

(January 27, 2022, Tokyo)

Nomura Research Institute, Ltd.

The Third Quarter of FY March 2022 Financial Results

Briefings Q&A Session

* FY (Fiscal Year) in the text below indicates the accounting year for Core BTS, January through December

First inquirer (analyst)

Q1: Your performance this year has been strong, and the upward revision to your operating profit forecast just added the amount which exceeded forecast through the third quarter so it seemed there would be room to outperform the forecast in the fourth quarter as well. However, in what areas do you expect to see growth next year and the year after, and what is your qualitative forecast for those years?

A1: Our domestic order backlog at the end of the third quarter was strong with a 9.4% increase year-on-year, and we believe this trend will continue. For example, business is brisk in consulting for DX-related and social problem-solving topics, in financial IT for modernization projects with non-life insurers, in industrial IT for projects where senior management of clients utilize IT to overcome business challenges, and in IT platform services with inquiries for security projects. Our momentum from the end of last year has carried over through this year, and we will likely remain on this trajectory for the time being.

Q2: Your business performance is exceeding forecast, but can you explain whether your state of expansion will continue? Will the current high levels of activity and performance continue as well? Is it correct to assume that you are taking action in terms of personnel and capacity to continue growing?

A2: We believe business will remain brisk. We are continuing to bolster our new graduate and mid-career hiring while also working to improve productivity

through the use of various IP. Through these efforts we are aiming for further growth.

Q3: You expect to achieve your target operating profit in the Medium-Term Plan one year earlier than originally forecast. What will be your objective heading into the final fiscal year of the Medium-Term Plan next year?

A3: There are targets and KPIs other than operating profit set in each different segment, and we have not achieved all of them. Beyond just our target operating profit for NRI as a whole, we will be striving to complete the Medium-Term Plan by achieving all of these targets and KPIs.

Q4: Has Core BTS in North America been impacted by the Omicron variant? Also, you are forecasting that Core BTS will be a positive contributor to consolidated operating profit starting in FY 2023, but will that be attributable to revenue growth? Is there some cost factor?

A4: The Omicron variant has partially impacted procurement of semiconductors in their network business. As for when Core BTS will contribute to profit, there is some impact from the sale of intangible assets and post-merger integration costs. We believe that increasing revenues through cross-sales to Japanese clients and others will also contribute to profit.

Second inquirer (analyst)

Q1: Your domestic order volume in the third quarter increased in financial IT due to factors such as strong performance in insurance, but what is driving order volume when you look specifically at each of the four industry types? Also, why is there no change in the growth rate of domestic order volume in industrial IT from the second to the third quarter?

A1: In securities we are getting more systems integration projects. In insurance we are receiving orders for modernization in the public sector, mutual insurance, and non-life insurance. In banking, large projects came to an end, but an increasing number of systems integration projects in other financial business is making up for that. Next in industrial IT, we achieved significant growth last year and are maintaining that high level.

Q2: In financial IT, is there anything in particular driving order volume, such as prioritized industry types? Also why has order volume in industrial IT not increased from the second to the third quarter? Is there a structural problem?

A2: In financial IT, insurance contributed the most to order volume in the third quarter. Next were banking and other financial, but in some ways the boundary between these two types is vague. If you lump them in to one, they would be second. Last is securities, but we have had significant growth in all four business types. In industrial IT, the impact from the sudden increase last year was major, but I believe DX projects will increase since there is strong demand from clients who want to leverage IT to grow their business.

Q3: Regarding your segment performance results in the third quarter, why is operating margin decreasing in consulting? If this is due to quarterly fluctuations it should be no concern, but is competition to acquire talent costing more?

A3: This third quarter decrease is within the range of quarterly fluctuation. We do not think it will be an ongoing trend.

Q4: Are you reflecting rising personnel costs in unit costs?

A4: Rather than reflecting personnel in unit costs, our approach is to continuously acquire projects where we can provide high added value and turn these into increases in profit margin.

Q5: Regarding your future growth expectations for Core BTS, about how much of an increase in their FY 2025 profit margin do you envision? For example, will it be around the same level as operating margin in Australia at around 10%?

A5: We are aiming for an operating margin of around 10%.

Third inquirer (analyst)

Q1: How much order volume did Core BTS have in the third quarter?

A1: Core BTS recorded roughly 13 billion yen of the order backlog for overseas subsidiaries, but they are considering all of their order backlog at the end of the quarter when we acquired them through M&A to have been received as orders. In other words, roughly 13 billion yen was the third quarter order volume for Core BTS.

Q2: DX projects in consulting are robust, but what characterizes NRI's DX projects?

A2: We have projects where we develop systems in conjunction with our consulting. Examples of this include inventory management and optimized deliveries. We also have projects in non-face-to-face and contactless resulting from the pandemic. We provide consulting for clients to determine what type of business they should create.

Q3: Are you indeed receiving inquiries for DX projects in all business types as you explained before?

A3: That is correct. DX projects are particularly robust in industrial IT.

Fourth inquirer (analyst)

Q1: Looking ahead to future growth potential, demand remains strong in each segment, so could NRI's ability to handle it (capabilities, personnel) become a bottleneck to growth?

A1: We will continue working to secure personnel while at the same time improving productivity so that personnel does not become a bottleneck.

Q2: Personnel at NRI has been increasing by around 2-3% per year. Does that mean your productivity has been improving by around 5%?

A2: If our personnel increases by 5% and sales grows 7%, the 2% difference is productivity improvement. This year we are hiring around 400 new graduates and more than 200 mid-career hires. If roughly 200 people leave the company, our personnel growth would be around 5%. We must continue compensating for the difference between sales growth and personnel by improving productivity.

Q3: Does this 7% represent organic growth, and is total growth the amount after M&A is factored in?

