



Internet Initiative Japan

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***IIJ Announces 4<sup>th</sup> Quarter and Full Fiscal Year 2002 Results***

*– Record quarterly and annual revenues surpass expectations –  
Expected continued revenue growth and positive operating margin in 2003*

**Tokyo, May 21, 2003 / New York, May 20, 2003** – Internet Initiative Japan Inc. (Nasdaq: IJJI) (IIJ), one of Japan's leading Internet access and comprehensive network solutions providers, today announced its financial results for the 4th quarter and full fiscal year 2002, ending March 31, 2003 ("fiscal 2002"). On May 21 at 9:00 am (EST), the Company will host a conference call to discuss the results and its outlook. There will be a simultaneous webcast available at [www.vcall.com](http://www.vcall.com). A replay will also be available at the same URL.

**The 4th Quarter and full fiscal year 2002 Results Summary**

**4<sup>th</sup> Quarter 2002:**

- Revenues totaled JPY 13 billion (\$ 110 million), an increase of 7.7% compared to 4Q01 and 23.4% from 3Q02. Despite the lethargic Japanese economy, IIJ was able to maintain its steady growth, surpass guidance and achieve the highest total revenue amount in the Company's history.
- Operating loss narrowed to JPY 446 million (\$ 3.8 million) from JPY 567 million in 3Q02. This compares to a profit of JPY 186 million in 4Q01. The 4Q02 results include a non-recurring expense related to the IIJ Group's move to its new headquarters in March.
- Adjusted EBITDA<sup>(1)</sup> was JPY 459 million (\$ 3.9 million), a decrease of 52.6% compared to 4Q01 and an increase of 31.5% from 3Q02.

**Full fiscal year 2002:**

- Revenues increased to JPY 44 billion (\$ 373 million), a 10.3% increase from the previous year which was in line with our guidance.
- Operating loss was JPY 1.7 billion (\$ 14 million).
- Adjusted EBITDA was JPY 1.8 billion (\$ 15 million).

**Outlook:**

- For the 2003 fiscal year, IIJ expects total revenues to grow by more than 10% compared to fiscal 2002. The Company also anticipates that operating margins will move into positive territory.
- IIJ expects to raise additional equity capital on June 6, 2003. We believe that the equity capital financing in a private placement will provide IIJ with the financial means to continue the implementation of its growth strategy.

<sup>(1)</sup> Adjusted EBITDA represents operating income (loss) plus depreciation and amortization. Adjusted EBITDA is provided because it is a measure commonly used by investors to analyze and compare companies on the basis of operating performance. Adjusted EBITDA is not a measurement of financial performance under generally accepted accounting principles and should not be construed as a substitute for operating income, net income or cash flows from operating activities for purposes of analyzing our operating performance, financial position and cash flows. Our adjusted EBITDA is not necessarily comparable with similarly titled measures for other companies.

Note: Translations of Japanese yen amounts into US dollars are solely for the convenience of readers outside of Japan and have been made at the rate of JPY118.07 = US\$1, the approximate exchange rate on March 31, 2003.

## **Overview of 4Q02 and full fiscal year 2002 Results and Business Outlook**

**Overview** “Despite a difficult economic climate in fiscal 2002, IIJ has continued to implement its strategy for achieving greater shareholder value,” said Koichi Suzuki, President and CEO of IIJ. “Our strategy for the Japanese corporate market has been validated with the addition of several large-scale contracts, including the Ricoh Group, and we have achieved a record level of revenues. In fiscal 2002, we invested heavily in new services that will enable us to increase overall revenues in fiscal 2003 and beyond. We also worked hard to control our international and domestic backbone expenses through contract renegotiations and the rationalization of our infrastructure; we expect the full benefit of these efforts to generate significant cost reductions in 2003 and beyond. Furthermore, we believe that the recent establishment of our Network Integration Division will increase our penetration in the corporate sector, stimulate corporate network outsourcing demand and help improve our cross-selling efforts. Finally, we will soon complete a capital increase that will strengthen the Company’s financial base. We are confident that these measures and our increased focus on high margin products will position IIJ for operating and financial success in 2003.”

**Operating Profitability** IIJ’s revenues for the fourth quarter were the highest in IIJ’s history and surpassed the Company’s guidance. Despite the non-recurring expenses that were caused by the move to the new headquarters in March, the operating loss in the fourth quarter improved from the previous quarter’s loss, but was worse than the operating profit achieved in the same quarter of the previous fiscal year. The moving expenses are considered an operating cost under US GAAP.

Revenue from the full 2002 fiscal year also marked the highest annual amount in the company’s history. “Unfortunately, this was not sufficient to deliver a full year operating profit. An increase in certain connectivity services revenues was not sufficient to offset a loss of connectivity service revenues. This was the result of contract cancellations by the telecom service arm of regional electric power company and by the shift of several smaller corporate clients from the IIJ T1 Standard Service and the IIJ Economy Service to cheaper services. We do not expect a repeat of such revenue losses and we believe that we will continue to expand our connectivity revenues as has been the case for many years. To make up for the loss of revenues, IIJ launched the OEM service through the CDN (Content Delivery Network) platform and IIJ VPN Standard, a VPN (Virtual Private Network) service in the fiscal 2002 year. Though it will take some time to acquire new customers, we believe that these new services will contribute to make IIJ more profitable in fiscal year 2003. We expect total revenues to grow by more than 10% compared to fiscal 2002,” said Yasuhiro Nishi, CFO of IIJ. In addition, we expect to continue to increase the number of CATV customers. About fifty CATV operators were connected to IIJ, which represents more than 60% of Japan’s CATV Internet market in the 2002 fiscal year.

