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# Financial Results and Earnings Outlook for the First Quarter of the Fiscal Year Ending March 2007 (Consolidated)

August 15, 2006

**Company Name:** Japan Communications Inc.

**Stock Code:** 9424

**URL:** <http://www.j-com.co.jp/>

**Exchange:** Osaka Securities Exchange, Hercules

**Representative:** Frank Seiji Sanda, President and Representative Director

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1. Quarter consolidated financial results • General matters related to achievement

- ① Were there any changes in the accounting method for the current fiscal year? Yes (details reported in attachments)
- ② Were there any changes in the scope of consolidation or use of the equity method? Yes (as follows)  
Consolidated companies added: 1
- ③ Was there any involvement of a certified public accountant or auditor? No

2. Financial results and earnings outlook for the first quarter of the Fiscal Year ending March 2007 (April 1, 2006 – June 30, 2006)

(1) Progress report of management results (consolidated) (Amounts rounded down, percentages rounded)

	Net Sales		Operating Profit		Ordinary Income		Net Income (this quarter)	
	million yen	%	million yen	%	million yen	%	million yen	%
Q1 for FY ending March 2007	928	△23.9	△195	—	△197	—	△192	—
Q1 for FY ending March 2006	1,219	—	60	—	△10	—	△20	—
FY ending March 2005 (for reference)	4,943		173		113		107	

	Net income per share (this quarter)	Diluted net income per share (this quarter)
	yen	yen
Q1 for FY ending March 2007	△858.07	—
Q1 for FY ending March 2006	△110.34	—
FY ending March 2005 (for reference)	495.40	474.61

Note: 1. The percentages displayed in sales, operating profit, etc. show the relative change in relation to the same quarter of the previous year.

2. Diluted net income per share is not shown for the first quarter of the fiscal year ended March 2006 and the first quarter of the fiscal year ending March 2007 due to the fact that there was a quarterly net loss per share.

### Qualitative Progress Report on Results of Operations (Consolidated)

In the first quarter of the FY ending March 2007, data communication service revenue totaled 639 million yen, while telecom service revenue totaled 289 million yen, resulting in combined quarterly total revenue of 928 million yen.

With regards to enterprise data communications services, although demand for a shift from PHS to third generation mobile communication services (hereafter 3G) is increasing (in particular from large-scale customers), JCI has not yet established a 3G interconnection with a 3G-network operator. This fact has slowed our ability to respond to this demand. Further, as companies seek to comply with the stipulations of the Protection of Personal Information Act, an increasing number of companies have forbidden employees from taking laptops outside the office. This fact also contributed to the company showing only a small increase in enterprise service growth over the same period last year.

For data services for individuals, the release last year of a strong new product, “b-mobile hours”, saw a substantial increase in sales for the first quarter of the FY ending March 2006. This, coupled with the sluggish market performance of PHS data communication cards this quarter, meant that sales were lower than in the first quarter of the FY ending March 2006. Accordingly, in this quarter, the data communication service as a whole showed a small decrease over the corresponding quarter last year.

With regards to JCI telecom services, while we are continuing our planned scale-back of these services, as a result of a change in the revenue recognition method used from this FY, the total sales year for JCI telecom services has been reduced to 11 months. Only two of these months fell in Q1, a fact that led to a considerable decrease in sales compared with Q1 of the FY ending March 2006. The change of revenue recognition method has resulted in a decrease in revenue of 146 million yen, and decreases of 34 million yen each to operating profit, ordinary profit and net profit. Further details are provided in the attached documentation.

In relation to profit, as a temporary solution to the demand for a shift from PHS to 3G services, JCI has been offering certain corporate customers 3G network services, which have not been procured through an interconnection with the network operator. It is extremely difficult to provide differentiated services under such procurement conditions and, accordingly, these services are not very profitable. Nevertheless, factors such as the increase in these 3G services have led to a decrease in JCI's gross profit to net sales ratio, as compared to the same period last year. At the end of this quarter, the gross profit to net sales ratio of JCI data communication services stood at 42.5%.

