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Nomura Research Institute, Ltd.
The Third Quarter of FY March 2025 Financial Results Briefings Q&A Session

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Q1: Continuing the trend from the first half, your profitability improved markedly in financial IT. Was this primarily attributable to higher transaction revenue due to an active market? Or, is it a contribution from systems integration projects, and could we expect the profitability improvement to continue going forward?

A1: Both are contributing factors. Profitability is also improving in systems integration projects for industries such as banking and insurance. We believe that this trend will also continue going forward.

Q2: Will your transaction revenue next fiscal year depend on market activity?

A2: That is correct.

Q3: Orders in industrial IT recovered earlier than anticipated. In your previous explanations you had been putting effort into bringing in orders in real estate and manufacturing. Have the results in terms of orders and revenue come early because you spent time preparing? Or was it because there were projects you could get in shorter periods of time?

A3: These orders were not received through short-term efforts. They resulted from relationships we had built over the long term. In the small meeting held after our second quarter results briefing, we explained that we had added a total of eight companies to our pipeline as new clients—four in manufacturing, two in real estate, one in transport, and one in energy. Three of these companies have already placed orders. Two companies were added to the pipeline as new clients in the third quarter. We have been explaining since before that industrial IT is in a transitional period, but our ongoing sales efforts to this point are now coming to fruition.

Q4: Will orders in industrial IT domestically trend toward growth after seeming to have bottomed out? Or will the contribution to revenue be next fiscal year?

A4: Orders in the third quarter were in upstream process phases such as requirements definition and outline design. They do not contribute much to revenue. Contributions to revenue should grow once entering the development phase, and leverage effects should also make profit higher.

Q5: Around when next fiscal year will the development phase start and the scale increase?

A5: All of the new projects we received orders for in the third quarter will not enter the development phase at the same time. Some will enter the development phase in the first quarter of next fiscal year, others will in the second quarter or later. At the same time, some (existing projects) will end. Still, we expect industrial IT to be strong overall next fiscal year.

Q6: Your quarterly revenue growth rate has remained in the low single-digit percent during FY March 2025. Could we expect a growth rate in the mid- to high-single-digit percent in FY March 2026? Your overseas business bottomed out, and although it is hard to predict how it will go from there, could we expect around 5% revenue growth year-on-year if financial IT remains strong and industrial IT grows moving forward?

A6: As circumstances overseas were harsh, our cumulative revenue growth rate was 3.3% in the third quarter of this fiscal year. We believe that we can achieve a rate in the mid-single-digit percent next fiscal year.

Second inquirer (Analyst)

Q1: How are your orders trending in domestic industrial IT? What kind of projects are you handling for new clients? Are these for core systems, or for front-end? Is there any particular perspective that would be beneficial in considering the profitability, such as the characteristics of the clients?

A1: The new clients who placed orders are two companies in manufacturing and one in transport. Although there are two companies both in manufacturing, they are in different industry types, and the project types also differ.

Q2: Do the characteristics of the systems you will build in the newly ordered projects differ?
A2: One is a core system project and the other is front-end system, so they are not the same.

Q3: How about the profitability of new projects? In previous explanations, you have often said that your profit margin in projects with new clients starts at a somewhat lower level. Are these new projects the same?
A3: For new clients, we sometimes make proposals with restrained profit margins with the expectation that the business could expand in the future. On the other hand, for clients with whom we have forged deeper relationships, we make proposals with profit margins commensurate with the added value we provide. Another case is with upstream phases, where our profit margin is relatively lower. We determine the profit margin in light of our relationship with the client and factors such as the added value we provide.

Q4: In distribution, I understand you are forecasting a drop in revenue for the fourth quarter. About when do you expect the investment stance of your main clients in distribution to turn around? Will revenue there remain in roughly the same range next fiscal year, or can we expect a rebound?
A4: Investment by clients in distribution has been stagnating. The situation seems to be that other large project (that other vendors are handling) are in progress, so investment is not being directed to the areas that we handle. Clients' business conditions could also be a factor. However, in distribution they will need to continue investing in areas such as DX to stay competitive. We will continue discussing with clients about the timing of when full-scale investment will resume.

Q5: What is the breakdown by region of your 700 million yen in overseas operating profit during the third quarter?
A5: In Australia we generally broke even, in North America we recorded a loss in the low hundreds of millions of yen, and in Asia and others we had profit in the high hundreds of millions of yen.

Q6: Australia and Core BTS did not seem to show any major improvement compared to the second quarter if transitory profit is excluded. Is there any change to your outlook of having bottomed out overseas, including in terms of orders?
A6: Interest rates are not really coming down, which is one reason why clients' appetite for investment has not yet returned. To this point we have brought back profits by focusing on cost reductions but going forward we would prefer to focus on developing new clients

through stronger collaboration between Core BTS, NRI-ITSA, and NRI-A in North America rather than wait for an economic recovery. In Australia, we are in the process of revising our business strategy under a new CEO. We are anticipating the results from both of these efforts, and also the return of appetite for investment through an economic recovery. For now, I would rather not speculate about when that recovery will occur.