**Capital Improvement Plan** IIJ is planning to issue 8,400 new shares of common stock at a price of JPY418,200 in a private placement to third parties. The subscription and payment date for the new shares is expected to be June 6, 2003. We believe that the capital improvement will secure the financial means to allow IIJ to continue the implementation of its growth strategy. "Demonstrating a significant vote of confidence in IIJ's strategy, several major Japanese institutions will increase their financial commitment to IIJ while others will contribute capital for the first time," commented Yasuhiro Nishi. Details for the plan will be announced when finalized.

**Strategies for Enterprise Markets** IIJ’s focus on the enterprise market, which is based on the Company’s Systems Integration(SI) business and is further supported by company-wide cross-selling efforts, contributed to the Company’s steady growth in fiscal year 2002. Revenue from the SI business increased 33% sequentially as a result of strong demand for network solutions, equipment sales that were directed to the enterprise market.

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Cross-selling IIJ has continued to successfully cross-sell its Value-added, Systems Integration and Data Center Services to existing users of its Dedicated Access Services. “With a strategic marketing focus on Data Center Services and a base of 6,000 corporate customers that value the quality of our technology and support services, IIJ is well positioned to further increase our cross-selling rates in 2003,” said Yasuhiro Nishi, CFO of IIJ. In fiscal year 2002, revenues from IIJ’s top 150 customers accounted for approximately half of the Company’s total revenues. Cross-selling rates for these customers in fiscal 2002 year are detailed in the following table.

### Approximate Cross-selling rates among Top 150 Customers in fiscal 2002

The following table shows the percentage of Dedicated Access Service customers who also use our Value-added Service, our System Integrations Service and our Data Center Service.

	Value-added Service		System Integration		Data Center Service	
	2001	2002	2001	2002	2001	2002
Dedicated Access Service	69.7%	70.6%	49.2%	58.2%	30.4%	35.3%

Change in the Organizational Structure In an effort to continuously maintain our competitive advantage, IIJ brought together parts of IIJ, Crosswave Communications, IIJ Technology and NetCare in order to create a new division called the “Network Integration (NI) Division,” as of April 1, 2003. This division groups all technology and information platforms, from the planning and development to the maintenance and operation of various services. This division will make it possible to rapidly respond to demand in the construction of network communication systems for enterprises

### Status of Overview and Business Outlook

This Overview and Business Outlook contains forward-looking statements and projections, such as statements regarding future total revenues and operating profitability, that are subject to known and unknown risks and uncertainties that could cause actual results to differ materially from those expressed or implied by these statements. These risks and uncertainties include, but are not limited to, the factors noted at the end of this release and to the risk factors and other information contained in IIJ’s filings on Form 20-F and Form 6-K, as well as other filings and documents furnished to the Securities and Exchange Commission. IIJ plans to keep this press release publicly available on its Web site ([www.iij.ad.jp](http://www.iij.ad.jp)), but may discontinue this practice at any time.

## 4th Quarter and full fiscal year 2002 Operating Highlights

### Large-Scale Contracts

Several major Japanese companies awarded large-scale contracts to IIJ during the 4<sup>th</sup> quarter, including the Ricoh Group and Japan Leisure Channel. In February 2003, IIJ won a large-scale outsourcing contract for email gateway solutions, “IIJ Mail Gateway service,” from the Ricoh Group, one of the world’s leading suppliers of office automation equipment. In March, the Japan Leisure Channel Co. Ltd. (JLC) chose the IIJ Group to build and operate a large-scale broadband motorboat racing site called “Kyotei B.B.” where IIJ “CDN JAPAN” service has been utilized.

Additionally, IIJ launched “IIJ Web Gateway Service,” a new security service that will be provided in cooperation with IIJ Technology Inc. (IIJ-Tech), our 64.1% owned subsidiary. The service meets a variety of enterprise needs by providing proxy-caching server operation and management functions that boost Web access efficiency.

### Service Development

IIJ has continued to develop new services. In 4Q02, IIJ developed the IIJ SEIL Management Framework system (IIJ SMF), the world’s first network service operating system that enables corporations to substantially automate network configuration, and realize “plug-n-join” network services to control all networking processes, including network construction and operation. Customers

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can enjoy large cost reductions for the construction of network configurations by using this system. In addition, IIJ recently launched a new outsourcing solution of web-access filtering, "IIJ URL Filtering Service," to enable corporate customers to block access from their internal network to undesirable web sites in order to improve their productivity. IIJ's subsidiary, Net Care, Inc., launched a new IP (Internet Protocol) telephony solution service for enterprises. The new service provides a comprehensive VoIP (Voice over IP) solution that seamlessly integrates the operation of telephone and data networks. The service includes consulting, equipment selection, system construction and implementation, supervision, operation and maintenance.

### Data Center

In January 2003, Crosswave Communications Inc. (a company which IIJ owns 37.9%) opened new data centers in Yokohama and Saitama. Unlike conventional data centers, these two new data centers offer a full range of integrated network and SI (Systems Integration) services that use the IIJ Group's extensive range of network, system and engineering resources. The two new data centers are linked to other IIJ Group data centers nationwide, which help in dispersing capacity while providing further system back-up.

### Network Infrastructure Development

In 4Q02, IIJ increased the capacity of seven of its domestic backbone network lines. IIJ also upgraded its US backbone network that runs between Los Angeles, California and Ashburn, Virginia.

