

# Profile

KDDI Corporation was established in June 1984 as the Dai-ni Denden Planning Company, changing its name to DDI Corporation in April 1985. In June 1985, in the wave of liberalization sweeping the telecommunications sector, DDI received permission to operate as a Type 1 Telecommunications Carrier. DDI began to provide leased circuits in October 1986 and long-distance telephone services in September 1987, thus introducing competition into the Japanese telecommunications market for the first time. In 1989, the companies of the DDI CELLULAR Group—which, excluding OKINAWA CELLULAR TELEPHONE Co., have since merged to form au Corporation—began offering cellular phone services. In 1995, the DDI POCKET Group companies—which have since merged to form DDI POCKET, Inc.,—launched personal handyphone system (PHS) services.

In October 2000, DDI Corporation merged with KDD Corporation and IDO Corporation to form the new DDI Corporation (KDDI\*). On April 1, 2001, the Company changed its name officially to KDDI Corporation. In line with its “Mobile and IP” strategy, which prioritizes mobile communications and IP businesses, KDDI is maximizing its predecessors’ accumulated expertise in domestic, international and mobile telecommunications, as well as their extensive R&D capabilities and management resources, notably a sophisticated optical fiber network-based infrastructure. Through these efforts, the Company is contributing to the advancement of telecommunications and reinforcing its position as a provider of comprehensive communications services that satisfy the needs of its customers.

*\* References to KDDI in this report in the context of fiscal 2000, ended March 31, 2001, refer to DDI Corporation, which was unofficially known as KDDI from the time of the merger and officially became KDDI Corporation on April 1, 2001.*

## Contents

<b>Selected Financial Data</b> .....	<b>1</b>
<b>To Our Shareholders</b> .....	<b>2</b>
<b>Interview with the President</b> .....	<b>4</b>
<b>Review of Operations</b> .....	<b>10</b>
<b>Management Discussion and Analysis</b> .....	<b>18</b>
<b>Consolidated Financial Highlights</b> .....	<b>22</b>
<b>Consolidated Balance Sheets</b> .....	<b>24</b>
<b>Consolidated Statements of Income</b> .....	<b>26</b>
<b>Consolidated Statements of Shareholders’ Equity</b> .....	<b>27</b>
<b>Consolidated Statements of Cash Flows</b> .....	<b>28</b>
<b>Notes to Consolidated Financial Statements</b> .....	<b>29</b>
<b>Report of Independent Accountants</b> .....	<b>37</b>
<b>Corporate Data</b> .....	<b>38</b>
<b>Directors, Auditors and Managing Officers</b> .....	<b>38</b>
<b>Organization</b> .....	<b>39</b>
<b>Corporate History</b> .....	<b>40</b>
<b>Stock Information</b> .....	<b>41</b>
<b>Investor Information</b> .....	<b>41</b>

## Disclaimer Regarding Forward-Looking Statements

Statements contained in this annual report concerning plans, strategies, beliefs, expectations or projections about the future, and other statements other than those of historical fact, are forward-looking statements based on management’s assumptions in light of information currently available and involve risks and uncertainties. Actual results may differ materially from these statements.

Potential risks and uncertainties include, but are not limited to, domestic and overseas economic conditions; fluctuations in currency exchange rates, particularly those affecting the U.S. dollar, euro and other overseas currencies in which KDDI or KDDI Group companies do business; and the ability of KDDI and KDDI Group companies to continue developing and marketing services that enable it to secure new customers in the communications market—a market characterized by rapid technological advances, the steady introduction of new services and intense price competition.

Note: All references to fiscal years in this annual report refer to the fiscal period ended, or ending, March 31.

# Selected Financial Data

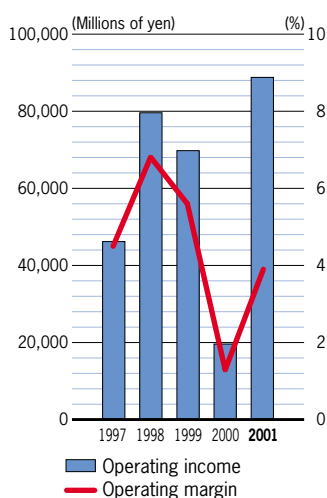
KDDI Corporation and Consolidated Subsidiaries

Years ended March 31, 1997-2001	Millions of yen					Millions of U.S. dollars
	2001	2000	1999	1998	1997	2001
<b>Consolidated Statements of Income:</b>						
Total operating revenues	¥2,268,646	¥1,525,953	¥1,246,582	¥1,178,345	¥1,016,398	\$18,310
Operating income	88,783	19,614	69,874	79,611	46,194	717
Income (loss) before income taxes and minority interests	45,902	(42,786)	49,715	65,018	37,880	370
Net income (loss)	13,427	(10,468)	17,061	8,310	(26,161)	108
<b>Consolidated Balance Sheets:</b>						
Total assets	¥3,639,364	¥1,999,008	¥1,585,848	¥1,296,747	¥1,005,673	\$29,373
Interest-bearing debt	2,097,627	1,433,128	1,068,616	779,786	614,537	16,930
Total shareholders' equity	845,091	228,574	231,208	218,321	175,556	6,821
<b>Per Share Data (Yen):</b>						
Net income (loss)	¥4,467	¥(4,603)	¥7,501	¥3,807	¥(12,031)	\$36.05
Cash dividends	1,790	1,790	1,790	1,790	1,790	14.45
<b>Other:</b>						
Return on equity (%)	2.5%	-4.6%	7.6%	4.2%	-13.7%	
Return on assets (%)	0.5	-0.6	1.2	0.7	-2.8	
Depreciation and amortization	¥334,647	268,447	199,176	159,767	115,476	2,701
Capital expenditure	442,040	395,164	395,366	331,187	326,604	3,568
Number of shares issued and outstanding (thousands)	4,241	2,274	2,274	2,274	2,174	
Number of employees	6,812	2,586	2,990	2,927	2,796	

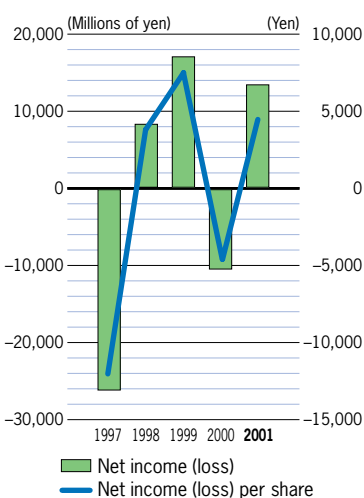
Notes: 1. U.S. dollar amounts above and elsewhere in this report are converted from yen, for convenience only, at the rate of ¥123.90=\$1, the approximate exchange rate on March 31, 2001.

2. Interest-bearing debt consists of short-term loans and current portion of long-term loans, long-term loans, bonds and long-term accounts payable.

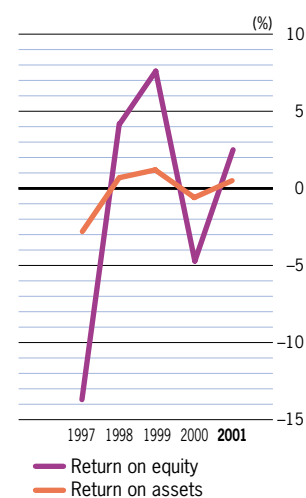
Operating Income and Operating Margin



Net Income (Loss) and Net Income (Loss) per Share



Return on Equity and Return on Assets



# To Our Shareholders

## From DDI to KDDI

DDI's merger with KDD and IDO on October 1, 2000, marked the debut of the new DDI—now KDDI—a new core telecommunications provider with an extensive customer base and global network, and substantial resources in fixed, mobile, domestic, international, voice, data and IP services.