Third inquirer (Analyst)

Q1: The environment surrounding your main clients in distribution who are reluctant to invest will probably not change soon. Does NRI have no choice but to wait? Or, are you considering any measures in response? Since clients cannot hold back from investing forever, do you expect investment to return sometime next fiscal year?

A1: We have been able to exercise strong control over earnings in distribution by temporarily shifting some human resources to other businesses.

Q2: Could you break down the factors behind your strong profits in financial IT? And how sustainable are they? Please share NRI's analysis. For example, if projects are for systems integration, profits will fall when they end, or cost structures will improve in shared online services, so those profits are sustainable.

A2: Looking at it by industry type, we also have many systems integration projects in securities. Nearly all of our projects in insurance are systems integration, but many of these are long term. In banking, we received an order from a third bank for BaaS/CORE implementation. In other financial, systems integration projects are also increasing in asset management. Systems integration projects might appear transitory at a glance, but we have increasingly deep relationships with many of the clients. Continuing to strengthen our relationships with the clients leads to sustainable business.

Q3: Can we expect the same level of margin or an improvement next fiscal year in financial IT?

A3: Our margin in financial IT is already at a high level, but we will raise it even higher through efforts such as productivity improvements, moving toward shared platforms, and decluttering (eliminating and consolidating software functions).

Fourth inquirer (Analyst)

Q1: What were the factors behind the improvement in your gross margin in the third quarter, and how sustainable are they? Also, what caused the year-on-year decrease in SG&A expenses?

A1: The biggest factor behind our improvement in gross margin was cost reductions overseas, including reversions from one-time costs the previous year. More than a few overseas factors are included in the decline in SG&A expenses. Another factor is that amortization expenses for intangible assets we learned of through M&A are decreasing.

Q2: Can we assume that restructuring of inactive personnel overseas was a factor behind improvement in gross margin?

A2: That is correct.

Plus, lower amortization expenses and less inactive personnel overseas also lower SG&A expenses.

Q3: Your SG&A expenses in the fourth quarter (subtracting the figures through the third quarter from the forecasted figure for the full year) are higher than in the fourth quarter last year. Does that include any necessary costs?

A3: This is when various preparations must be made for the next fiscal year. This is not entirely SG&A expenses, but we expect costs to increase in the fourth quarter compared to our costs through the third quarter.

Q4: What is the current progress of your efforts in AI, what is your outlook for next fiscal year onward, and how are you feeling about topics such as DeepSeek?

A4: We have two different directions for our efforts in AI. One is efforts to improve the productivity of our own development work. We have previously explained this as Steps 1, 2, and 3. Step 1 is using AI to support testing, Step 2 is to generate programs through AI, and Step 3 is to apply AI to entire development processes. Step 1 is progressing. We currently have more than 60 projects that are either already implemented or in consideration. Depending on the nature of the system, we are only achieving around 20% reductions in some, while we can reduce as much as 80% in others. Since the effects are undeniable, we believe that generative AI implementation will accelerate going forward. For Step 2, we currently have just under 30 projects that are either already implemented or in consideration. These also vary in effects depending on the nature of the project. Some only achieve around a 10% reduction, while we can achieve around 60% in others. Since we were able to verify a certain level of effects, we believe the application of generative AI will advance from here. For Step 3, we conducted a trial project applying AI to roughly half of all processes in systems development. In this trial, we were able to confirm the effects of roughly 25% reductions to our current arrangements in terms of both project length and man-hours. However, AI cannot be applied to every project. Since we have moved to shared development platforms in financial IT where we are working on the trial, wide-ranging application of AI is possible there. We intend to use shared platforms in financial IT, and then implement Step 3.

After that are the AI-related services and related systems that we offer to clients. Although we have many inquiries, these have not led to any projects where we perform real systems development yet. In FY March 2024 we had 130-140 orders totaling roughly 7 billion yen. In FY March 2025 we had around 170 orders by December totaling roughly 6 billion yen, so we have exceeded last year's pace, but many of the projects are trial phases. Going forward, we want to actively utilize AI together with our clients.

Regarding DeepSeek, we have little information at this time. If a model such as DeepSeek were to become widespread, we might also be able to offer even more high-performance, lower cost services utilizing generative AI. We are in an industry that can reap the benefits of technological evolution, and we believe that technology will advance even more quickly in the future. This is why we want to choose and implement the superior generative AI.

Fifth inquirer (Analyst)

Q1: Are you projecting that unreceived orders in your industrial IT sales pipeline will be received in the fourth quarter?

