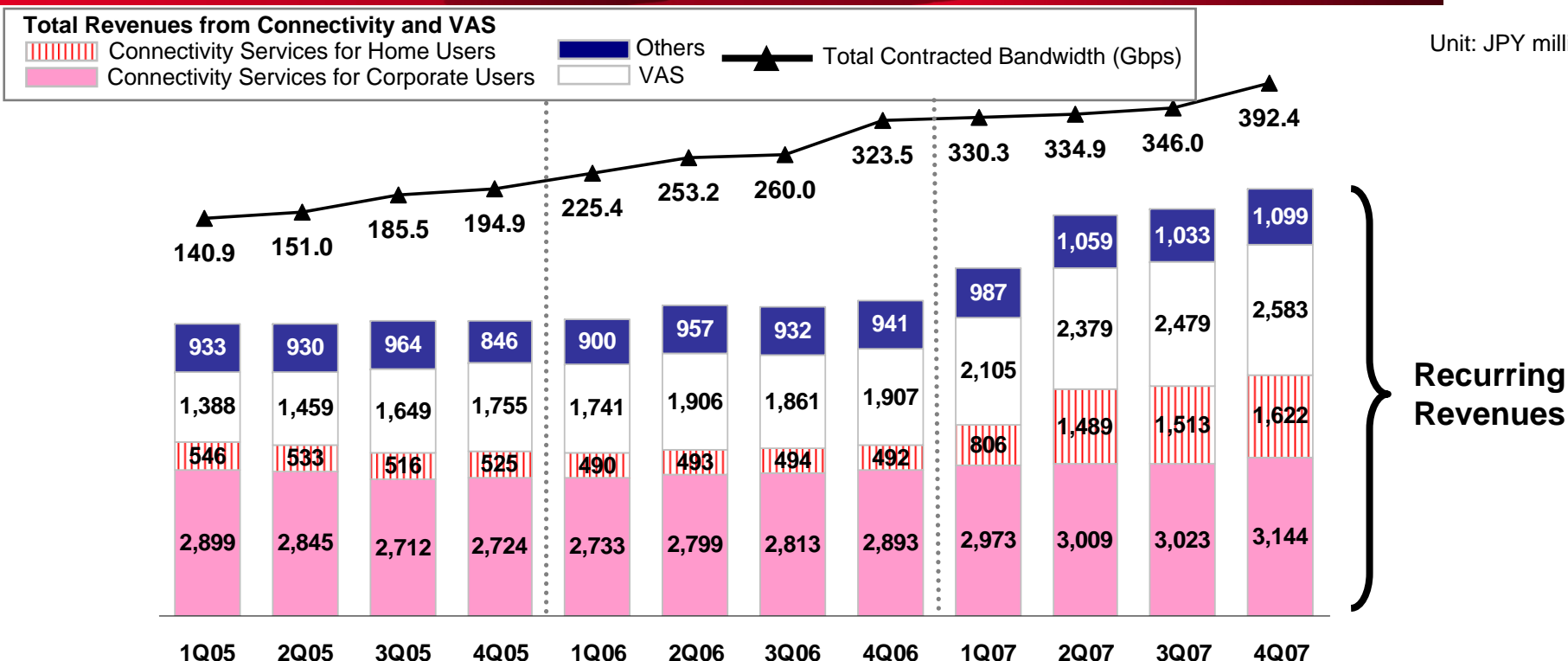
◆ **Operating income:**  
**Operating margin ratio in 4Q07 was 9.8%, up 3.6 points QoQ.**  
**JPY4,759 million in FY07, up 36.0% YoY (Highest operating income in history).**  
 > The Growth in operating income covered the Initial Business Cost of JPY303million.

◆ **Net Income:**  
**JPY5,177million in FY07, down 4.3% YoY.**  
**JPY1,089 million in 4Q07, up 78.3% QoQ.**  
 > Net loss or gain from impairment loss and capital gain from equity securities: JPY 71 million in FY07, JPY1,867 million in FY06.  
 > Income tax benefit of JPY861 million due to deferred tax benefit of JPY1,653 million in FY07.  
 > Minority interests in losses of subsidiaries was JPY97 million in FY07, related to GDX, Trust Networks.  
 > Equity in net loss of equity method investees was JPY143 million in FY07, mainly affected by Internet Revolution.

