Consolidated Financial Results for 1Q FY2019

We changed our accounting principles from the Generally Accepted Accounting Principles in the U.S. (“U.S. GAAP”) to the International Financial Reporting Standards (IFRS) from the filing of FY2018 annual report “Yuka-shoken-houkokusho” which was filed on June 28, 2019.

Because reporting period of foreign consolidated subsidiaries under IFRS is different from that of under U.S. GAAP, some figures disclosed in the past are different.

IIJ
Internet Initiative Japan

Internet Initiative Japan Inc.
TSE1 (3774)
August 7, 2019

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Agenda

Ⅰ. Summary of 1Q19 Financial Results

Ⅱ. Consolidated Financial Results for 1Q19

Ⅲ. Other Information

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Ⅰ. Summary of 1Q19 Financial Results

% =Year over Year (YoY) comparison

Solid business developments & strong earnings along with favorable demand

Total Revenues JPY49.8 billion +11.1%

Operating Profit JPY1.4 billion +58.8%(*)

(*) The growth rate shows the comparison for the normalized 1Q18 operating profit which is calculated by allocating JPY2.05 billion of additional NW service cost recorded in 4Q18 as a result of NTT Docomo's mobile interconnectivity unit charge revision to attributable each quarter of FY2018

◆Enhancement of enterprise NW service development

Enterprise recurring revenue*(excluding WAN) continued to grow: +8.9%

*Enterprise recurring revenue is calculated by subtracting revenues of WAN, MVNE and consumers from recurring revenue

- **Expansion of Full-MVNO & IoT service lineups**
  - First in Japan to launch eSIM services (July), Developing and preparing to launch eSIM services for enterprises
  - SoftSIM (May), Services to visualize and monitor IoT data (July) etc.
- **Execution of Multi cloud strategy: Cloud revenue +10.7%**
  - Adding connecting points for multi cloud: AWS, MS, Google
  - IIJ Omnibus Service's function expansion: optimizing route control when accessing SaaS such as MS Office365
- **Strong demands continue for Security: Revenue +20.0% Each service grew such as SOC, DDoS Protection**
- **CDN: Providing Internet live platform for "Virtual High School Baseball Championship" 5 years in a row**
- **JOCDN: Data migration of a large contents holder is approximately 80% completed**

◆Gross profit for both NW & SI started with improving trend

- **NW gross profit +14.0%, +JPY0.6 billion YoY(*) with recurring revenue accumulation & rebound effect of Full-MVNO profitability improvement by increasing its revenue against its fixed cost**
- **SI gross profit +23.3%, +JPY0.4 billion YoY with continuing effect of FY18 profitability improvement strategies**

◆DeCurret, new company for digital currency trading and settlement business, raised capital by private placement

- **Expect even stronger synergy with enterprise shareholders**
- **11 new shareholders: KDDI, Konami, Sumitomo Life, Daido Life, Meiji Yasuda Life, Chubu Electric Power, Hankyu Hanshin Holdings, Matsui Securities, Energia Communications, ALSOK, Toppan Printing**
- **IIJ ownership 30%, Total enterprise shareholders 30** (including IIJ)**, Capital raised to JPY8.63 billion** (including capital reserve)

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Ⅱ - 1. Consolidated Financial Results for 1Q19

Unit: JPY billion

	1Q19 Results Apr. 2019 - Jun. 2019	% of Revenues	1Q18 Adjusted Results (*1) [1Q18 Results] Apr. 2018 - Jun. 2018	% of Adjusted Revenues [% of Revenues]	Compared to 1Q18 Adjusted Results [Compared to 1Q18 Results]	1H19 Targets Apr. 2019 - Sep. 2019	% of Revenues	FY19 Targets Apr. 2019 - Mar. 2020	% of Revenues
Revenues	49.8		44.8		+11.1%	97.7		204.0	
Cost of Sales	42.4	85.2%	38.5 [38.0]	85.8% [84.8%]	+10.3% [+11.7%]	83.5	85.5%	172.6	84.6%
Gross Profit	7.4	14.8%	6.3 [6.8]	14.2% [15.2%]	+16.3% [+8.1%]	14.2	14.5%	31.4	15.4%
SG&A etc. (*2)	6.0	12.0%	5.5	12.2%	+9.5%	12.0	12.3%	24.4	12.0%
Operating Profit	1.4	2.8%	0.9 [1.4]	1.9% [3.0%]	+58.8% [+2.2%]	2.2	2.3%	7.0	3.4%
Profit before tax	1.4	2.7%	0.9 [1.4]	2.1% [3.2%]	+45.2% [-3.9%]	1.5	1.5%	6.3	3.1%
Net Profit (*3)	0.8	1.6%	0.5 [0.9]	1.2% [1.9%]	+42.9% [-11.1%]	0.6	0.6%	3.5	1.7%

(*1) Adjusted results is calculated by allocating JPY2.05 billion of additional NW service cost recorded in 4Q18 as a result of NTT Docomo's mobile interconnectivity unit charge revision (March 2019) to attributable each quarter of 1Q19. For details, please refer to page 5 of this presentation material.
(*2) SG&A etc. shows the sum of SG&A, which includes R&D expenses, and other income/expenses.
(*3) Net profit is "Profit for the period/year attributable to owners of the parent"

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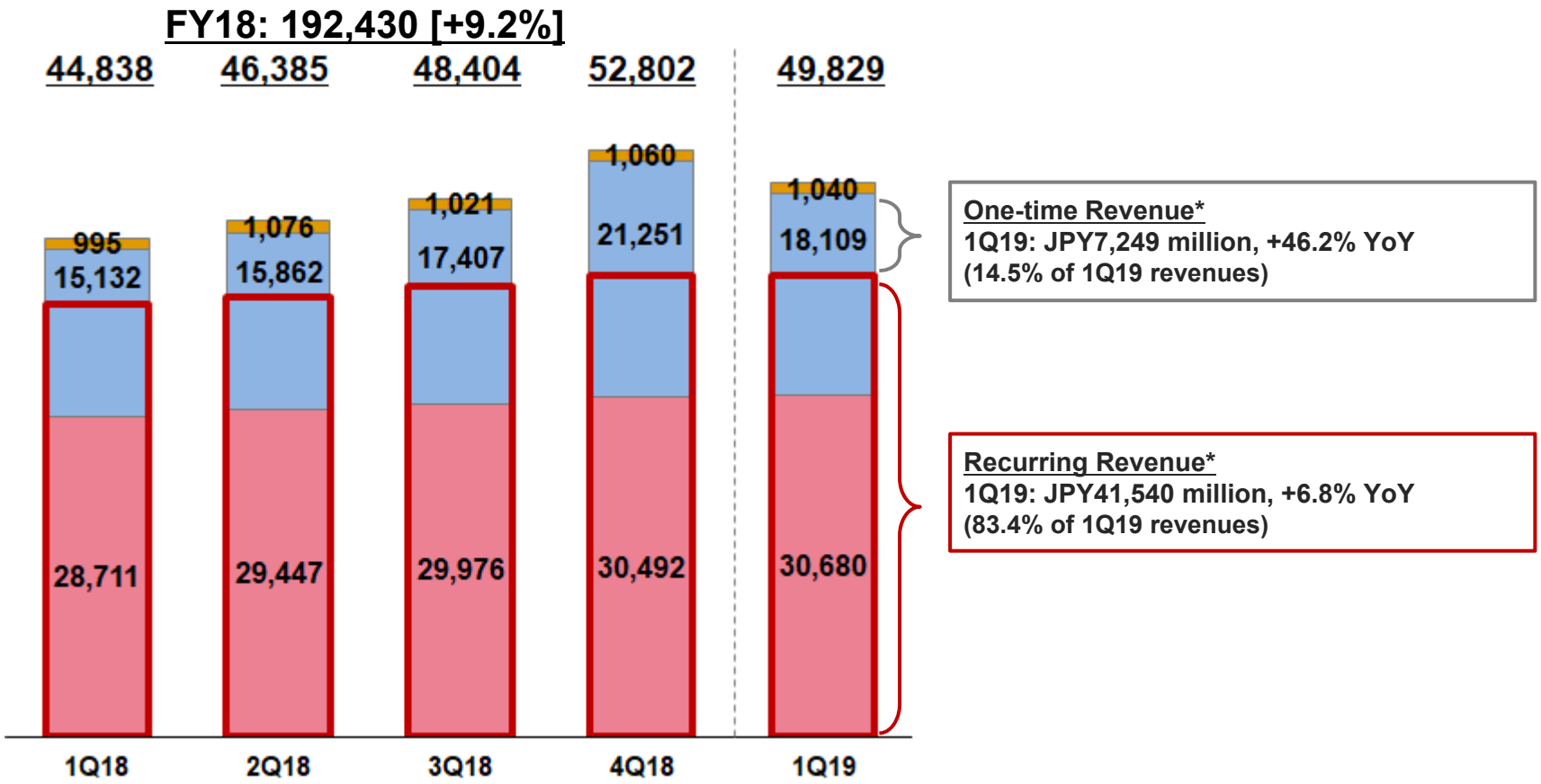
Ⅱ - 2. Revenues

