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Nomura Research Institute, Ltd.
Q&A from Small Meeting for Analysts
Part 2

Speakers: ・ Kaga Yanagisawa
President & CEO
・ Hidenori Anzai
Senior Executive Managing Director
Memberof the Board, Representative Director
・ Masaaki Yamazaki
Senior Corporate Managing Director

（Questioner No. 1 ）

Q1: This question is from an overseas investor. You are the new president, but there are executives who are older than you. Do you have an environment for free-minded decision making?

A1: There is no feeling of being hindered whatsoever. In the succession for president we have a mechanism called "next cabinet members" for ushering in the next generation in each team. The next president is chosen from among the corporate officers in charge who comprise the next cabinet members. We spent quite some time on team building, and over the course of one year established relationships open enough to consult each other about anything. Age has no bearing on the company's decision making. My senior colleagues are offering helpful counsel such as the histories behind certain things.

（Questioner No. 2 ）

Q1: Business execution is left up to each person responsible. What only the president can determine is allocation of management resources, particularly human resources and investments. That changes the company significantly. What can you see at this point in time?

A1: Medium-Term Plan 2025 is positioned as the preparation period within V2030. Although we are not sacrificing short-term performance, our plan is to thoroughly invest in the

future while maintaining a growth curve that is more moderate than analysts' expectations. In looking back on FY March 2024, we see things that we can still do more of, and also things that we absolutely must do. Some businesses we can grow even more. Those also require investments and allocations of human resources. For example, the information security business at NRI SecureTechnologies is steadily growing. It is also gaining the public's attention. We are conducting market research and discussing the necessary investments. There is also the new element of generative AI. Aside from that, we are also discussing which fields we should allocate management resources to, although only on a hypothetical level.

Q2: You probably need a straightforward slogan or catch phrase. It might be a good idea to make bold statement like "20% improvement through AI." For example, it might also be easy for employees to understand if you say that each individual will achieve sales and profit growth through AI utilization, or something like that. Some companies are doing that. Please hammer out something like this. (Previous president) Mr. Konomoto had been pushing DX.

A2: Your opinion has been noted.

（Questioner No. 3）

Q1: Generative AI is in the Proof of Concept (PoC) stage focused in consulting. Before DX there was the concept of the Internet of Things (IoT), but there seem to have been many projects that never reached the point of monetization. What are your thoughts regarding generative AI? In what scenarios can you envision monetization from the PoC, and what proportion will move forward to the next phase?

A1: Nearly all of NRI's clients will utilize AI. We are likely to see lots of AI usage like Microsoft's Copilot in the business domains of other companies and outside the domain of systems integrators such as NRI. This relates to ongoing demand for DX. Many Japanese companies are facing challenges such as the social issue of labor shortages due to the declining population and maturity of their existing businesses. They are taking on new challenges such as consumer point alliances and entering other industries. We consider AI usage to be one technological element to create differentiation. NRI engages in consulting that boosts competitive advantage through AI usage while leveraging the distinctive strengths of our clients. First we are utilizing generative AI in front-end, contact points with consumers, and in-store staff guidance. Generative AI is capable of assisting consumers who cannot properly find the products they want on e-commerce

sites and are only able to ask vague questions, as well as in-store staff with little IT skill. Once front-end utilization proceeds, needs arise for linkage with data in core systems. This is where companies with capabilities to handle things like moving core systems to the cloud are desired, as opposed to startups who specialize in front-end. Also, consulting functions are prerequisite for business model transformation. NRI's business domain is in high added-value initiatives such as real-time data linkages with core systems to discover the areas where clients can grow their top lines.

Q2: Will the success rate be higher than the IoT era, and do you think you will be able to link core systems?

A2: We think so, but caution is required since there will inevitably be a period of disillusionment.

（Questioner No. 4）

Q1: Does it seem that you have AI usage in production innovation under control? It is broken down into three stages, but will you be likely be able to deliver significant efficiency in step 3? And can we expect further top-line growth by diverting human resources to proposal-related activities?