	1Q07	2Q07	3Q07	4Q07	FY2007
<b>Income tax expense (benefit)</b>	175	(1,980)	392	552	861
<b>Minority interests</b>	9	15	27	45	97
<b>Equity in net loss of equity method investees</b>	(20)	(29)	(42)	(52)	(143)

# -9. Results by Service – Connectivity and VAS

Unit: JPY million



◆ **Connectivity services for corporate users: JPY12,148 million in FY07 (up 8.1% YoY, up 4.0% QoQ), mainly due to an increase in contracted bandwidth and the number of contracts.**

- IP Service: JPY9,022 million in FY07, up 7.0% YoY. The number of contracts at end of 4Q07 was 1,414 contracts, up 157 contracts YoY. The number of contracts for over 1 Gbps was 70.
- Broadband Services: JPY2,663 million in FY07, up 22.9% YoY. The number of contracts at end of 4Q07 was 23,539 contracts, up 7,121 contracts YoY.
- Others: JPY463 million in FY07, down 27.9% YoY.

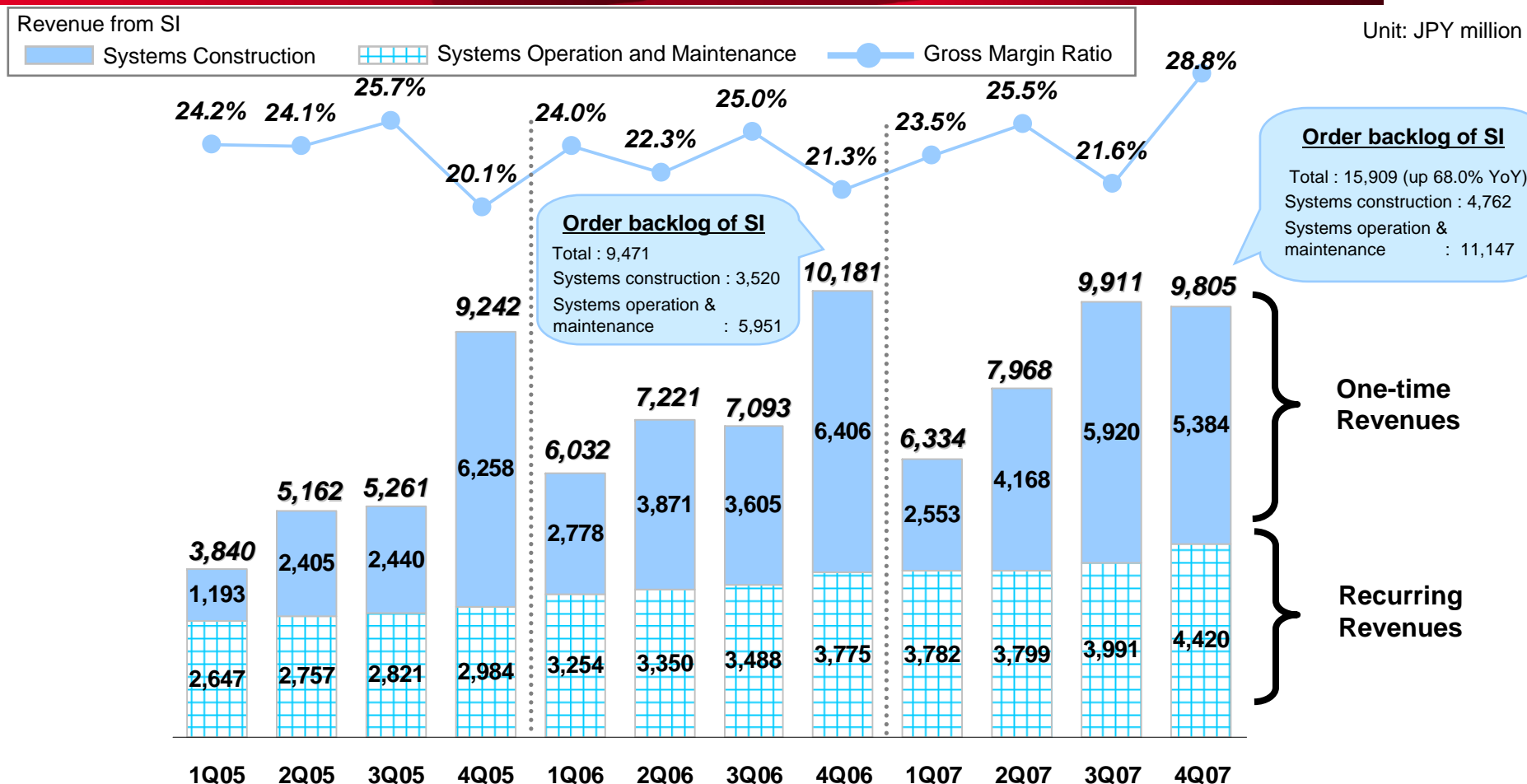
◆ **Connectivity services for home users: JPY5,430 million in FY07, up 175.8% YoY, up 7.2% QoQ.**

- Lead by revenues from hi-ho of JPY3,765 million (10 months, 189,700 contracts at the end of 4Q07).

