(Tokyo – 27th May, 2020)

Nomura Research Institute, Ltd.

Q & A from Small Meeting for sell-side analysts

2nd

- In order to make it easier to understand, the contents of the question and answer are partially revised and modified.

(Questioner No.1)

Q: I understand that you are having conversations remotely with overseas investors. What is a frequent topic in these discussions?

A: The topics have completely changed compared to before. Right now 80% to 90% of these discussions are about post-coronavirus subject matter. These investors have strong interest in whether NRI's business opportunities will increase going forward. Some overseas investors do not know much about coronavirus circumstances in Japan, so I think they want to ask about this.

Q: With various changes anticipated in the post-coronavirus world including new business models and workstyles, are you explaining to them that the impact on NRI's business will be positive?

A: Fundamentally I think the positive impact will be significant, but there are also some cases such as with clients currently struggling performance-wise, in which projects are postponed even though the clients really want to get started on them right away. At the same time, there are also clients who do get started right away, and their sense of speed is different. However, generally I believe nearly all managers in Japan are thinking about working on post-coronavirus reforms.

Q: I have heard that other companies have less work in areas such as consulting and new systems development. While around 60% of NRI's revenue is steady, is the other 40% of revenue suffering any impact? And will your performance be worsening in the near future due to the current negative impact of the virus before post-coronavirus IT demand increases?

A: At our financial results briefing in April we explained that our performance forecast assumes the spread of the coronavirus will be contained by July or August, and business activities will start returning to normal around September. In consulting we cannot receive orders until we begin face-to-face operations again, so we forecasted a significant impact in the latter part of the first half. On the other hand, with the lifting of the state of emergency declaration the other day, many companies have now begun preparing to restart face-to-face operations. Of course there is concern about the impact if a second wave of the virus appears between now and winter, but in the immediate term it seems companies have begun ramping up their operations to return to normal starting about one month earlier than we originally forecasted.

Financial IT generally has a high proportion of steady revenue and is hardly showing any impact from the coronavirus at all. However, in insurance we need a buildup of separate development projects, and decisions on projects tend to be delayed in telecommuting environments. Additionally the project with the major life insurer which is our largest client is also halted, and a round of core systems projects for online non-life insurers seems to have completed, so we have forecasted a revenue drop for this year.

Industrial IT tends to be diverging into two extremes. New projects in airlines, the travel industry, and global manufacturing have stopped, and the impact is already being felt. On the other hand, investment in telecom is already on the rise. In logistics we have inquiries for urgently bolstering core systems since the existing ones are stretched beyond their limits due to the increase in e-commerce. Mass retail outlets suddenly have need to devote attention to e-commerce investment and due to the coronavirus they are showing a tendency to expedite those investments. Looking at the overall balance, there seem to be more negative factors than positive ones, similarly to our performance forecast.

（Questioner No.2）

Q: I have heard that IT investments at automakers have not necessarily stopped, but has investment uniformly halted in your business with global manufacturing clients?

A: Systems development projects that were already ordered have not stopped, but new projects at automakers have stopped. Outside of automotive, new projects have also generally stopped at clients in North America and Europe with high expense ratio, and I believe these clients are significantly impacted.

Q: When the 2008 financial crisis happened it took at least two years from bottoming out until recovery. When do you think you will bottom out this time?

A: When the financial crisis happened 10 years ago, NRI worked with regular investment cycles referred to as Corporate IT with core systems updates as the main area of IT investment. Companies whose Corporate IT investment period coincided with the crisis ended up postponing investments. The financial crisis caused IT investment to slump for a while and performance for systems integrators including NRI stagnated, but after two or three years, investment demand for updates reappeared all at once. This caused a boom and performance recovered.

Now several companies are migrating their core systems to the cloud. This situation is different from the Corporate IT investment cycle of 10 years ago. Additionally, business-side DX is the focus of new investment demand as opposed to platforms, so it is not a situation where postponed demand arises all at once later on. And this may depend on when a second wave of the coronavirus occurs and how bad it is, but order backlog was also at a very high level at the end of March before the impact of the coronavirus hit, and potential demand is robust. If business operations continue returning to normal, investment demand could still gradually arise as next year approaches even if some gets postponed this year.

(Questioner No.3)

Q: If it becomes harder to bring in new projects, is it possible that your profit margin could rise as it did in Industrial IT last year?