During fiscal 2001, ended March 31, 2001, KDDI focused on integrating the accumulated cutting-edge technological capabilities of its three predecessors, as well as on consolidating personnel and organizational systems and enhancing the efficiency of capital investment. Prior to the merger, in June 2000, IDO and the DDI CELLULAR Group acquired a license to offer cellular phone services based on IMT-2000, and the following month adopted *au* as the integrated brand name for jointly provided seamless mobile communications services. Since then, KDDI has focused on expanding these services nationwide and establishing the *au* brand. To enhance the efficiency of *au* services, in November 2000 seven of the eight DDI CELLULAR Group companies (excluding OKINAWA CELLULAR) merged to form au Corporation. On March 31, 2001, an exchange of shares with au Corporation made the company a wholly owned subsidiary of KDDI.

In network and IP services, we began offering a number of attractive new discount services in preparation for the May 2001 launch of the MYLINE preferred carrier selection service. We worked to integrate and enhance the DION Internet access service and NEWEB, a similar service previously offered by KDD. In November 2000, we commenced operations at the newly completed Odaiba Data Center in Tokyo. This large-scale facility will play a crucial role in our efforts to expand e-business services. Prior to this, in October 2000 we began construction of PERSEUS, a next-generation terabit-level IP network, and introduced its first PERSEUS service, ANDROMEGA IP-VPN, which allows customers to create Internet-based private internal telecommunications networks.

We also promoted selective cultivation of operations, in line with which we concentrated investment in high-growth KDDI Group businesses and divested Brazilian cellular phone services affiliate GLOBAL TELECOM S.A.

Our efforts in fiscal 2001 contributed to a 48.7% increase in consolidated operating revenues, to ¥2,268.6 billion. Operating income soared 352.7%, to ¥88.8 billion, while net income climbed ¥23.9 billion from a loss in fiscal 2000, to ¥13.4 billion.

## The Mobile and IP Strategy

Deregulation and technological progress are transforming Japan's telecommunications industry, intensifying cross-border and cross-industry competition. At the same time, revolutionary advances in information technology (IT) and the rapid diffusion of cellular phones and the Internet are spurring demand for increasingly personalized and diverse communications options, as well as accelerating the shift to multimedia services combining voice-, data- and image-based communications. In the area of mobile communications and data transmission, various new rate plans and services have been introduced. We also see the launch of next-generation mobile communications services in fiscal 2002 as an important new opportunity for us to expand operations.

To capitalize on this opportunity and ensure sustained growth in corporate value, we have set forth concrete numerical targets for fiscal 2005, namely, total operating revenues of ¥3,900.0 billion and earnings before interest, taxes, depreciation and amortization (EBITDA) of ¥900.0 billion. To facilitate achievement of these targets, we have launched a new management restructuring program, which will run from fiscal 2002 through fiscal 2005.

In line with this program, which identifies our *au* and IP businesses as key focus areas, we are pursuing our Mobile and IP strategy, which calls for the concentrated investment of management resources in high-growth mobile telecommunications and IP services. We have already announced several key moves. These include the merger of au Corporation into KDDI on October 1, 2001, which will reinforce and consolidate mobile communications services, and the introduction of CDMA2000 1x, a next-generation cellular phone system, which will enable us to expand our share of the next-generation mobile multimedia communications market, in the second half of fiscal 2002. To enhance IP services, we will emphasize assertive marketing of our data center services under the integrated brand name *dotsquare* and broaden our focus to include e-business platforms for small and medium-sized companies as well as major Internet service providers (ISPs) and application service providers (ASPs).

Strategies for noncore businesses focus on cultivating businesses that maximize existing strengths—such as DDI POCKET's PHS data transmission services. At the same time, we will also undertake a drastic reorganization of noncore businesses by, for example, consolidating the



From left to right: Jiro Ushio, Tadashi Onodera, Yusai Okuyama

operations of affiliates and certain businesses overseas and divesting unpromising businesses.

Another crucial goal is to increase the efficiency of capital investment. To this end, we will maintain total consolidated capital investment below total depreciation and amortization, while at the same time concentrate more than 90% of investment in our core *au* and IP businesses. Finally, we will endeavor to lower interest-bearing debt, which has ballooned owing to the merger, to ¥1.0 trillion by fiscal 2005, by improving free cash flow, securitizing real estate assets and selling assets.

### Management System Reform

Effective June 26, 2001, former president Yusai Okuyama assumed the position of vice chairman, and former vice president Tadashi Onodera took over as president. These new appointments were accompanied by a drastic reform of the Company's management system and the establishment of a new management structure. To accelerate decision making and implementation, we have reduced the number of directors on the board to 13, from 53.

We have also made structural reforms, replacing our conventional, business division-led order with a flatter organization in which divisions and departments are answerable directly to the president. As part of this reorganization, we have established a system whereby six directors on the board oversee 16 division general managers who are responsible for supervising day-to-day operations.

### Toward Higher Corporate Value

The change of our name to KDDI on April 1, 2001, marked the real debut of the new company created through the merger of DDI, KDD and IDO. We recognize, however, that the real test of its corporate value is still ahead. Accordingly, we intend to allocate the resources necessary to ensure its ability to provide innovative, exclusive services that respond to the needs of customers, thereby securing the trust of shareholders, business partners and other stakeholders, and facilitating communications that contribute to the advancement of the global community. In these and all our endeavors, we look forward to the support and encouragement of our shareholders.

August 2001

**Jiro Ushio**

Chairman, Member of the Board, Representative Director

**Yusai Okuyama**

Vice Chairman, Member of the Board, Representative Director

**Tadashi Onodera**

President, Member of the Board, Representative Director

## Interview with the President

### Rebuilding *au* and IP Services

**Q: Nine months have passed since the merger of DDI, KDD and IDO and the debut of KDDI. The original merger announcement and the creation of a new company in December 1999 was accompanied by the introduction of the Mobile and IP strategy. What does this strategy involve?**



As you know, Japan's telecommunications industry is experiencing particularly sharp growth in the subscriber base for mobile telecommunications. The number of cellular phone and PHS subscribers surpassed that of fixed-line telephone service subscribers in March 2000, and continued rising to almost 66.8 million as of March 31, 2001. We are also seeing rapid growth in Internet services, with 47.1 million users in Japan as of December 31, 2000, and more than 87.2 million expected to be online by the end of 2005. The Mobile and IP strategy positions these two high-growth fields as the new company's core businesses, to be cultivated through intensive, focused investment of management resources

to enhance the company's profitability and growth potential, thereby contributing to continuous growth in corporate value. Specifically, this means we will focus investment of resources—people, facilities, funds and technologies—to the development of our *au* and IP businesses.

Among noncore businesses, we will concentrate on high-speed data transmission services that capitalize on the features of DDI POCKET's PHS systems. We will also continue to promote TU-KA personal digital cellular (PDC) system services by focusing on reasonably priced voice-transmission and low-speed data-transmission services. For the businesses of affiliated companies, we will apply the concept of selective, concentrated investment. We have divided these companies into three categories: candidates for initial public offerings (IPOs) in the foreseeable future, low-profit earners, and those that are unprofitable and likely to remain that way. We will make forward-looking investments in companies in the first category. We will restructure companies in the latter two categories, and divest businesses when appropriate.

We have set concrete numerical targets for the Mobile and IP strategy. As a consequence of the measures I have just outlined, we are aiming to achieve total operating revenues of ¥3,900.0 billion and EBITDA of ¥900.0 billion in fiscal 2005.