◆ **VAS: JPY9,546 million in FY07, up 28.7% YoY, up 4.2% QoQ.**

- Lead by the overall growth in anti-spam services, Internet VPN and data centers.
- The number of contracts for anti-spam services was about 700,000 at the end of FY07 (about 200,000 at the end of FY06).

# -10. Results by Service - SI



- ◆ **Systems construction: JPY18,025 million in FY07, up 8.2% YoY.**
  - Down 9.1% compared to 3Q07 due to the completion of a remarkably large-scaled network and application development project in 3Q07.
  - Order backlog at the end of 4Q07 was JPY 4,762 million, 35.3% YoY.
- ◆ **Systems operation and maintenance: JPY 15,993 million in FY07, up 15.3% YoY.**
  - Up 10.8% compared to 3Q07 due to start the operation of large-scale network and application development project in 3Q07.
  - Order backlog at the end of 4Q07 was JPY 11,147 million.
- ◆ **Gross margin : 24.9% in FY07, up 2.0% YoY.**

## -12. Consolidated Balance Sheets



Internet Initiative Japan

Unit: JPY million

	March 31, 2008	March 31, 2007	Changes	
Cash	11,471	13,555	2084	Used cash to acquire of subsidiary shares etc.
Accounts Receivable	12,255	9,676	+2,579	Increased along with business expansion
Inventories	1,184	1,111	+73	
Prepaid Expenses	2,005	1,053	+952	
Available-for-sale Securities	857	1,310	453	Increased by network related assets and assets from the acquisition of hi-ho etc.
Property and Equipment	11,740	9,832	+1,908	
Intangible Assets	5,907	2,877	+3,030	Increased by acquisition of subsidiary shares and of hi-ho etc.
Other Assets	4,177	3,260	+917	
Borrowings (Short-term)	9,150	6,340	+2,810	Increased by short-term borrowings for the acquisition of subsidiary shares (JPY 2,000 million) etc.
Accumulated Deficit	19,555	24,271	+4,715	
Accumulated Other Comprehensive Income	91	950	859	
Total Shareholders' Equity	24,981	20,112	+4,869	
Total Assets	55,703	47,693	+8,010	

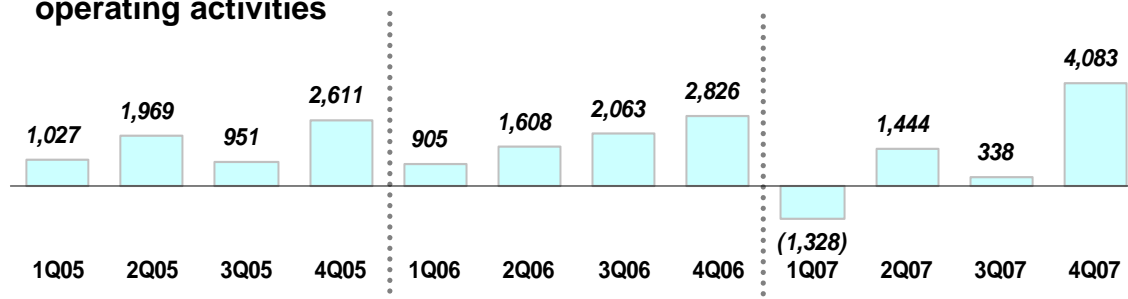
# -13. Consolidated Cash Flows



Internet Initiative Japan

Unit: JPY million

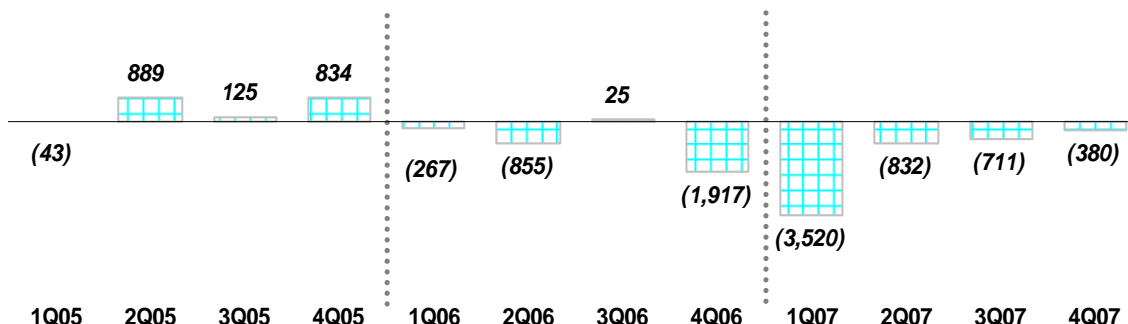
## Net cash provided by (used in) operating activities



### Net cash provided by operating activities: JPY 4,538 million in FY07.

- Increase in accounts receivable along with the expansion of business
- Expenditure inventories, prepaid expenses by SI projects
- Decrease in accounts payable etc.