Unit: JPY million
[ ] , YoY = Year over year comparison

NW Services
- Internet Connectivity Services (Enterprise)
- Internet Connectivity Services (Consumer)
- Outsourcing Service
- WAN Service

Systems Integration (SI)
- Systems Construction (including equipment sales)
- Systems Operation and Maintenance

ATM Operation Business



One-time Revenue*
1Q19: JPY7,249 million, +46.2% YoY
(14.5% of 1Q19 revenues)

Recurring Revenue*
1Q19: JPY41,540 million, +6.8% YoY
(83.4% of 1Q19 revenues)

* One-time revenue, systems construction revenues which includes equipment sales, is mainly recognized when systems or equipment are delivered and accepted by customers

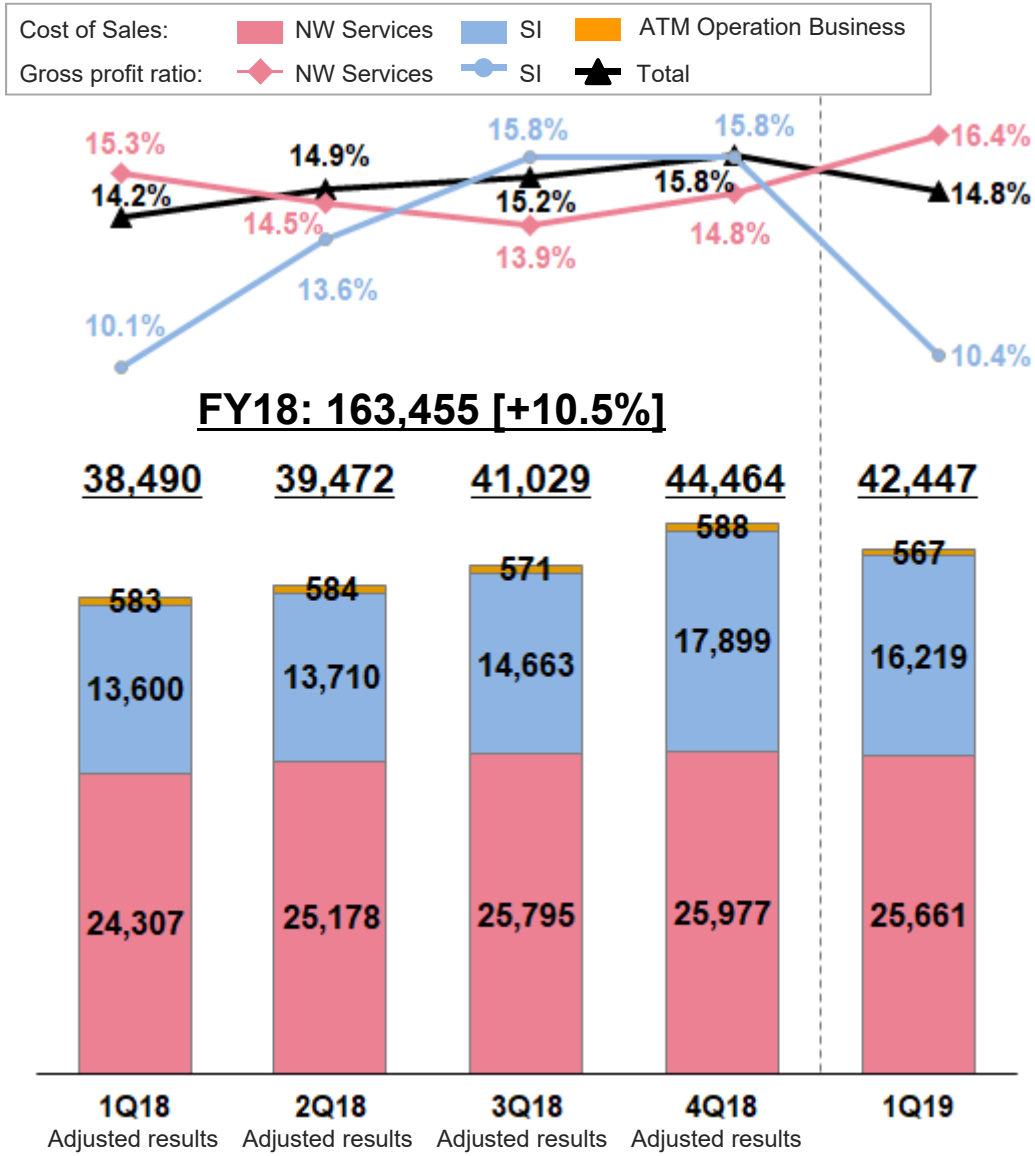
* Recurring revenue represent the following monthly recurring revenues: Internet Connectivity Services for Enterprise, Internet Connectivity Services for Consumer, Outsourcing Services, WAN Services, and Systems Operation and Maintenance

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Ⅱ - 3. Cost of Sales & Gross Profit Ratio

Unit: JPY million

[ ], YoY = Year over year comparison



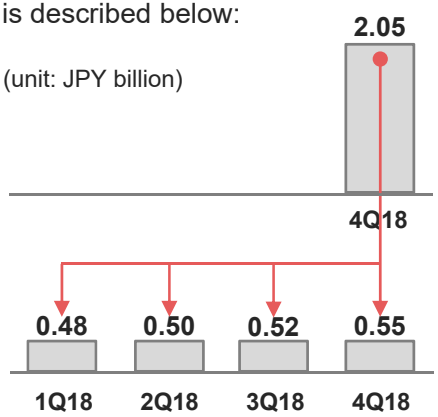
Gross profit

◆ **Total**

- 1Q19: JPY7,382 million
  +16.3% YoY from 1Q18 adjusted results

◆ **NW Services**

- 1Q19: JPY5,019 million
  +14.0% YoY from 1Q18 adjusted results
  - Allocation of JPY2.05 billion, additional NW service cost recorded in 4Q18 as a result of NTT Docomo's mobile interconnectivity unit charge revision, to attributable each quarter of FY2018 is described below:



  - Full-MVNO related fixed cost increased by over JPY0.3 billion per quarter (from Mar. 2018)

