

(Tokyo-20<sup>th</sup> December, 2023)

## **Nomura Research Institute, Ltd.**

### **Q&A from Small Meeting for Analysts**

#### **Part 2**

##### **(Questioner No. 1)**

Q1: The new president Ms. Yanagisawa gave the impression of being Mr. Konomoto's protégé, but it appears that she has little to no experience in the field of IT solutions. Do you have a structure in place in the management team and worksites to assist her?

A1: The Public Sector Projects Department where she initially worked is a systems department, and she worked there for five years. In consulting, she has accumulated 23 years of experience with telecom, global strategy, consumer goods, business management, finance, ICT media and services, and more. She then served as deputy head of HR and has been a corporate officer for five years. Her systems knowledge may be old, but our business operations are sound in every segment and division at NRI, so the role of the president is not to micromanage but rather serves as a management mechanism to obtain information from corporate officers and division managers and manage based on overarching policies. Mr. Konomoto has experience as head of an overseas location, but his background was basically in consulting only. Ms. Yanagisawa has sat in on the Board of Directors as deputy head of HR and as a corporate officer. As such, she has had many opportunities to learn about our overall management.

Q2: Your business in North America has been at a standstill since acquiring Core BTS. Since the Japan and US sides are kept separate locally, senior management there is likely making the decisions (as pertains to overseas business). The decision-making process is hard to see from the outside, so how will you go about reforming your overseas business? If the status quo will not continue, how will you go about making decisions?

A2: Hiroyuki Kawanami who had been president of NRI Australia is managing our global business as a whole. Mr. Kawanami was heavily involved in the business we do in Australia. Currently he is overseeing both the business and governance sides as the person in charge of global. Therefore, Ms. Yanagisawa will be receiving reports from the person in charge of global (from Mr. Kawanami). Until now, she has also been

accompanying our current president Shingo Konomoto in traveling to the US and communicating directly with the local management. We have relationships in place to gather information as input and engage in direct dialogues locally.

Q3: Has Mr. Kawanami returned from Australia and been put in charge of global?

A3: That is correct. Currently he is managing with a focus on Core BTS in North America. For example, starting in November he has been advancing an initiative for Core BTS to work with NRI-ITSA which supports Japan-based clients by contributing development capabilities to them. Decisions are made in discussions between Mr. Konomoto, Ms. Yanagisawa, and Mr. Kawanami.

Q4: In the financial results briefing, it was mentioned that the external environment bottomed out and had remained flat. Is that situation still ongoing?

A4: Going forward, we believe that interest rates will decrease. While we do not foresee the IT investment environment getting any worse, we are unsure if IT investment will immediately return once interest rates fall. The situation is still harsh both in Australia and North America. For Core BTS, we bolstered the areas they had been lacking for cross-selling network and cloud, but recovery in the IT investment environment has not caught up.

## **(Questioner No. 2)**

Q1: How responsive are interest rate changes and IT investment?

A1: IT was thriving and hiring was brisk in North America during the pandemic, but we are scaling down personnel there now. IT investment tends to lag behind movements in the economy. Intuitively, it seems there is a lag of around one year. We explained in the previous financial results briefing that there would be a recovery in the second half, but now we expect the recovery in North America to happen next fiscal year.

Q2: Is it the same in Australia?

A2: We spent seven years establishing business infrastructure in Australia, and our business there has gotten off the ground. Although the profit margin has declined, we are turning a profit there. We conducted layoffs and structural cost reforms due to the impact of the economic downturn. Now we are looking forward to a recovery.

Australia bottomed out in the first quarter of this fiscal year. Recovery is happening,

albeit slowly. Meanwhile, the stagnated situation in North America is ongoing. We anticipate a recovery next fiscal year.

It would be preferable to turn around our overseas business while our domestic business is performing well.

Q3: During Mr. Kotomoto's tenure as president, DX grew. Human capital management is garnering attention, but NRI seems to already have an advantage in terms of human capital. How will your new president Ms. Yanagisawa leverage this advantage in human capital management, and in which areas?

