

# Internet Initiative Japan Inc.

**TSE1:3774 NASDAQ:IIJI**

**December 2007**

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



# Forward-looking Statements

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").

# Key Investment Highlights

- ▶ Top IP engineering company in Japan
- ▶ Shifted to Total Network Solution Provider
- ▶ Target Blue-chip and Governmental Organizations with dominant position
- ▶ Shifting to IP related system and spreading IT expenditure
- ▶ Convincing revenue and income growth
- ▶ Business Development for Mid/Long-term growth

details to follow

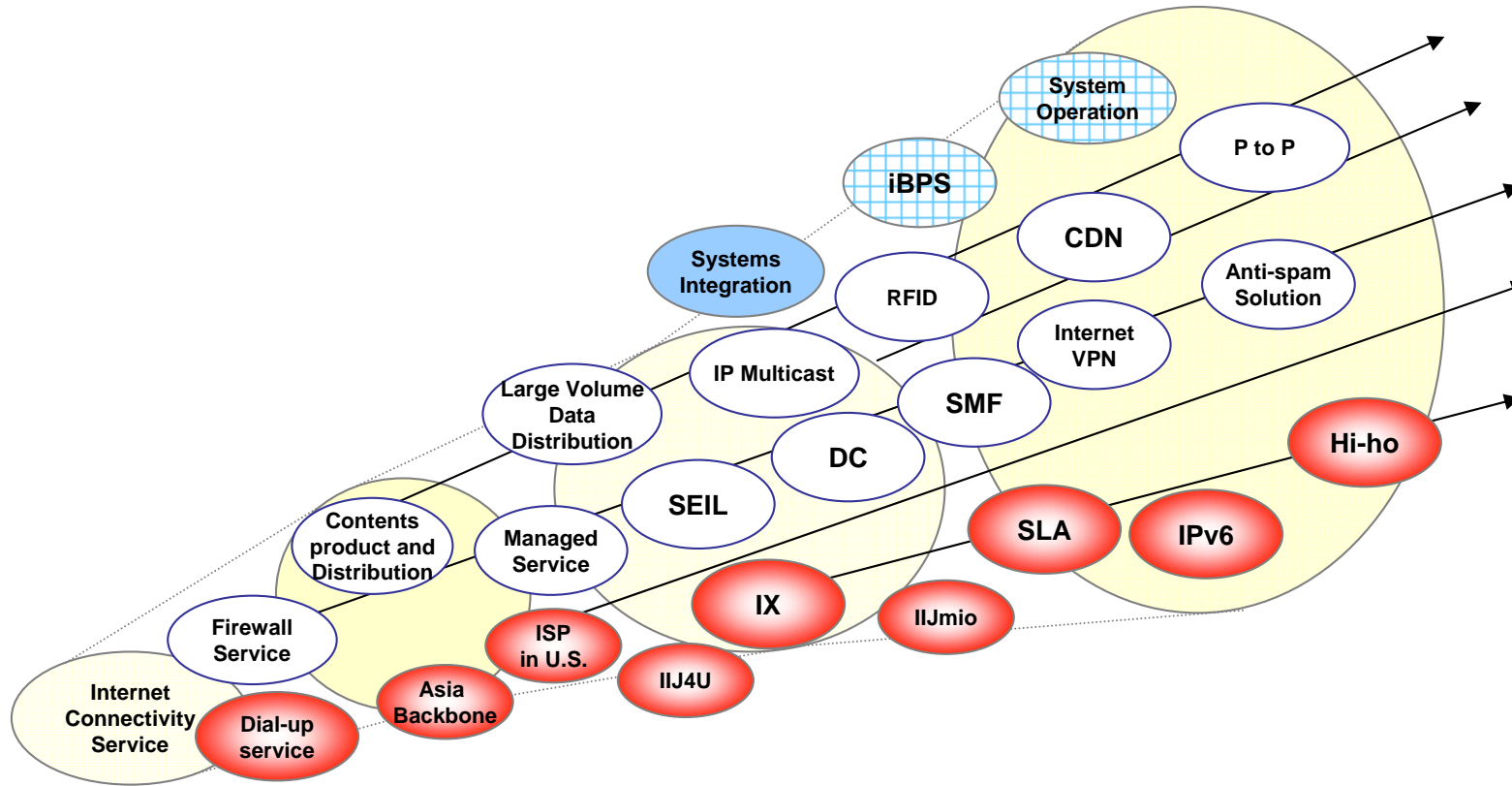
# TOP IP Engineering Company in Japan

- ▶ The first established full-scale ISP in Japan
  - A group of highly motivated and skilled TOP Level IP Engineers
  - Introduced and standardized internet related services in Japan
- ▶ In-housed development
  - Operate the largest Internet Backbone in Japan
  - Fully develop its service and back office facilities
    - Internet Connectivity & Firewall Service, IP Multicast Delivery Service
    - Service Level Agreement (SLA)
    - IPv6 Service
    - Router Products (SEIL Series)
- ▶ “IIJ” brand among the Japanese IT market
  - Well known for its high engineering skills and network support skills
  - High customer Satisfaction with long term relationship
- ▶ At the leading edge of IP R&D
  - IPv6, Mobile IPv6(MIPv6), NetBSD
  - Participation in the MIC Grant Research
  - Board Member of “Telecom-ISAC Japan”











Company Profile (as of September 2007)	
Established	December 1992
Number of Employees	Consolidated: 1,327 (70% engineers)
Listed Markets	NASDAQ(IIJI), TSE1(3774)
Top Shareholders	NTT(24.5%), Koichi Suzuki (6.2%), Itochu Corp.(5.1%), NTTCom(5.0%)

# Pioneer of Network Technologies

## Business and Service Development to Initiate the Market

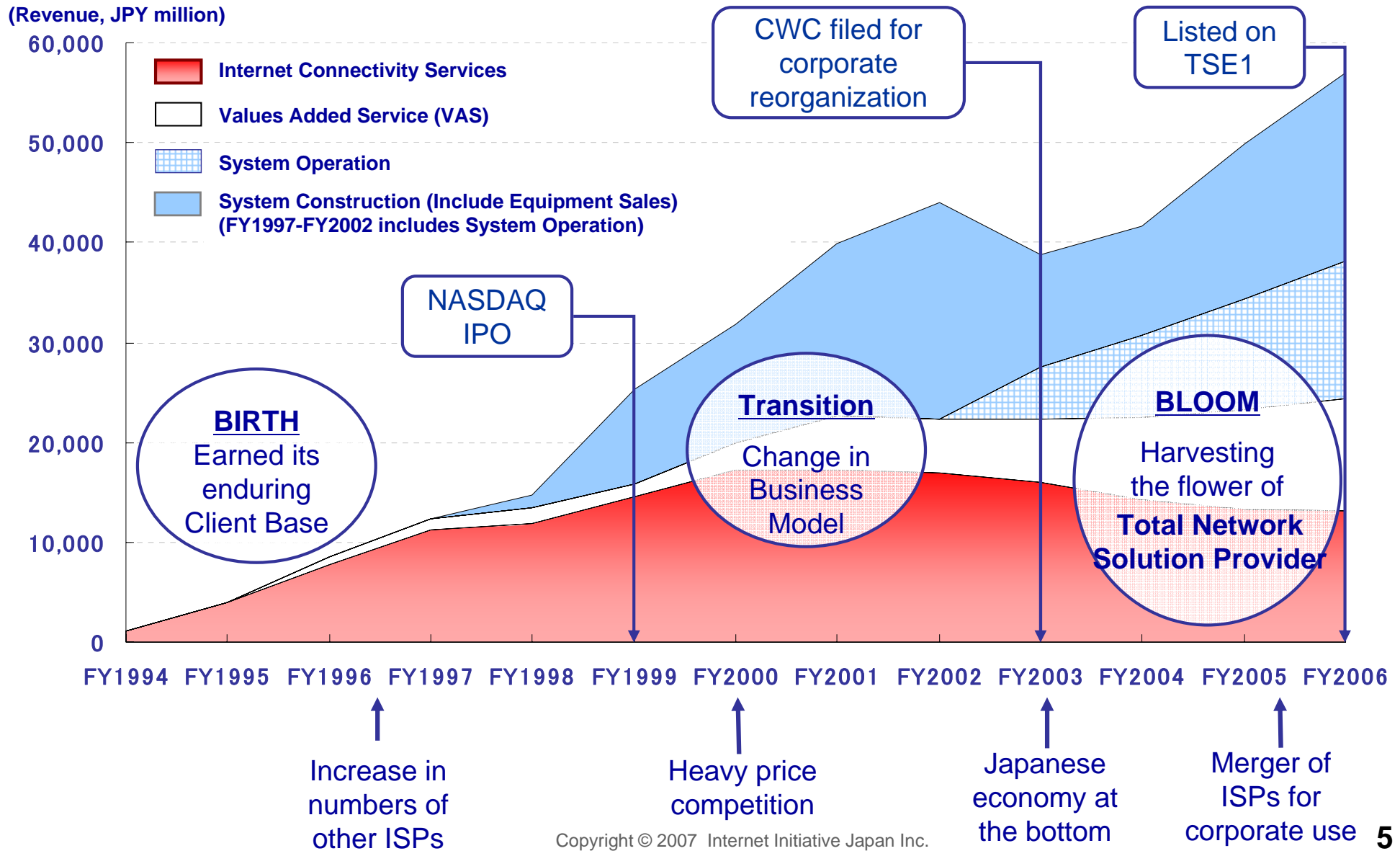


[Development of new businesses]