◆ **SI**

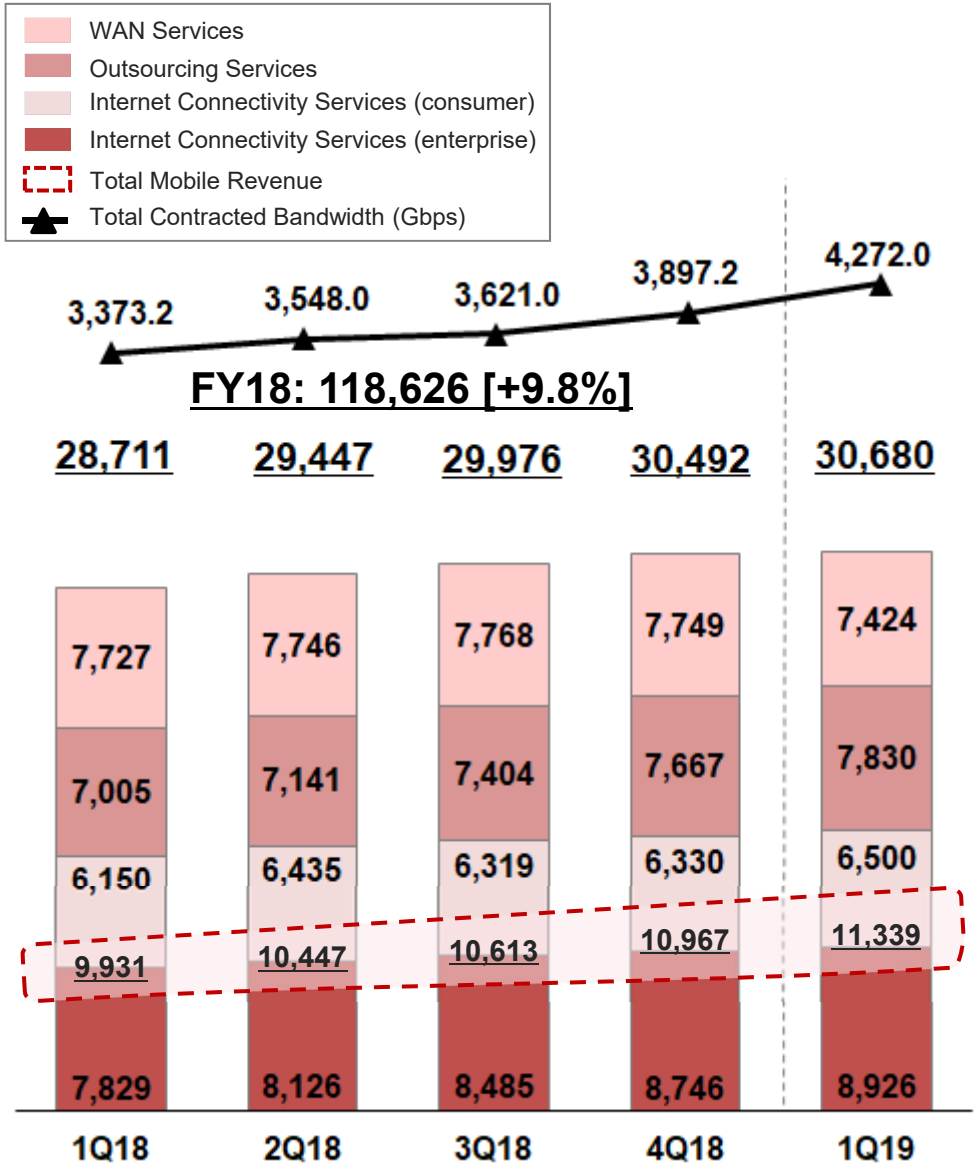
- 1Q19: JPY1,890 million, +23.3% YoY

- Adjusted results are calculated by allocating JPY2.05 billion of additional NW service cost recorded in 4Q18 as a result of NTT Docomo's mobile interconnectivity unit charge revision to attributable each quarter of FY2018. FY2018 figures disclosed in this presentation material from this page reflect such adjustment
- SI includes equipment sales

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Ⅱ - 4. Network Services (1) Revenues

Unit: JPY million
[ ], YoY =Year over year comparison
QoQ = 1Q19 compared to 4Q18



NW Services Revenues

◆**Internet Connectivity (Enterprise)**

- 1Q19: +14.0% YoY, +2.1% QoQ
  - Mobile revenue continued to increase
    - ✓ 1Q19-end total subscriptions: 2,786 thousand (up 342 thousand YoY)
    - ✓ 1Q19-end MVNE clients: 152 (+9 clients YoY)
    - ✓ IP services and others achieved YoY growth with no significant pricing pressure from clients: IP services +2.2% YoY

◆**Internet Connectivity (Consumer)**

- 1Q19: +5.7% YoY, +2.7% QoQ

◆**Outsourcing Services**

- 1Q19: +11.8% YoY, +2.1% QoQ
  - Strong demands for Security and Omnibus
    - ✓ 1Q19 Security revenue: +20.0% YoY
    - ✓ 1Q19 Omnibus revenue: +51.4% YoY

◆**WAN Services**

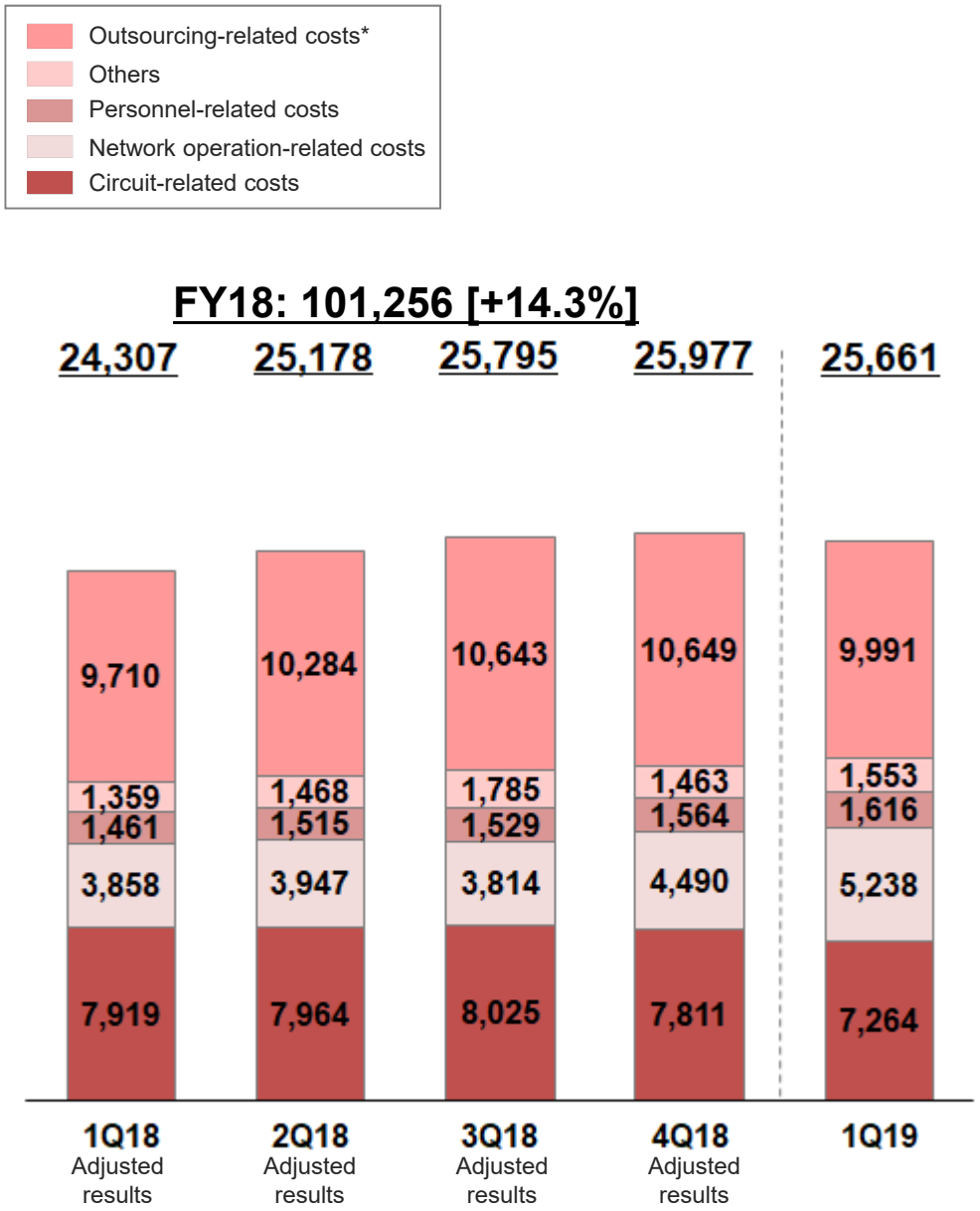
- 1Q19: -3.9% YoY, -4.2% QoQ
  - FY19 revenue is expected to decrease by approx. JPY4.0 billion YoY, due to existing large clients migrating to mobile.

- Total contracted bandwidth is calculated by multiplying number of contracts by contracted bandwidths respectively for IP service (including data center connectivity service) and IIJ FiberAccess/F and IIJ DSL/F of Internet connectivity services (Enterprise).

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Ⅱ - 4. Network Services (2) Cost of Sales

Unit: JPY million
[ ] , YoY =Year over year comparison
QoQ = 1Q19 compared to 4Q18



Cost of NW Services

- 1Q19: +5.6% YoY, -1.2% QoQ from 1Q18 adjusted results, respectively
- Along with changes in accounting for operating lease from 1Q19, data center rent costs were reclassified from outsourcing-related costs to network operation-related costs (depreciation of assets)

◆ **Regarding NTT DOCOMO's ("Docomo") mobile interconnectivity cost recognition:**

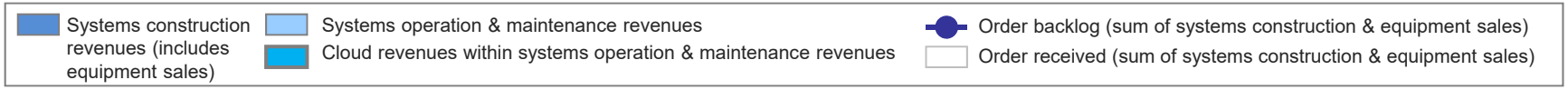
- Regarding our FY18 & FY17 usage charge, Docomo's mobile interconnectivity telecommunications charge was fixed in Mar. 2019 and it decreased by 5.0% YoY As for FY18, we recorded JPY2.05 billion of additional network services cost as a difference between our estimate (14% decrease) and actual (5.0% decrease)
- Regarding our FY17& FY16 usage charge, Docomo's mobile interconnectivity telecommunications charge was fixed in Mar. 2018 and it decreased by 18.2% YoY As for FY17, we recorded JPY0.89 billion of positive cost reduction impact as a difference between our estimate (14% decrease) and actual (18.2% decrease)
- Regarding our FY19 & FY18 usage charge, Docomo's unit charge is expected to be revised in Mar. 2020. Docomo's payment arrangement is 5% off temporarily from Apr. 2019
- In FY19, we estimate a certain decrease for the unit charge by considering decrease rate fixed in Mar. 2019 and FY18 Docomo cost trends, and apply our own decrease rate to recognize costs quarterly

* Outsourcing-related costs include interconnectivity charge for mobile infrastructure and customer support center operation costs etc.