A3: In human capital, it is more important to operate in growth cycles for human resources than it is to improve any one particular area. Starting with hiring talented human resources, we then give them challenging assignments to build systems that are high-added-value, complex with high-traffic, and/or high in difficulty. While raising employee engagement levels toward their work, we balance the growth of individuals with the growth of our organizations. As General Manager of the Human Resources Department, Ms. Yanagisawa's focus was on implementing the new human resources system. Compensation and other conditions are determined according to mission, thus the new system is called Mission Grade. Rather than being based on seniority or executing what was written in a job description, it was designed to be a system suited particularly to NRI. This new human resources system will energize the environment in our company and help to properly compensate those who challenge themselves. Internally, we are communicating the danger that remaining stagnant in the same situation will result in (relatively) lower standing.

We are also making it a multi-track human resources system. Previously, there was only a path from project manager to general manager. In addition to that, we have added a path to compensate experts as "chief experts" at the same level as office and department heads.

### **(Questioner No. 3)**

Q1: What will the big changes be with your new leadership starting in April 2024? I understand there will be no major deviations leading up to 2030, but what appears likely to change from this point in time?

A1: What we absolutely must focus on is improving productivity. As new graduate hires decrease in number, so too will our level of talented personnel. As previously explained, our major topics are utilizing AI to improve productivity, and also making our engineering

more sophisticated.

Q2: Although you have a long-term vision for DX 3.0, what could happen when combining it with AI?

A2: We have two ways to use AI. One is to improve productivity by automating test processes and coding. The other is to use AI for our clients' business. For example, it can be used to produce responses to inquiries in call centers by combining local databases with LLMs (Large Language Models). Ultimately the responders in call centers are humans, so the AI's responses can be adjusted if they are off. It can also probably be used in opening convenience store locations, but no incredible-sounding usage applications have been announced as of yet. Microsoft's Copilot is an example of something simple, but it has a risk of hallucinations. I think it is important to carefully determine how probable the responses by AI are, and build safe, secure frameworks accordingly.

#### **(Questioner No. 4)**

Q1: During Mr. Konomoto's tenure as president, you drafted roadmaps such as DX 1.0, 2.0, and 3.0. Your new president Ms. Yanagisawa will be focusing on human capital, but I hope you will draft a technology-related roadmap going forward. With no technology-related roadmap, your global business is unlikely to make any progress. Will your team arrangements and cabinet stay the same?

A1: There may be some shuffling, but our current leadership is comprised of Shingo Konomoto (President), Ken Ebato (Vice President), Shuji Tateno (Senior Executive Managing Director), and Hidenori Anzai (also Senior Executive Managing Director). Under them are our corporate officers. The next level down is our division managers. Our "next cabinet members" refers to those currently at the corporate officer level. Roughly half of our corporate officers were shuffled into leadership in April 2023, and others in the same generation as Ms. Yanagisawa are at the corporate officer level. These next cabinet members had many discussions about the execution of our Medium-Term Plan. Ms. Yanagisawa exercised leadership in these discussions, and we chose her as president. Her career experience as a consultant is also extensive, and she has the ability to ascertain what clients want. Our next cabinet members will be working together as we move forward. We still practice team management rather than having one person pull the others forward as president. The president decides the overall direction while each corporate officer defends their own position.

Q2: Each individual probably has their own vision for NRI as you move forward creating the new form of the company. What do you think will change about NRI in 2030, Mr. Anzai? And how will it change?

A2: The ways in which IT is created are changing. Before the pandemic, core systems were the focus and IT was seen as a cost. During the pandemic, non-face-to-face and contactless served as springboards for advancing initiatives to utilize IT and front-end DX in business. Once front-end DX was established, the movement to address problems in connectivity with core systems began. There is momentum behind the usage of IT for business. What clients want are frameworks directly linked to their businesses. Technologies from the US, which is ahead in this area, must also be incorporated. Our long-term management vision was formulated collectively with the next cabinet members over the course of two years. We will continue to refine our consulting and usage of cutting-edge technologies to go on being a company that provides systems which contribute to our clients' business.