**Q: What measures have you implemented to date in line with this strategy?**

In June 2000, prior to the merger, we acquired a license to offer cellular phone services based on IMT-2000, recognized as the global standard for the next generation of mobile telecommunications services. The following month, IDO and the DDI CELLULAR Group adopted *au* as the integrated brand name for nationwide jointly provided seamless mobile telecommunications services offered—a brand name we have worked to establish in the year since. Following the merger, in November 2000 we significantly improved the e-mail function of the EZweb mobile Internet access service. Also in November, seven of the eight DDI CELLULAR Group companies—excluding OKINAWA CELLULAR, which is already listed on the over-the-counter market—merged to form *au* Corporation, in a move aimed at enhancing the efficiency of the *au* business and facilitating the rapid expansion of services. The company became a wholly owned subsidiary of KDDI after an exchange of shares on March 31, 2001.

In the IP business, we integrated the DION and NEWEB Internet access services under the DION name. In November 2000, we completed construction of, and commenced services at, the Odaiba Data Center in Tokyo, a large-scale facility that will play a crucial role in our efforts to expand e-business services.

**Q: How do you evaluate your achievements so far?**

To reinforce noncore businesses, we promoted selective and concentrated investment. Of note, we divested GLOBAL TELECOM of Brazil.

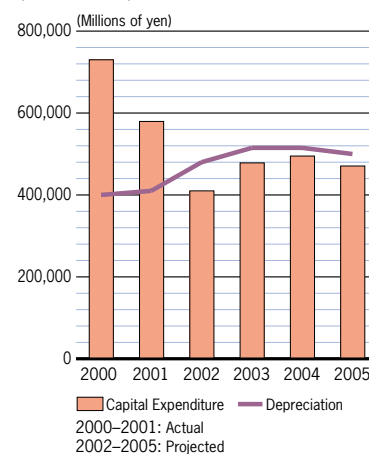
We have taken several key steps to increase the appeal of *au* services, including introducing Japan's first discount rate plan for students—called *Gakuwari*—in November 2000, enhancing EZweb's color content and offering attractively colored terminals. As a consequence, the number of *au* service subscribers as of March 31, 2001, reached approximately 11.0 million, 8.5% higher than the combined *au* subscriber bases of IDO and the DDI CELLULAR Group on March 31, 2000. Subscribers for the DION dial-up Internet access service exceeded 1.8 million on March 31, 2001, approximately double the number a year earlier. Such achievements contributed to total operating revenues of ¥2,268.6 billion and net income of ¥13.4 billion, so I think we have been fairly successful. Many tasks remain, however, including reducing interest-bearing debt, which increased as a result of the merger; integrating the mobile, fixed-line and IP services of the three original companies; and reforming our management system to expedite decision making.

### Implementing Management Reform

**Q: Was the new management reform plan you announced immediately following your appointment as president of KDDI intended as a concrete scheme to address these remaining tasks?**

Yes. Before the merger, we announced a target for interest-bearing debt for fiscal 2005 that required us to shave close to ¥1,000 billion. Immediately after the merger, interest-bearing debt amounted to ¥2,240.9 billion. By the end of fiscal 2001, we had reduced this to ¥2,097.6 billion. The new management reform plan takes this effort one step further by outlining a strategic focus that emphasizes stability and growth as well as the reduction of interest-bearing debt. Specifically, the plan calls for maintaining Groupwide capital investment within the bounds of depreciation and amortization and concentrating investment in core businesses. It also calls for using free cash flow generated by *au* and other core services and the securitization of real estate and sale of assets to reduce interest-bearing debt by ¥600.0 billion and ¥400.0 billion, respectively.

Capital Expenditure and Depreciation  
(As of March 31)



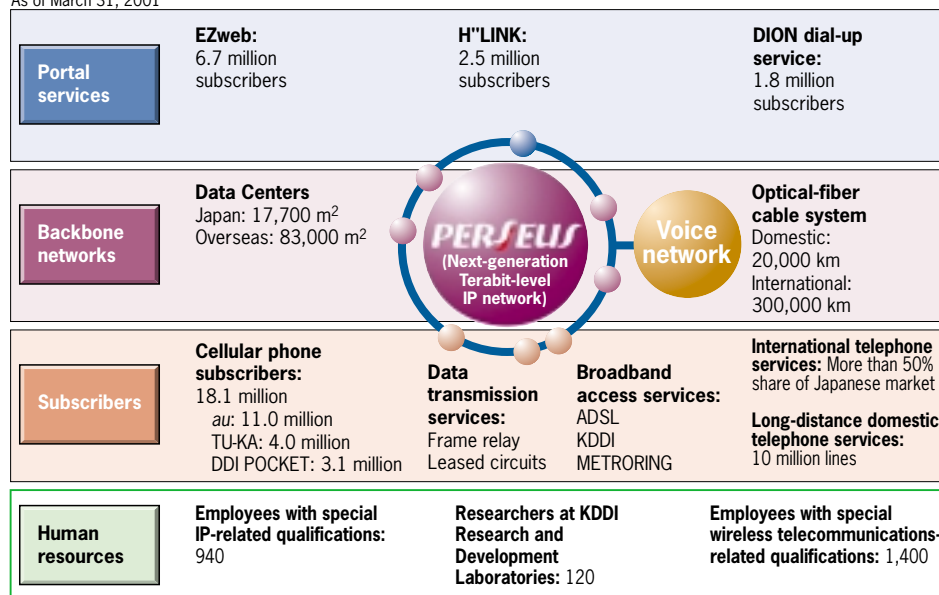
**Q: Is it possible to grow core businesses, such as *au* and IP services—especially when you are looking at launching next-generation cellular phone systems—and lower interest-bearing debt at the same time?**

Yes, I think it is. We will introduce our first next-generation cellular phone service in the current period, but will focus initially on systems operating in the 800MHz bandwidth, enabling us to use the existing cdmaOne infrastructure and therefore maximize profitability. We expect to spend only ¥200.0 billion for capital investment in new systems—the 2GHz CDMA2000 1x and the 800MHz CDMA2000 1xEV—between fiscal 2002 and fiscal 2004, as well as a maximum of ¥780.0 billion to expand facilities for 800MHz CDMA2000 1x, to accommodate an increased number of subscribers. In contrast, other carriers launching 2GHz wideband CDMA (W-CDMA) systems are likely to require a minimum of ¥1,000.0 billion—in addition to the capital investment they are committed to for their existing 800MHz or 1.5GHz PDC systems. In other words, we will be able to maximize our forward-looking investment in cdmaOne infrastructure.

**Q: What resources does KDDI have to ensure achievement of the medium-term strategic goals it has set ?**

We offer three Internet portal services: EZweb, H"LINK and DION. As of March 31, 2001, subscribers to EZweb reached 6.7 million, while subscribers to H"LINK and DION dial-up services numbered 2.5 million and 1.8 million, respectively. We have fiber-optic cable backbone networks of more than 20,000 kilometers in Japan and over 300,000 kilometers overseas, as well as data center space of 17,700 square meters in Japan and 83,000 square meters overseas. The combined subscriber base for our three mobile telecommunications services—*au*, TU-KA and DDI POCKET—is 18.1 million. We command more than 50% of Japan's international telephone services market and have more than 10.0 million long-distance domestic subscriber lines. To corporate users, we offer frame relay services and leased circuits, as well as asynchronous digital subscriber line (ADSL) services, KDDI METRORING (local optical fiber networks) and other broadband access options. Finally, we have highly trained people to support these services, including 940 IP specialists and 1,400 mobile telecommunications experts, as well as KDDI Research and Development Laboratories, Inc., a world-renowned R&D facility staffed by 120 top-flight researchers working in such leading-edge areas as video transmission and voice recognition technology, and Internet Protocol Version 6 (IPV6), which will play a major role in the future expansion of our mobile and IP businesses.