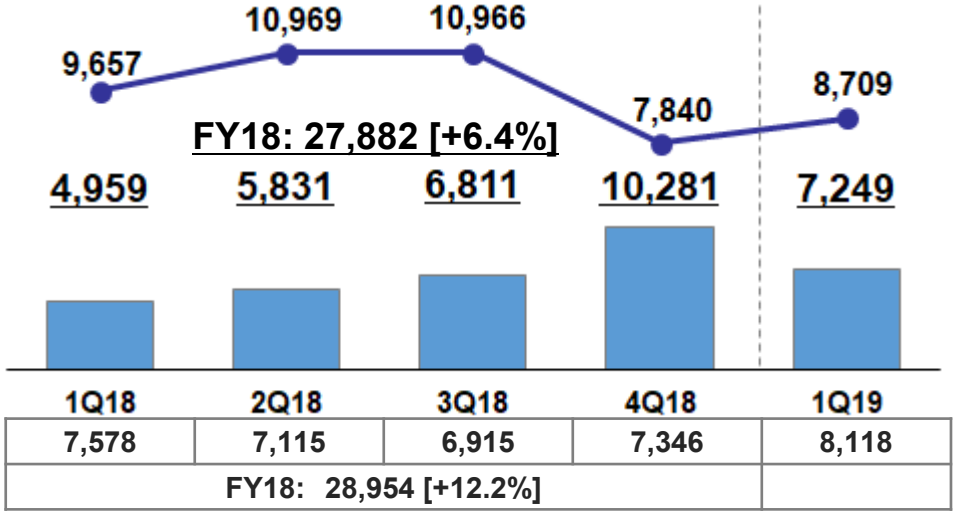
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Ⅱ - 5. Systems Integration (SI) (1) Revenues

Unit: JPY million
[ ], YoY = Year over year comparison
QoQ = 1Q19 compared to 4Q18



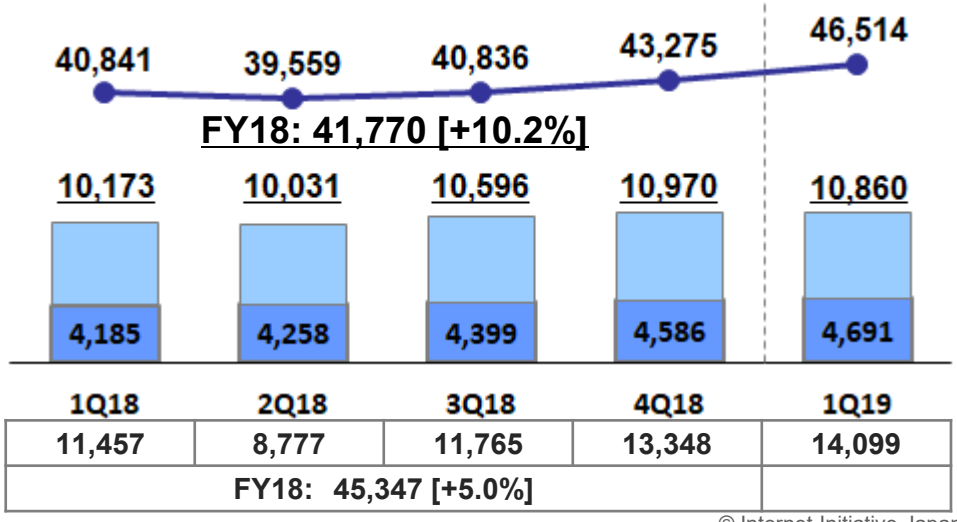
Systems Construction (one-time revenue)



1Q18	2Q18	3Q18	4Q18	1Q19
7,578	7,115	6,915	7,346	8,118
FY18: 28,954 [+12.2%]				

- 1Q19 revenue: +46.2% YoY
  - Revenue growth includes JPY1.34 billion of revenue recognition due to percentage-of-completion method
- 1Q19 order received: +7.1% YoY
  - Favorable systems construction order environment continued
- Large-scale construction orders received in 1Q19:
  - Home page renewal for a central government agency
  - Security monitoring for a major telecommunications service provider
  - Office work IT environment for a prominent real estate agency
  - Virtual desktop environment for a prominent amusement park operator etc.

Systems Operation & Maintenance (recurring revenue)



1Q18	2Q18	3Q18	4Q18	1Q19
11,457	8,777	11,765	13,348	14,099
FY18: 45,347 [+5.0%]				

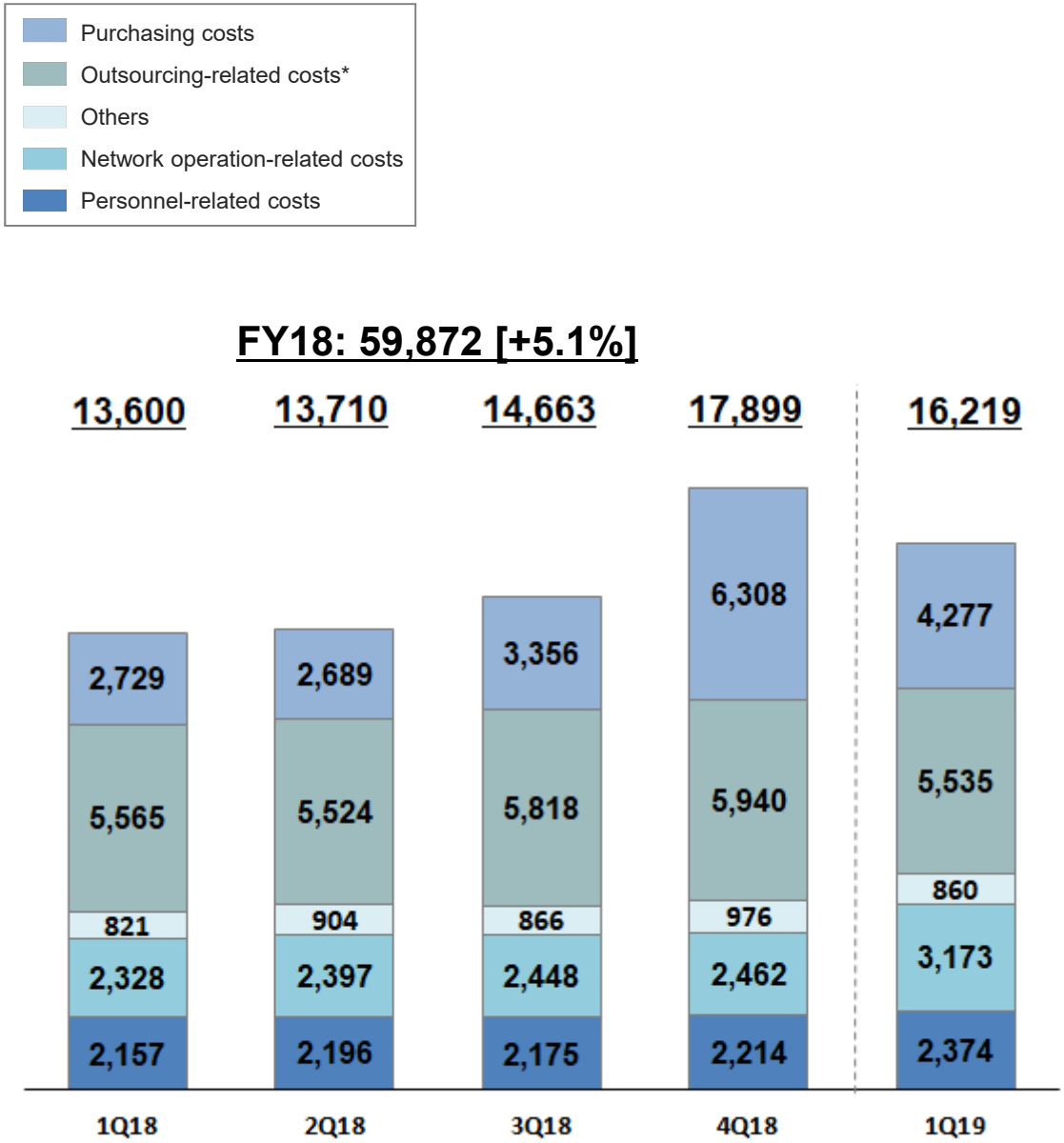
- 1Q19 revenue: +6.8% YoY
- Continuous revenue growth mainly due to the accumulation of systems construction which are migrated to systems operation & maintenance phase as well as continuous increase in private cloud revenue
  - 1Q19 revenue from private cloud: +12.1% YoY
  - 1Q19 revenue from SI construction: +3.0% YoY