#### **(Questioner No. 5)**

Q1: My hope is that a new, immediately recognizable field will emerge. NRI was all about securities and finance before Mr. Konomoto took over as president. Now you are working on DX in the services and manufacturing businesses. Financial IT and industrial IT comprise equal parts of your business. NRI looks different. Do you have a vision or further transformation five to ten years into the future, beyond the Medium-Term Plan, to shift toward top-level and engage in revenue sharing with clients, or something of that nature?

A1: One noteworthy example of our revenue sharing is EARTHBRAIN in DX 2.0. However, we do not have many such initiatives, and they take time. DX 3.0 must be worked on starting with rule formation, and what we have been able to deliver at this point in time is individual number (My Number) related business. We were engaged in conversations with government agencies and public offices starting from the business conceptualization phase, and this also requires a considerable amount of time. We will be delivering DX 3.0 that contributes toward building a better society, but it takes time.

Q2: Is the public sector your next big area of business after finance and industrial?

A2: We are not targeting public sector clients in our My Number-related business. NRI works on linking the My Number framework with private companies. In digitalization, including

for government, we ascertain what private companies need. For My Number, we built things such as a document gathering function that keeps track of individual numbers and provides them to portal sites, which is being used to open accounts at financial institutions and for year-end income tax adjustments that use certificates issued by insurance companies, among other uses. Going forward, I believe this will also spread beyond just financial institutions.

**(Questioner No. 6)**

Q1: You probably receive lots of feedback from investors advising you to increase the proportion of your domestic business in order to raise your profit margin. How do you answer them?

A1: There are investors who think about portfolios for investing in earnings-generating companies in Japan while investing in different companies outside of Japan. While I believe that type of perspective has merit over the next five to ten years, IT is driven by domestic demand and goes into greater use as populations rise. Since Japan's population is not expected to increase, we are not anticipating major increases in IT investment in Japan as we look toward NRI's continuous growth. As a company, we believe in our strategy to enter the US and Australia, which are industrialized countries with growing populations. In our dialogues with investors, we also hear opinions that NRI would be better off abstaining from business overseas. On the other hand, some also tell us that we should do business overseas.

Q2: Is overseas next on top of finance and industrial, then?

A2: Our approach is not to see overseas and domestic as separate businesses. We are engaged in our overseas business within the contexts of industrial IT and financial IT. We also want to execute our approach of involvement starting from consulting which we use in Japan with overseas clients as well. Core BTS's consulting function is weak, so we have to plug in the missing pieces. Shared online services for financial institutions perform well domestically, but they are hard to roll out overseas since the regulations differ in each country. We are providing I-STAR/GV for foreign-owned securities brokerages to AUSIEX in Australia, but the regulations for retail are different, so it cannot be rolled out as-is.

Q3: Looking out over a period longer than ten years, what do you aim to become? For

instance, a company like Accenture employs 700,000 people around the globe. You probably aim to be something different from that, but what would be your appropriate size, market share, and positioning?

A3: We have announced our numerical outlook for 2030. If we achieve 250 billion yen in overseas revenue, I think we will feel some form of positive response from our efforts. We will consider just how high we can raise the overseas proportion of our sales at that time. We are feeling a positive response from our growth in Australia, but the business environment there has worsened recently. First we hope to achieve our targets for 2030, then consider our next vision from there.

Q4: Do you have the goal of perhaps being within the top 20 globally?