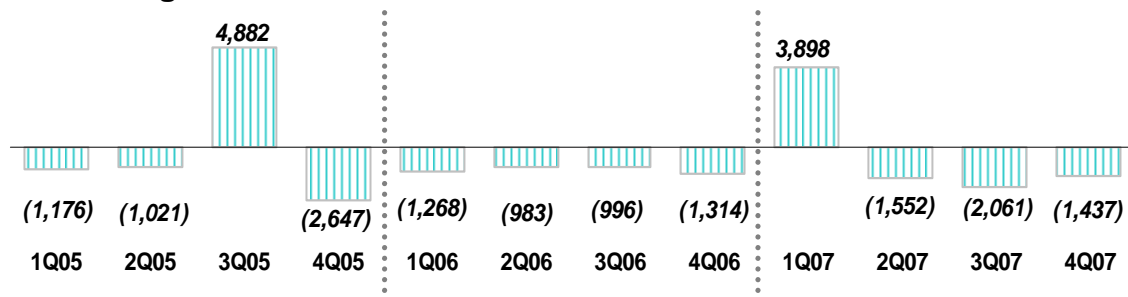
## Net cash provided by (used in) investing activities



### Net Cash used in investing activities: JPY 5,444 million in FY07.

- Payments in acquisition of subsidiary shares
- Payments for the purchase of property and equipment
- Capitalize for newly consolidated subsidiary, TN, and acquisition of cash from it etc.

## Net cash provided by (used in) financing activities



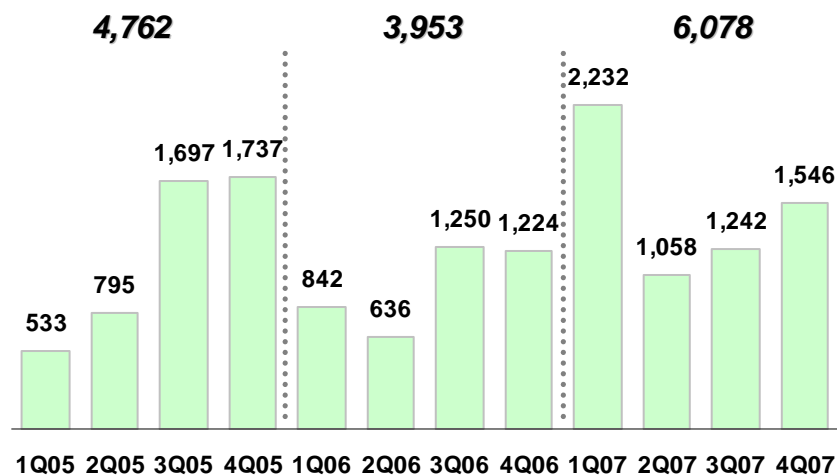
### Net cash provided by financing activities: JPY 1,152 million in FY07.

- Borrowing of short-term borrowing for the acquisition of the consolidated subsidiaries
- Principle payments under capital lease obligations
- Payments of dividend etc.

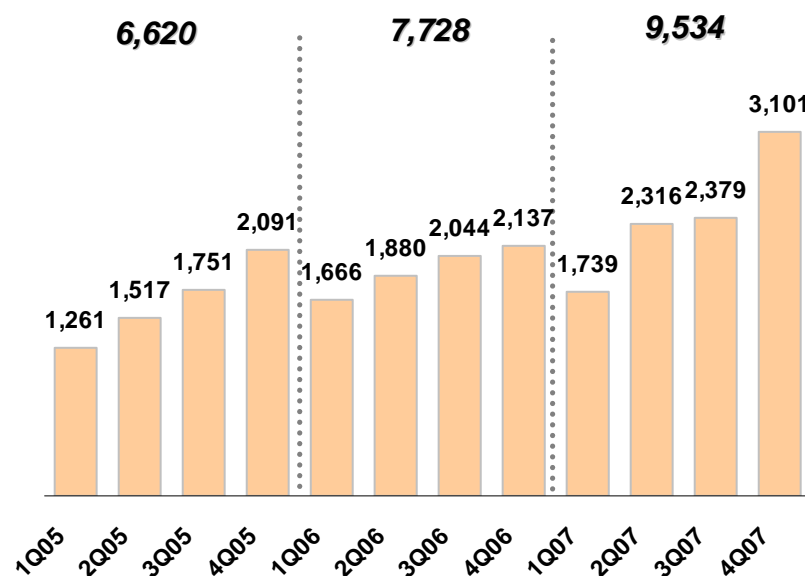
# -14. Other Financial Data (CAPEX etc.)