A: What we have to be most careful of is to not produce unprofitable projects. For example, if the quality of our communication with clients to define requirements worsens and the projects turn unprofitable, profit margin will suffer the largest impact. We will be dedicating the highest level of attention to our quality management activities. Profit margin is relatively high for the recurring revenues that comprise around 60% of our sales, and these revenues are not impacted by the coronavirus. Therefore, if we do not bring in any new development projects it is possible that our profit margin could rise this year. However, NRI's stable revenue base has been built by linking new development projects with recurring revenues later in the future, so we do need to continue bringing in a certain amount of new projects in order to maintain a high profit margin next year and beyond. In Industrial IT our top line might fall a bit, but as long as we don’t produce unprofitable projects we think that we can maintain our profit margin. In some cases, profit margin might even temporarily increase.

Q: What is your current situation overseas?

A: The demand reduction from the coronavirus is harsher overseas than in Japan. Brierley+Partners in North America has its strength in loyalty marketing, and its main customers are airlines, rental car, and other travel-related companies. Due to the harsh business climate we made personnel cutbacks in March and are shrinking the organization to a level that will keep them out of the red. At this time it is uncertain when demand will return, but once it does we plan to increase the size of the organization again.

The original ASG in Australia is focused on managed services and they have not been significantly impacted by the coronavirus. On the other hand, SMS mainly does consulting and application development, so they have been hit hard by shrinking demand. We laid off over 100 staff at the end of March and plan to operate there while maintaining a balanced budget for the time being.

(Questioner No.4)

Q: How will NRI itself change post-coronavirus?

A: On the business side there are two major changes at NRI post-coronavirus, one of which is workstyles. The results of the surveys that NRI conducted independently in March and May showed that around 40% of employees at Japanese companies on the whole were telecommuting, and that around 60% of employees who work for large companies with at least 1,000 employees are telecommuting. Also, around 60% of those who are telecommuting also said that telecommuting is causing various problems in their work.

It appears that telecommuting is producing side effects, and solving these problems involves some big challenges. These include switching from the traditional function-oriented work allocation to job-oriented allocation, building human resources development mechanisms to replace on-the-job training, and investments to create virtual offices on the cloud. We believe there are lots of business opportunities in finding solutions to these problems and we want to prepare for these.

The second major change is acceleration of the move to non-face-to-face. Manufacturers who had previously refrained from increasing their e-commerce out of consideration for wholesalers have changed course. Now they are indeed bolstering their e-commerce. Salespeople in insurance also need non-face-to-face sales tools. The circumstances are changing drastically. I believe this is an area where we can leverage NRI's strengths in consulting and IT solutions.

Within NRI many employees are currently telecommuting, and we plan for this to continue post-coronavirus. If we can effectively address the issue of lower productivity in telecommuting, we will be able to enjoy the benefits of both work-life balance and high productivity which telecommuting offers.

Also, aside from NRI itself, our partners in Japan must also be equipped with environments for telecommuting, or else outsourcing will perform poorly and productivity will fall. We encountered such a problem in April, but we began providing partners with a platform called Aslead Remote where they can also develop in a telecommuting environment, and since the end of the Golden Week holiday we have been maintaining and improving this system. We intend to implement workstyle reforms that incorporate telecommuting going forward.

(Questioner No.5)

Q: If DX investment accelerates post-coronavirus, would that boost your medium-term growth curve?

A: One of the current trends that stands out is the creation of business reform committees headed directly by the company president. Bottom-up proposals initiated at the worksites had previously been the norm, but since that takes too long it seems companies are working to implement major reforms top-down. NRI consultants are supporting such initiatives at several companies, but these past few months seem to have been a plan formulation phase to conceive overall reform concepts and milestones. We expect these initiatives to gradually trend toward IT investment in the second half, but we will need to wait and see whether the magnitude will be large enough to boost our growth curve. Whatever the case, we intend to leverage our strength in consulting, get involved from the conceptual stage, and facilitate connections to NRI's IT business.

We plan to hire new staff according to our plan regardless of the coronavirus, so as long as we can capture demand we will not have any problems with production resources.

Q: Will you need to bring in even more resources if demand increases more than expected?

A: Our plan includes the resources we need to achieve an operating profit of 100 billion yen. We will need to watch over the developments for a while to figure out what we would do if any additional upside arises, but we could possibly further increase mid-career hiring. We do not think production resources will be a constraint.