A4: In Australia it is easy to know the size of each company, and we are currently positioned roughly within the top 10. The market is large in the US, which makes it hard to know what position we occupy there. Rather than handling package solutions, NRI works in the area of creating what companies cannot build in-house, which was explained earlier as advanced DX. Overseas, it is typical to utilize outside manpower when installing package solutions and have in-house personnel operate them. However, we target midsize enterprises that large players like Accenture do not target, particularly those companies that seek more advanced usage methods. It is important to ascertain the size of target companies suitable for NRI as well as areas where we can produce added value.

### **(Questioner No. 7)**

Q1: You have already entered the North American market. Do you not already know the sweet spot in terms of your target companies?

A1: We are gauging company sizes, but there are regions that Core BTS cannot reach. First we will convert clients in the regions that Core BTS covers.

Q2: In other words, you are targeting so-called local midsize companies? Do you have a competitive advantage there?

A2: Large companies have large in-house teams, so they can handle in-house production. We want our advantage to be high added value in aspects such as handling complex frameworks and high transaction volume. Currently, Core BTS has yet to reach that point.

Q3: How will they be able to? The clients you seek are not in the top class. Core BTS does not possess a clear advantage. It sounds like you are saying that you have no competitive advantage there for the time being, but will work hard in the future.

A3: We are bolstering our involvement from Japan. NRI-ITSA began cooperating in November. We will broaden communication between Core BTS and the Japan side through arrangements such as having Core BTS handle development in projects for Japan-based clients. Core BTS has a client base in the network business, so we will sell cloud and DX to them.

### **(Questioner No. 8)**

Q1: If you can succeed in the US, you can expand throughout the world. There is no need to work on Australia either. Looking from a global perspective, NRI (domestically) is more like a boutique firm similar to AUSIEX in Australia that does not operate on a global scale. While you may not need to conform to the perspective of investors who see NRI as a constituent of their portfolios, why not set standards to observe for aspects such as finance and actively try not to exceed them? Those standards can be changed according to the times. You might be concerned about how much leverage to use, but investors will be more at ease if you disclose your standards.

A1: The environment is not bad enough to lament, but we did change our net debt to equity ratio and net interest-bearing debt standards to use leverage on our financial ratios. We revised our financial rules in order to use a certain degree of leverage for conducting M&A. However, investors would likely feel uneasy if we were to explain an intention to conduct M&A in our current state. We will consider M&A after turning around Core BTS.

Q2: I have doubts about whether there is shared awareness at NRI about the significance of doing business in the US. Why does it seem there is nothing shared with everyone regarding whether to do business in North America? And it is probably good to have various ways of thinking that differ from other companies, but why is it only communicated to investors and analysts in a halfhearted manner when no in-depth discussion has taken place about whether to do business in the US?

A2: Looking out over the long term, Japan's IT market will shrink. IT is an industry driven by domestic demand. The market shrinks when the population declines. We must think about growing globally, but that growth cannot be achieved right away. Possessing the power of capital, we acquired various companies. Some of them have not been



successful. The time frame might be too long from an investor's standpoint, but we want to thoroughly compile the optimal portfolio of both domestic and overseas businesses. It might be difficult to communicate the thought process of globalization to IT solutions worksites in Japan. Overseas currently comprises around 10% of our total sales, but when that increases to 20% the number of personnel involved will also increase, and everyone's perspectives will likely change. Management must be thinking ahead to the future.

Q3: NRI should probably place a global headquarters in the US, with Mr. Konomoto and Mr. Anzai building global business from there. Otherwise, we are just buying stock and leaving money in the US. If you are going for it, go all out instead of just asking opinions here and there. Management must be present in the US, and governance systems are also needed there.

A3: I may have spoken with too much emphasis on details about procedural steps. In our current organization we have a global headquarters mechanism in Japan, but we will be sending personnel to NRI-Holdings America in the US going forward. Core BTS is currently in our industrial IT segment, but we must consider what to do with our global business segment.