### R&D (IPv6)

In March 2003, IIJ launched a new IPv6 (Internet Protocol Version 6) service called "IPv6 Gateway Service". The new service will target leading companies in a variety of different industries. Besides offering IPv6 connectivity through IIJ's network, the service provides approximately  $3 \times 10^{26}$  IP addresses (a block of /40) per contract, which enables customers to roll out their own IPv6 services by assigning an IP address to each of their products or services. Hitachi Ltd. has already contracted this service from IIJ.

### Appointment of IIJ Engineers as IESG & IAB Members

In March 2003, two of IIJ's engineers were appointed as Members of IESG\* (Internet Engineering Steering Group) and IAB\* (Internet Architecture Board). Mr. Randy Bush, Chief Scientist of IIJ America, has become a Member and Area Director of IESG and is responsible for the Operations & Management area. Dr. Jun-ichiro Itojun Hagino, a senior researcher in the IIJ Laboratory, is serving as a Member of IAB. The assignments are two-year terms and are effective from March 2003 until February 2005.

\*IESG and IAB are organizations which are part of the IETF (Internet Engineering Task Force), which is a large open international community of network designers, operators, vendors, and researchers who are concerned with the evolution of the Internet's architecture and the smooth overall operation of the Internet. The IETF activities are grouped into eight areas, which are administered by the IESG Area Directors. The IAB is an international organization that provides architectural oversight and adjudicates appeals of complaints.

## **4<sup>th</sup> Quarter of FY2002 Financial Results**

### **Revenues**

Revenue in 4Q02 totaled JPY13,036 million, an increase of 7.7% compared to 4Q01, and an increase of 23.4% compared to 3Q02.

**Connectivity and value-added services** revenue was JPY5,419 million in 4Q02, a decrease of 7.3% compared to 4Q01 and a decrease of 2.6% compared to 3Q02.

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Dedicated access services revenues were JPY3,341 million in 4Q02, a decrease of 8.3% compared to 4Q01 and a decrease of 1.8% compared to 3Q02. The decrease in year-over-year comparison was mainly due to the cancellation by the telecom service arm of a regional electric power company, but in sequential comparison, the downward trend in dedicated access services is being compensated by the rapid revenue growth of IIJ FiberAccess/F service(10-100Mbps) and the steady growth of Data center connectivity service.

Dial-up access service revenues were JPY765 million in 4Q02, a decrease of 9.4% compared to 4Q01 and a decrease of 1.4% compared to 3Q02. The revenues of IIJ's various OEM services, which include NTT's regional L-mode service and other network services that use the CDN platform, increased steadily, which offset the decline of IIJ4U service and other dial-up services for corporate customers.

**Value-added services** revenues increased 13.2% to JPY931 million in 4Q02 compared to 4Q01 and 2.0% compared to 3Q02. These increases were mainly due to the revenue growth of security related services.

**Systems integration service** revenues decreased 8.0% to JPY4,905 million in 4Q02 compared to 4Q01, but increased 33.2% compared to 3Q02.

**Equipment sales** revenues were JPY2,712 million in 4Q02, an increase of 190.4% compared to 4Q01 and an increase of 105.7% compared to 3Q02. These revenues included sales of network equipment for the educational industries and governmental agencies, which we expect to develop as significant clients for our SI business.

**Table 1. Number of Contracts**

<b>Internet Access Services</b>	<b>4Q02</b>	<b>3Q02</b>	<b>4Q01</b>
<i>IP Service</i> 64kbps – 128kbps	<b>112</b>	130	142
192kbps – 768kbps	<b>35</b>	37	42
1Mbps – 2Mbps	<b>268</b>	279	270
3Mbps – 1.2Gbps	<b>248</b>	212	156
<i>Internet Data Center Connectivity Services</i> <sup>(2)</sup>	<b>156</b>	139	110
<i>Others</i> <sup>(3)</sup>	<b>4,489</b>	3,922	2,900
<b>Total Dedicated Access Services Contracts</b>	<b>5,308</b>	4,719	3,620

<sup>(2)</sup> The figures of Internet data center connectivity services do not include contracts for data center housing services.

<sup>(3)</sup> Others include, IIJ FiberAccess/F, IIJ Ethernet Standard, IIJ DSL/F, IIJT1 Standard and IIJ Economy.

<i>IIJ4U</i> (dialup services for individuals)	<b>79,464</b>	82,193	89,213
<b>Others</b>	<b>450,320</b>	370,543	171,363
<b>Total Dial-up Access Services Contracts</b>	<b>529,784</b>	452,736	260,576

**Table 2. Revenue Breakdown in Dedicated Access Services** (JPY in millions)

	<b>4Q02</b>	<b>3Q02</b>	<b>4Q01</b>
<b>Total IP Service + DC connectivity</b>	<b>2,518</b>	2,548	2,651
<b>Others</b>	<b>823</b>	856	992

**Table 3. Contracted Bandwidth** (Unit: Giga bits per second)

	<b>4Q02</b>	<b>3Q02</b>	<b>4Q01</b>
<b>Dedicated Access Services</b>	<b>32.1</b>	23.3	9.4
<b>Internet Data Center Connectivity Service</b>	<b>9.9</b>	7.0	2.0
<b>Total Contracted Bandwidth</b>	<b>42.0</b>	30.3	11.4

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### *Cost and expenses*

**Cost of total revenues** was JPY11,919 million in 4Q02, an increase of 11.3% compared to 4Q01, and an increase of 24.1% compared to 3Q02.

### Backbone Costs

International backbone costs were JPY315 million, a decrease of 28.8% compared to 4Q01 and a decrease of 27.0% compared to 3Q02.