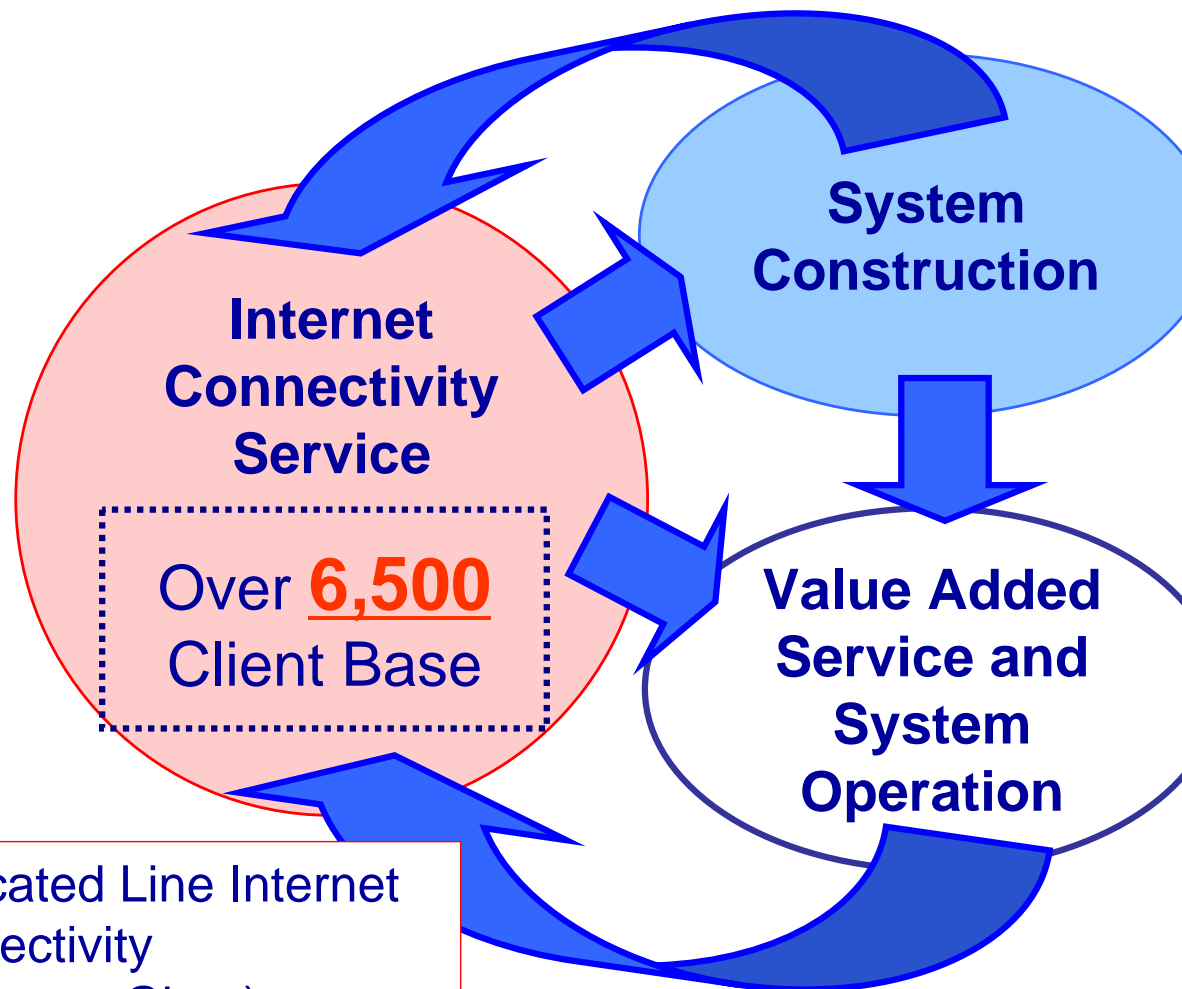
1992	1995	1996	1997	1998	2004	2006	2007
 Internet Initiative Japan Established	 II Media Communication  A-Bone	 IIJ America  IIJ Technology	 Internet m/s	 Net Care	 II Financial Systems	 Net Care Japan  i-revo	 GDX  hi-ho

# Strategic Shift in Business Model

## From "ISP" to "Total Network Solution Provider"



## Cross Selling of Total Network Solutions



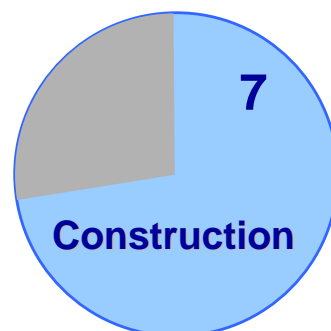
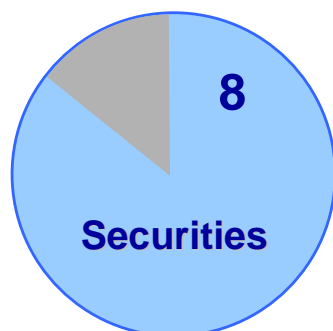
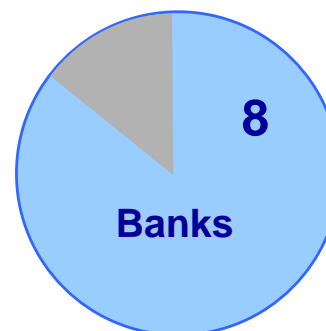
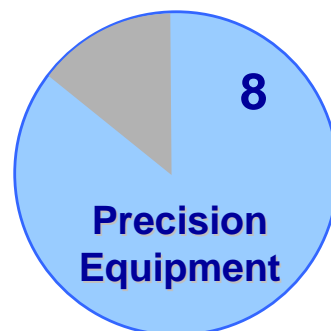
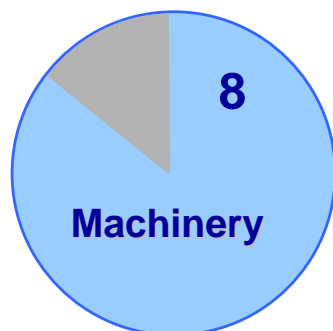
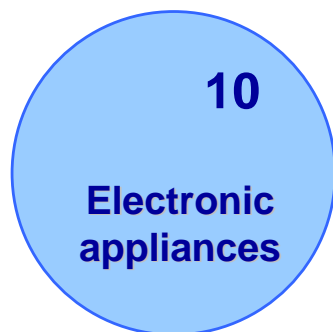
- Network Consultation
- Network Construction (ex. Site-to-Site Network)
- System Construction (ex. On-line security system to B to C)

- Security Solution
- Email Solution
- DDoS Solution
- Data Center
- Web Hosting
- Online Storage
- Network Operation
- SEIL/SMF

- Dedicated Line Internet Connectivity (64kbps ~ Gbps)
- Broadband Connectivity (Best Effort)

# Excellent Blue-chip Client Base

## Penetration rate in Each Industry



- **10 major companies** listed by annual consolidated revenue in each industry.
- Revenue data based on Toyo Keizai Shimpo "Kaisha Shikiho, 3rd edition, 2006" and Nihon Keizai Shimbun "Nikkei Industry Map 2006"