Further, starting this quarter, Arxceo Corporation (headquarters Alabama, USA), a network security company acquired by JCI on March 3, 2006, impacts JCI profit and loss, and Communications Security and Compliance Technologies Inc. (headquarters Georgia, USA), established as the US base of operations for JCI on April 3, 2006, has been newly included in consolidation. The 94 million yen in losses recorded by these two companies in this quarter has been consolidated to operating profit, ordinary profit and net profit.

## (2) Changes in financial condition (consolidated)

	Total Assets	Net Assets	Equity Ratio	Shareholder's equity per share
	million yen	million yen	%	yen
Q1 for FY ending March 2007	5,133	3,598	70.1	16,049.08
Q1 for FY ending March 2006	4,605	3,487	75.7	15,933.81
FY ending March 2005 (for reference)	5,364	3,823	69.6	16,657.01

## (3) Consolidated cash flow situation

	Cash flow from operations	Cash flow from investing	Cash flow from financing	Cash and cash equivalents and end of period
	Million Yen	Million Yen	Million Yen	Million Yen
Q1 for FY ending March 2007	86	△286	1	1,674
Q1 for FY ending March 2006	△56	△303	1,793	2,413
FY ending March 2005 (for reference)	154	△1,609	2,375	1,885

### Qualitative information report on management results (consolidated)

Total assets for this quarter were 5,133 million yen, a decrease of 230 million yen from the end of the previous period. Net assets at the end of the quarter totaled 3,598 million yen, 224 million yen less than at the end of the previous period. The primary cause of this was a decrease in accounts receivable attributable to a change in the revenue recognition method for JCI telecom services. There was very little change in debt from the previous quarter.

### 3. Dividends for the fiscal year ending March 2007 (individual)

As our Group has not yet paid dividends, there is no information to report

### Reference

Consolidated forecast for the fiscal year ending March 2007 (April 1, 2006 – March 31, 2007)

The forecast is unchanged from the forecast announced on May 25, 2006.

	Net Sales	Ordinary Income	Net income (this period)
	Million Yen	Million Yen	Million Yen
Interim Period	—	—	—
Full year	6,193	283	277

Reference: Estimated Net Income per Share (Full Year): 1,235.50 yen

- In relation to Net sales for our Telecom Service, as the component ratio breakdown has changed, the accounting standard for Telecom Service net sales will be changed as of March 2007. This change will mean that the target sales period for our Telecom Service will be 11 months. While this will reduce net sales by 156 million yen and profit by 31 million yen, this fact was taken in to account when calculating the above prediction.
- The above materials may contain items concerning forward-looking statements or perspectives based on predictions. The world economy, state of competition, currency exchange fluctuation, etc. contains risks and uncertainties, thus financial performance by the company may differ distinctly from expectations.