**KDDI Group Resources**  
As of March 31, 2001



**Q: Are you also investing management resources in MYLINE preferred carrier selection services?**

Yes, we are allocating considerable resources to MYLINE services at the moment, primarily because we believe any loss of our share of the markets for domestic long-distance and international fixed-line telephone services would weaken the foundation of our network operations. We are aiming for 10 million MYLINE subscriber lines by the end of October 2001, and will continue to market services intensively until then, after which we will shift human and financial resources to our *au* and IP businesses. As of July 2001, we had achieved approximately 60% of our MYLINE target, indicating we will have no trouble reaching 10 million by October 2001. Of course, our primary focus remains on domestic long-distance and international services. We are newcomers in the market for local services; nonetheless, we recognize the importance of this business to our future marketing capabilities and will continue to approach it from this angle.



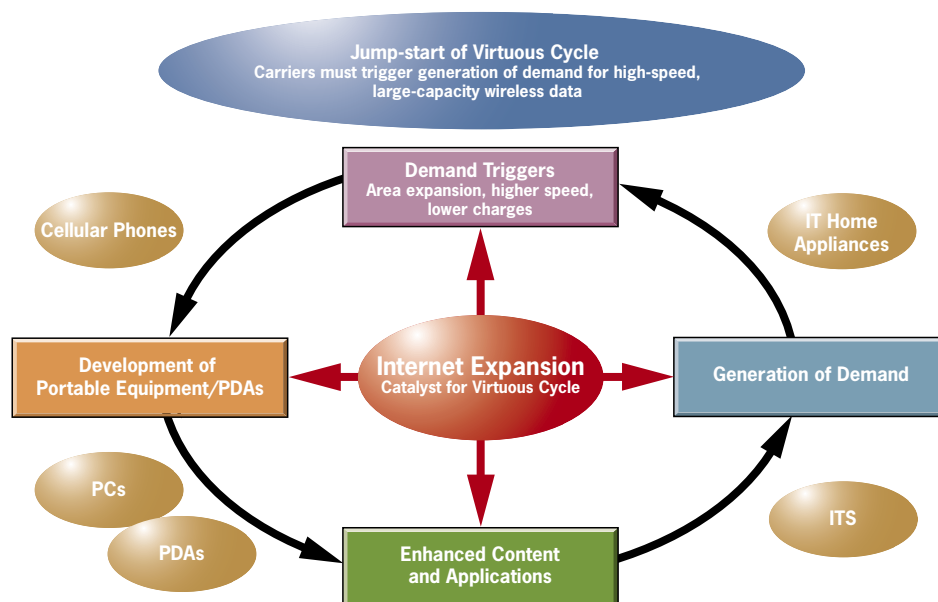
**Q: What strategies will you implement in the au business?**



We are targeting a market share in excess of 20% and more than 17 million *au* subscribers by the end of fiscal 2005. We see the coming months—prior to the full-scale launch of W-CDMA services—as a crucial opportunity to increase our market share. We will take advantage of this opportunity by taking decisive steps to differentiate our services from W-CDMA, particularly by launching innovative new services that maximize the features of CDMA2000 1x and CDMA2000 1xEV. We expect to make CDMA2000 1x services available nationwide in the second half of fiscal 2003. We also launched Bluetooth-compatible terminals in June 2001 and Java-compatible terminals in July. Later on, we will also introduce terminals that are compatible with wireless application protocol version 2.0 (WAP2.0), enabling us to offer Java-based data exchange, gpsOne location positioning services, music downloading, video playing and other attractive new functions. We will enjoy a particular advantage in the area of gpsOne services: whereas W-CDMA subscribers will require a special terminal to use gpsOne, subscribers to CDMA2000 1x will be able to use the service from standard terminals.

After the launch of CDMA2000 1xEV, we will emphasize initiatives aimed at maximizing our capabilities as a carrier to expand our service area, further increase transmission speeds and reduce rates. Through such initiatives, we will encourage efforts to develop mobile telecommunications and personal digital assistant (PDA) terminals and to enhance content and applications. We will also strive resolutely to cultivate new demand for high-speed, high-capacity wireless data transmission services encompassing such concepts as intelligent transportation systems (ITS) and networked household appliances. In the area of content and applications development, we expect to see increased use of new development schemes, such as revenue sharing, in addition to more conventional approaches, such as providing funding and lending server and transmission routes. New development approaches have already yielded considerable results in the realization of new services and business models, such as mobile virtual network operator (MVNO) services, which are mobile telecommunications services provided by firms leasing network capacity from other carriers. For example, in April 2001 SECOM Co., Ltd., Japan's leading security services provider, launched Coco-Secom, a positioning system that incorporates *au*'s cdmaOne network. This is similar to an MVNO service.

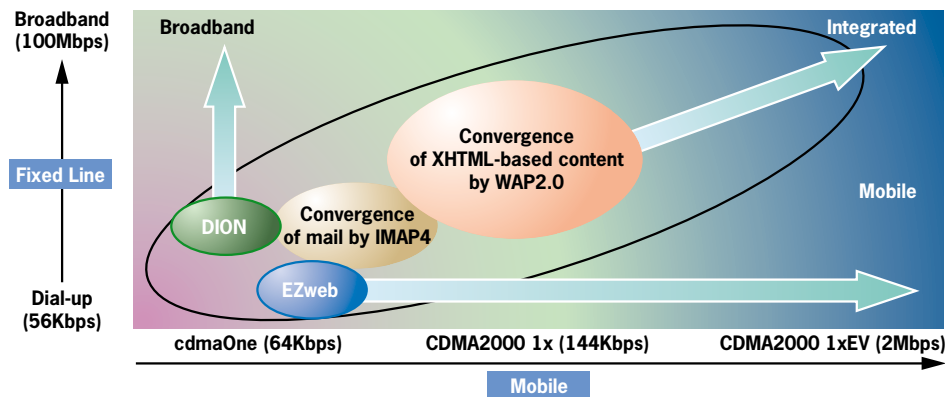
#### Creation of New Markets—CDMA2000 1xEV



**Q: How do you plan to improve the profitability of *au* services?**

Approximately 80% of *au* subscribers have already shifted from PDC to cdmaOne. This is expected to boost average revenue per user (ARPU), particularly for data transmission services. Moreover, efforts by our purchasing department to integrate purchasing of terminals have also lowered terminal-related costs, enabling us to factor costs into the selection of suppliers and choose manufacturers in, for example, the Republic of Korea. We achieved further reductions by introducing Binary Runtime Environment for Wireless (BREW), which will significantly reduce software development costs, the largest component of terminal development costs. Such strategies are helping us eliminate the considerable cost burden of *au* services, and we expect, therefore, to see a steady recovery in profitability.

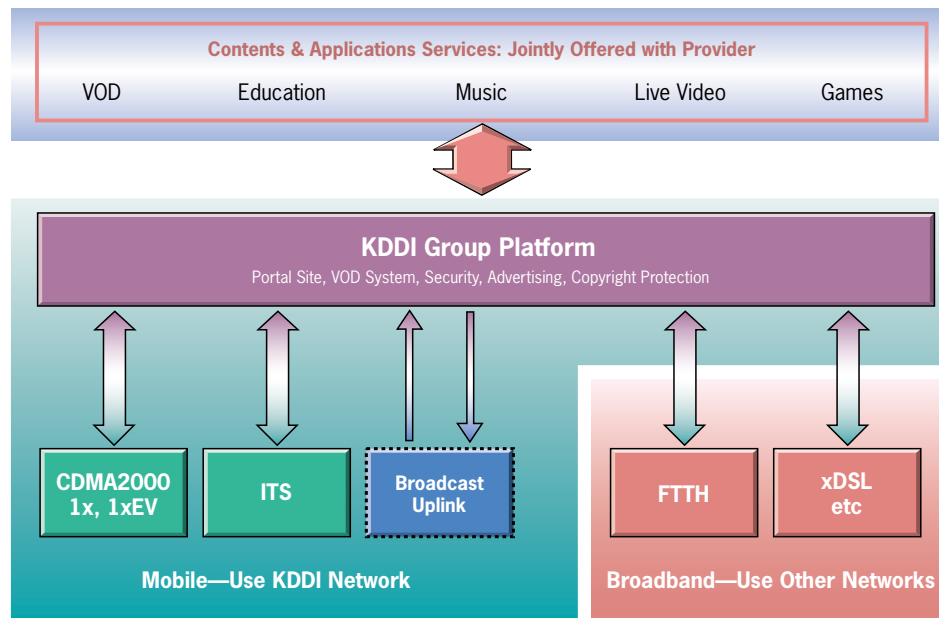
**Integration of Mobile and Fixed-Line Internet Use**