# Representative IIJ Customers

## Enduring Relationship with leading companies

THE DOCUMENT COMPANY  
**FUJI XEROX**

**excite**

**h**  
*hi-ho*

**Q**  
QNet

**NTT** Communications

**plala**

**kabu**  
com

**MOS BURGER.**

**SMBC** 三井住友銀行

**JOMO**

**ドンキホーテ**

**The Asahi Shimbun**  
Japan's Leading National Newspaper | English Edition

The Yomiuri  
Shimbun

Ministry of  
Justice

Ministry of  
Environment

Imperial Household  
Agency

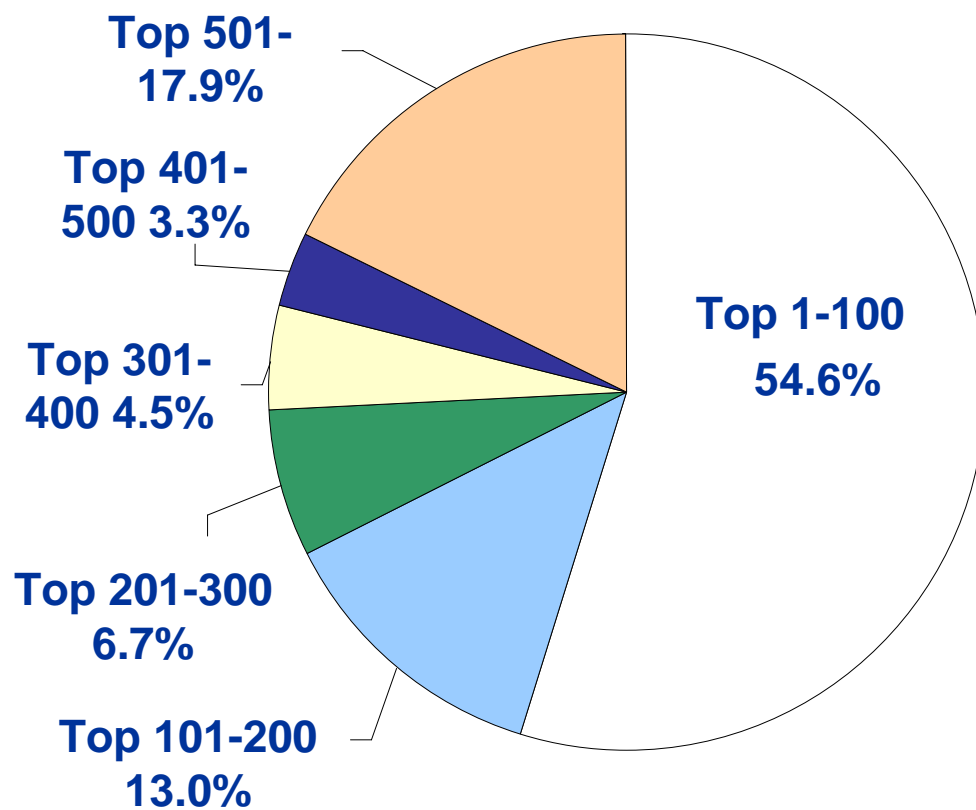
National Police  
Agency

and more...

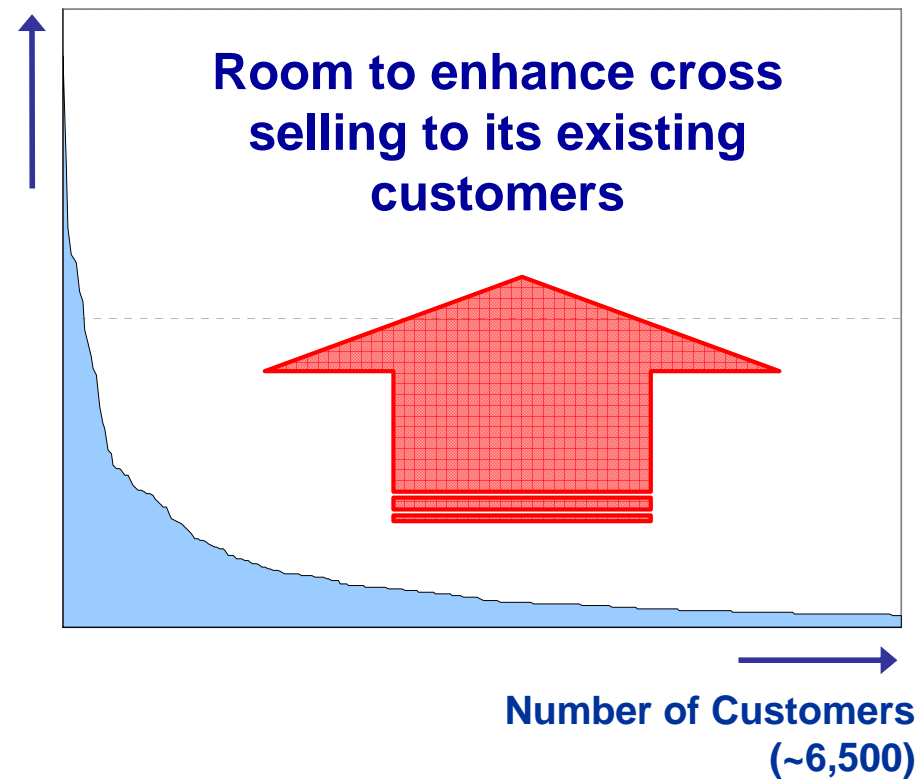
# Enhancing Cross Selling

## Occupation of Total Revenues by Top Customers

## Distribution of Customers by Annual Revenues



(JPY million)

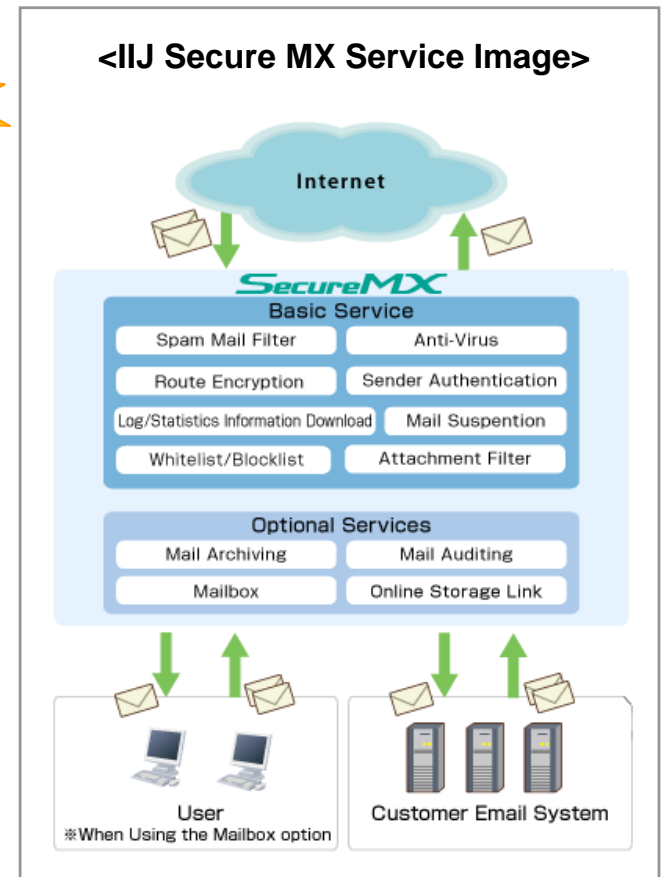
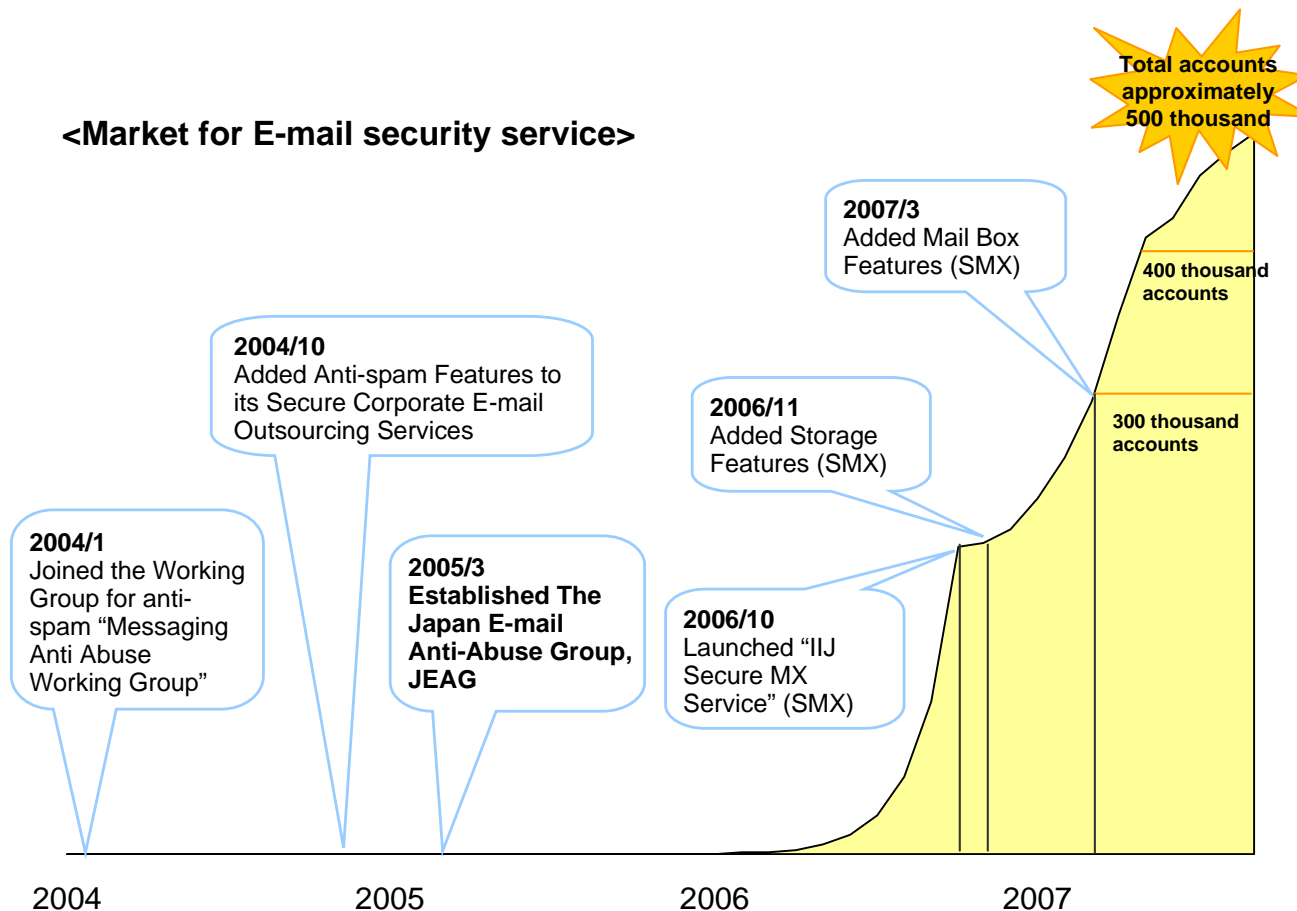