Unit: JPY million

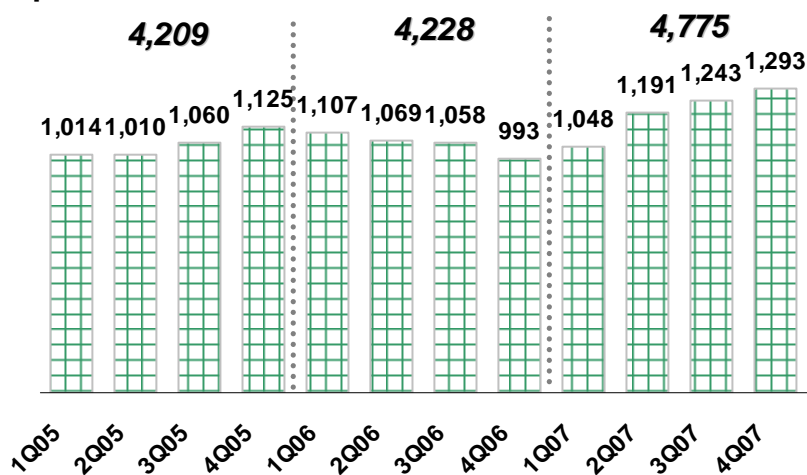
## CAPEX



## Adjusted EBITDA

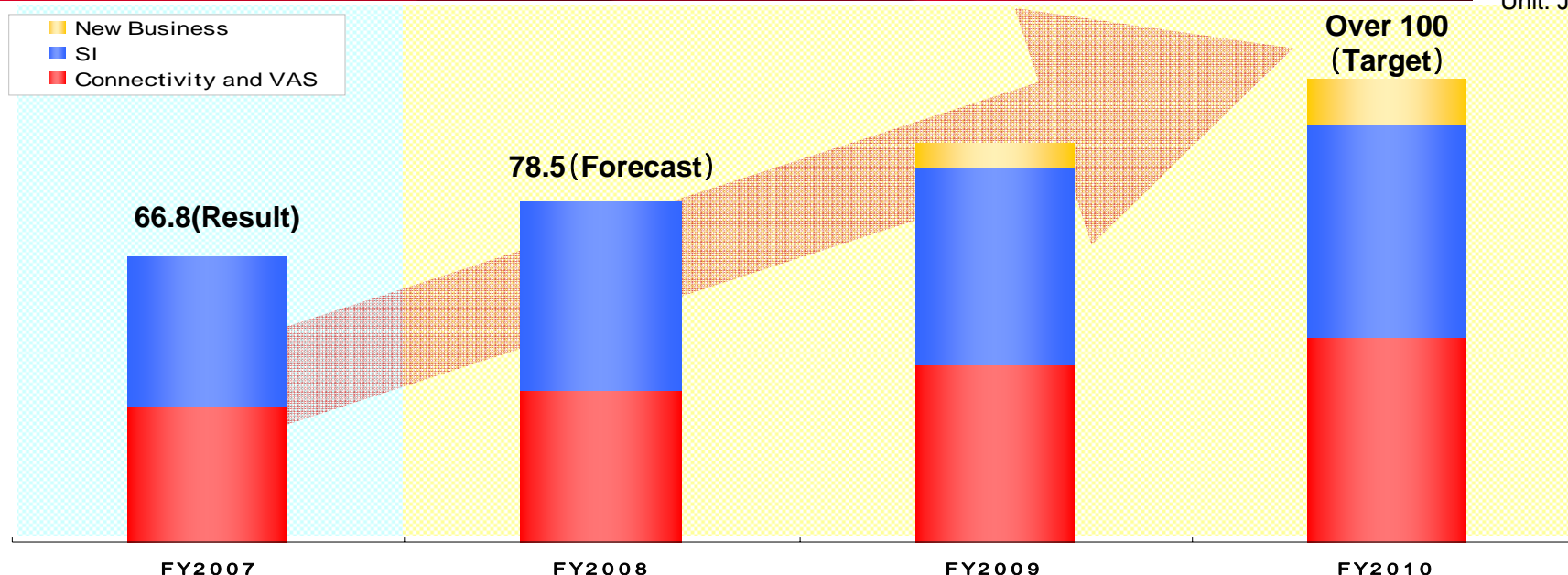


## Depreciation and Amortization





# -1. Medium-term target



Expansion the Growth basis by Recurring Revenues  
Ensuring the increase of Operating Income  
Approach to large-scale SI project  
Seeding to new business development

Acceleration of the growth speed by Recurring Revenues  
Expansion of SI business, Income basis strengthen  
Initiated new business development  
Full-Operation