# 1. Consolidated balance sheet for the quarter

	This Quarter (Q1 for FY ending March 2007)		Same Quarter Last Year (Q1 for FY ending March 2006)		Last Fiscal Year (FY ending March 2006 for reference)		
	Amount (thousand yen)	(%)	Amount (thousand yen)	(%)	Amount (thousand yen)	(%)	
<b>Assets</b>							
<b>I Current Assets</b>							
1 Cash and equivalents		1,201,948		2,378,003		1,200,408	
2 Accounts receivable-trade		439,655		606,186		678,706	
3 Marketable securities		472,197		35,119		684,725	
4 Merchandise		47,760		34,630		65,972	
5 Inventory		215,339		89,871		272,002	
6 Accounts receivable-others		—		15,288		23,578	
7 Advances		—		136,080		—	
8 Other		181,313		24,565		49,676	
Allowance for doubtful accounts		△1,000		△1,000		△1,000	
<b>Total current assets</b>		<b>2,557,216</b>	<b>49.8</b>	<b>3,318,745</b>	<b>72.1</b>	<b>2,974,071</b>	<b>55.4</b>
<b>II Fixed Assets</b>							
<b>1 Tangible fixed assets</b>							
(1) Buildings	19,448			16,673		20,314	
(2) Vehicles	2,785			4,437		3,043	
(3) Tools, furniture and equipment	231,695			208,178		234,427	
(4) Mobile Devices	56,084	310,013		87,834	317,123	67,534	
<b>2 Intangible fixed assets</b>							
(1) Trademarks	3,127			3,230		3,096	
(2) Patents	2,108			1,076		950	
(3) Telephone subscriber rights	1,294			1,294		1,294	
(4) Software	629,981			882,520		653,937	
(5) Software in progress	1,066,473			—		841,854	
(6) Consolidated adjustments	453,841	2,156,826		—	888,121	459,586	
<b>3 Investments and other assets</b>							
(1) Security deposits	55,493			46,687		53,296	
(2) Other	37,992			9,312		32,582	
Allowance for doubtful receivables	△19	93,466		△19	55,979	△19	
<b>Total fixed assets</b>		<b>2,560,306</b>	<b>49.9</b>	<b>1,261,225</b>	<b>27.4</b>	<b>2,371,899</b>	<b>44.2</b>
<b>III Deferred assets</b>							
1 New share issuing expenses		16,210		25,474		18,526	
<b>Total deferred assets</b>		<b>16,210</b>	<b>0.3</b>	<b>25,474</b>	<b>0.6</b>	<b>18,526</b>	<b>0.3</b>
<b>Total assets</b>		<b>5,133,734</b>	<b>100.0</b>	<b>4,605,445</b>	<b>100.0</b>	<b>5,364,497</b>	<b>100.0</b>

	This Quarter (Q1 for FY ending March 2007)			Same Quarter Last Year (Q1 for FY ending March 2006)			Last Fiscal Year (FY ending March 2006 for reference)		
	Amount (thousand yen)	(%)		Amount (thousand yen)	(%)		Amount (thousand yen)	(%)	
<b>Liabilities</b>									
I Current liabilities									
1 Accounts Payable	278,018			310,853			287,996		
2 Short-term debt	500,000			—			500,000		
3 Current portion of long term debt	—			37,500			—		
4 Accounts payable - other	139,352			143,376			132,370		
5 Accrued corporate and other taxes	4,764			4,439			13,520		
6 Deferred revenue	496,354			466,362			567,957		
7 Data communication service cost reserves	—			16,749			—		
8 Other	116,613			138,230			39,537		
Total current liabilities	1,535,104	29.9		1,117,510	24.3		1,541,382	28.7	
II Fixed liabilities									
1 Long-term debt	—			—			—		
Total fixed liabilities	—	—		—	—		—	—	
Total liabilities	1,535,104	29.9		1,117,510	24.3		1,541,382	28.7	
<b>Net Assets</b>									
I Shareholders' Equity									
1 Capital stock	2,270,697	44.2		2,193,780	47.6		2,269,710	42.3	
2 Capital surplus	1,577,232	30.7		1,529,475	33.2		1,576,246	29.4	
3 Retained earnings	△225,279	△4.4		△161,376	△3.5		△32,899	△0.6	
4 Treasury stock	△1,741	△0.0		△1,616	△0.0		△1,741	△0.0	
Total Shareholders' Equity	3,620,909	70.5		3,560,263	77.3		3,811,316	71.1	
II Adjustment for valuation and exchange									
1 Unrealized gains of other marketable securities	△17,428	△0.3		—	—		△8,471	△0.2	
2 Exchange conversion adjustment account	△67,565	△1.3		△72,328	△1.6		△69,134	△1.3	
Total adjustment for valuation and exchange	△84,994	△1.6		△72,328	△1.6		△77,606	△1.5	
III Minority shareholders' equity	62,715	1.2		—	—		89,404	1.7	
Total net assets	3,598,629	70.1		3,487,934	75.7		3,823,114	71.3	
Total Liabilities and Net Assets	5,133,734	100.0		4,605,445	100.0		5,364,497	100.0	