**Q: What is your outlook for the IP business?**

First, we will continue to take decisive steps toward integration of EZweb and H<sup>2</sup>LINK with DION and other fixed-line IP services. In November 2000, we introduced Internet Messaging Access Protocol version 4 (IMAP4), enabling us to consolidate the e-mail functions of these services. In the coming months, we will introduce WAP2.0, and

**IP Business Domains**





**Q: What time frame have you set for realizing the strategic goals you have outlined?**

**Q: In closing, what are your views on having been appointed to guide the new KDDI?**

launch intensive efforts to consolidate XHTML-based content. In the area of ADSL, fiber-to-the-home (FTTH), fixed wireless access (FWA) and other broadband access services, our efforts will focus on applications, rather than speed. In March 2002, we plan to launch FTTH services on a trial basis in Tokyo and Nagoya. To this end, we will work with local content developers, household electronics manufacturers and broadband service-related firms to offer high-quality IP-based telephone services and high-speed Internet access with a view to eventual coordination with mobile telecommunications services. The results of this trial will serve as the basis for a new commercial service in the future.

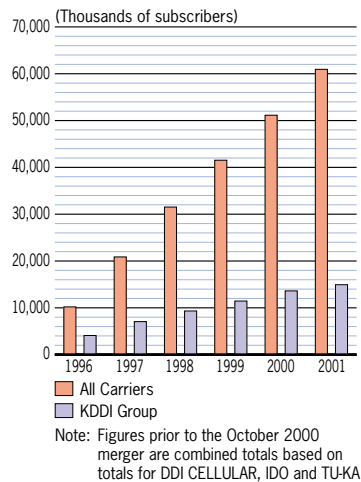
We will also broaden the focus of our data center business beyond large-scale ISP and ASP services to include the provision of common platforms for portal sites, video-on-demand (VOD) systems and security, advertising and certification services for small and medium-sized corporations. In the solutions business, we will expand operations by offering services that make use of fixed-line and mobile telecommunications. ITS development will focus on constructing a new business model through ongoing, cooperative research with Toyota Motor Corporation, as well as trials using the CDMA2000 1x and CDMA2000 1xEV cellular telephone systems.

Until recently, KDDI had 53 directors, a fact that understandably gave rise to questions about the efficiency of decision making. Top management addressed this problem by establishing a 10-person management committee and a management strategy development department, and, at the annual shareholders' meeting on June 26, 2001, voters approved a management system reform program that reduced the number of directors on the board to 13. This number includes five non-standing directors, so decision-making authority actually rests with the eight standing directors. We also made major structural modifications, replacing our top-down divisional organization with a flatter configuration under which operations departments and divisions are answerable directly to the president. In line with this change, we decreased the number of division general managers to 16, from 22. We are confident these reforms have positioned us better to respond to a rapidly changing operating environment.

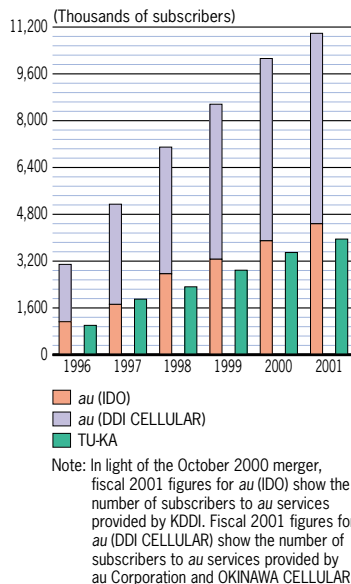
Despite the fact that my background is in engineering, I believe that all three of the original companies—DDI, KDD and IDO—have traditionally placed too much emphasis on technology. This has carried over to the new company. To date, we have put too little effort into ascertaining customer needs and how we might best meet them. Simply having networks will not be enough to ensure the success of the Mobile and IP strategy or the generation of sufficient profits. Moving away from the traditional telecommunications carrier mentality—that is, the idea that our business is to sell units of time, speed and line capacity—and toward a mentality that focuses on the efficient provision of attractive applications and content will be essential to improving our profitability. KDDI's ultimate goal is to provide a full range of telecommunications services that facilitate the transmission of voice, text and video data, using fixed-line and mobile systems, from the office, the home and eventually—using ITS—from vehicles. While leading-edge technology will certainly be necessary, our success will depend on our ability to understand the market and provide services that respond to customer needs. By narrowing our focus to highly profitable, high-growth services that maximize our specific capabilities, we will continue striving to ensure customer satisfaction and, by doing so, to achieve solid growth in corporate value.

# Review of Operations

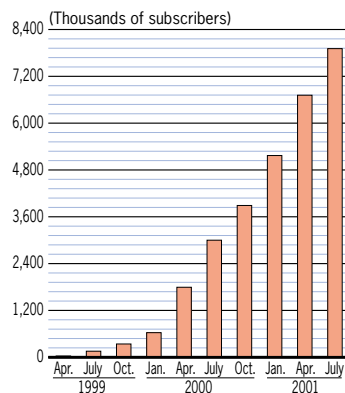
Total Cellular Phone Subscribers:  
All Carriers and KDDI Group  
(As of March 31)



Total *au* and TU-KA Subscribers  
(As of March 31)



Total EZweb Subscribers  
(As of the 1st of each month)



## Expanding mobile telecommunications for individual users

### Designing the future of mobile telecommunications with a wide range of technologies and advanced systems

Japan's telecommunications market totaled an estimated ¥17.5 trillion in fiscal 2001, an increase of 7.3% from fiscal 2000. Mobile telecommunications accounted for approximately ¥7.4 trillion of the total, rising 8.8% from the previous period. As of March 31, 2001, the number of subscribers for cellular phone contracts amounted to 60.9 million, up 19.2% and equivalent to 48.0% of the country's population.

A major player in the rapidly growing mobile telecommunications market, KDDI offers a full range of services encompassing *au* and TU-KA cellular phone services and DDI POCKET's PHS services. We are working to respond to the needs of customers by maximizing the distinguishing features of each of these systems. We are also expanding our share of this market by offering mobile Internet connection services, such as EZweb, available with *au* and TU-KA, and DDI POCKET's H"LINK.

#### *au* Services

Subsequent to receiving approval for the future operation of IMT-2000 services, IDO and the DDI CELLULAR Group adopted the integrated *au* brand name and began working to expand operations nationwide and encourage brand recognition. In November 2000, seven of the eight DDI CELLULAR Group companies merged to form *au* Corporation, which was made a wholly owned subsidiary of KDDI in March 2001 through a share exchange.

During the period under review, efforts to expand *au* services focused specifically on young cellular phone users. We developed new terminals featuring color liquid crystal (LC) displays, fold-up models, memory sticks and a host of other exciting features. In November 2000, we introduced *Gakuwari*, Japan's first discount cellular phone service plan for students. Also in November, we sought to increase the attractiveness of EZweb by launching a new, easier-to-use e-mail service, dubbed @mail.

To enhance content, we launched an advertising service and EZnavigation, a road and rail navigating service using a location finding function. We also introduced EZportal, which enables users to choose their own first-page default setting. New features and services have also facilitated greater access to lifestyle- and entertainment-related web sites, bringing the total number of official sites accessible from an *au* phone to 752 as of March 31, 2001.