Domestic backbone costs were JPY1,075 million, an increase of 28.6% compared to 4Q01 and an increase of 19.2% compared to 3Q02. These increases were a result of an increase in connection fees with NTT's regional access networks (FLET'S).

**Table 4. Backbone Costs** (JPY in millions)

	4Q02	3Q02	4Q01
<b>International Backbone Costs</b>	<b>315</b>	432	443
<b>Domestic Backbone Costs</b>	<b>1,075</b>	902	836

### Cost of SI (Systems Integration) revenues

Cost of SI revenues was JPY 4,248 million in 4Q02, a decrease of 10.3% compared to 4Q01 and an increase of 33.9% compared to 3Q02. The gross margin ratio for SI improved to 13.4% in 4Q02 compared to 11.2% in 4Q01, and was almost flat compared to 3Q02.

### Sales and Marketing Expenses

Sales and marketing expenses were JPY789 million in 4Q02, an increase of 5.5% compared to 4Q01 and a decrease of 11.8% compared to 3Q02.

### General and administrative expenses

General and administrative expenses were JPY662 million in 4Q02, an increase of 37.7% compared to 4Q01 and an increase of 29.3% compared to 3Q02. General and administrative expenses for 4Q02 included the cost of the move to new office.

### *Operating loss*

The operating loss was JPY446 million in 4Q02 as compared to the operating income of JPY186 million in 4Q01 and a loss of JPY567 million in 3Q02. The operating loss for 4Q02, net of the cost of the move to the new headquarters, improved considerably from the previous quarter due mainly to the steady growth of our SI business. The operating income (loss)-to-revenue ratio for 4Q02 was (-)3.4%, compared to 1.5% in 4Q01, and to (-)5.4% in 3Q02.

### *Other expenses*

Other expenses for 4Q02 were JPY360 million, compared to JPY338 million in 4Q01 and JPY228 million in 3Q02. Other expenses for 4Q02 were mainly composed of a JPY175 million impairment loss on certain equity security investments and a JPY190 million interest payment.

### *Equity in net loss of equity method investees*

Equity in net loss of equity method investees amounted to JPY1,254 million in 4Q02, compared to JPY1,647 million in 4Q01, and JPY1,375 million in 3Q02. This is mostly attributed to the equity loss in Crosswave.

### *Net loss*

Net loss was JPY2,137 million in 4Q02, compared to JPY1,667 million in 4Q01 and JPY2,266 million in 3Q02. Basic net loss per ADS equivalent was JPY(-)47.52 in 4Q02, compared to JPY(-)37.07 in 4Q01 and JPY(-)50.40 in 3Q02.

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**Table 5. Other Financial Statistics** (JPY in millions)

	4Q02	3Q02	4Q01
Adjusted EBITDA	459	349	968
CAPEX, including capitalized leases	936	1519	913
Depreciation and amortization	933	943	812

### **Reconciliation of Non-GAAP Financial Measures**

The following table summarizes the reconciliation of adjusted EBITDA to operating income (loss) per the consolidated statements of operations prepared and presented in accordance with the U.S. generally accepted accounting principles in Appendices 1 and 2:

(JPY in millions)

	4Q02	3Q02	4Q01	FY2002	FY2001
Adjusted EBITDA	459	349	968	1,799	2,960
Depreciation and amortization <sup>(4)</sup>	-905	-916	-782	-3,470	-2,906
Operating income(loss)	-446	-567	186	-1,671	54

<sup>(4)</sup> Depreciation and amortization excludes amortization of issuance cost of convertible notes and of goodwill that were presented as other expenses.

The following table summarizes the reconciliation of capital expenditures to purchase of property and equipment per the consolidated statements of cash flows prepared and presented in accordance with the U.S. generally accepted accounting principles in Appendices 4 and 5:

(JPY in millions)

	4Q02	3Q02	4Q01
Capital expenditures	936	1,519	913
Acquisition of assets by entering into capital leases	772	1,014	411
Purchase of property and equipment	164	505	502

## Company Information

Founded in 1992, Internet Initiative Japan Inc. (IIJ, NASDAQ: IJJI) is Japan's leading Internet-access and comprehensive network solutions provider. The company has built one of the largest Internet backbone networks in Japan, and between Japan and the United States. IIJ and its group of companies provide total network solutions that mainly cater to high-end corporate customers. Services range from the delivery of new generation network services over an optical-fiber infrastructure that is optimized for data communications, to the construction of pan-Asian IP backbone networks. The company also offers high-quality systems integration and security services, internet access, hosting/housing, and content design.

*Statements made in this press release 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 4Q02 and fiscal year 2002 total revenues and operating 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 expectation that net losses will continue; IIJ's ability to raise additional capital to cover its accumulated deficit; IIJ's ability to continue to increase subscribers to its connectivity services, particularly at higher bandwidths; IIJ's ability to generate significant revenues from its other services such as systems integration; the success of IIJ's investments in Crosswave; the ability to compete in a rapidly evolving and competitive marketplace; the impact of technological changes in its industry; and other risks referred to from time to time in IIJ's filings on Form 20F of its annual report and other filings with the United States Securities and Exchange Commission.*

**Tables to follow**

**CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)**

For the Three Months Ended Mar 31, 2003, Mar 31, 2002 and Dec 31, 2002

(Expressed in Thousands of Japanese Yen (JPY) and U.S. Dollars (USD) Except for Per Share and ADS Data) (1)