Source: IIJ's non-consolidated data for FY2006

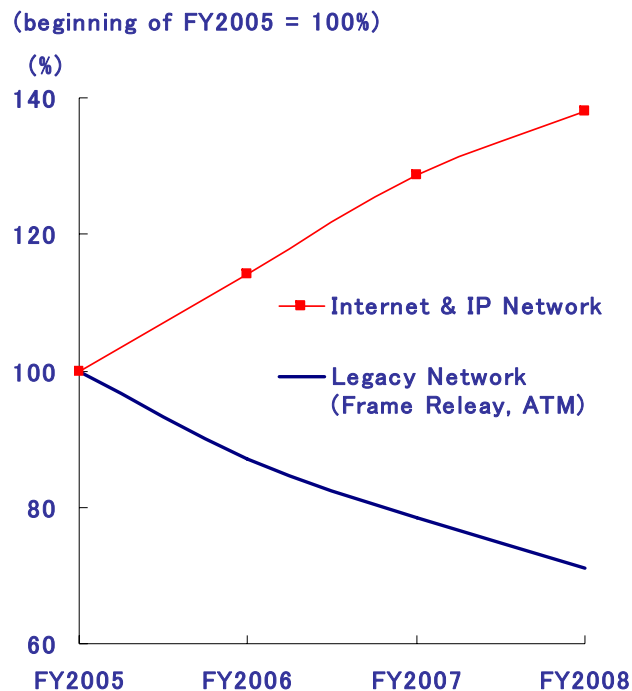
## Service Development before Realize in Demands

- Begun its studies for anti-spam years before service launch
- Growing damage from spam are driving demands for “IIJ Secure MX Service”
- Similar trend in “IIJ DDoS Service”

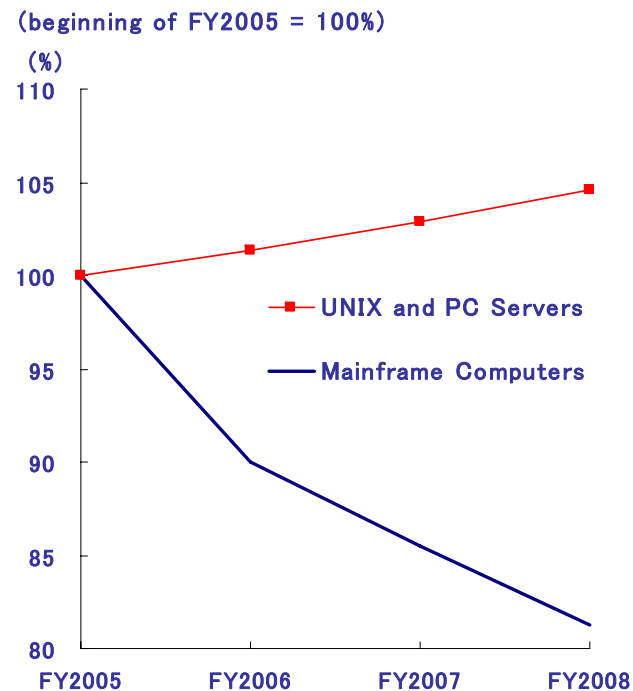
<Market for E-mail security service>



## Expected Growth in IP Network



## Expected Growth in Corporate IT Spending



**From: Legacy Networks by Carrier**



**To: IP Networks**

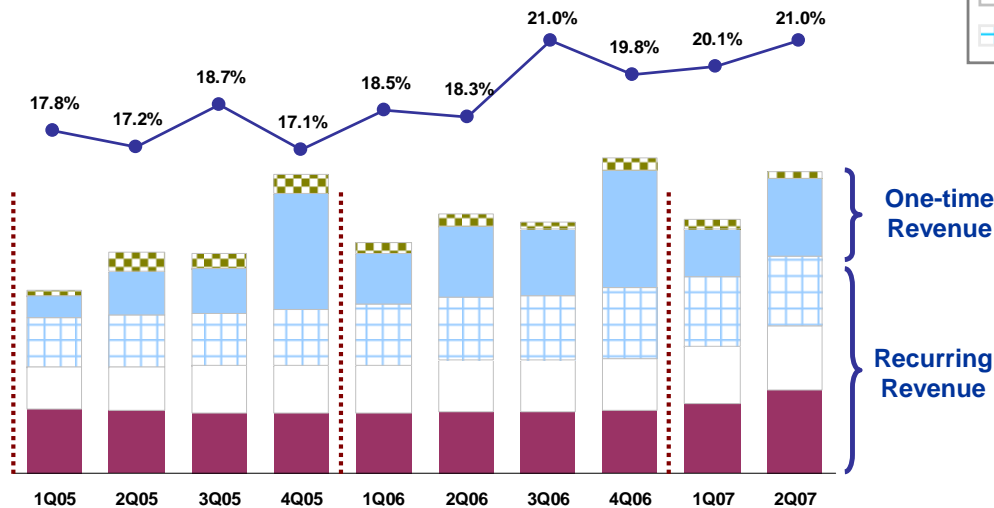
**From: Mainframe by host vendor**



**To: Open System**

# Convincing Revenue and Income Growth

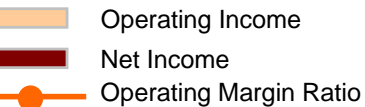
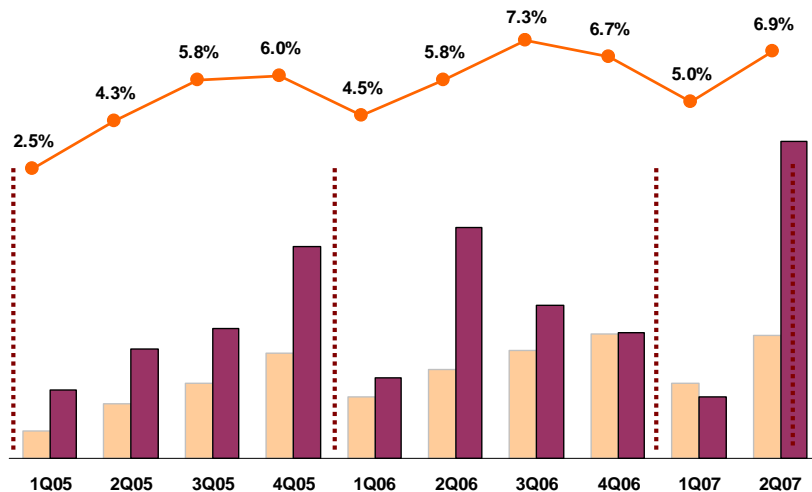
## Revenue