Bluetooth-compatible handset

ezplus-compatible handset

On the sales front, we expanded our nationwide network of *au* Shops, which numbered 2,360 at the end of the period. We also stepped up training for our own marketing staff and shop salespeople. In another move aimed at reinforcing sales capabilities, we cooperated with Toyota to post information on *au* services via Toyota's 750 PiPit Information Corners, which are located in dealerships. To enhance cdmaOne-based services, we introduced GLOBAL PASSPORT, a global roaming service that currently enables subscribers to use their *au* phones and phone numbers for voice communications in six countries overseas, as well as in Japan.

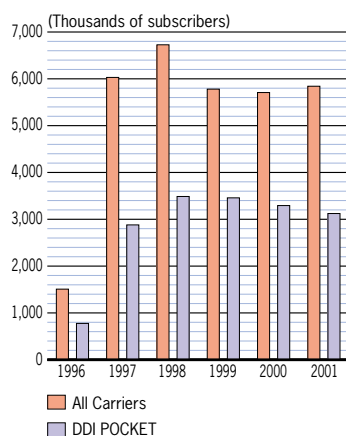
As of March 31, 2001, there were approximately 11.0 million *au* subscribers in Japan. We will continue to take steps to enhance *au* services and increase our market share. In July 2001, we introduced *ezplus*, a Java-based Internet access service. In autumn 2001, we will launch *gpsOne*, a high-precision geographical information system based on GPS, and in fiscal 2002, we will commence CDMA2000 1x services. At the same time, we will work to make *au* Japan's leading cellular phone service brand.

### TU-KA

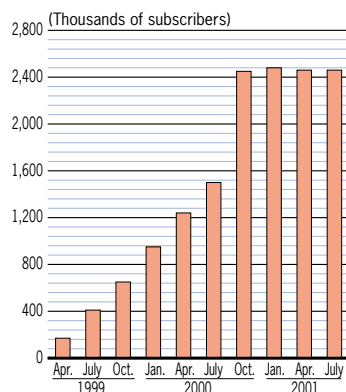
The three companies comprising the TU-KA Group provide PDC-system cellular phone services in the 1.5GHz bandwidth. Basic, reasonably priced services, plus access to EZweb, have helped make TU-KA one of the most popular services among young cellular phone users. As of March 31, 2001, there were nearly four million TU-KA subscribers nationwide.

In July 2000, we introduced CM Call, which enables users to call up a specified number and listen to commercial advertisements, thereby earning a specified period of free calling time. To enhance TU-KA's appeal to noncore users, in January 2001 we launched new rate schemes for families and businesses. We will continue to reinforce the popularity of TU-KA by maximizing the innovative features of the PDC system to expand EZweb access to entertainment-related sites and improve e-mail functions.

Total PHS Subscribers:  
All Carriers and DDI POCKET  
(As of March 31)



Total H<sup>2</sup>LINK Subscribers  
(As of the 1st of each month)



### DDI POCKET

As of March 31, 2001, DDI POCKET's PHS services had approximately 3.1 million subscribers, or more than 50% of Japan's PHS services market. DDI POCKET's H<sup>2</sup> (pronounced "edge") hybrid mobile terminal offers excellent sound quality, high resistance to call dropout and high-speed 64Kbps data transmission, earning it a particularly solid following among corporate users.

In August 2000, DDI POCKET began offering H<sup>2</sup>LINK, an innovative package combining Internet access, e-mail, ASP, e-business, high-capacity content downloading and other attractive services. In November 2000, DDI POCKET launched Feel H<sup>2</sup>, which enables users to enjoy simple graphics and music as well as the system's basic features, thereby attracting considerable attention as a new download medium suited to the demands of the multimedia telecommunications age. In the years ahead, we will work to maximize the high speed of PHS to offer more attractive data transmission-oriented services. At the same time, we will bolster profitability by raising the efficiency of personnel and sales costs and capital investment.

### CDMA2000 1x and CDMA2000 1xEV

The IMT-2000 system is attracting attention worldwide as the global standard for the next generation of mobile telecommunications systems. In fiscal 2002, KDDI will launch *au* cellular telephone services based on CDMA2000 1x—an IMT-2000-based system that supports communications at a maximum of 144Kbps—in major metropolitan areas. In autumn 2002, we plan to launch CDMA2000 1xEV, a high-capacity system capable of supporting data transmission at a maximum of 2.4Mbps.

CDMA2000 1x is an enhanced version of *cdmaOne*. Accordingly, the necessary infrastructure is already in place, enhancing the efficiency of capital investment. CDMA2000 1xEV is a mobile data transmission system optimized for Internet communications with an average data throughput per frequency 2.4 times that of standard

Next-generation mobile telecommunications service concept models



W-CDMA. We will take advantage of the shift toward next-generation mobile telecommunications services to promote the integration of mobile telecommunications and data transmission services and expand our share of this new, multimedia telecommunications market.

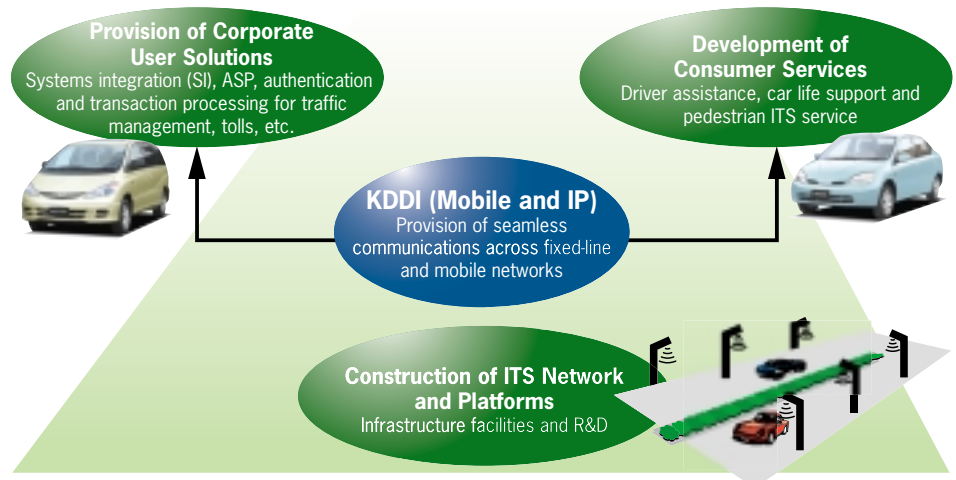
**CDMA2000 Launch Plan**

	Fiscal 2001		Fiscal 2002		Fiscal 2003		Fiscal 2004	
	1st half	2nd half	1st half	2nd half	1st half	2nd half	1st half	2nd half
<b>Product Roll Out</b>			<ul style="list-style-type: none"> <li>Bluetooth (June)</li> <li>Java (July)</li> </ul>					
<b>System Roll Out</b>								

**ITS**

ITS refers to new transport and road management systems that are comprised of an advanced information and telecommunications network for motor vehicle users, roads and vehicles. ITSs already in use include the Vehicle Information and Communication System (VICS), launched in April 1996, which transmits real-time information on slowdowns, accidents and other traffic problems to drivers, and the Electronic Toll Collection (ETC) system, launched in March 2000, which enables drivers to make automatic payments at tollgates, as well as several other systems. Furthermore,

**KDDI (Mobile and IP)**



**ITS Business Foundation of KDDI**

- Mobile phone services (cdmaOne, CDMA2000), DSRC, digital broadcasting, etc.
- Highway optical-fiber network, next-generation basic network, broadband platforms
- R&D (wireless, image, network management, mobile IP and mobile commerce technologies)

Dedicated Short-Range Communications (DSRC) system technologies are expected to be put into practical use by 2005.