	Year-over-year Comparison						Sequential Comparison		
	Mar 31, 2003			Mar 31, 2002			Dec 31, 2002		
	USD (1)	JPY	% of Total Revenues	JPY	% of Total Revenues	YOY Chg %	JPY	% of Total Revenues	QOQ Chg %
<b>Revenues:</b>									
Connectivity and value-added services:									
Dedicated access services (2)	28,299	3,341,255	25.6%	3,643,141	30.1%	(8.3%)	3,404,016	32.2%	(1.8%)
Dial-up access services	6,479	764,958	5.9	844,279	7.0	(9.4)	776,173	7.4	(1.4)
Value-added services (2)	7,888	931,399	7.2	823,137	6.8	13.2	913,152	8.6	2.0
Other	3,229	381,206	2.9	533,191	4.4	(28.5)	467,629	4.4	(18.5)
Total connectivity and value-added services	45,895	5,418,818	41.6	5,843,748	48.3	(7.3)	5,560,970	52.6	(2.6)
Systems integration revenues	41,547	4,905,429	37.6	5,331,986	44.0	(8.0)	3,683,978	34.9	33.2
Equipment sales	22,971	2,712,192	20.8	934,040	7.7	190.4	1,318,630	12.5	105.7
<b>Total revenues</b>	<b>110,413</b>	<b>13,036,439</b>	<b>100.0</b>	<b>12,109,774</b>	<b>100.0</b>	<b>7.7</b>	<b>10,563,578</b>	<b>100.0</b>	<b>23.4</b>
<b>Costs and expenses:</b>									
Cost of connectivity and value-added services	42,630	5,033,266	38.6	5,110,291	42.2	(1.5)	5,179,920	49.0	(2.8)
Cost of systems integration revenues	35,976	4,247,690	32.6	4,734,363	39.1	(10.3)	3,173,211	30.0	33.9
Cost of equipment sales	22,345	2,638,334	20.2	865,354	7.1	204.9	1,254,073	11.9	110.4
Total costs	100,951	11,919,290	91.4	10,710,008	88.4	11.3	9,607,204	90.9	24.1
Sales and marketing	6,684	789,234	6.0	665,204	5.5	18.6	894,340	8.5	(11.8)
General and administrative	5,603	661,502	5.1	480,376	4.0	37.7	511,604	4.9	29.3
Research and development	956	112,845	0.9	68,090	0.6	65.7	116,950	1.1	(3.5)
<b>Total costs and expenses</b>	<b>114,194</b>	<b>13,482,871</b>	<b>103.4</b>	<b>11,923,678</b>	<b>98.5</b>	<b>13.1</b>	<b>11,130,098</b>	<b>105.4</b>	<b>21.1</b>
<b>Operating income (loss)</b>	<b>(3,781)</b>	<b>(446,432)</b>	<b>(3.4)</b>	<b>186,096</b>	<b>1.5</b>	<b>(339.9)</b>	<b>(566,520)</b>	<b>(5.4)</b>	<b>(21.2)</b>
<b>Other expenses</b>	<b>(3,052)</b>	<b>(360,292)</b>	<b>(2.8)</b>	<b>(337,694)</b>	<b>(2.8)</b>	<b>6.7</b>	<b>(228,058)</b>	<b>(2.1)</b>	<b>58.0</b>
<b>Loss before income tax expense(benefit)</b>	<b>(6,833)</b>	<b>(806,724)</b>	<b>(6.2)</b>	<b>(151,598)</b>	<b>(1.3)</b>	<b>432.1</b>	<b>(794,578)</b>	<b>(7.5)</b>	<b>1.5</b>
<b>Income tax expense(benefit)</b>	<b>823</b>	<b>97,256</b>	<b>0.8</b>	<b>(140,381)</b>	<b>(1.2)</b>	<b>(169.3)</b>	<b>137,936</b>	<b>1.3</b>	<b>(29.5)</b>
<b>Minority interests in consolidated subsidiaries</b>	<b>181</b>	<b>21,342</b>	<b>0.2</b>	<b>(8,849)</b>	<b>(0.1)</b>	<b>(341.2)</b>	<b>41,813</b>	<b>0.4</b>	<b>(49.0)</b>
<b>Equity in net loss of equity method investees</b>	<b>(10,620)</b>	<b>(1,253,875)</b>	<b>(9.6)</b>	<b>(1,646,603)</b>	<b>(13.6)</b>	<b>(23.9)</b>	<b>(1,375,338)</b>	<b>(13.0)</b>	<b>(8.8)</b>
<b>Net loss</b>	<b>(18,095)</b>	<b>(2,136,513)</b>	<b>(16.4%)</b>	<b>(1,666,669)</b>	<b>(13.8%)</b>	<b>28.2%</b>	<b>(2,266,039)</b>	<b>(21.4%)</b>	<b>(5.7%)</b>
<b>Basic Net Loss Per Share</b>		(95,041)		(74,140)			(100,802)		
<b>Basic Net Loss Per ADS Equivalent</b>		(47.52)		(37.07)			(50.40)		
<b>Weighted Average Number of Shares</b>		22,480		22,480			22,480		
<b>Weighted Average Number of ADS Equivalents</b>		44,960,000		44,960,000			44,960,000		

Note (1): The translations of Japanese yen amounts into US dollar amounts with respect to the three months ended Mar 31, 2003 are included solely for the convenience of readers outside Japan and have been made at the rate of JPY 118.07 = \$1, the approximate rate of exchange on Mar 31, 2003.

Note (2): IJ datacenter connectivity services revenues have been reclassified from value added services revenues into dedicated access services revenues since the 1st quarter of FY200

The 4th quarter of FY2001 presented has been reclassified to conform to the current presentation and such reclassification resulted in an increase of dedicated access services revenue by Y257,599, as compared to the previous classification method.