### **(Questioner No. 9)**

Q1: Could your original assumption of no growth in Japan possibly be mistaken? Automation and loosening of regulations in IT investment could keep a falling population from equating to a fall in GDP. If you assume that a company pays 10 million yen in labor costs including benefits packages per employee, multiply a population decrease of 10 million people by 10 million yen and that decrease in population would generate a new market worth 100 trillion yen. The current DX is also part of that. Taking 3% of a 100 trillion yen market would work out to 3 trillion yen in sales. This may not be that same perspective that NRI has, but as opposed to developing tens of billions of yen in business overseas, NRI handles 80% of the in-store capabilities at physical storefronts in the securities industry through their operations systems. Why not try to capture a market worth 10% of all industry, or 50 trillion yen out of a GDP of 500 trillion yen, by doing the same thing in other fields as well? Will NRI not change in any significant way? The field of replacing human labor represents a large market. This is not to say that overseas expansion is wrong, but other companies will probably go there. Paper-based

management is still being done in financial accounting, accounting, and human resources management. There is still plenty of room for IT solutions to penetrate. From one particular company, I have heard that clients only using financial accounting solutions comprise 70% of their business. If you also take other types of solutions into consideration, there should be around 10 times the sales potential. Is that not the same for NRI? Your main line of business is replacing areas that are not clients' core competencies with IT such as STAR, right?

A1: Manpower shortages will bring about growth in industrial IT. In finance, significant progress has been made in systemization. NRI has 80% of securities brokerages and 50% of account transactions. We will maintain this market share. At the same time, we are targeting industries that utilize temp staffing. NRI might not get as far as capturing the entire high-added-value market, but we will work on DX that expands what can be done without human intervention and capture growth in our domestic business. Still, we also must expand overseas. In Australia we have acquired multiple companies and learned knowledge, which we will utilize in the US. We will gain an inside presence as quickly as possible in the US, where the technological advancements happen quickly, and we will acquire new technologies. The US is a market we do not want to give up on.

Q2: Why even keep announcing your overseas business results? Overseas comprises a small proportion of your sales. Investors will likely ignore it if you are not continuously mentioning it. Your (profit) numbers there are only in the hundreds of millions of yen. For example, you also have an overseas branch that turns no profit in the finance industry, and nobody complains. If Core BTS is able to work organically and sustainably serving the function of ascertaining local trends, you can just explain having established a presence because establishing one after a chance comes along would be too late. Then nobody would dig any deeper into it.

Conversely, you should explain more about where your growth is happening domestically. It seems wrong for your overseas business to be a discount factor. There were also securities brokerages that gave NRI negative outlooks around the fourth quarter of last fiscal year. Doesn't the responsibility to insist on brazenly ignoring them also lie with NRI? There is room for growth in domestic business, and nobody will complain about producing double-digit annual profit growth supporting business companies in dealing with manpower shortages, having NRI support everything other than clients' core competencies, and things of that nature. Your overseas results can go in the accompanying materials. As opposed to overseas results, it would be well received

if you were to disclose the quarterly performance of NRI SecureTechnologies.

A2: The figures would look just alright if our results by segment combined domestic with overseas. The breakdown would be good domestically and poor overseas. If domestic is compared with overseas, the results from Core BTS which is its own category within the segment would stand out.

Q3: Why not disclose the results of NRI non-consolidated side-by-side with the results of subsidiaries? You have a large number of subsidiaries including DSB, and Core BTS is one of them. You can show the proportion of your subsidiaries that Core BTS comprises. If domestic and North America are shown side-by-side, attention will focus on North America. Disclosures should focus attention on the important things.

A3: Your opinion has been noted.

#### **(Questioner No.10)**

Q1: Is your expectation for the domestic IT market to remain unchanged in FY2024 or for its growth rate to accelerate?

A1: The business environment has not changed much. Our order pipeline is also in good shape. We will be fine through the duration of Medium-Term Plan 2025.

Q2: Would it be better to have the perspective that the high growth rate in the domestic market will trend lower, decelerating from 8% to around 5%?

A2: We believe that growth will continue at the same pace.