(April 27, 2022, Tokyo)

Nomura Research Institute, Ltd.

FY March 2022 Financial Results Briefings

Q&A Session

First inquirer (analyst)

Q1: Regarding order volume in the fourth quarter, although your pipeline is robust, the growth rate of your order volume in domestic industrial IT has been flat through the third quarter (nine months). Can you let us know the reason, as well as your forecast going forward? In which segments and industry types is your pipeline strong?

A1: Order volume was strong in industrial IT last year. Although order volume in the fourth quarter was down 0.4%, our pipeline is robust. The problem is the timing of orders received in April rather than March. Our pipeline is particularly robust in projects involving development of new services such as deliveries utilizing the internet, and projects to integrate logistics systems that utilize e-commerce with conventional core logistics systems.

Q2: I understand that order volume in industrial IT during the fourth quarter of last year set the bar high, but growth in order volume has been flat for nine months. Are there any concerns in areas such as resources?

A2: Our resources have been squeezed for over a year now, but we have made efforts to remedy this ongoing situation through leverage effects in our resources. Order potential and demand are robust, and we are working to expand our business to be able to overcome this squeeze.

Q3: This question is about your assumptions for profitability in this year’s plan. You had explained that your business profit margin, excluding profits and expenses unrelated to your primary business, would not decrease. However, even taking the consolidation effect of Core BTS into consideration, the plan seems conservative in assuming that what had been increasing before would not increase even more. Your profit margin decreases when gains from the sale of real estate assets are excluded, but for what reason?

A3: In industrial IT, we are continuously investing single-digit billions of yen annually to bolster our digital IP. We expected this to generate more than 1,000 MM (man months) in spare development capacity. There are no factors such as unprofitable projects suppressing profit margin.

Q4: Your operating margin overseas was around 10% last year. Roughly what level are you anticipating in your plan for this year? Will it decrease due to the consolidation of Core BTS?

A4: Taking the scale of Core BTS's sales into consideration, we do expect the operating margin to decline this year. However, we anticipate an increase in the actual amount of profit compared to last year's results.

Q5: Around what level of operating margin are you targeting overseas in NRI Group Vision 2030 (V2030)? Also, your goal for productivity improvement seems ambitious. How do you see your platform business developing outside of banking and securities?

A5: We explained our estimation at the present time for our overseas operating margin in 2030 as our long-term outlook on operating profit (slide 27). We will be reviewing this in detail over the next year. Increased profit effects from increasing the proportions of platform business and high-margin consulting business will comprise one-third of the 30% for improvement in productivity (30% of profit increase factors). Specifically, this involves developing business with financial institution clients who are not currently using our platforms, acquiring clients through new front-end platforms, and investments related to shared online services such as dedicated cloud migration. We believe that these will be built up incrementally and that we are highly likely to achieve this goal.

Second inquirer (analyst)

Q1: Your board members will likely have changed in 2030. Can you talk about any medium-term goals that the current board members can commit to?

A1: We plan to disclose our target levels for 2025 in the Medium-Term Management

Plan which we expect to announce in April 2023.

Q2: It would be good to have specific measures such as resource allocation plans outlined in the Medium-Term Management Plan. I want to know your approach to matters such as capital investment, M&A, and investing in human resources. When Nomura Holdings sold shares of NRI stock in March 2022, you did not execute a share buyback. In the past NRI would have bought back shares, so do you plan to actively invest rather than buy back shares?

A2: We have executed eight M&A transactions over the last six years. We will also likely be executing M&A at the same pace over the next eight years, primarily in North America. We are running simulations on the financial side, but we plan to look at it more carefully and then make an announcement in April 2023. Basically, our policy and approach are to allocate one-third for investments to update existing systems such as THE STAR, one-third for transactions such as M&A, and one-third for shareholder returns.

Q3: Please share what has been better than anticipated and tougher than anticipated with Core BTS in North America. And regarding the speed of your business development (M&A) in North America, will you be actively engaged, or will that have to wait until things are more settled with Core BTS?