A1: In the overall application of step 3, we are accelerating the schedule for some of the business platform overhauls we had planned for next year to handle them this year and are thoroughly utilizing AI. Since NRI owns software assets, we can apply it throughout all development. If we were to achieve a 20% improvement in productivity, we could invest that in activities for those human resources to grow the top line. Also, if productivity improves by applying AI to modernization projects at insurance companies, we can also help to grow their bottom lines. We want to share the benefits with our clients in win-win scenarios. (If we are able to share the benefits of productivity improvements) We expect to see clients who want to work on modernizations.

Q2: The financial results briefing in April 2024 gave a sort of wait-and-see impression.

A2: We are currently in a state of making preparations. Until around December 2024 we plan to work on utilizing AI in everything from requirements definition to release for some of our business platforms. Starting around January 2025, we expect to start seeing the effects of productivity improvements and some response from how it is improving development methods.

Q3: Based on subsequent decisions, will you hit the accelerator in FY March 2026 and reap the benefits in the next Medium-Term Plan?

A3: Even if our investments planned for FY March 2026 decrease, it will not immediately impact our P&L and we will be able to utilize human resources effectively.

（Questioner No. 5 ）

Q1: In what fields do you think you can leverage the value of generative AI? The part about raising accuracy when implementing it in society is likely a challenge, but in which industry types are you thinking to implement it?

A1: Interest in generative AI is high, and we have projects regardless of industry type. Generative AI is characterized by how it can handle natural language. Like the example of e-commerce sites, its effects will be greater in industry types with lots of interactions with consumers who are unaccustomed to IT and in many settings where natural language is used. It can produce effects in industry types with B-to-C business and where there are large numbers of employees and it is hard to uniformly train all of them, such as the parcel deliveries business. As you pointed out, the fine-tuning is difficult and we surmise that the tolerance for hallucinations will vary by industry type. It can be used in operator support at call centers since humans are present to mediate, but it probably cannot be used for dealing with investors or in customer service points at banks. Financial institutions have taken a careful stance. First it should likely be used in non-financial business operations where large numbers of personnel work, and in fields that deal with natural language. Various types of expertise and technology are being generated in the fine-tuning of AI. We have sent as many as 10 personnel to NRI Pacific from various business divisions to gather the latest information. They are communicating closely with researchers and startup companies, providing reports, and also working on solutions to issues that arise in projects on the Japan side. We are engaged in task force activities that horizontally span the entre company as opposed to operating vertically in business divisions.

（Questioner No. 6 ）

Q1: Before a Large Language Model (LLM) is released there is the black box problem. Do you have any concerns in terms of quality control?

A1: What LLMs that are not open source are learning is not visualized. We are dealing carefully with the language written into contracts, including consultations with lawyers.

New problems arise along with the deployment of technologies, so we are working on this continuously.

Q2: Can NRI make business out of AI governance?

A2: NRI Secure has large numbers of inquiries about AI governance and AI security. For example, they provide consulting for formulating in-house rules and guidelines and building governance systems, and support initiatives such as implementations of monitoring tools.

Q3: Are you providing these examples you have shared as supplementary services?

A3: Information security services alone tend to descend into price wars in situations when it is hard to raise added value and the effects cannot easily be seen. We are discussing ways to raise added value such as bundling with other services.

NRI Secure provides individual services, but management at financial institutions have needs in operating entire global entities as opposed to individual services. Thus, we are considering services packages to accommodate them. Major financial institutions have large numbers of group companies. Often, those group companies each practice their own form of governance. There are needs in consulting to explain the status of each group company and in operations of service systems such as for responding to threats. The further addition of AI makes these needs more sophisticated.

（Questioner No. 7）

Q1: Is your US business necessary? Why not just withdraw?

A1: It is necessary. Japan's IT services market is confronting issues such as labor shortages. Demand will probably remain strong for around 10 years. Replacing people with IT and accepting large numbers of immigrants are a couple ways to address this, but these are limited. From the perspectives of our employees and our business partners including clients, we think it is important to increase our business value over a period of 30 to 50 years, not just over a handful of years or a decade. As management, we are pondering the viability of only being firmly rooted in this one country, with Japan's declining working population. Some people might think that we should wait seven to eight years before entering overseas markets if the Japanese market will remain strong for 10 years. However, even in Australia with its more lenient competitive environment than the US, it still took us six years to build up our capabilities. It takes time to establish new business infrastructure in a new market. We will take our time working on the North American

market, learning as we go. North America is a growth market with a rising population. Various technologies are born there, being the market where IT originated. As opposed to just hearing discussions through alliance partners looking over from Japan, we want to get hands-on in learning clients' needs and the actual state of business as we get established. At NRI-ITSA which has Japan-owned companies as clients, those clients say that they want NRI's support when they enter global markets. NRI will be more competitive in business with Japan-owned companies by absorbing new business models and technologies. In North America, information on AI is updated every few months. Core BTS is also gathering new information. We will fully engage in turning around Core BTS, but will also invest when necessary. Changes in the market environment could lead to differences from what we initially anticipated. We are considering various options from a neutral perspective, including whether to make the acquired Core BTS into our base.