## 2. Consolidated income statement for the quarter

	This Quarter (Q1 for FY ending March 2007)		Same Quarter Last Year (Q1 for FY ending March 2006)		Last Fiscal Year (FY ending March 2006 for reference)	
	Amount (thousand yen)	(%)	Amount (thousand yen)	(%)	Amount (thousand yen)	(%)
I Net Sales						
1 Operating revenue	928,640	100.0	1,219,571	100.0	4,943,987	100.0
II Cost of Sales						
1 Cost of sales	604,802	65.1	757,245	62.1	3,035,560	61.4
Gross profit	323,838	34.9	462,325	37.9	1,908,427	38.6
III Selling, general and administrative expenses	519,666	56.0	401,684	32.9	1,734,476	35.1
Operating profit (△ indicates loss)	△195,828	△21.1	60,641	5.0	173,950	3.5
IV Non-operating income						
1 Interest received	8,342		180		8,607	
2 Foreign exchange income	—		165		22,852	
3 Miscellaneous income	341	8,684	244	590	557	32,017
V Non-operating expenses						
1 Interest paid	931		187		493	
2 Foreign exchange loss	7,001		—		—	
3 Expenses relating to share issuance	—		69,369		69,369	
4 New share expense amortization	2,315		2,315		9,263	
5 Loss on sale of securities	520		—		12,800	
6 Other	—	10,768	—	71,873	161	92,088
Ordinary income (△ indicates loss)	△197,912	△21.3	△10,641	△0.9	113,880	2.3
VI Extraordinary loss						
1 Loss on disposal of fixed assets	—		7,551		115	
2 Amortization of consolidated adjustments	5,744	5,744	—	7,551	—	115
Net income before taxes this quarter (△= net loss)	△203,657	△21.9	△18,192	△1.5	113,764	2.3
Taxes	1,452	0.2	2,330	0.2	5,810	0.1
Minority shareholders' earnings	12,729	1.4				
Net income this quarter (△=net loss)	△192,380	△20.7	△20,522	△1.7	107,954	2.2

**3. Quarterly statement of change in consolidated shareholder's equity**  
 Consolidated for this quarter (April 1, 2006 – June 30, 2006)

(unit: million yen)

	Shareholder's Equity					Adjustment for valuation and exchange			Minority Shareholdings	Total Net Assets
	Capital Stock	Capital Surplus	Retained Earnings	Treasury Stocks	Total shareholder's equity	Unrealized gains of other marketable securities	Exchange conversion adjustment account	Total adjustment for valuation and exchange		
Balance at end of previous consolidated accounting period	2,269,710	1,576,246	△32,899	△1,741	3,811,316	△8,471	△69,134	△77,606	89,404	3,823,114
Change during current quarter										
Exercise of stock options	986	986			1,973					1,973
Net income (current quarter)			△192,380		△192,380					△192,380
Changes in items other than shareholder's equity during current quarter (net)						△8,957	1,568	△7,338	△26,289	△34,077
Total change during current quarter	986	986	△192,380		△190,407	△8,957	1,568	△7,338	△26,289	△224,485
Balance at the end of current quarter	2,270,697	1,577,232	△225,279	△1,741	3,620,909	△17,428	△67,565	△84,994	62,715	3,598,629

#### 4. Consolidated cash flow for the quarter

	<b>This Quarter</b> (Q1 for FY ending March 2007)	<b>Same Quarter Last Year</b> (Q1 for FY ending March 2006)	<b>Last Fiscal Year</b> (FY ending March 2006 for reference)
	Amount (thousand yen)	Amount (thousand yen)	Amount (thousand yen)
I Cash flow from operations			
Net income before taxes and others	△190,928	△18,192	113,764
Depreciation and amortization	33,506	38,936	161,201
Intangible fixed asset depreciation	48,148	41,886	188,750
Amortization of new stock expenses	2,315	—	9,263
Amortization of consolidated adjustments	5,744	—	—
Data communication service cost reserve	—	△11,622	△28,372
Interest and dividends received	△8,342	△180	△8,607
Interest charges	931	187	493
Loss on disposal of fixed assets	—	7,551	115
Profit on currency exchange (△=loss)	31,500	—	△15,302
Loss on sale of securities	—	—	12,800
Decrease in notes and accounts receivable	261,738	△43,265	△115,113
Decrease in inventories	74,875	29,328	△175,039
Increase in trade payables	△9,536	8,728	△15,450
Increase in deferred revenue	△71,602	△16,377	85,217
Increase in accrued consumption tax	—	△61,394	△64,703
Other	△91,921	△29,472	9,898
Subtotal	86,428	△53,886	158,916
Net receipt of interest and dividend	8,342	180	8,607
Interest paid	△931	△187	△1,263
Corporate and other income taxes paid	△7,262	2,330	△11,620
Net cash flows from operations	86,577	△56,224	154,640