(Questioner No.6)

Q: How quickly do you expect client-side investment to arise post-coronavirus?

A: I can't really say how quickly overall but the definitive difference from last year is that senior managers themselves are getting hands-on in forming teams, assigning COO-class executives to lead them, and jumping straight into the formulation of plans. DX projects up until last year were approved by senior management, but mainly led by division managers. I think there are lots of senior managers who feel the urgency to act now, even if it involves a certain level of risk.

Q: Do you think, for instance, that these efforts will have enough impact to increase IT budgets next fiscal year and the year after?

A: There may be a variety of topics that come up in the consulting stage, but it seems that not many companies will be deciding on IT investments in the billions or tens of billions of yen this fiscal year. Many companies will likely decide on full-scale investments only after observing how well their immediate performance recovers. There were companies who announced plans for large investments along with their financial results, and among those companies some will probably make investments ahead of the others regardless of the size of the coronavirus impact. At NRI, our approach is to get involved starting in the conceptual stage with companies whose senior managers are taking the lead, and to work together with them to achieve results.

(Questioner No.7)

Q: Your M&A overseas targets both new IP and new clients, but what is your plan going forward?

A: In North America we acquired Brierley+Partners which has appealing IP in loyalty marketing. North America is at the forefront of cloud technology and has companies with highly productive cloud-native development technology, so we are looking there with interest. In Australia we plan to acquire Commonwealth

Bank of Australia (CBA) subsidiary AUSIEX as announced at our financial results briefing. The company provides back office services in securities, including back office operations for large online securities brokerage CommSec which is a subsidiary of CBA. This gives us a platform to enter back office operations in Australia's wealth management market which is expected to grow, and should also strengthen our relationship with CBA. This will be a positive first step for developing our business in Australia's finance industry going forward.

In the future we can introduce NRI's services in the workings of AUSIEX, and possibly bring in a broad range of direct finance expertise other than wealth management. Considering how harsh the business climate is in North America, I think it might be better to focus on business expansion in Australia for the next few years.

Q: Will you develop business in finance centered on AUSIEX or will you continue laying more groundwork through additional M&A?

A: We can certainly consider having AUSIEX work on back office and some front office in wealth management and acquiring other companies to supplement the functions that AUSIEX can offer. This could include expanding their services beyond only wealth management to direct finance in general and providing services even for platforms in indirect finance. We cannot completely rule out the possibility of acquiring entirely different types of company than AUSIEX, but we will prioritize the idea of building up AUSIEX by adding the necessary functions.

(Questioner No.8)

Q: What were the background details behind making DSB a wholly owned subsidiary, and what is the plan for it going forward?

A: Since we are in the middle of the takeover bid, please allow me to wait until after the takeover bid is complete before providing details about future strategy. Generally speaking, when you look at examples of direct finance operations in North America, I doubt you will see any companies that have IT and back office operations provided together by a third party, which the companies themselves operate. In front office operations there are even cases of third parties providing services that utilize technologies such as AI.

Financial institutions in Japan are bringing many of their operations in-house, but as the business climate gets worse, third parties could come into wider use as they are in North America. Looking at the current state of affairs, I think that will happen. For example, NRI and DSB could join together to boost business operations overall by combining NRI's technology with the high added-value services for front office provided by DSB.

(Questioner No.9)

Q: What do you think of your medium to long-term growth potential in Financial IT?

A: Currently we have THE STAR migration projects under way with multiple securities brokerages including Mizuho Securities, but we are also in discussions with companies for other projects that could be implemented over the next several years. It seems the trend in the securities industry for brokerages to commission their own assets to third parties rather than hold the assets themselves is accelerating, and by all appearances demand for this will likely be robust over the next four to five years. As for the future, we need to think about new business models, which is why we moved forward with the takeover bid for DSB.

Looking at Financial IT overall, we have more of the same type of systems development as before in the insurance industry and I don't sense any changes like those taking place in securities. For example, we must take proper action according to the timing of core systems updates of major life insurers.

In banking, NRI has strength in online banking but there will soon be a lull in the core system overhauls we are currently working on. We are lining up subsequent projects for next fiscal year and onward, and our sales activities seem to be moving smoothly in that regard. I believe we can expect stable growth in banking for a while.

Overall, we are not worried about growth in Financial IT over the next few years.

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