**INTERNET INITIATIVE JAPAN INC.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)**

**Appendix 2**

For the Years Ended Dec 31, 2003 and Mar 31, 2002

(Expressed in Thousands of Japanese Yen (JPY) and U.S. Dollars (USD) Except for Per Share and ADS Data) (1)

	Year-over-year Comparison					
	Mar 31, 2003			Mar 31, 2002		
	USD (1)	JPY	% of Total Revenues	JPY	% of Total Revenues	YoY Chg %
<b>Revenues:</b>						
Connectivity and value-added services:						
Dedicated access services(2)	117,007	13,814,977	31.4%	14,303,342	35.8%	(3.4%)
Dial-up access services	26,723	3,155,137	7.2	3,644,091	9.1	(13.4)
Value-added services(2)	30,514	3,602,847	8.2	3,099,791	7.8	16.2
Other	14,616	1,725,736	3.9	1,667,986	4.2	3.5
Total connectivity and value-added services	188,860	22,298,697	50.7	22,715,210	56.9	(1.8)
Systems integration revenues	127,150	15,012,633	34.1	14,355,325	36.0	4.6
Equipment sales	56,799	6,706,231	15.2	2,834,078	7.1	136.6
<b>Total revenues</b>	<b>372,809</b>	<b>44,017,561</b>	<b>100.0</b>	<b>39,904,613</b>	<b>100.0</b>	<b>10.3</b>
<b>Costs and expenses:</b>						
Cost of connectivity and value-added services	172,668	20,386,887	46.3	19,799,402	49.6	3.0
Cost of systems integration revenues	110,868	13,090,220	29.7	12,314,158	30.9	6.3
Cost of other equipment sales	54,345	6,416,525	14.6	2,540,089	6.4	152.6
Total costs	337,881	39,893,632	90.6	34,653,649	86.9	15.1
Sales and marketing	26,901	3,176,165	7.2	3,038,412	7.6	4.5
General and administrative	18,671	2,204,504	5.0	1,839,525	4.6	19.8
Research and development	3,508	414,149	1.0	319,370	0.8	29.7
<b>Total costs and expenses</b>	<b>386,961</b>	<b>45,688,450</b>	<b>103.8</b>	<b>39,850,956</b>	<b>99.9</b>	<b>14.6</b>
<b>Operating income(loss)</b>	<b>(14,152)</b>	<b>(1,670,889)</b>	<b>(3.8)</b>	<b>53,657</b>	<b>0.1</b>	<b>(3,214.0)</b>
<b>Other expenses</b>	<b>(10,751)</b>	<b>(1,269,433)</b>	<b>(2.9)</b>	<b>(943,142)</b>	<b>(2.3)</b>	<b>34.6</b>
<b>Loss before income tax expense</b>	<b>(24,903)</b>	<b>(2,940,322)</b>	<b>(6.7)</b>	<b>(889,485)</b>	<b>(2.2)</b>	<b>230.6</b>
<b>Income tax expense</b>	<b>7,719</b>	<b>911,365</b>	<b>2.1</b>	<b>1,099,035</b>	<b>2.8</b>	<b>(17.1)</b>
<b>Minority interests in consolidated subsidiaries</b>	<b>1,298</b>	<b>153,251</b>	<b>0.4</b>	<b>24,467</b>	<b>0.1</b>	<b>526.4</b>
<b>Equity in net loss of affiliated companies</b>	<b>(47,644)</b>	<b>(5,625,299)</b>	<b>(12.8)</b>	<b>(5,482,082)</b>	<b>(13.8)</b>	<b>2.6</b>
<b>Net loss</b>	<b>(78,968)</b>	<b>(9,323,735)</b>	<b>(21.2%)</b>	<b>(7,446,135)</b>	<b>(18.7%)</b>	<b>25.2%</b>
<b>Basic Net Loss Per Share</b>		(414,757)		(331,234)		
<b>Basic Net Loss Per ADS Equivalent</b>		(207.38)		(165.62)		
<b>Weighted Average Number of Shares</b>		22,480		22,480		
<b>Weighted Average Number of ADS Equivalents</b>		44,960,000		44,960,000		

Note (1): The translations of Japanese yen amounts into US dollar amounts with respect to the year ended Mar 31, 2003 are included solely for the convenience of readers outside Japan and have been made at the rate of JPY 118.07 = \$1, the approximate rate of exchange on Mar 31, 2003.

Note (2): IIJ datacenter connectivity services revenues have been reclassified from value added services revenues into dedicated access services revenues since the 1st quarter of FY2002. The 4th quarter of FY2001 presented has been reclassified to conform to the current presentation and such reclassification resulted in an increase of dedicated access services revenues by Y761,362, as compared to the previous classification method.