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Ⅱ - 5. Systems Integration (SI) (2) Cost of Sales

Unit: JPY million

[ ] , YoY = Year over year comparison
QoQ = 1Q19 compared to 4Q18



*Outsourcing-related costs include SI project-related outsourcing personnel costs

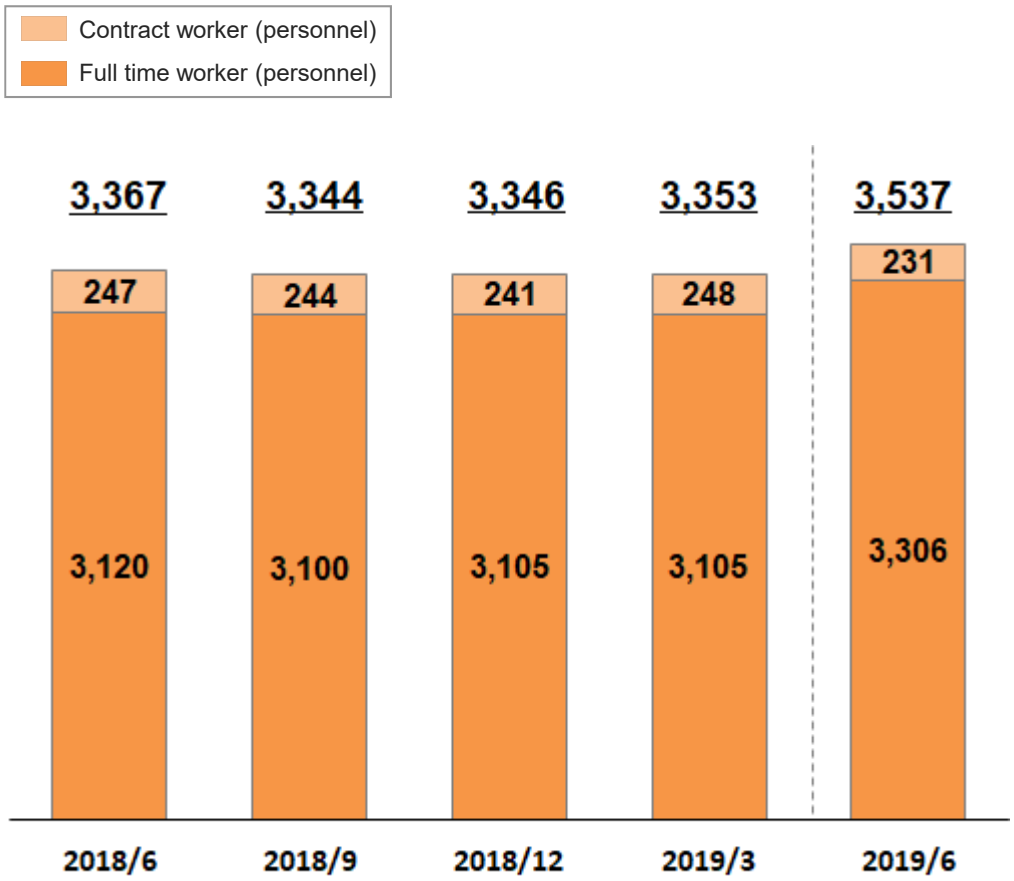
Cost of SI

- 1Q19: +19.3% YoY
  - 1Q19-end number of SI-related outsourcing personnel: 1,075 personnel (increased by 36 personnel YoY, decreased by 27 personnel QoQ)
  - SI-related outsourcing personnel and costs decreased QoQ. Outsourcing-related and personnel-related costs tend to increase along with increase in projects
- System engineers productivity rate continue to be stable, following the trend of gross profit improvement in FY18
- Along with changes in accounting for operating lease from 1Q19, a portion of systems operation and maintenance costs such as outsourcing were reclassified from outsourcing-related costs to network operation-related costs (depreciation of assets)

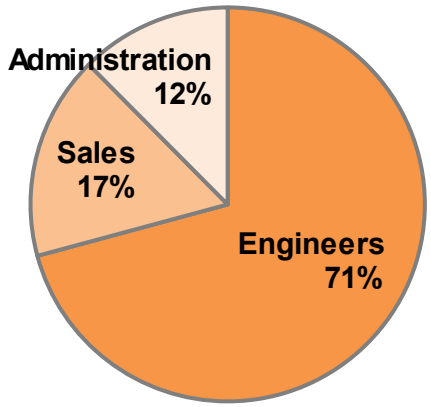
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Ⅱ - 6. Number of Employees

YoY = Year over year comparison



Employee Distribution



- Hired 171 new graduates in Apr. 2019 (175 in Apr. 2018, 148 in Apr. 2017)
- FY19 net addition of employees is planned to be approx. 230.
- Incremental volume of FY19 annual personnel-related costs and expenses is expected to be larger than usual level due to revision of personnel remuneration structure, etc.

Personnel-related costs & expenses

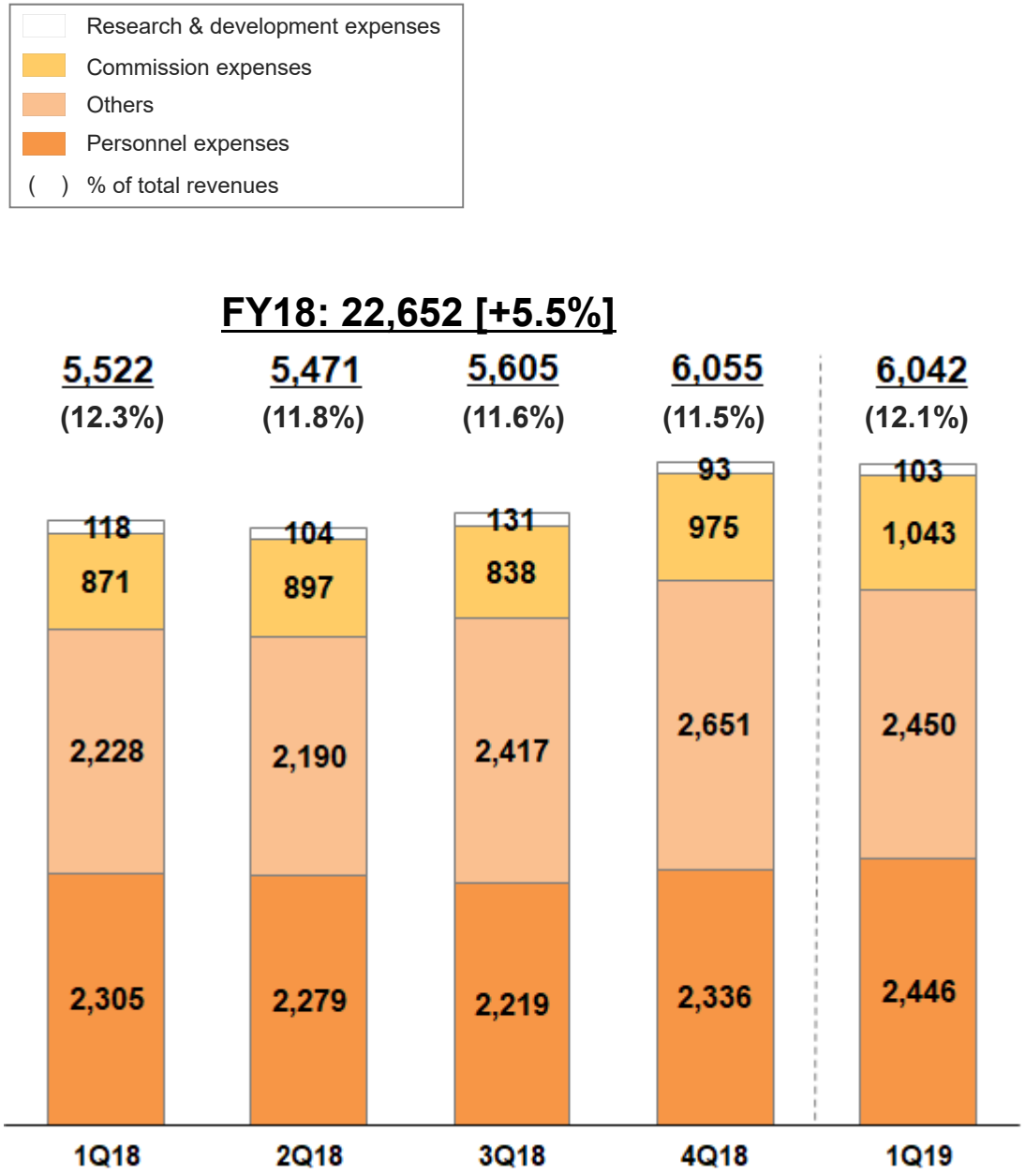
Unit: JPY million
( ) = % of revenue

1Q18	2Q18	3Q18	4Q18	1Q19
5,920 (13.2%)	**6,003** (12.9%)	**5,920** (12.2%)	**6,100** (11.6%)	**6,402** (12.8%)
FY18: 23,942 (12.4%)				

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Ⅱ - 7. SG&A etc.