### Growth Trend:

- Continuous growth from Recurring revenues from Internet Connectivity Service, Value-added Service and System Operation
- One time revenues from System Construction are pushing up the overall growth
- Have seasonal fluctuations in SI
- Gross margin ratio continue to improve

## Operating and Net Income



- Operating income grow continuously YoY
- Increasing gross margin from Connectivity and VAS contribute to the improvement in operating income

Figures in Appendix

## IIJ to provide High-quality content delivery platform for “acTVila”

- “acTVila” is a portal site that provides high-definition video for digital television over broadband access lines.
- Established by Sony, Panasonic and three other home electronics company
- IIJ has extensive experience in the streaming distribution market through its CDN Japan distribution platform and a download distribution service that uses P2P technology.
  - ➔ Another step towards providing the best video distribution environment available with IP technology

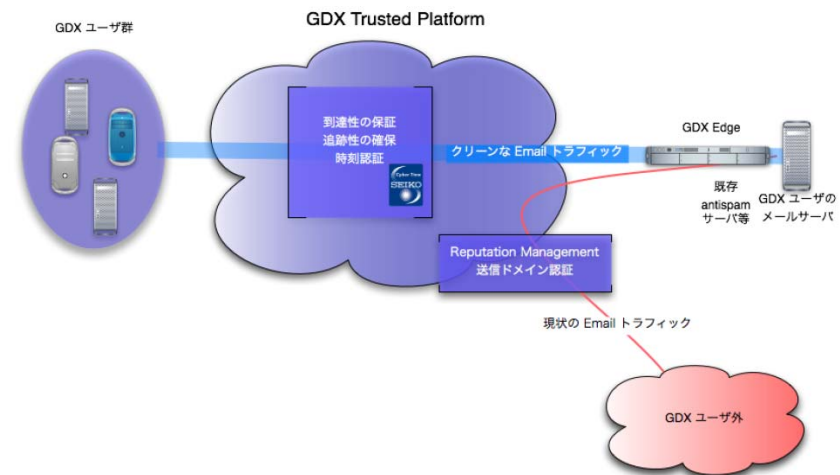


- Content distribution will be done by streaming using **MPEG2/H.264** and will conform to specifications developed by the Digital Television Study Group, a group established primarily by home appliance manufacturers
- A download distribution is also scheduled to be release soon

## “GDx Trusted Platform”

- GDx Japan Inc., IIJ's 51% owned subsidiary
- Established to create a new-generation messaging environment
- Different from the current anti-spam counter measures which are mainly based on filtering technologies, often resulting in the refusal or loss of legitimate business e-mail.

【GDx トラストドプラットフォーム イメージ図】



## IPv6

- R&D for IPv6, Mobile IPv6(MIPv6)
- Necessary study before the run out of IPv4 address
- In Japan, JPNIC announced that IPv4 address would run out by Year 2010  
→ IIJ is and will be ready to lead the new IPv6 Network Environment

# Appendix

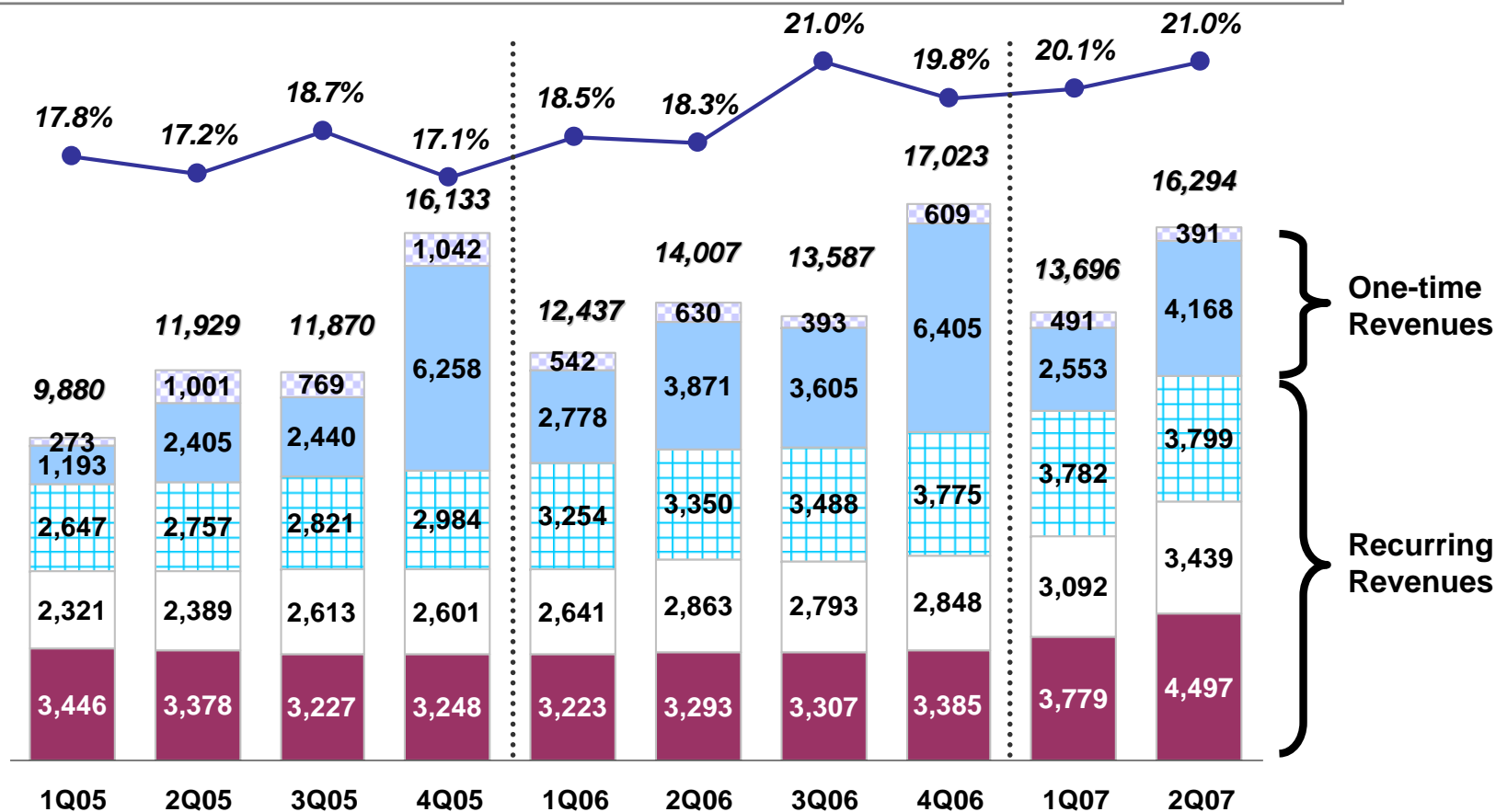
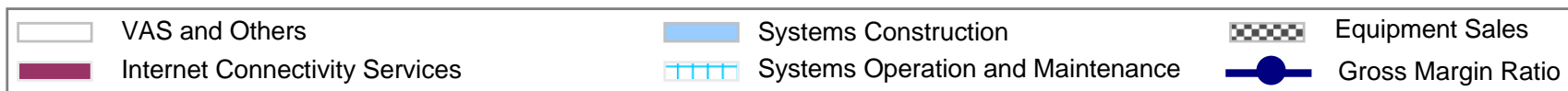