**Total Revenues;  
over JPY 100 billion**  
**Operating Income;  
JPY 10 billion**

**(Market Environment)**  
IP Network Market in Japan continuously expand (From Legacy Network to IP Network)  
Continuously Growth in Corporate IT Spending (From Mainframe to Open System)  
Market Size of IT Outsourcing Services in Japan :28.6% expand for 5 years (JPY3,596 billion in 2012) ( By MIC Research Institute Ltd.)  
Market Size of Data Center in Japan :40.8% expand for 5 years (JPY1,634 billion in 2012) ( By MIC Research Institute Ltd.)  
Internet traffic enlarge by image distribution etc. (Total traffic enlarge about 2.5 times from 2005 to 2007)  
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## -2. Forecast for FY2008

Unit: JPY billion

	Interim Period of FY08 Target (08/4 ~ 08/9)	FY08 Target (08/4 ~ 09/3)	FY07 Actual (07/4 ~ 08/3)	YoY		
Total Revenues	34.5	78.5	668.4	11.7	17.5%	Recurring revenues continue to increase, Scale up of Systems construction.
Operating Income	1.9	5.2	47.6	0.4	9.3%	Operating income continue to increase along with the recurring revenues. Operating Costs include JPY0.9 billion loss for new subsidiaries related costs.
Income before Income Tax Expense (Benefit)	1.7	4.7	43.6	0.3	7.8%	Doesn't include gains from the sale of available-for-sale securities.
Net Income	0.8	5.2	51.8	0.2	0.5%	
Net Income per Share	JPY3,875	JPY25,184	JPY25,100	JPY84	0.3%	Include Deferred tax benefit of JPY 0.5 billion in 4Q08.
Cash Dividend per Share	JPY1,000	JPY2,000 (Annual)	JPY1,750 (Annual)	JPY250	14.3%	Cash Dividend per Share increases JPY2,000 in FY08, up FY250 YoY.

# -1. Reference: Consolidated Financial Results for 4Q07 (3 months)

Internet Initiative Japan

Unit: JPY billion

	<i>% of Revenues</i> <b>4Q07</b> (08/1 ~ 08/3)	<i>% of Revenues</i> <b>4Q06</b> (07/1 ~ 07/3)	<b>YoY</b>
Total Revenues	<b>18.5</b>	<b>17.0</b>	<b>8.6%</b>
Total Costs	<i>76.9%</i> <b>14.2</b>	<i>80.2%</i> <b>13.7</b>	<b>4.1%</b>
Gross Margin	<i>23.1%</i> <b>4.3</b>	<i>19.8%</i> <b>3.4</b>	<b>26.7%</b>
SG&A/R&D	<i>13.3%</i> <b>2.5</b>	<i>13.0%</i> <b>2.2</b>	<b>10.6%</b>
Operating Income	<i>9.8%</i> <b>1.8</b>	<i>6.7%</i> <b>1.1</b>	<b>58.0%</b>
Income before Income Tax Expense	<i>8.9%</i> <b>1.6</b>	<i>7.6%</i> <b>1.3</b>	<b>26.6%</b>
Net Income	<i>5.9%</i> <b>1.1</b>	<i>6.8%</i> <b>1.2</b>	<b>5.4</b>