Unit: JPY million
[ ], YoY = Year over year comparison



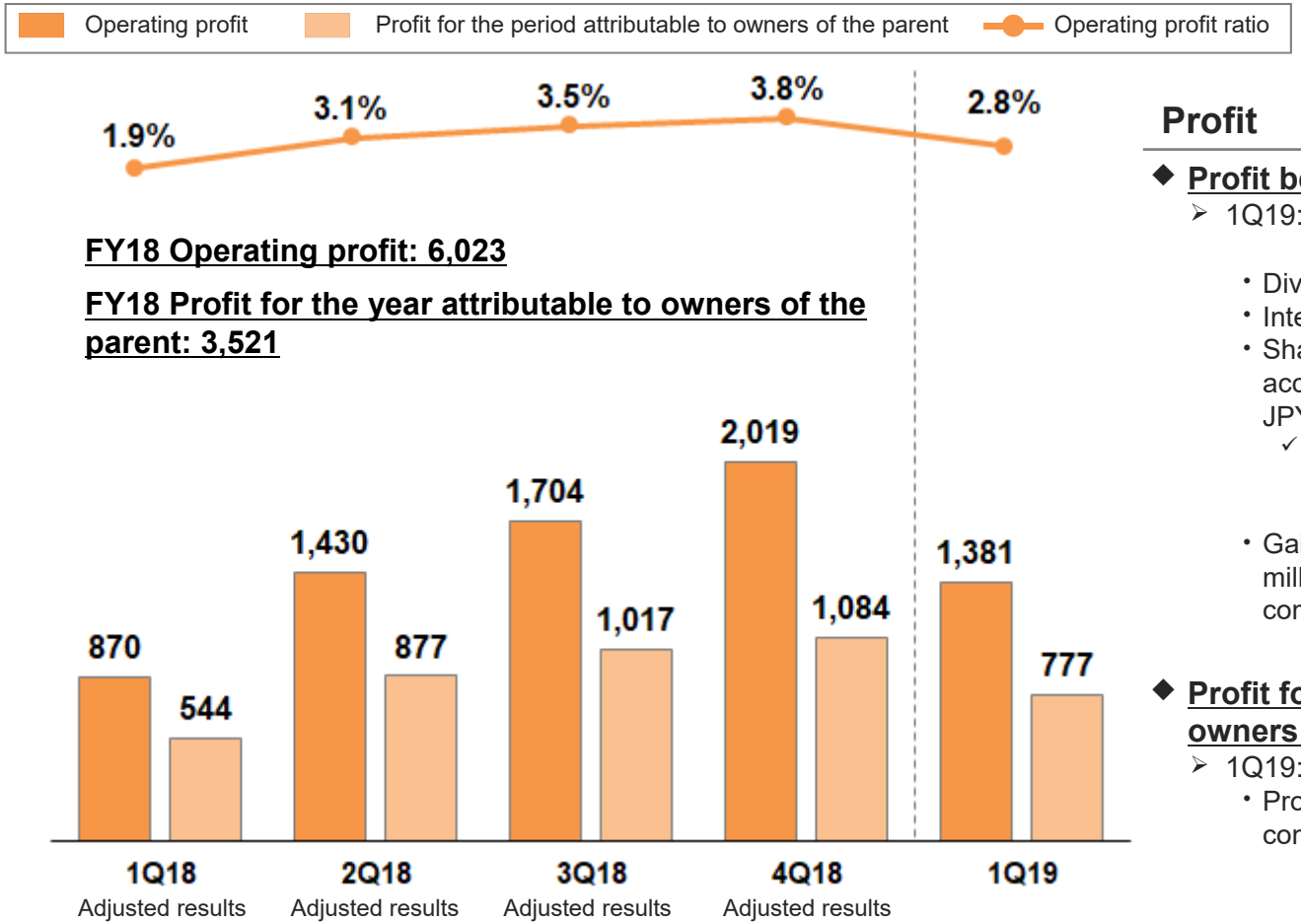
SG&A etc.

- 1Q19 commission expenses +JPY172 million YoY
  - Commission expenses such as for mobile services increased
- 1Q19 others +JPY222 million YoY
  - Advertising expenses increased +72 million YoY
- 1Q19 personnel expenses +JPY142 million YoY

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Ⅱ - 8. Profit

Unit: JPY million



FY18 Operating profit: 6,023

FY18 Profit for the year attributable to owners of the parent: 3,521

Profit

◆ **Profit before tax**

- 1Q19: JPY1,369 million
  (+45.2% from 1Q18 adjusted results)
  - Dividend income: JPY61 million
  - Interest expense: JPY126 million
  - Share of loss of investments on DeCurret accounted for using equity method: JPY337 million
    - ✓ DeCurret's plan: FY19: loss of JPY0.7 billion, FY20: equity in net gain will be expected
  - Gains on changes in equity of JPY374 million arisen from the issuance of common stock of DeCurret

◆ **Profit for the period attributable to owners of the parent**

- 1Q19: +42.9% from 1Q18 adjusted results
  - Profit for the period attributable to non-controlling interests: JPY49 million

103	65	(46)	16	(124)	Finance income (expense), net
(30)	6	(43)	(252)	112	Share of profit (loss) of investments accounted for using equity method
(511)	(738)	(716)	(179)	(543)	Income tax expense
(40)	(45)	(45)	(47)	(49)	Less: Profit for the period attributable to non-controlling interests

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Ⅱ - 9. Consolidated Statements of Financial Position (Summary)

Unit: JPY million

	Mar. 31, 2019	June 30, 2019	Changes	
Cash and cash equivalents	31,958	32,893	+935	
Trade receivables	33,376	31,264	(2,112)	
Inventories	3,403	1,836	(1,568)	
Prepaid expenses (current and non-current)	16,560	20,230	+3,670	
Tangible assets	33,136	18,855	(14,281)	Note 1
Right-of-use assets	-	51,880	+51,880	
Goodwill and intangible assets	24,901	24,027	(875)	
Investments accounted for using the equity method	4,838	5,331	+494	
Other investments	11,402	9,691	(1,711)	
Others	7,715	8,384	+669	
Total assets:	**167,289**	**204,390**	**+37,101**	
Trade and other payables	21,962	17,531	(4,431)	
Borrowings (current and non-current)	26,750	29,000	+2,250	
Deferred income (current and non-current)	10,980	11,716	+735	
Income taxes payable	1,139	1,130	(10)	
Retirement benefit liabilities	3,489	3,532	+44	Note 2
Other financial liabilities (current and non-current)	19,183	57,332	+38,149	
Others	6,666	6,327	(339)	
Total liabilities:	**90,170**	**126,567**	**+36,398**	
Share capital	25,519	25,519	-	
Share premium	36,226	36,240	+14	
Retained earnings	12,335	14,075	+1,740	
Other components of equity	4,089	3,043	(1,046)	Note 3
Treasury shares	(1,897)	(1,897)	-	
Total equity attributable to owners of the parent:	**76,271**	**76,979**	**+708**	

Note1: Breakdown of right-of-use assets as of June 30, 2019: JPY36,589 million for operating leases (office rent contracts etc.), JPY15,291 million for finance lease (transferred from tangible and intangible assets)

Note 2: Details of other financial liabilities as of June 30, 2019: JPY36,623 million for operating lease (office rent contracts etc.)