# Consolidated Financial Results for 1H07

Unit: JPY billion excluding net income per share

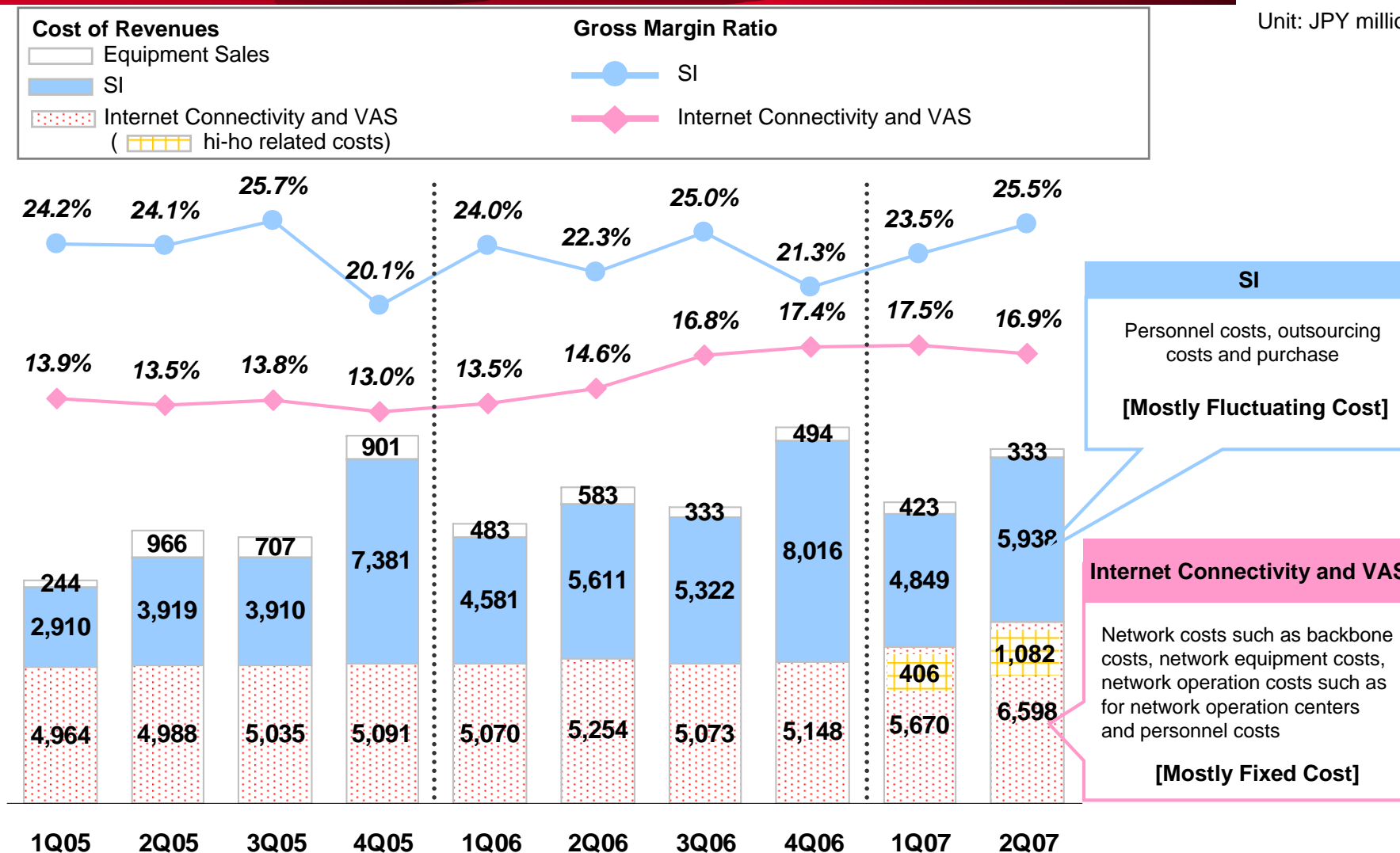
	<i>% of Revenues</i> <b>1H07</b> (2007/4-9)	<i>% of Revenues</i> <b>1H06</b> (2006/4-9)	<b>YoY</b>
Total Revenues	<b>30.0</b>	<b>26.4</b>	<b>13.4%</b>
Total Costs	<i>79.4%</i> <b>23.8</b>	<i>81.6%</i> <b>21.6</b>	<b>10.3%</b>
Gross Margin	<i>20.6%</i> <b>6.2</b>	<i>18.4%</i> <b>4.9</b>	<b>27.1%</b>
SG&A/R&D	<i>14.5%</i> <b>4.4</b>	<i>13.2%</i> <b>3.5</b>	<b>25.0%</b>
Operating Income	<i>6.1%</i> <b>1.8</b>	<i>5.2%</i> <b>1.4</b>	<b>32.5%</b>
Income before Income Tax Benefit	<i>5.7%</i> <b>1.7</b>	<i>8.1%</i> <b>2.1</b>	<b>(20.8%)</b>
Net Income	<i>11.6%</i> <b>3.5</b>	<i>10.8%</i> <b>2.9</b>	<b>21.8%</b>

# Revenues



- ◆ Steady growth in connectivity services for corporate users (up 8.1% YoY) and the additional revenues from hi-ho of JPY 1,419 million contributed to the overall growth for Internet Connectivity Services (up 27.0% YoY).
- ◆ VAS showed steady growth (up 23.0% YoY) as revenues from anti-spam services or data centers etc. grew.
- ◆ Systems Integration ("SI") was up 7.9% YoY. Recurring revenues from systems operation and maintenance continued to grow. Systems construction projects are becoming larger in scale to be completed in the latter half of FY2007.
- ◆ Gross margin ratio was 21.0% in 2Q07, up 2.7 points from 2Q06.

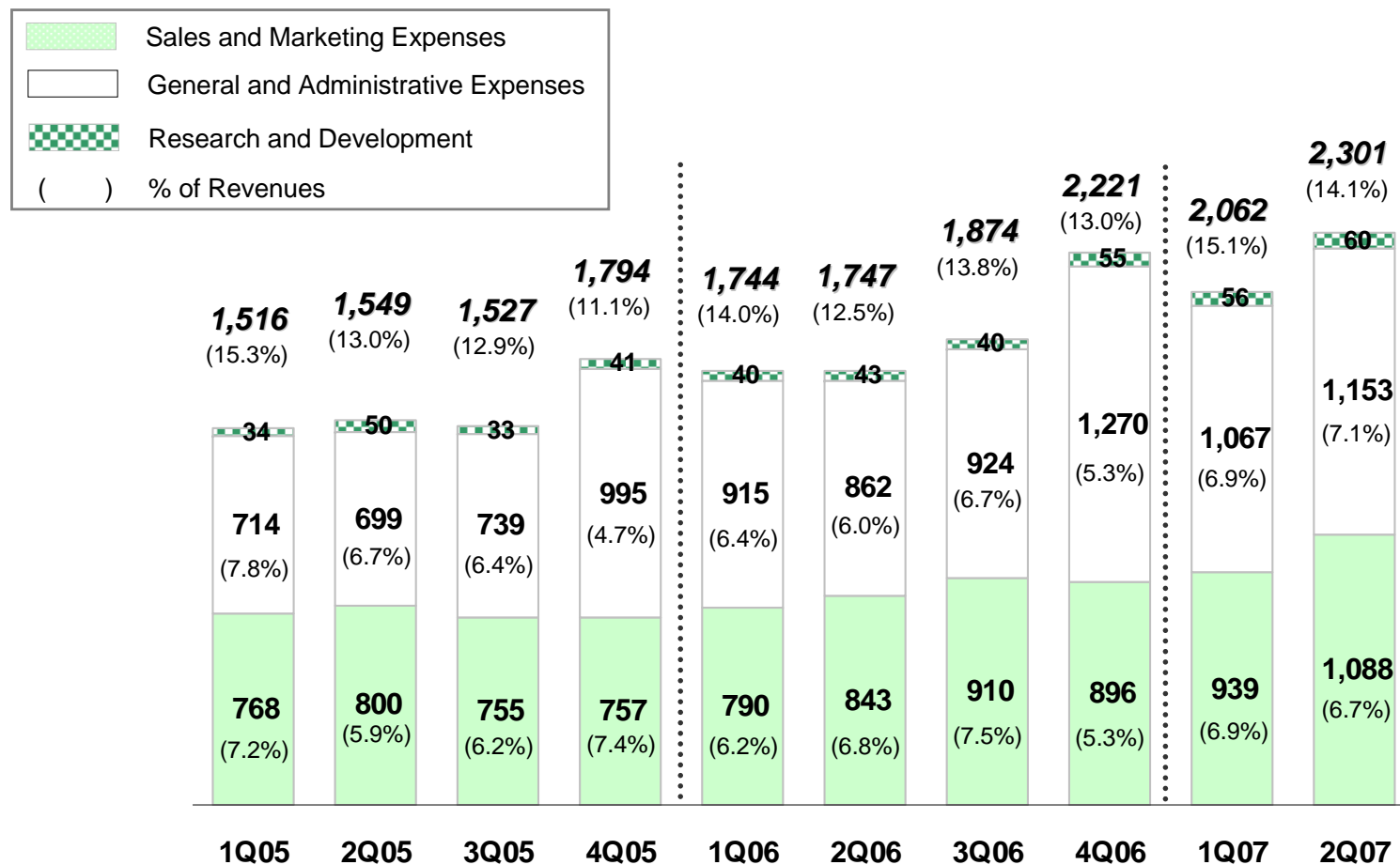
# Cost of Revenues and Gross Margin Ratio



◆ Cost of Connectivity Service and VAS revenues: Increased by 18.8% YoY in 1H07. Additional cost from hi-ho, we acquired on June 1st 2007 was JPY 1,488 million.