A3: Core BTS operates both a network business and a cloud business. In the three months since the acquisition, their network business has fallen a bit behind plan due to shortages in procurement for semiconductors, but their cloud business is steadily growing. In cloud, their business models include modernizing core systems in stages starting with Office 365, to migrate from on-premises to the cloud. We recognize the need to strengthen their capabilities in the application layer and upstream consulting at this point in time. We consider our current challenge to be expanding our business area which is centered mainly in the Northeastern US. It is very likely that we will proceed with M&A from this year onward in order to address these issues.

Third inquirer (analyst)

Q1: Your overseas operating profit has increased, but I would like to know the cumulative total through the third quarter and the breakdown of the fourth quarter. Business appears to be strong in Australia. In North America, you answered questions about Core BTS, but I would also like to know about Brierley+Partners (b+p).

A1: Through the third quarter, profit margin has been higher than cumulative for the year, primarily in Australia. Core BTS had sales of around 6 billion yen in the fourth quarter but has virtually zero contribution to consolidated operating profit and their operating margin in the fourth quarter is decreasing. Since this is the first time that we are compiling the overseas portion, we have not disclosed the portion for the quarter. We will disclose this portion at our next financial results presentation.

Due to the impact of lockdowns, b+p broke even in terms of income and expenses last year. They began offering a new loyalty program. We forecast positive profit growth for b+p this year through efforts to acquire clients. We expect them to get orders from major retailers that are open for business and expand from there.

Q2: Roughly what portion of your order volume for this year is attributable to newly consolidated subsidiaries?

A2: We are recording all of the order backlog on the books of the three companies we acquired last year (Core BTS, Planit, AUSIEX) at the time we acquired them as order volume. This has raised our order volume. In system management solutions, we also recorded one year's worth of order volume as having been received in the fourth quarter, which is different from other quarters. Roughly 17 billion yen of our fourth quarter order volume is attributable to our new acquisitions.

Fourth inquirer (analyst)

Q1: Your sales, general and administrative expenses had increased by roughly 3 billion yen above forecast as of January 27. What was the background behind that? Were there any short-term expenses?

A1: There were short-term expenses in the IT platform services segment in the fourth quarter. Those were part of the increase.

Q2: Will those have an ongoing impact this year?

A2: The impact of increased short-term expenses in the IT platform services segment will not be ongoing. However, sales, general and administrative expenses attributable to newly consolidated companies are increasing, and that will also continue this year.

Q3: Will your gain from the sale of the Yokohama Nomura Building be recorded in the first quarter of this year?

A3: We will record 2 billion yen in gain from that sale during the first quarter of this year.

Q4: You had explained that your business profit margin this year would not change from last year, but will there actually be any change? Your capacity utilization is consistently high, so is there any reason why profit margin would not increase?

A4: The scale of our business in North America (sales) is expanding this year through M&A. However, business there does not contribute to consolidated operating profit, which in turn pushes down operating margin. Profit margin in our domestic business continues to trend upward as it has until now.

Q5: Does that mean that your forecasted profit margin for this year has room for error?

A5: The 115 billion yen was the result of a flat estimate.

Fifth inquirer (analyst)

Q1: IT business operators have more price negotiation power in this business climate with strong demand from clients. Even if increases in employee numbers and the head counts of external partners are limited, the improved profitability effects of using negotiation power to increase sales per employee would be significant. Have you incorporated improved profitability effects from boosting sales per employee into your future business forecast at NRI?

A1: Our hiring head count to NRI payroll as indicated on page 56 of the presentation materials is directly connected to domestic business growth, and this head count is increasing. Our utilization of partners including in China is also increasing. High rates of capacity utilization are limiting our top-line growth, but this is not a major bottleneck. Profitability improvement through price negotiation is hard to quantitatively explain in numbers. Even when we end up in competition when making proposals, we are not under pressure to significantly reduce costs. If you consider demand from clients and our capability to address it, this situation seems likely to continue for the time being. Just to add to that from the perspective of comparing NRI with other companies, sales per employee could be quantitatively explained if we operated a business similar to temp staffing. Since our business model is different, I cannot easily provide a quantitative response.

Q2: Is your in-house standard profit margin increasing?

A2: We are making conscious efforts to propose added value that exceeds our standard profit margin. There is no pricing pressure to go below our standard margin.

Q3: NRI had been cash rich in the past, but currently your net cash flow is negative. Why has your capital investment increased so significantly from FY March 2021 to FY March 2022? Also, do you plan to continue being net cash flow out? Will you be buying back shares at a slower pace?