Q2: Do you consider acquiring Core BTS to be a mistake?

A2: We do not. However, there have also been changes in the market environment and things that we could not see at the time of acquisition. We are regularly reflecting on whether it was the best choice.

（Questioner No. 8)

Q1: Australia and North America are both investments, not businesses. Participating in board of directors meetings at acquired companies is not business. For investments, you should cut losses and lock in profits. If you are going to nurture it as NRI's business, you should hire people there as employees of NRI and unite all of NRI's global human resources as one. Then, you should work toward moving NRI's headquarters to North America after a few years. It might take 10 to 15 years, but Japan will be left behind as a boutique local country. The management team in Japan should move there and tackle things hands-on.

A1: We are selecting who we will send to the US. Not to change the subject, but we are thinking about a North American-style modified version of Con-Solution for our North America business model. Based on the weakness of the yen, we are also considering the use of Japan as an offshoring destination. We are using South America a little for offshoring, but the labor cost is rising. On the other hand, offshoring to Japan could be profitable. Including our nearshoring business partners, we can understand the actualities of elements such as the quality standards and development methods required

for North American projects. Aside from the management level, there are many accounting and finance people and consultants among our current global human resources. Although it might not be possible in sales, we will enable ourselves to transplant operations such as quality management in development by having our system engineers gain an in-depth understanding. Costs will probably run high if we transplant the way things are done in Japan as-is, but our assumption will likely be to transplant expertise from Japan, up to and including offshore development. This has not been implemented yet, but we are considering getting hands-on to deepen our understanding of business in the US.

Q2: It would be a good thing to combine businesses. Supply chains can be built between Japan and the US.

A2: We have learned things through the collaboration between NRI-ITSA and Core BTS, including about strengths in engineering. Handing over leads to Core BTS from NRI America's consulting also helped us understand what Core BTS is good at and poor at.

（Questioner No. 9）

Q1: What are you emphasizing as KPIs in North America? Last year you explained that you were watching over your sales pipeline, but in this briefing you talked about sending people over. If you manage too rigidly, there is also the risk that turnover could increase.

A1: The KPI we emphasize most is profit. We anticipate it will gradually rise from the current low point. Profit will not make a strong recovery without top-line growth. We are also watching over our sales pipeline. Aside from KPIs, we are also watching over the details of what kinds of projects we have received orders for, and from which clients. Our focus is on quality, such as whether the project order came in by chance, or whether it was the result of targeted effort. Activity levels are rising, including numbers of contacts. For the progress of consulting and application development projects, we are finely analyzing elements such as what kind of channels they came through, what we promoted, and the competitive situation.

（Questioner No. 10）

Q1: One company has employed a strategy to expand its market share with the idea that they will get requests for proposals (RFPs) if they crack the top 10 in overseas markets. NRI's North America business is not that large in scale. What level do you want to raise

it to? What are you aiming for?

A1: Currently we do not have any specific goals in terms of ranking, but we do intend to become a Microsoft recommended provider. Microsoft keeps a list of contractors according to vendors' specialty areas and client size. From our perspective, earning Microsoft's trust is a more certain goal for turning our efforts into results.

（Questioner No.１１）

Q1: Domestically, how high can you raise your margin over the medium to long term? You are making various moves ahead of other companies. Will you aim for an operating margin of 25%?

A1: If we can reap the benefits of investments in new business during that time, we should be able to aim for 25%. I cannot say how many years it will take since there are problems with timing and balance, but 25% is not a wild fantasy.

（Questioner No.１２）

Q1: Over the long term, will industrial IT grow together with clients who are able to capture external demand?

A1: NRI is also aiming to support companies that operate not only in Japan but globally as well.