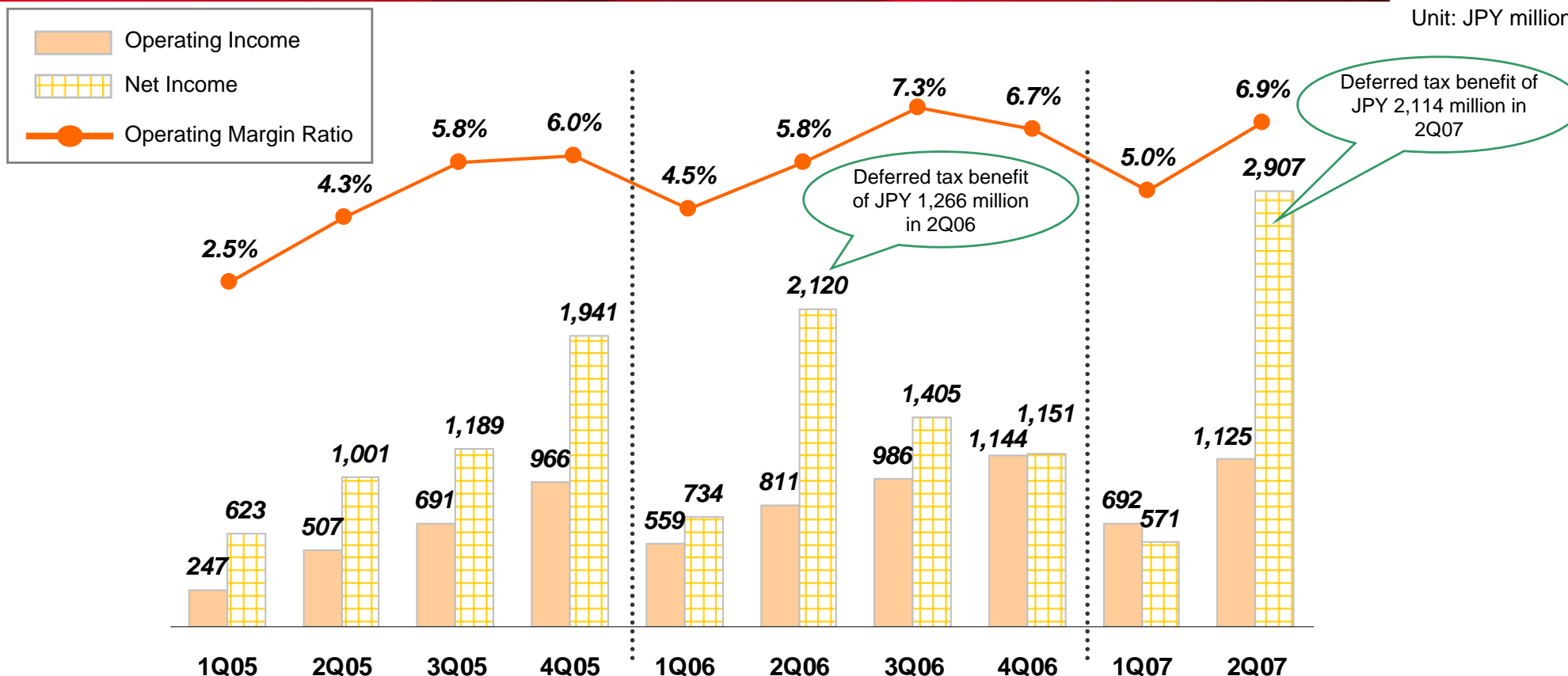
◆ Cost of SI revenues: Increased by 5.8% YoY in 1H07, due to an increase in personnel costs, outsourcing costs and purchase.

# SG&A Expenses/R&D



- ◆ Sales and Marketing Expenses (JPY 2,027 million, up 24.2% YoY in 1H07)  
Growth in personnel related and advertising expenses, and the addition from hi-ho related sales and marketing expense of JPY 184 million from June 1, 2007.
- ◆ General and Administrative Expenses (JPY 2,220 million, up 24.9% YoY in 1H07)  
Growth in personnel related expenses, and an increase in rent expenses due to increase in office space affected by business growth.

# Operating and Net Income



◆ Operating Income: JPY 1,816 million for 1H07 (up 32.5% YoY) as gross margin from connectivity and VAS, and SI grew steadily.

◆ Net Income:

- Other Income (expense) decreased to other expense of JPY 119 million as gains from sales of available-for-sale securities decreased to JPY 214 million compared to JPY 925 million in 1H06.
- Income tax benefit was JPY 1,805 million compared to the benefit of JPY 960 million in 1H06 mainly because of deferred tax benefits of JPY 1,970 million resulting from a revision of valuation allowance against deferred income tax assets.
- Minority interest in losses of subsidiaries in 1H07 was JPY 24 million, affected by the elimination of minority interests related to our 4 consolidated subsidiaries wholly owned by us, after we made our two subsidiaries, IIJ-Tech and Net Care, wholly owned through the share exchanges in May 2007. Minority interest in losses of subsidiaries were related to GDx.
- Equity in net loss of equity method investees in 1H07 was JPY 49 million, mainly affected by Internet Revolution Inc.

# Consolidated Balance Sheets

	September 30, 2007	March 31, 2007	Changes
Cash	11,670	13,555	(1,885)
Accounts Receivable	9,107	9,676	(568)
Inventories	1,878	1,111	+767
Prepaid Expenses	1,736	1,053	+682
Available-for-sale Securities	1,043	1,310	(266)
Property and Equipment	11,301	9,832	+1,468
Intangible Assets	5,817	2,877	+2,940
Other Assets	4,478	3,260	+1,217
Borrowings (Short-term)	10,650	6,340	+4,310
Accumulated Deficit	(21,100)	(24,271)	+3,171
Accumulated Other Comprehensive Income	440	950	(509)
Total Shareholders' Equity	23,786	20,112	+3,674
<b>Total Assets</b>	<b>53,238</b>	<b>47,693</b>	<b>+5,545</b>

Increased as on-going SI projects increased

Increase in maintenance expenses for SI projects

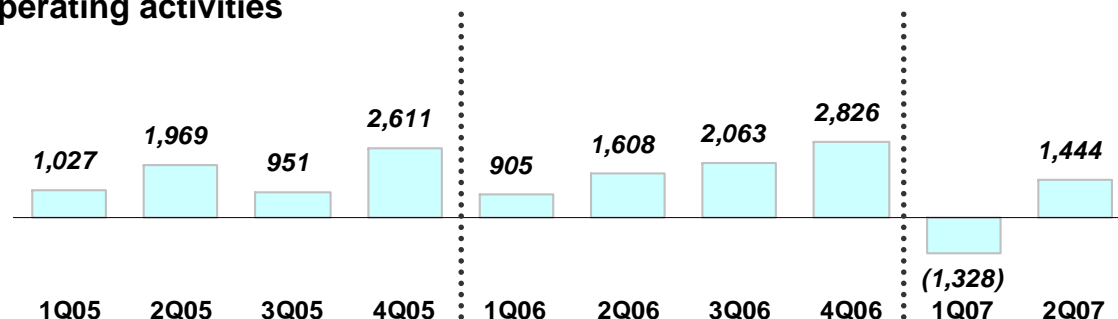
Acquisition of hi-ho and an increase in property for us and to provide services to our customers

Recording of intangible assets of JPY 2,302 million related to acquisition of subsidiary shares and JPY 659 million related to our acquisition of hi-ho (includes amortizable intangible assets of JPY 289 million).