A1: Previously I mentioned that we have as many as eight new client companies in the pipeline. We have not failed to receive any orders from them, and our sales activities are ongoing. The certainty of receiving the orders is high, and we aim to receive them either in the fourth quarter of FY March 2025 or in FY March 2026. We expect to receive the orders from the two companies added in the third quarter during FY March 2026. Including projects from existing clients, FY March 2026 is when we will be able to secure significant orders.

Q2: If you total up all the orders from new clients, will it compensate for the shortfall among your main clients in distribution?

A2: The total amount for the projects is large, but we will continue balancing our resources while making proposals since we cannot receive those orders all at once. At the same time, we will also work on building deeper relationships with clients in distribution. We have projects totaling in the mid-single-digit billions of yen with new clients, and we expect these to contribute to profit.

Sixth inquirer (Analyst)

Q1: Could you clarify the overseas portion of your performance forecast revision? You downwardly revised your overseas revenue to 115 billion yen in the previous financial results briefing. Will this revision bring it down to 110 billion yen? And operating profit had been revised to 3 billion yen, but what will it be now?

A1: In the second quarter we had revised overseas revenue downward by 5 billion yen, but our profit forecast is unchanged.

Q2: Do you think there is room to ride the momentum from exceeding forecast domestically to exceed forecast for the fiscal year?

A2: This performance forecast revision was made with the likely March results in view. While I understand it has been pointed out that profit in the fourth quarter looks weak, we plan to make preparations in the fourth quarter that involve incurring cost. This was also based on costs particular to the fourth quarter that will arise to some extent, such as property tax expenses to be recorded and revaluations of software assets when we take inventory of assets.

Q3: What is your outlook for the final year of the Medium-Term Plan, FY March 2026? How likely could you exceed the forecast, and how confident are you?

A3: Our targets in the Medium-Term Plan are 810 billion yen in revenue, 145 billion yen in operating profit, and an operating margin of 17.9%. Compared to FY March 2025, we will need to increase revenues by more than 5% and operating profit by around 8%. We aim to achieve these with certainty in FY March 2026, but I would like to announce the extent to which we could exceed them in April 2025 after discussing the matter. First, I think it will be important to make sure that we clear the targets in the Medium-Term Plan.

Q4: How has the response been in your efforts to secure new large projects to achieve the performance targets for FY March 2026?

A4: I had explained that industrial IT is in a transitional period, but results are starting to show from the preparatory activities, and we now have large projects in our pipeline. It feels like we are recovering as anticipated.

Seventh inquirer (Institutional investor)

Q1: You plan to increase revenue by 10 billion yen in consulting this fiscal year. Could you break that down into factors such as personnel headcount and unit prices? And around how much growth is possible in terms of resources, capacity utilization, and demand in FY March 2026?

A1: As business has been strong in consulting projects, profit margin has risen along with the increase in high added-value projects. In terms of personnel, we are increasing both our new graduate and mid-career hiring. It takes time until new graduate hires can be business contributors, but we do have sufficient personnel coverage in place.

Q2: Does this mean that you have inquiries enough to raise revenues by tens of billions of yen from FY March 2026 onward, and you also have the personnel in place?

A2: We have large numbers of consultants joining us as new graduates in April 2025, and we are also hiring consultants mid-career. We aim to thoroughly bolster our personnel and grow our revenue.

Q3: What specifically do your high-revenue projects involve?

A3: In AI consulting, there are currently few projects that lead directly to systems development projects, but we have many that go very in-depth into business operations. In DX, we have more projects that use new systems to transform business and grow the top line.

Q4: Your performance has been steady. What risks do you anticipate domestically and internationally in FY March 2026 and onward?

A4: Overseas, we have done what we needed to. Our capacity utilization has risen due to cost reductions including layoffs. We have worked hard to grow the top line, but the truth is that business confidence has a major impact. There appears to be risk in the unpredictability of trends in the US government under Trump and the change of government in Australia.

Domestically, the fervor for the use of IT to address labor shortages is even apparent in the Bank of Japan's “Tankan” (Short-term Survey), so we expect demand to remain. Risk for us seems relatively low.

Eighth inquirer (Analyst)

Q1: What proportion of earnings in financial IT is dependent on transactions, and what is the profit margin on those?

A1: We are not disclosing figures for those.

Q2: What was different (in the business environment) in industrial IT overseas between the second and third quarters?

A2: Overseas, some projects charge by the number of business days. The third quarter includes Christmas season, so there are less business days. It also coincides with summer vacation in Australia, so the regular seasonality of the quarter trends lower than the second quarter.

Q3: Your business overseas seems ready to rebound. What is the overseas situation now in areas such as shuffling management and bolstering sales?

A3: The new CEO in Australia who assumed the role in December is working aggressively, and we have high expectations for her. The CRO who has newly assumed the role in North America is taking on business reforms. It will likely take a little more time for their efforts to reflect in our results.