With 9,000 kilometers of optical-fiber cable paralleling the nation's expressways and advanced wireless technologies honed in the competitive mobile telecommunications market, we are particularly well positioned to play a key role in this effort. In the belief that ITS will ultimately require the development of new vehicle steering systems, we are currently working with Toyota to develop related technologies.

The ITS market, including communications, content, equipment and infrastructure segments, is estimated to amount to ¥60.0 trillion between 2000 and 2016. We will continue to push forward with the aim of securing the top share of communications aspects of this market.

As part of our ITS development efforts, we recently developed a road information service for pedestrians. The Pedestrian ITS Portal Service enables pedestrians to ask for directions and receive answers verbally via cellular telephone. We intend to begin sales of this service in fiscal 2002.

## Capitalizing on a superior infrastructure and state-of-the-art technologies to promote advanced network and IP services

### Using our high-capacity global optical fiber network to increase this segment's share of operating income

While the number of fixed-line telephone subscribers in Japan continues to decline, the number of Internet users is rising steadily, reaching 47.1 million as of December 31, 2000.

Our 20,000-kilometer domestic optical-fiber cable network enables us to offer advanced, integrated domestic and international telecommunications services. Since the early days of the Internet in Japan, we have cooperated with leading research institutes to establish an infrastructure and promote Internet use. By building on expertise gained through such efforts, we have developed a broad range of cost-effective Internet services for private and corporate users. We have also established a data center business and a built a next-generation IP network, positioning us to provide total solutions to customer needs.

During the period under review, we began offering a number of attractive new discount services in preparation for the May 2001 launch of the MYLINE preferred carrier selection service. In January 2001, we introduced DYNATALK II PLAN DX, a discount plan combining domestic long-distance and international calling for fixed-line subscribers. To our cellular phone, PHS and DION Internet access service customers, we offered the KDDI Discount Set, which is essentially DYNATALK II PLAN DX without the monthly subscription fee. We integrated the DION Internet access service with NEWEB, a similar service previously offered by KDD, with the aim of enhancing services. In January 2001, we launched Mighty Course, a new Internet service lineup for medium-volume users. We also introduced new rate schedules and implemented across-the-board fee reductions. In November 2000, we commenced operations at the newly completed Odaiba Data Center in Tokyo. This large-scale facility will play a crucial role in our efforts to expand e-business services. Prior to this, we began construction of PERSEUS, a next-generation terabit-level IP network, and in October 2000 introduced its first PERSEUS service, ANDROMEGA IP-VPN.



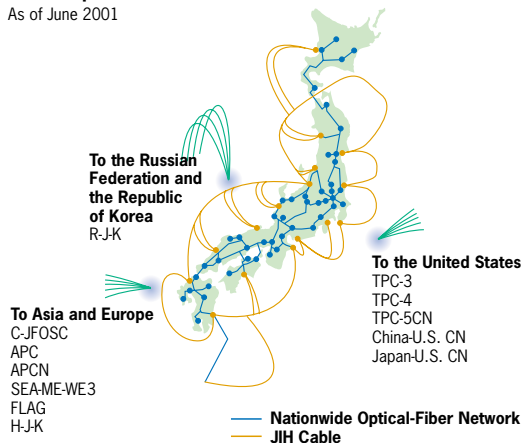
Yamaguchi Satellite Earth Station



Chikura Cable Landing Station

**KDDI's Optical-Fiber Cable Networks**

As of June 2001



**KDDI's Networks**

KDDI boasts one of Japan's largest backbone networks. Approximately 30,000 kilometers in total length, this network includes the Japan Information Highway (JIH), a submarine cable system approximately 10,000 kilometers in length that encircles the archipelago in a loop configuration; an optical-fiber cable system encompassing 9,000 kilometers of cable laid along the nation's expressways; and a microwave network of about 7,000 kilometers. Through cooperation with telecommunications carriers overseas, we have also built one of the world's largest global communications networks, comprising approximately 300,000 kilometers of submarine optical-fiber cable. These two massive high-speed cable networks enable us to provide seamless domestic and international telecommunications services.



Network Center (KDDI Building, Shinjuku)

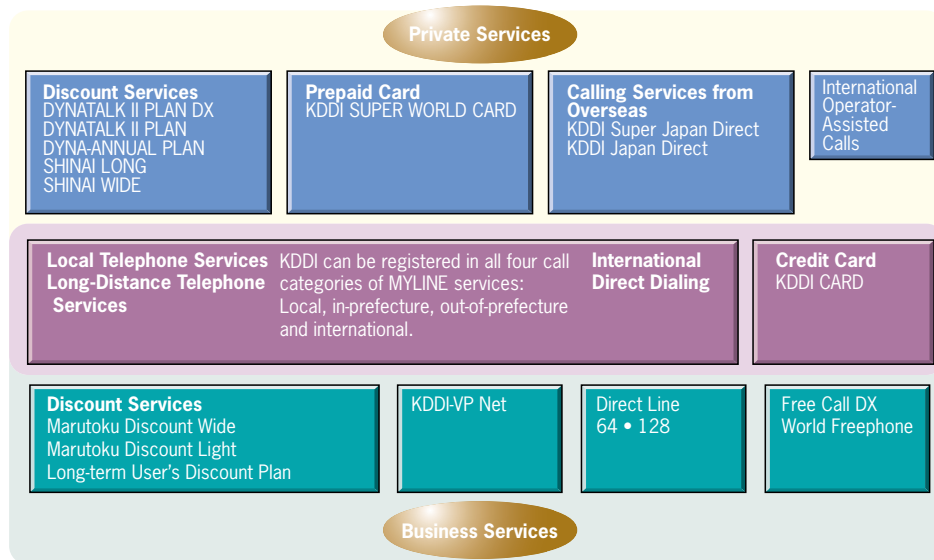
Our network centers nationwide form the nucleus of our domestic telecommunications system. These facilities, which are staffed by specialists, provide around-the-clock, real-time surveillance and maintenance. We have also established a back-up system and taken other precautions to ensure network safety.

Our network centers are linked with overseas carriers, facilitating around-the-clock monitoring of our global network and control of telecommunications routes. The KDDI Group has two specialized cable-laying and cable-maintenance ships that respond promptly in the event of unforeseen problems.

**Domestic and International Telephone Services**

KDDI launched local telephone services in May 2001, enabling it to offer its customers throughout Japan seamless local, domestic long-distance and international services. We have developed an extensive range of convenient and reasonably priced domestic and international services tailored to the needs of private and corporate users.

**KDDI Telephone Services**





In response to rising demand for lower-priced services, we have taken decisive steps to reduce costs. These efforts enabled us to implement steady rate cuts throughout fiscal 2001. We currently offer international telephone services to 237 countries and territories, more than any other Japanese carrier, and command more than 50% of Japan's international telephone services market. In addition to maximizing our superb networks and our accumulated expertise to ensure stable services, we will continue to cut costs to further reinforce competitiveness.

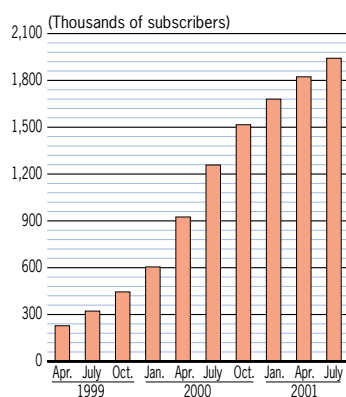
### Global Services

The KDDI Group has operations in 20 countries and offers an extensive range of global network services via its optical-fiber cable network. We offer a variety of support services overseas under the KDDI brand name, including telecommunications services in Europe, the United States and Australia, telecommunications-related consulting, sales and maintenance of telecommunications facilities, and data center services.