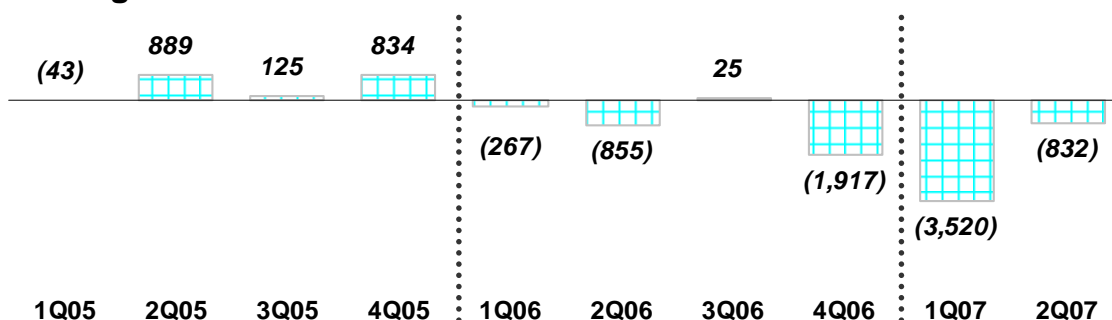
Increase in short-term borrowings of JPY 4,310 million for the acquisition of subsidiary shares from minority shareholders

# Consolidated Cash Flows

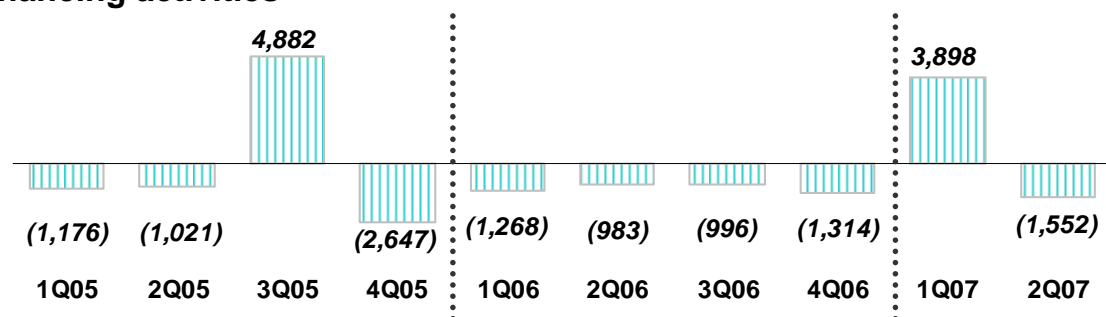
## Net cash provided by (used in) operating activities



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



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



Net cash provided by operating activities was JPY 117 million in 1H07.

- Operating income grew in both 1Q07 and 2Q07 due to the growth in recurring revenues from connectivity and VAS
- 1Q: Recorded net cash used in operating activities of JPY 1,328 million due to payments for inventories and pre-paid expenses related to on-going SI projects, a decrease in accounts payable related to SI projects completed in 4Q06 and payments of income tax.
- 2Q: Recorded net cash provided by operating activities of JPY 1,444 million as effect from changes in operating assets and liabilities weakened.

Net cash used in investing activities was JPY 4,352 million in 1H07.

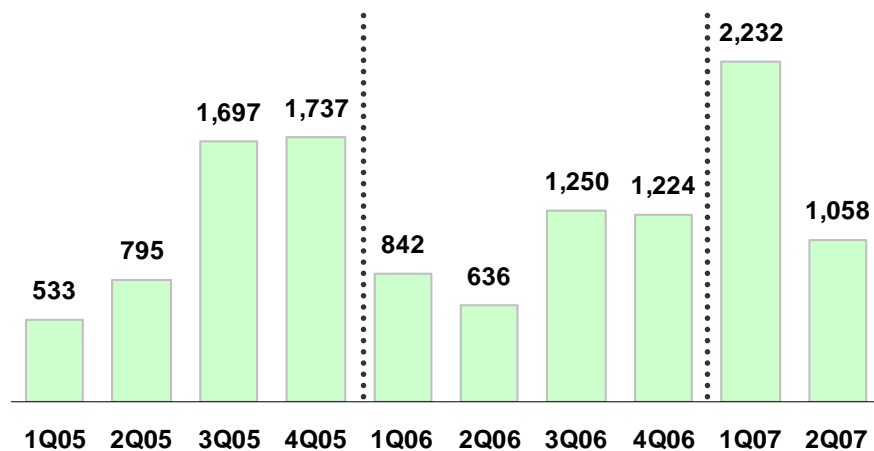
- 1Q: acquisition of shares of consolidated subsidiaries from minority shareholders of JPY 1,975 million, JPY 912 million for the acquisition of hi-ho and purchase of property and equipment of JPY 570 million
- 2Q: purchase of property and equipment of JPY 422 million and investment in an equity method investee of JPY 250 million

Net cash used in financing activities was JPY 2,346 million in 1H07.

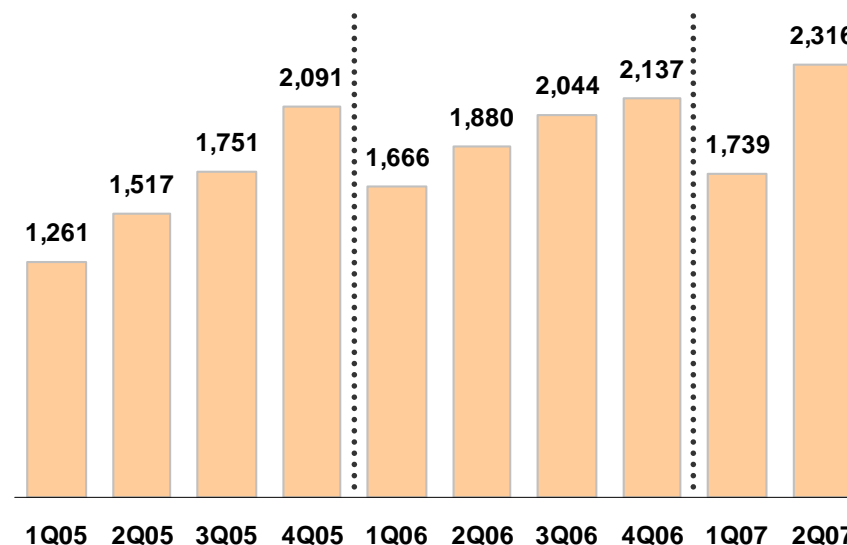
- Borrowing of JPY 4,310 million for 1H07 including short-term borrowings for the acquisition of the two consolidated subsidiaries.
- Principal payments under capital leases of JPY 1,658 million
- Dividend Payments of JPY 306 million

# Other Financial Data (CAPEX etc.)

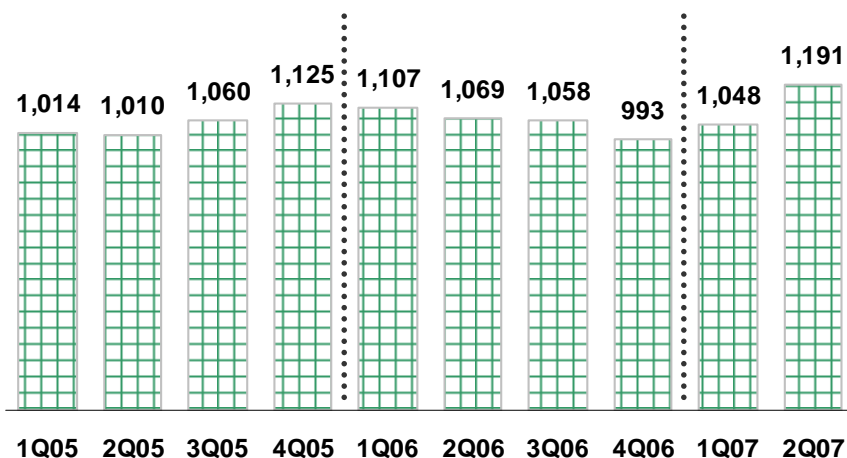
## CAPEX



## Adjusted EBITDA



## Depreciation and Amortization





# Financial Target for FY2007

Unit: JPY billion excluding net income per share and cash dividend per share

	<i>% of Total Revenues</i> <b>FY2007 Target</b> (2007/4-2008/3)	<i>% of Total Revenues</i> <b>FY2006 Actual</b> (2006/4-2007/3)	<b>YoY</b>
<b>Total Revenues</b>	<b>69.0</b>	<b>57.1</b>	<b>+ 20.9%</b>
<b>Operating Income</b>	6.7% <b>4.6</b>	6.1% <b>3.5</b>	<b>+ 31.4%</b>
<b>Income before Income Tax Expense (Benefit)</b>	7.4% <b>5.1</b>	8.8% <b>5.0</b>	<b>+ 1.0%</b>
<b>Net Income</b>	8.1% <b>5.6</b>	9.5% <b>5.4</b>	<b>+ 3.5%</b>
<b>Net Income per Share</b>	<b>JPY 27,122</b>	<b>JPY 26,519</b>	<b>+ 2.3%</b>
<b>Cash Dividend per Share</b>	<b>Annual JPY 1,500</b> (Interim Period JPY 750 End of Year JPY 750)	<b>Annual JPY 1,500</b>	<b>—</b>