A3: The biggest factor behind the increase in capital investment was our increased investment in software for building next-generation platforms. As for share buybacks, we will execute buybacks as needed at the appropriate times and generally have no plan to change the policy we have followed up to now. Although we are currently doing more capital investment and M&A, we do not think there will be any impact on shareholder returns. We intend to maintain the approach we have taken to this point.

Q4: Will you be increasing your investments in next-generation platforms again this year?

A4: We plan to make 50 billion yen in capital investments during FY March 2023, which represents a slower rate of increase than the previous year.

Q5: Taking your medium to long-term cash flow into consideration, around when do you expect to reach the payback period?

A5: We are making large investments to lower our infrastructure costs in financial IT. These will take tangible form sometime this year or next, and from then on will be the payback period.

Sixth inquirer (analyst)

Q1: The macro environment has changed significantly since three months ago, but what changes are there in demand for IT services? And how has NRI been impacted? Also, how severe does your top management consider these changes in the environment to be?

A1: NRI's business is focused on Japan, North America, and Australia. We are far away from the circumstances currently unfolding in Europe. At present, the conflict in Ukraine is not impacting orders in IT solutions. However, we believe that if the conflict is prolonged, it could impact our clients' businesses and performance, which could curtail IT investment. Orders in consulting have not been impacted at this point in time, but we must remain vigilant since there are many internationally oriented topics in consulting.

Q2: Typically, the initial Medium-Term Plan of a long-term vision will probably feature a large number of investments, but is that the case in V2030? Also, what will you have to work at in order to achieve V2030? And what kind of impact will that have on expenses during the initial Medium-Term Plan?

A2: We do not see the initial Medium-Term Plan as a time to keep performance goals low to make various investments toward achieving goals for 2030, and we have not done that in the past either. If we do not constantly achieve growth while making investments at the same time, we will not be able to achieve ambitious goals. We will formulate the next Medium-Term Plan over the next year. We might be actively investing in North America (M&A) in the next plan. Investment in THE STAR is passing a turning point leading up to next year, after which we will enter the payback period. I think that cash out from M&A in North America will have an impact on the expenses side in the next Medium-Term Plan.

Seventh inquirer (analyst)

Q1: The increase in your overseas orders in the fourth quarter was at the same level as in the third quarter. Taking exchange rate effects into consideration, organic growth would appear to be slowing. Is that a correct assessment?

A1: Organic growth in the fourth quarter was focused in Australia, but on a local currency basis, orders there still grew by about 10%.

Q2: Your approach to operating profit growth (presentation materials page 27) indicates plus factors, but what do you think the risk factors (staffing shortages, outsourcing cost increases, room for profit margin to increase, etc.) are between now and 2030?

A2: As far as the ratios that comprise our profit growth, we believe that the 40% comprised of increased revenue effects and the 30% comprised of productivity improvements are highly achievable. Also, the 20% comprised of overseas expansion must increase our profitability in Australia. We have acquired subsidiaries under NRI Australia, and we are planning their reorganization, including the integration of their back-office departments. We think that social DX will comprise 10% of our new business. We need to build highly profitable platform businesses. Investments have begun, but it will take some dedication to turn these into the businesses we envision. We will properly plan our overseas expansion and new business, and we will manage them well. That includes flexibly changing the way we do things.

Q3: Will the percentages in the NRI management concept of having a 20-60-20 ratio of "high profit margin business, to standard profit margin business, to investment business" change in the operating profit growth process?

A3: I think the 20-60-20 structure will change. Efforts to convert standard profit margin business into high profit margin business are included in the 30% for productivity improvements. We are running numerical simulations, but reviews will be needed in order to be able to provide an explanation.

Eighth inquirer (institutional investor)

Q1: Does the 20% for overseas expansion growth in your approach to operating profit growth apply only to organic growth, or does it also include new business?

A1: It is mainly organic growth.

Q2: You touched on automating testing processes as part of productivity improvements, but over the medium to long-term do you expect to expand Planit's solutions to domestic IT? Is there any affinity?

A2: Discussions about expanding Planit's solutions to Japan are ongoing. Australia has a different style of IT development than Japan does, so we cannot simply apply their solutions as-is with clients here. We are considering the suitable means for application in Japan.