A3: That is correct.

Q4: You have positioned Core BTS as a springboard to business in North America, but how much M&A do you plan to conduct in North America going forward?

A4: Our M&A of Core BTS was valued at roughly 50 billion yen. We do not expect future M&A to be that large, but we have not decided on any monetary amounts.

Q5: Taking M&A into consideration, can we also expect sales growth of around 11% to continue in the future?

A5: Overseas sales is being reviewed for our next Vision and we plan to make an announcement at our financial results presentation in April, but we expect to continue conducting M&A in the tens of billions of yen.

Q6: For NRI, is it better to focus on handling capacity (personnel, capabilities) than in-depth book building?

A6: We create our business plans after having viewed the book building.

Fifth inquirer (analyst)

Q1: Roughly how much amortization of intangible assets did Core BTS record in the third quarter? And could you also explain the breakdown of the roughly 100 billion yen increase in goodwill over these past nine months?

A1: Payments for advisory services involved in the acquisition were recorded in the third quarter, but amortization has not yet occurred in the third quarter. As for goodwill, we are sorting out which parts are amortizable and which parts are not, and we are not in a situation to comment on any specific amounts.

Q2: Please explain the basis for your valuation of this acquisition.

A2: Adjusted EBITDA in FY 2021 was roughly 21 million US dollars. The EBITDA multiple is around 21, which we do not consider particularly high. However, we will need to achieve growth on the level that was indicated in order to avoid goodwill impairments.

Q3: Roughly how much of Core BTS's business is comprised of hardware sales?

A3: Their network business is related to Cisco, and about half of it can be conceptualized as related to hardware. Roughly half of that is hardware sales.

Sixth inquirer (analyst)

Q1: About how much is the new consolidation effect of Core BTS on third quarter order volume?

A1: Orders increased by 18.4 billion yen in the third quarter, which includes 13 billion yen from Core BTS. It also includes around 3 billion yen from the two

companies in Australia that had not been consolidated at this point last year. After subtracting these, the remaining 2 billion-plus yen represents organic growth in overseas order volume.

Q2: Does this mean that order volume in the fourth quarter will continue to be recorded the same way, so there will no longer be any significant impact?

A2: That is correct.

Q3: How profitable do you think Core BTS currently is?

A3: Our accounting standards differ from those of Core BTS in FY 2021. This is explained by the graphs in our presentation materials, including the contribution of companies acquired during FY 2021 to past performance. Since we only presented the pure financial statements in our December press release without taking this into consideration, the levels of sales and profits do not match those in the presentation materials, so I think it is difficult to compare. Amortization of intangible assets is also expected in FY 2022, although the amounts have not yet been determined. We therefore expect Core BTS to have no net contribution to consolidated operating profit in FY 2022.

Q4: Is the semiconductor shortage having any impact of the Cisco-related business of Core BTS?

A4: Some projects in FY 2021 had to be postponed due to semiconductors being unavailable, but the impact was not significant since these projects comprised less than 10% of their network business.

Seventh inquirer (analyst)

Q1: About how much room for additional operating capacity improvement will you have through next year?

A1: Since we work in projects, there are peaks and valleys in operating capacity utilization. We are constantly coordinating our resources while planning how best to deploy them.

Eighth inquirer (analyst)

Q1: Did the STAR implementation for the major securities brokerage go live in

January as scheduled? And how much does it contribute to sales per year?

A1: Since this is about an individual client, unfortunately I must refrain from answering that question.

Q2: Is it behind schedule?

A2: I am not at liberty to speak about individual clients. The development is proceeding smoothly.

Q3: Are you making any efforts to improve employee retention, such as raising the pay scale?

A3: At NRI we are not raising the pay scale. We reflect the magnitude of increased operating profit and added value in bonuses, with the idea of determining how the company's profits should be allocated. Rewards are given in the form of increased bonuses.

Ninth inquirer (analyst)

Q1: What areas are driving DX-related sales growth? And is DX-related profitability improving at a faster pace than business overall?

A1: Sales growth is not heavier in any particular area. Clients are recognizing the added value we provide and paying an appropriate price. We are not setting higher prices for DX.

Q2: Is it correct to assume that DX-related profitability improvements are moving at the same pace as improved profitability throughout your business overall?

A2: We are turning higher profit than the standard profit margin by thoroughly capturing the increasing volume of DX-related work in the market.

Tenth inquirer (analyst)

Q1: What impact will Core BTS have on fourth quarter operating profit?

A1: It will have a net zero effect on operating profit from January through March.

Q2: How much have advisory expenses for M&A and amortization of intangible assets in Australia pushed up sales, general and administrative expenses in the third quarter relative to the second quarter? And what intangible assets are being amortized?

A2: Amortization of intangible assets in Australia is increasing year-on-year but compared to the second quarter the increase is rather small. The biggest factor behind the large increase in sales, general and administrative expenses was the large increase in outsourcing costs, which includes advisory expenses. Labor costs are also increasing, mainly in Australia. Additionally, travel and transport costs increased due to the loosening of movement restrictions in the third quarter. The higher expenses derive from these multiple factors.

Q3: Why did your operating margin in consulting fall short of 30% in the third quarter?

A3: The topics that we handle in consulting are often short-term, and there is not always a set profit margin. In the third quarter, profit margin just happened to temporarily decline.

Q4: If there are no changes in the business environment, is it safe to assume that profit in the fourth quarter will be about the same as the third quarter?

A4: We believe that profit will exceed our current fourth quarter forecast (deducted from the full-year forecast). However, since there are many uncertain elements including the Omicron variant, we are just adding the amount by which we have exceeded forecast through the third quarter to our original fourth quarter forecast. We are not anticipating any temporary expenses like those that arose last year.