**INTERNET INITIATIVE JAPAN INC.**  
**CONSOLIDATED BALANCE SHEETS (UNAUDITED)**  
As of Mar 31, 2003, Mar 31, 2002 and Dec 31, 2002  
(Expressed in Thousands of Japanese Yen (JPY) and U.S. Dollars (USD)) <sup>(1)</sup>

	Mar 31, 2003			Mar 31, 2002		Dec 31, 2002	
	USD <sup>(1)</sup>	JPY	%	JPY	%	JPY	%
<b>ASSETS</b>							
<b>Current Assets:</b>							
Cash	30,392	3,588,352	9.2%	11,045,919	24.4%	4,270,613	11.4%
Accounts receivable, net	86,839	10,253,096	26.1	8,981,912	19.9	7,305,169	19.5
Inventories	3,537	417,666	1.1	620,409	1.4	813,863	2.2
Prepaid expenses	4,781	564,501	1.4	416,945	0.9	882,854	2.4
Other current assets	7,901	932,873	2.4	143,798	0.3	135,828	0.4
<b>Total current assets</b>	<b>133,450</b>	<b>15,756,488</b>	<b>40.2</b>	<b>21,208,983</b>	<b>46.9</b>	<b>13,408,327</b>	<b>35.9</b>
Investments in and Advances to Equity Method Investees	27,704	3,271,032	8.3	8,854,028	19.6	4,522,602	12.1
Other Investments	25,749	3,040,189	7.8	5,406,065	11.9	3,461,695	9.2
Property and Equipment, net	77,510	9,151,572	23.3	7,755,426	17.1	8,898,123	23.8
Restricted Cash	42,348	5,000,000	12.8	0	0.0	5,000,000	13.4
Guarantee Deposits	18,681	2,205,652	5.6	1,266,055	2.8	1,369,596	3.7
Other Assets	6,729	794,455	2.0	772,226	1.7	699,998	1.9
<b>Total assets</b>	<b>332,171</b>	<b>39,219,388</b>	<b>100.0%</b>	<b>45,262,783</b>	<b>100.0%</b>	<b>37,360,341</b>	<b>100.0%</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>							
<b>Current Liabilities:</b>							
Short-term borrowings	40,854	4,823,599	12.3%	3,820,232	8.4%	4,510,000	12.1%
Accounts payable	71,196	8,406,170	21.4	7,085,579	15.7	5,852,779	15.7
Accrued expenses	3,299	389,495	1.0	247,606	0.5	364,366	1.0
Other current liabilities	4,675	551,985	1.4	506,797	1.1	570,719	1.5
Long-term borrowings-current portion	16,462	1,943,735	5.0	1,400,000	3.1	1,200,000	3.2
Capital lease obligations-current portion	23,007	2,716,386	6.9	1,973,769	4.4	2,424,701	6.5
<b>Total current liabilities</b>	<b>159,493</b>	<b>18,831,370</b>	<b>48.0</b>	<b>15,033,983</b>	<b>33.2</b>	<b>14,922,565</b>	<b>40.0</b>
Long-term Borrowings	29,273	3,456,265	8.8	3,400,000	7.5	3,400,000	9.1
Convertible Notes	127,043	15,000,000	38.2	15,000,000	33.2	15,000,000	40.1
Capital Lease Obligations-Noncurrent	30,793	3,635,780	9.3	2,861,556	6.3	3,463,132	9.3
Accrued Retirement and Pension Costs	683	80,601	0.2	100,841	0.2	75,047	0.2
Other Noncurrent Liabilities	1,569	185,201	0.5	108,376	0.2	184,847	0.5
<b>Total liabilities</b>	<b>348,854</b>	<b>41,189,217</b>	<b>105.0</b>	<b>36,504,756</b>	<b>80.6</b>	<b>37,045,591</b>	<b>99.2</b>
Minority Interest	7,449	879,495	2.3	1,032,746	2.3	900,837	2.4
<b>Shareholders' Equity:</b>							
Common stock	59,984	7,082,336	18.1	7,082,336	15.7	7,082,336	18.9
Additional paid-in capital	144,561	17,068,353	43.5	17,068,353	37.7	17,068,353	45.7
Accumulated deficit	(233,185)	(27,532,204)	(70.2)	(18,208,469)	(40.2)	(25,395,691)	(68.0)
Accumulated other comprehensive income	4,508	532,191	1.3	1,783,061	3.9	658,915	1.8
<b>Total shareholders' equity</b>	<b>(24,132)</b>	<b>(2,849,324)</b>	<b>(7.3)</b>	<b>7,725,281</b>	<b>17.1</b>	<b>(586,087)</b>	<b>(1.6)</b>
<b>Total liabilities and shareholders' equity</b>	<b>332,171</b>	<b>39,219,388</b>	<b>100.0%</b>	<b>45,262,783</b>	<b>100.0%</b>	<b>37,360,341</b>	<b>100.0%</b>

Note (1): The translations of Japanese yen amounts into US dollar amounts with respect to Mar 31, 2003 are included solely for the convenience of readers outside Japan and have been made at the rate of JPY118.07 = \$1, the approximate rate of exchange on Mar 31, 2003.

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)**

For the Three Months Ended March 31, 2003, March 31, 2002 and Dec 31, 2002

(Expressed in Thousands of Japanese Yen (JPY) and U.S. Dollars (USD))(1)