Our international services also include telecommunications services offered through joint ventures with local carriers. We offer cellular telephone services in Paraguay and Mongolia, and fixed-line telecommunications services in Russia. In line with the rapid globalization of the telecommunications market, we will continue to push forward with active efforts to expand our presence in the global market.



Total DION Dial-up Subscribers  
(At the 1st of each month)



Note: Figures prior to the integration of DION and NEWEB Internet access services in October 2000 have been combined.

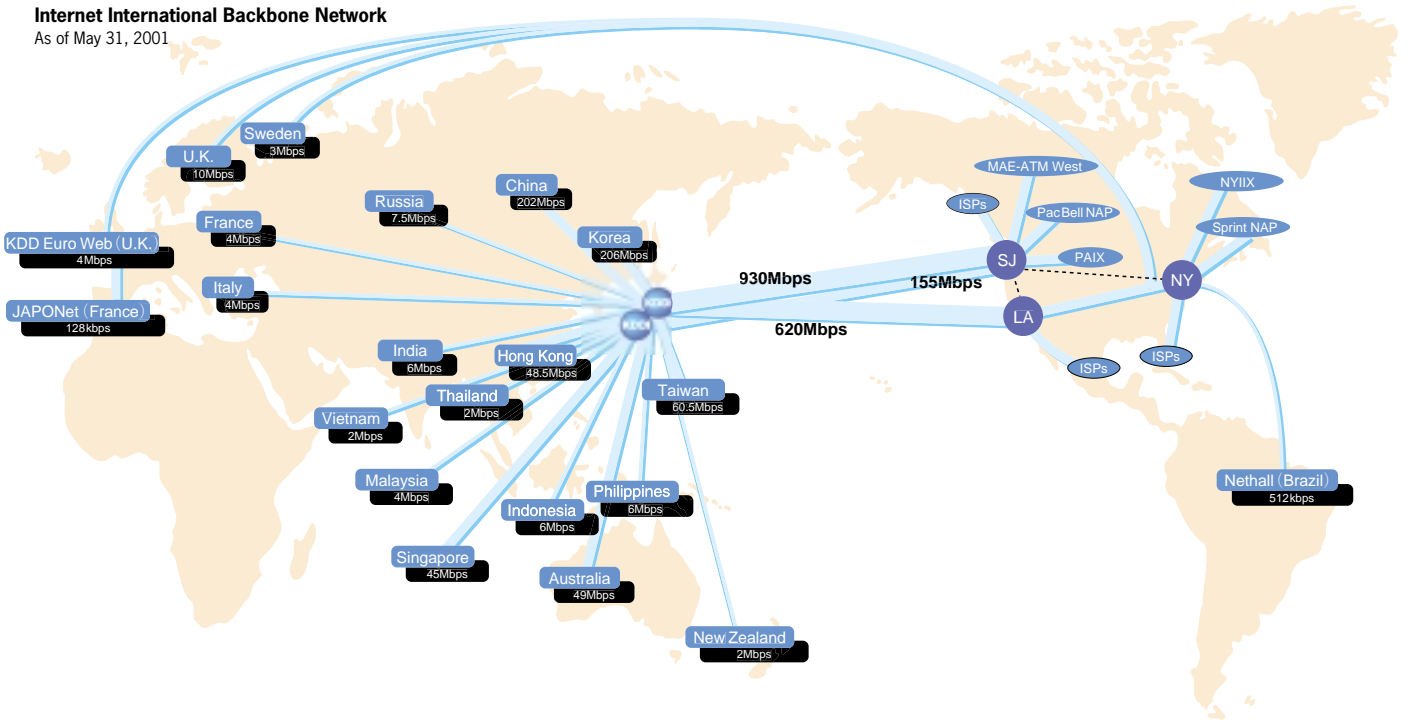
### DION

DION is the brand name of KDDI's Internet access service. With the merger, in October 2000, we integrated the DION Internet access service with NEWEB, a similar service previously offered by KDD. This move enabled us to improve the capacity and quality of the service, as well as improve the diversity of contents and support services and offer reasonable rates. As of March 31, 2001, the number of subscribers for DION dial-up service exceeded 1.8 million. DION services for corporate users use KDDI's backbone network to offer high-speed connection of up to 135Mbps. We also offer complementary services, such as server hosting and local-area network (LAN) connection, allowing us to design Internet environments to meet the needs of customers. We will continue to enhance broadband DION services to accommodate the full range of digital subscriber line (DSL) services, FTTH networks and other technologies. We will also promote integration with EZweb mobile Internet connection services, as well as the development of more attractive content, in an effort to further increase the number of DION subscribers.

### ANDROMEGA

KDDI offers a comprehensive range of solutions to the telecommunications needs of corporate customers under the ANDROMEGA brand name. Designed to respond to all conceivable needs in the areas of voice and data transmission and IP services, the ANDROMEGA lineup offers the best possible solution, whether the customer needs to build a global network linking multiple overseas business centers or simply raise intranet efficiency to lower transmission costs.

**Internet International Backbone Network**  
As of May 31, 2001



**KDDI Data Centers**

As of March 31, 2001

Data Center Site	Floor space (m <sup>2</sup> )
<b>Japan</b>	
Shinjuku (Tokyo)	5,400
Otemachi (Tokyo)	3,700
Odaiba (Tokyo)	2,200
Other	6,400
<hr/>	
<b>Overseas</b>	
<b>Europe</b>	
United Kingdom	27,400
France	15,100
Switzerland	2,300
Germany	10,700
<b>Americas</b>	
United States	25,900
Brazil	200
<b>Asia</b>	
Hong Kong	1,400
<hr/>	
<b>TOTAL</b>	<b>100,700</b>

**dotsquare and Telehouse**

Data center services, offered under the *dotsquare* name in Japan and the *Telehouse* name overseas, are a key component of KDDI's IP business. These services focus on colocation (space and rack rental) and server hosting (server maintenance and operation and server capacity rental). At present, we offer approximately 17,700 square meters of space in 13 cities in Japan and 83,000 square meters of space in 12 cities overseas. Our data center facilities feature a large-capacity telecommunications infrastructure, uninterruptible power and air-conditioning systems, highly effective security and sophisticated monitoring, thus enabling us to respond to rising demand for services spurred by the expansion of e-business. In November 2000, we commenced operations at the newly completed Odaiba Data Center in Tokyo, a large-scale facility that will play a crucial role in our efforts to expand e-business services. We are currently constructing a building to house a 14,700-square-meter data center in Tokyo's Shibuya area, which is scheduled to commence operations in fiscal 2003. We will also enhance services by adding such functions as streaming, settlements, customer management and ASP to our data centers, as well as promote ties and cooperative ventures with partners in other fields, including content providers and broadcasters.



Interior of colocation room (KDDI Building, Shinjuku)

New data center, Shibuya (Scheduled for completion in 2003)

## PERSEUS

KDDI is capitalizing on its state-of-the-art IP technologies to build PERSEUS, a next-generation terabit-level IP network that will realize terabit-level—that is, one trillion bit-per-second—ultrahigh-speed transmission at considerably less cost than is currently possible. We are also developing high-value-added services for the PERSEUS network. In the period under review, we introduced the first of these services, ANDROMEGA IP-VPN, which enables corporate customers to construct intranets that are entirely IP-based. We will continue to expand applications to include e-commerce, VOD and high-resolution videophones.

To further enhance the attractiveness of the PERSEUS network, we also offer a variety of access options, including fixed wireless access (FWA); KDDI Skycast, an interactive satellite-based IP service; and KDDI METRORING, a low-cost optical-fiber network access service. PERSEUS is also accessible from cdmaOne cellular phones and PHS terminals, and will offer a variety of other access options, including next-generation CDMA2000 1xEV phones and ITS terminals.

### PERSEUS Terabit IP Network