	<b>This Quarter</b> (Q1 for FY ending March 2007)	<b>Same Quarter Last Year</b> (Q1 for FY ending March 2006)	<b>Last Fiscal Year</b> (FY ending March 2006 for reference)
	Amount (thousand yen)	Amount (thousand yen)	Amount (thousand yen)
<b>II Cash flow from investing</b>			
Purchase of tangible fixed assets	△28,358	△77,832	△209,193
Purchase of intangible fixed assets	△250,440	△225,611	△984,284
Consolidated subsidiary acquisition expense	—	—	△388,056
Security deposit payment expense	△2,197	—	△5,290
Interest from loan collection	—	—	—
Other	△5,409	109	△23,161
Net cash flow from investing	△286,406	△303,334	△1,609,986
<b>III Cash flow from financing</b>			
Change in short-term borrowing	—	—	500,000
Income from share issuance	1,973	1,821,252	1,943,546
Repayment of long term debt	—	△16,500	△54,000
New share issuance expense	—	△10,624	△12,940
Treasury stock acquisition expense	—	△804	△929
Installment repayment expense	—	—	—
Other	—	△60	—
Net cash flow from financing	1,973	1,793,262	2,375,676
<b>IV Exchange difference in cash and cash equivalent</b>	△13,131	1,302	△13,314
<b>V Change in cash and cash equivalents</b>	△210,987	1,435,005	907,016
<b>VI Cash and cash equivalents at beginning of period</b>	1,885,134	978,117	978,117
<b>VII Cash and cash equivalents at end of interim period</b>	1,674,146	2,413,123	1,885,134

## **Regarding changes in the revenue recognition method for the current consolidated fiscal year**

Our company's telecom service procures mobile phone lines from mobile communications carriers and offers value-added services to enterprises such as separate billing for official and personal use. Specifically, we obtain users' communication records from mobile communications carriers and, on the basis of these records, process bills using our company's billing system. Where value-added services such as separate billing are implemented, we bill and collect fees from enterprises (and, if there are private usage portions that are separated, from individuals). Simply put, this process has two-steps: first, communication takes place on a user's mobile phone; and second, based on the record of this communication, charging and billing occurs.

In the past, the accounting standard for telecom services has been based on when the communication on the mobile phone occurred. However, starting this consolidated fiscal year, the accounting standard will be based not on when the communication occurred but when the bills have been processed and charged.

Making this change will increase the value add of our company's telecom service as this value depends on our clients awareness of what has qualitatively changed: the fact that it's not just about communication on mobile phones, but it's also about the included charging and billing system that takes place afterward. Moreover, a planned reduction in the telecom service, which peaked in March 2002, has taken place, in order to focus on the data communication service that began in the same year. In the quarter ending March 2006, the data communication service made up the majority of proceeds of this company. This, coupled with the fact that the telecom service had reached a turning point, led to this decision to change the accounting standard.

Additionally, the fact that this will allow our company and consolidated subsidiaries to produce our financial statements more quickly was also a key reason for implementing this change to the accounting standard.

As a result of the change in the accounting standard from this FY, the total sales for the year of JCI telecom services has been reduced to 11 months. Only two of these months fell in Q1. When compared with the results the telecom service would have achieved in Q1 of the FY ending March 2007 had this change not been implemented, earnings have decreased by 146 million yen, while net operating profit, ordinary profit and net profit have all decreased by 34 million yen.