	March 31, 2003		March 31, 2002	Dec 31, 2002
	USD (1)	JPY	JPY	JPY
<b>Operating Activities:</b>				
Net loss	(18,095)	(2,136,513)	(1,666,669)	(2,266,039)
Depreciation and amortization	7,905	933,374	811,652	942,854
Equity in net loss of equity method investees	10,620	1,253,875	1,646,603	1,375,338
Minority interests in net (loss) income of consolidated subsidiaries	(181)	(21,342)	8,849	(41,813)
Foreign exchange losses	1,264	149,262	3,990	32,834
Losses on other investments	1,565	184,723	104,700	-
Decrease (increase) in accounts receivable	(25,267)	(2,983,254)	(3,183,806)	493,961
Increase in accounts payable	18,636	2,200,392	3,696,329	1,033,939
Decrease (increase) in inventories	3,321	392,051	(398,876)	(398,092)
Deferred income taxes	771	91,033	(145,560)	132,230
Other	3,614	426,737	214,793	(52,956)
<b>Net cash provided by operating activities</b>	<b>4,153</b>	<b>490,338</b>	<b>1,092,005</b>	<b>1,252,256</b>
<b>Investing Activities:</b>				
Purchase of property and equipment	(1,385)	(163,592)	(501,667)	(505,169)
Proceeds from sale-leaseback	567	66,940	-	-
Investments in and advances to equity method investees	-	-	(24,123)	-
Purchase of other investments	-	-	(350,000)	(28,377)
(Payment) refund of guarantee deposits-net	(11,749)	(1,387,210)	(2,007)	22,972
Other	51	6,057	22,299	(30,506)
<b>Net cash used in investing activities</b>	<b>(12,516)</b>	<b>(1,477,805)</b>	<b>(855,498)</b>	<b>(541,080)</b>
<b>Financing Activities:</b>				
Proceeds from long-term borrowings	16,939	2,000,000	-	-
Repayments of long-term borrowings	(10,164)	(1,200,000)	-	(200,000)
Principal payments under capital leases	(5,558)	(656,238)	(535,906)	(651,546)
Net increase (decrease) in short-term borrowings	2,650	312,854	120,018	(322,254)
<b>Net cash provided by (used in) financing activities</b>	<b>3,867</b>	<b>456,616</b>	<b>(415,888)</b>	<b>(1,173,800)</b>
<b>Effect of Exchange Rate Changes on Cash</b>	<b>(1,282)</b>	<b>(151,410)</b>	<b>59,223</b>	<b>(39,516)</b>
<b>Net Decrease in Cash</b>	<b>(5,778)</b>	<b>(682,261)</b>	<b>(120,158)</b>	<b>(502,140)</b>
<b>Cash, Beginning of Period</b>	<b>36,170</b>	<b>4,270,613</b>	<b>11,166,077</b>	<b>4,772,753</b>
<b>Cash, End of Period</b>	<b>30,392</b>	<b>3,588,352</b>	<b>11,045,919</b>	<b>4,270,613</b>

Note (1): The translations of Japanese yen amounts into US dollar amounts with respect to the three months ended Mar 31, 2003 are included solely for the convenience of readers outside Japan and have been made at the rate of JPY118.07 = \$1, the approximate rate of exchange on Mar 31, 2003.

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)**

For the Year Ended March 31, 2003, March 31, 2002

(Expressed in Thousands of Japanese Yen (JPY) and U.S. Dollars (USD))(1)

	March 31, 2003		March 31, 2002
	USD (1)	JPY	JPY
<b>Operating Activities:</b>			
Net loss	(78,968)	(9,323,735)	(7,446,135)
Depreciation and amortization	30,323	3,580,212	3,027,587
Equity in net loss of equity method investees	47,644	5,625,299	5,482,082
Minority interests in net loss of consolidated subsidiaries	(1,298)	(153,251)	(24,467)
Foreign exchange losses (gains)	2,353	277,856	(219,524)
Losses on other investments	2,348	277,162	432,952
Increase in accounts receivable	(11,446)	(1,351,380)	(3,559,335)
Increase in accounts payable	10,548	1,245,431	2,808,704
Decrease (increase) in inventories	1,682	198,597	(671,177)
Deferred income taxes	7,498	885,331	1,081,241
Other	2,712	320,170	249,285
<b>Net cash provided by operating activities</b>	<b>13,396</b>	<b>1,581,692</b>	<b>1,161,213</b>
<b>Investing Activities:</b>			
Purchase of property and equipment	(11,141)	(1,315,390)	(1,237,434)
Proceeds from sale-leaseback	567	66,940	-
Investments in and advances to equity method investees	(476)	(56,250)	(362,714)
Purchase of other investments	(437)	(51,671)	(399,600)
Deposit to restricted cash	(42,348)	(5,000,000)	-
Payment of guarantee deposits-net	(12,602)	(1,487,911)	(430,455)
Other	(285)	(33,639)	(26,995)
<b>Net cash used in investing activities</b>	<b>(66,722)</b>	<b>(7,877,921)</b>	<b>(2,457,198)</b>
<b>Financing Activities:</b>			
Proceeds from long-term borrowings	16,939	2,000,000	2,000,000
Repayments of long-term borrowings	(11,857)	(1,400,000)	-
Principal payments under capital leases	(20,966)	(2,475,433)	(2,037,133)
Net increase (decrease) in short-term borrowings	8,498	1,003,367	(1,799,768)
Proceeds from issuance of common stock of a subsidiary	-	-	375,000
<b>Net cash used in financing activities</b>	<b>(7,386)</b>	<b>(872,066)</b>	<b>(1,461,901)</b>
<b>Effect of Exchange Rate Changes on Cash</b>	<b>(2,450)</b>	<b>(289,272)</b>	<b>233,098</b>
<b>Net Decrease in Cash</b>	<b>(63,162)</b>	<b>(7,457,567)</b>	<b>(2,524,788)</b>
<b>Cash, Beginning of Period</b>	<b>93,554</b>	<b>11,045,919</b>	<b>13,570,707</b>
<b>Cash, End of Period</b>	<b>30,392</b>	<b>3,588,352</b>	<b>11,045,919</b>

Note (1): The translations of Japanese yen amounts into US dollar amounts with respect to the year ended Mar 31, 2003 are included solely for the convenience of readers outside Japan and have been made at the rate of JPY118.07 = \$1, the approximate rate of exchange on Mar 31, 2003.