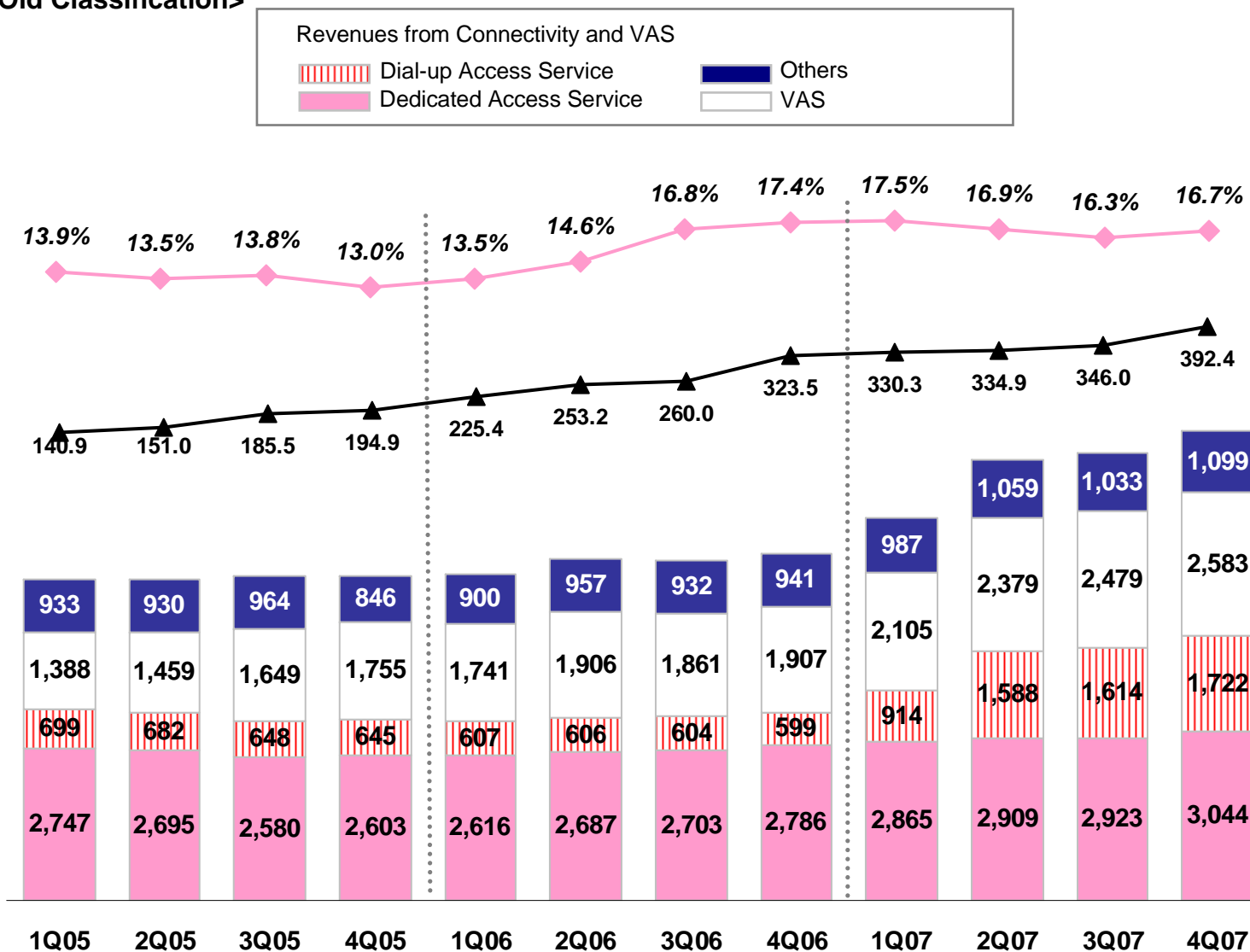
# -2. Reference: Revenues from Connectivity and VAS



Internet Initiative Japan

Unit: JPY million













<Old Classification>



## -3. Reference:FY2007 Press Releases

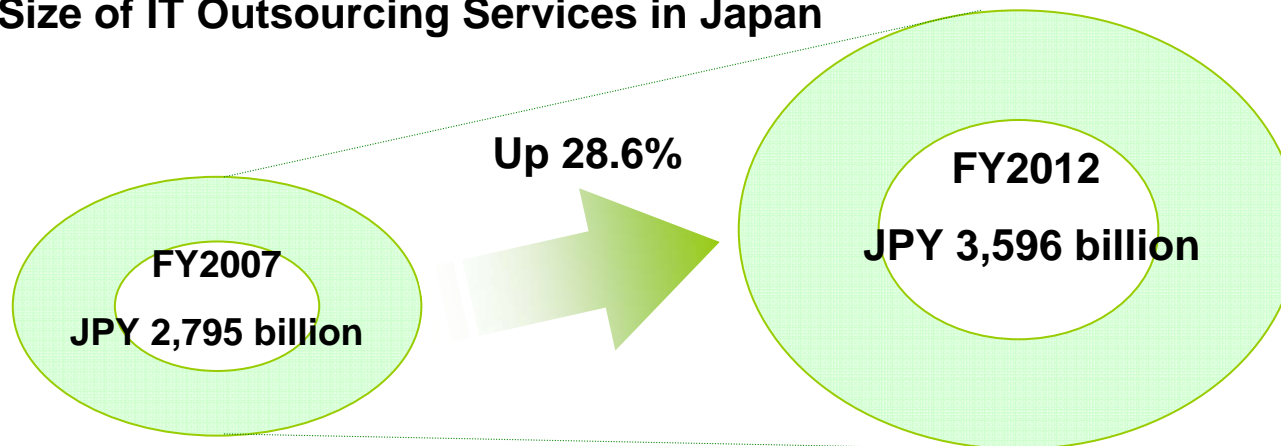
Date		Press Releases
1Q	2007/4/2	IIJ Group Opens New Ikebukuro Data Center
	4/5	IIJ Makes its Two Consolidated Subsidiaries 100% Owned through Exchanges of Shares
	4/9	IIJ to Create New Generation Messaging Services in Joint Venture with GDX Japan
	4/16	IIJ and Hirata Form Partnership for Joint Management of Taihei Computer
	6/1	IIJ Completes Acquisition of hi-ho Inc.
	6/27	IIJ to Launch the Unified Management Platform
2Q	8/9	IIJ to Provide High-Definition Content Delivery Platform to TV Portal Service acTVila
	8/29	IIJ to Launch IIJ Secure Web Platform
	9/13	GDX Japan Announces the Next Generation Messaging Network for the Enterprise
3Q	10/1	IIJ to Develop New SEIL/X Series
	10/31	IIJ Acquires Patent for SMF-LAN
	11/29	IIJ Group Opens New Shinsaibashi Data Center
	12/3	IIJ Introduces the IIJ Innovation Institute
	12/17	IIJ to Use DoCoMo 3G Network to Provide Corporate Data Communications Services as MVNO
4Q	2008/1/21	IIJ Launches IIJ Mobile for Corporate Customers as an MVNO
	2/6	IIJ and EMOBILE Agree to Start MVNO Service
	3/12	IIJ to Establish New Print-on-Demand Company