Note 3: Ratio of total equity attributable to owners of the parent: 45.6% as of March 31, 2019 37.7% as of June 30, 2019

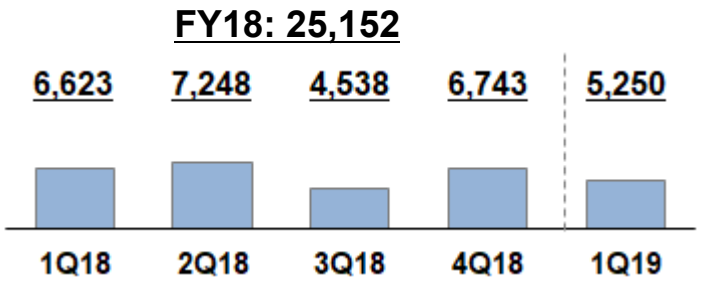
* Along with the adoption of IFRS 16, certain operating lease related assets and liabilities are recognized on Statements of Financial Position

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Ⅱ - 10. Consolidated Cash Flows

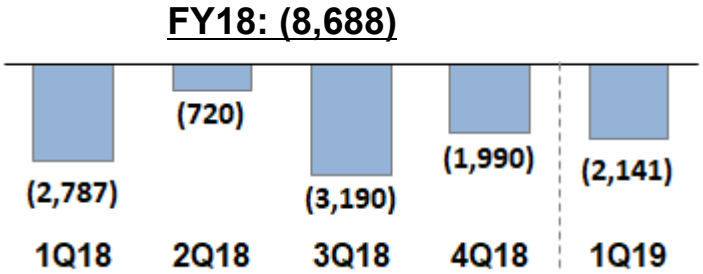
Unit: JPY million
YoY = Year over year comparison

Operating Activities



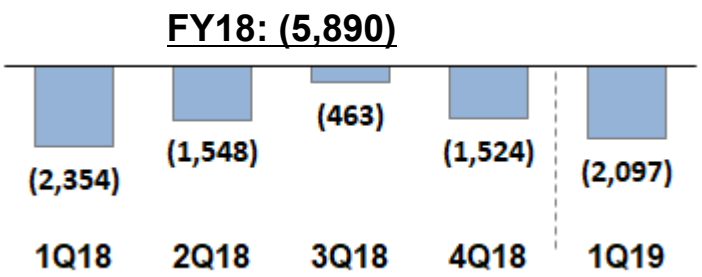
	Major Breakdown	YoY Change
Profit before tax	1,369	-56
Depreciation and amortization	7,164	+3,555
(related to right-of use assets under operating lease contracts	*3,127*	*+3,127)*
Changes in operating assets and liabilities	-2,057	-5,646

Investing Activities



	Major Breakdown	YoY Change
Purchase of tangible assets	-2,947	-1,376
Purchase of intangible assets such as software	-1,650	-87
Proceeds from sales of equity securities	2,650	+2,650

Financing Activities



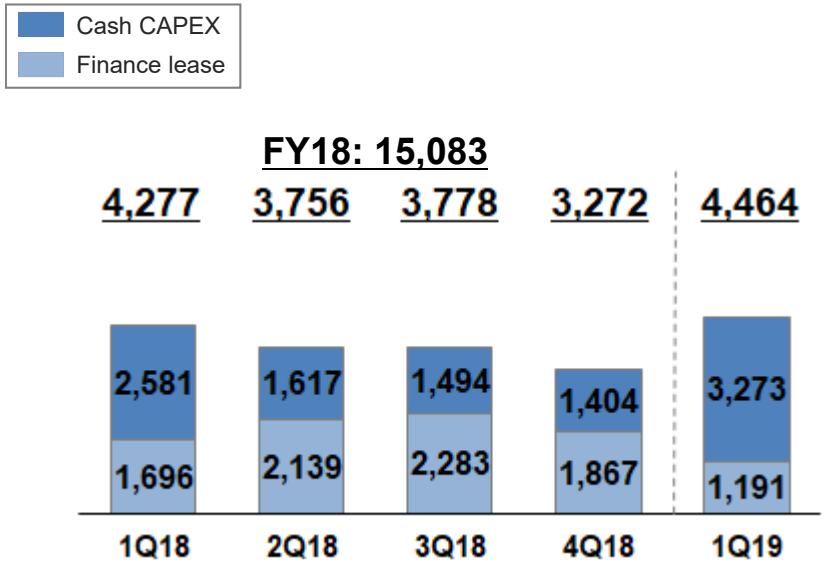
	Major Breakdown	YoY Change
Payments of other financial liabilities	-5,158	-3,461
(related to operating lease	*-3,142*	*-3,142)*
(related to finance lease	*-1,766*	*-246)*
Proceeds from short-term borrowings	3,000	+3,000

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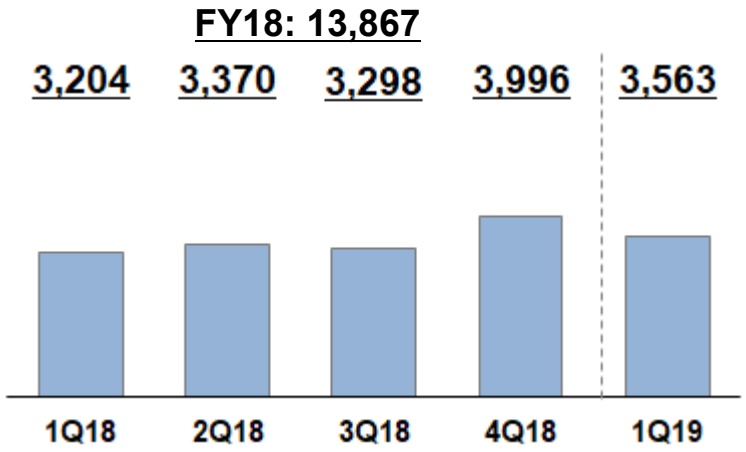
Ⅱ - 11. Other Financial Data

Unit: JPY million

CAPEX

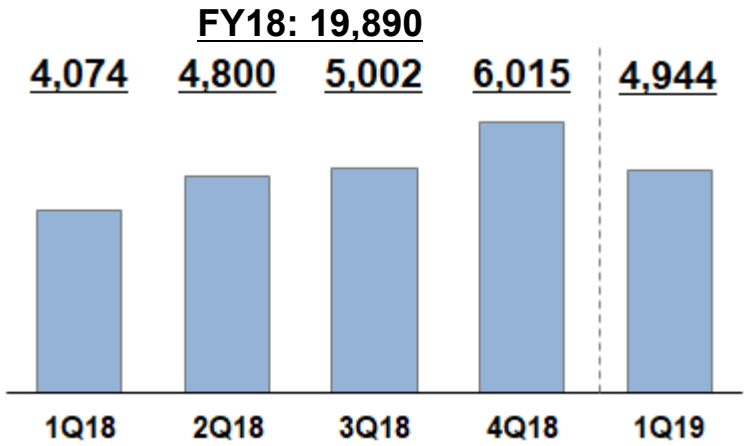


CAPEX-related depreciation and amortization*



* CAPEX-related depreciation and amortization is calculated by excluding depreciation and amortization of assets that do not have the nature of capital investment, such as right-of-use assets related to operating leases, small-amount equipment and customer relationship.

Adjusted EBITDA*



*Adjusted EBITDA is calculated by adding adjusted operating profit and CAPEX-related depreciation and amortization.

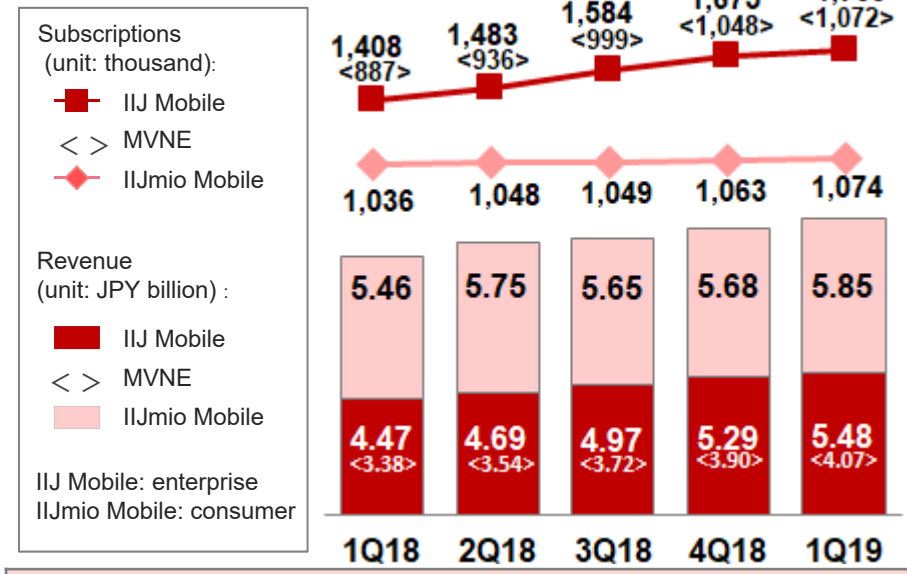
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Ⅲ - 1. KPIs of Services

Revenue unit: JPY billion
% = Year over year comparison

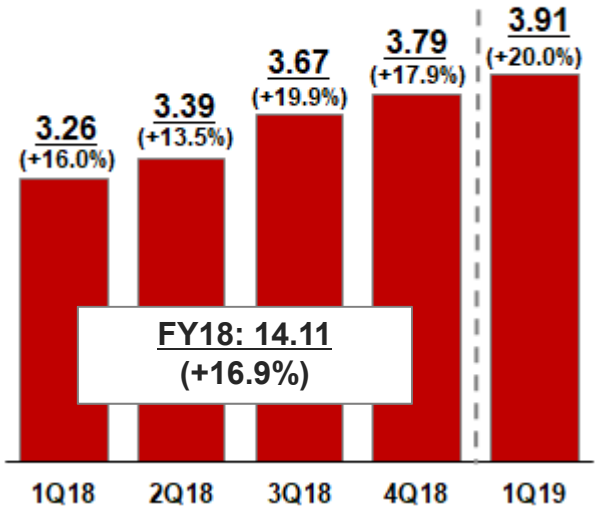
Mobile revenue & subscription

- 1Q19-end total subscriptions: 2,786 thousand (+14.0%)
- 1Q19 total revenue: JPY11.34 billion (+14.2%)
  - Full-MVNO: JPY0.34 billion (+49.9% from 4Q18)