## -4. Reference: IIJ Group Companies

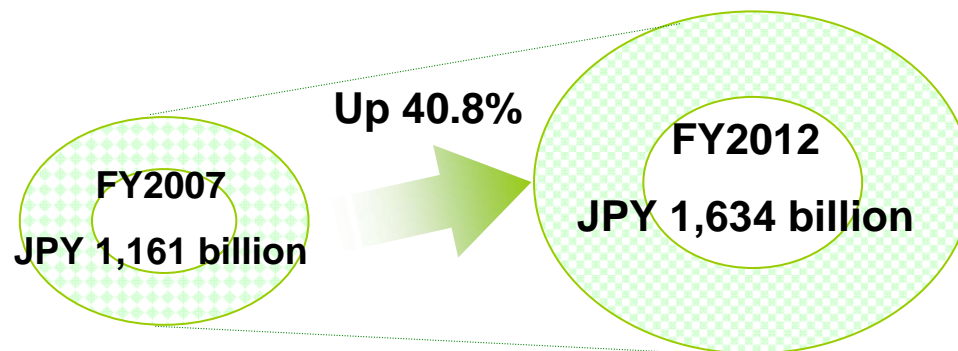
	Company Name	Ownership	Main Business
Consolidated Subsidiaries	 IIJ Technology Inc.	100%	Offers a comprehensive suite of systems integration services from design, physical installation, operation, and maintenance to monitoring for our customers' diverse network systems.
	 IIJ Financial Systems Inc.		Provides full outsourcing services for integration and operation of the front- and back-end for securities systems.
	 Net Care, Inc.		Provides a full range of network operation and management services, from customer support, end-user help desks, monitoring and troubleshooting to integrated management services.
	 Net Chart Japan Inc.		Provides network construction services, primarily for LANs, such as network installation wiring, installation and set-up of equipment, installation of applications, and operational support.
	 IIJ America Inc.		Provides quality Internet services in the U.S. with a focus on U.S.-based enterprises doing business in the Asia-Pacific region. Also IIJ-A constructs and operates on U.S. Internet backbone network.
	 hi-ho, Inc.		Supports customer's safe, secure and comfortable Internet life based on ISP business for personal users.
	 On-Demand Solutions Inc.		Print on demand and related services
	 Trust Networks Inc.		60.2%
	 GDX Japan, K.K.	51%	Building safe, reliable corporate messaging networks and providing message exchange services.
Equity Method Investees	 Internet Multifeed Co.	31%	Provides mutual access with other major ISPs and content distribution services based on Multifeed technology. Also MFEED operates JPNAP, a distributed IX service.
	 Internet Revolution, Inc.	30%	Operates a comprehensive portal site that provides various contents, such as SNS, blogs, stunning games, videos, and music.
	 Taihei Computer Co., Ltd.	45%	Provides operation of reward point management system

## -5. Reference:Market Trends

### Market Size of IT Outsourcing Services in Japan



### Market Size of Data Center in Japan



( Source : MIC Research Institute Ltd. )

# Forward-looking Statements



Internet Initiative Japan

Statements made in this presentation regarding IIJ's or management's intentions, beliefs, expectations, or predictions for the future are forward-looking statements that are based on IIJ's and managements' current expectations, assumptions, estimates and projections about its business and the industry. These forward-looking statements, such as statements regarding FY2007 revenues and operating and net profitability, are subject to various risks, uncertainties and other factors that could cause IIJ's actual results to differ materially from those contained in any forward-looking statement. These risks, uncertainties and other factors include: IIJ's ability to maintain and increase revenues from higher-margin services such as systems integration and value-added services; the possibility that revenues from connectivity services may decline substantially as a result of competition and other factors; the ability to compete in a rapidly evolving and competitive marketplace; the impact on IIJ's profits of fluctuations in the price of available-for-sale securities; the impact of technological changes in its industry; IIJ's ability to raise additional capital to cover its indebtedness; the possibility that NTT, IIJ's largest shareholder, may decide to exercise substantial influence over IIJ; and other risks referred to from time to time in IIJ's filings on Form 20-F of its annual report and other filings with the United States Securities and Exchange Commission ("SEC").