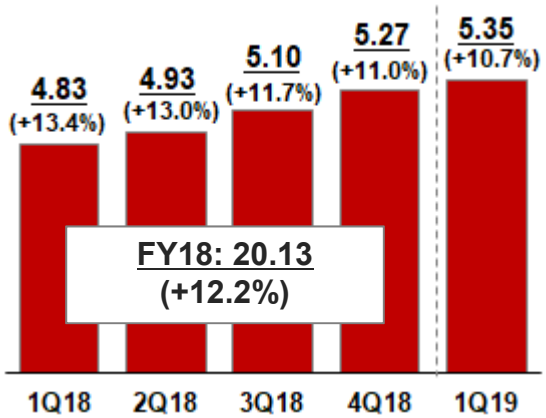
Security-related revenue

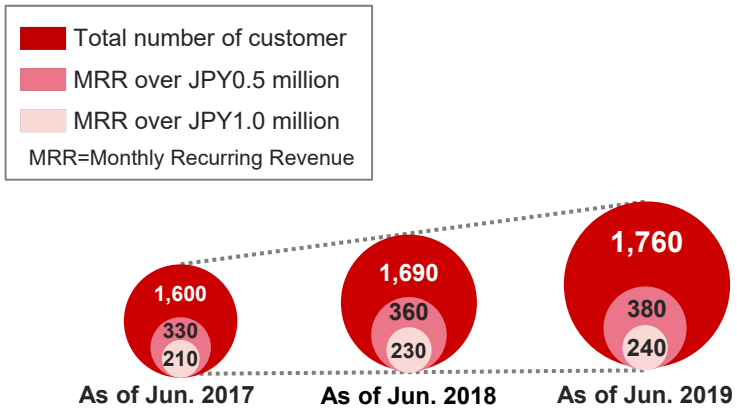
- Each services such as SOC, DDoS Protection, Cloud-based Web security, and Cloud-based ID management grew
- Security services revenues are recognized in outsourcing services revenue



Cloud-related revenue & Customer Base

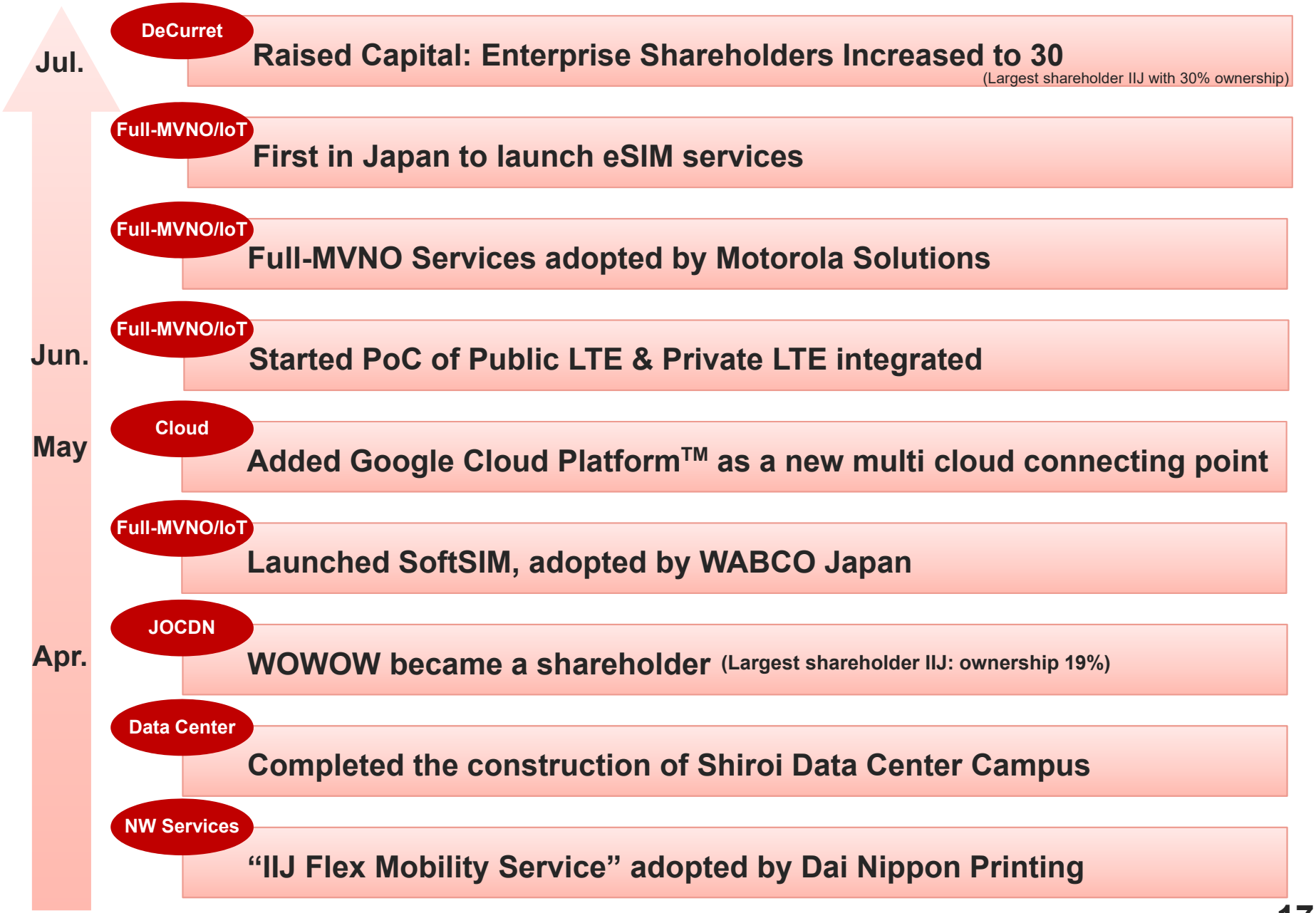
- 1Q19 IIJ Raptor revenue:
  IIJ Raptor JPY0.78 billion
  (+JPY0.12 billion from 4Q18)
- 1Q19 revenue recognition:
  - 87.6% SI operation & maintenance,
  - 12.4% outsourcing
- FY2019 revenue target:
  JPY22.5 billion





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Ⅲ - 2. Recent Business Developments



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Ⅲ - 3. Financial Targets (remain unchanged)

Unit: JPY billion
YoY = Year over year comparison

	% of Revenues 1Q19 Results Apr. 2019 - Jun. 2019	% of Revenues 1H19 Targets Apr. 2019 - Sep. 2019	Compared to 1H18 Adjusted Results [Compared to 1H18 Results]	% of Revenues FY19 Targets Apr. 2019 - Mar. 2020	YoY
Total Revenues	49.8	97.7	+7.1% [+8.5%]	204.0	+6.0%
Cost of Sales	85.2% 42.4	85.5% 83.5	+7.1% [+8.5%]	84.6% 172.6	+5.6%
Gross Profit	14.8% 7.4	14.5% 14.2	+7.1% [-0.3%]	15.4% 31.4	+8.4%
SG&A etc.(*1)	12.0% 6.0	12.3% 12.0	+9.5%	12.0% 24.4	+6.3%
Operating Profit	2.8% 1.4	2.3% 2.2	-4.3% [-33.0%]	3.4% 7.0	+16.2%
Shares of profit (loss) of investments accounted for using equity method	0.1	(0.7)	-	(0.6)	-
Profit before tax	2.7% 1.4	1.5% 1.5	-38.6% [-56.3%]	3.1% 6.3	+7.8%
Net Profit(*2)	1.6% 0.8	0.6% 0.6	-57.8% [-71.4%]	1.7% 3.5	-0.6%

(*1) SG&A etc. shows the sum of SG&A, which includes R&D expenses, and other income/expenses.
(*2) Net Profit is “Profit for the year (period) attributable to owners of the parent.”

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The internet started in Japan in 1992, along with IIJ. Since that time, the IIJ Group has been building the infrastructure for a networked society, and with our technical expertise, we have continued to support its development. We have also continued to evolve our vision for the future and innovate to make it a reality. As an internet pioneer, IIJ has blazed the trail so that others could realize the full potential of a networked society, and that will never change. The middle "I" in "IIJ" stands for "initiative," and IIJ alway starts with the future.

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