

(Tokyo – 26th May, 2023)

Nomura Research Institute, Ltd.

Q & A from Small Meeting for Institutional Investors

Part 2

(Questioner No.1)

Q1: Generative AI has gotten lots of press and attention recently, but how do you perceive it in the context of opportunities and threats for NRI's business?

A1: At NRI, we are also conducting large numbers of trials. However, when including factors such as the certainty and accuracy of the results produced by generative AI, it will still take a little more time until it can be used in production environments at the current level of the technology. For example, we are experimenting on whether using ChatGPT in the search services offered by travel agencies to their customers and making it interactive can improve the service level. Additionally, we are conducting demonstration experiments on automating interactions in initial calls made to call centers. There has even been talk about actually applying some of it. These cases are either in the consulting or demonstration experiment phases, so it will take some time before they have any impact on our core businesses.

(Questioner No.2)

Q1: How do you envision achieving the operating margin in your Medium-Term Management Plan? Do you foresee achieving it through improvements overseas? Or do you envision growth both domestically and overseas?

A1: The breakdown of our profit growth is roughly half from increased revenue effects domestically, just under 10 billion yen from productivity improvements, and around 8 to 9 billion yen from global business. For the part about generating roughly half of that profit domestically, there are no major concerns. As for productivity improvements, we have produced roughly the same level of results as in the past, so we have no concerns about that either. Global business is our main area of concern, but our amortization of intangible assets globally will decrease by single-digit billions of yen each year over the next three years. In March, we also completed the sale of Brierley+Partners which produced a loss last year.

The profit increase we have planned is conservative relative to our results in FY March 2023. Normally we would need more growth, but we do not consider the current numbers to be particularly ambitious.

Q2: Does that mean there will be a significant improvement in your overseas profit margin?

A2: That is correct. Our operating margin in FY March 2022 was close to 10%. We would like to get back to that level in 2025.

(Questioner No.3)

Q1: In what way is generative AI impacting Japan's IT services industry as a whole? Could it be possible that downstream processes become more efficient, or in upstream also, could the length of per-person per-month work time possibly shorten and cause sales to slump?

A1: It depends on the time span. When replacing one operation with a system, if you break down the operation into smaller pieces and replace each of them with a program, you can assure quality through generative AI to a certain degree. However, when systematizing the complex operations that we normally handle, the current generative AI technology stands no chance. Still, we have no way of knowing how advanced this technology will be five or ten years from now. We have been working on low-code and no-code for a long time, but we are unsure how extensively we will be able to automate with generative AI. Although the simplest multiple-structure jobs in system development could possibly be automated, we are not yet at a point where we could predict that the industry will be disrupted.

Also, it is possible that various models specialized in each particular field will emerge in the future, as opposed to ChatGPT. Currently the technology has not reached the level of ChatGPT in terms of absorbing new knowledge and natural conversation. We have also had R&D discussions with outside parties, but the technological level is still not mature. We cannot yet foresee its full-scale use in operations.

(Questioner No.4)

Q1: We have been hearing about DX 3.0 since a few years back, but what is its status now?

There was also mention in the Medium-Term Management Plan about strengthening your next-generation think tank, but why does that need strengthening now? Additionally, since I understand that NRI is not actively pushing for public-sector business, what

exactly is your vision of business with DX 3.0?

A1: Among the various new challenges we are taking on, the area of “My Number” individual number-related social DX is turning into business. We have already launched a number of related business initiatives and we hope it can grow to roughly 50 billion yen in sales and 10 billion yen in profit around the year 2030, but we are not fully convinced it will happen yet. Aside from that, we have an initiative in the public sector involving regional revitalization and DX in the city of Tsuruoka in Yamagata Prefecture. As you are aware, NRI does not match up with the public sector in terms of cost competitiveness. On the other hand, we are able to engage in some form of rule-making. If we can move things in the direction of having money flow through the private sector, we believe that we can create platforms and turn those into business. Our combination of regional revitalization and DX 3.0 is still in the trial and error stage.

We are also interested in GX. Since tracking which utilizes IT is essential in this area, we believe there is some opportunity. We are involved in the GX League office and we have a certain level of understanding of Japan’s road map. Since we are getting work in the creation of rules and frameworks for measuring emissions, which also lead to external recognition, it would be interesting to evolve that for use by the private sector in the future. As for combining GX with DX 3.0, we have things that have produced a number of effects, but nothing big yet.

Topics such as this require hands-on engagement in communities to build consensus between local governments and people, including resident groups, and create schemes on the assumption of doing business. This is what we call our next-generation think tank. In the past, we have offered consulting within the scope of business contracted from government offices, but this is different. Here we will be making rules and building consensus between stakeholders. Starting this year we are formulating hypotheses in the area of DX 3.0 and making preparations. Regarding My Number, life insurance companies using My Number in the collection of people’s lifetime information to mechanically comprehend that information can reduce social costs. We have created various applications that utilize My Number, and it will be a focal point of our efforts throughout the duration of the current Medium-Term Management Plan.

Q2: DX 3.0 gives the impression of being platforms. It does not connect with the local image of regional revitalization.

A2: Fundamentally, we want to set it up where we move things to a platform and earn money through metered billing. When dealing with communities, their various circumstances need to fit. Therefore, we do not consider horizontal deployment such as with Smart City

to be possible. In the case of communities, an example is the Digital Suggestion Box that we operate in Tsuruoka, which is a mechanism to swiftly gauge public opinion via smartphone. If applications like this are made into packages, they can also be used by other local governments. Rather than large-scale platforms, we want to offer individually-specialized packages. We have not yet figured out how large of a business this can become, so it feels like more trials will be needed for the time being.

(Questioner No.5)

Q1: In the framework of V2030 announced in April 2022, it was mentioned that overseas expansion would account for 20% of profit growth. Looking at the current Medium-Term Management Plan, it would appear that you're behind on that. What changed from your original blueprint? Do you think the level you previously set for 2030 has become less realistic? Or, will re-establishing your business infrastructure to reach that level be one of your main efforts during this Medium-Term Management Plan?

A1: We want to proceed toward our profit targets with confidence, but our breakdown between domestic and overseas and the size of our overseas business are just general concepts. We hope to be able to achieve these targets while advancing one step at a time. At this point, we do not intend to change our target of 250 billion yen in overseas sales. On the other hand, looking at the current situation in Australia, we have not yet established business infrastructure robust enough to offset changes in the surrounding environment such as the country's rising wages, difficulty in hiring, and slumping finance market. In Australia, we had double-digit profit margin after depreciation and amortization in FY March 2022, and we believe we have that level of capability. We must find a way to return to that level. In North America as well, sales at Core BTS did not grow because progress was not made in integrating the sales departments of their cloud business from previous acquisitions. In response, we made drastic organizational reforms. We would like to get bigger while carrying out M&A in North America, but over these three years we will need to dedicate effort to solidifying the business infrastructure there. Taking the 250 billion yen into consideration, we are indeed behind the numbers in the Medium-Term Management Plan right now as you mentioned, but we would be better served dedicating effort to turning around our current business as opposed to chasing numbers. When the three years are over, we will reconsider whether we can achieve 250 billion yen in the subsequent plan.

Q2: Is it correct to say that the Tokyo side is aware of the issues facing your North American

business, and that measures are being taken?

A2: That is correct. We shuffled the sales organization there significantly. It will take a few months for the newly hired salespeople to begin operating. The new sales organization that launched in January should start producing results around the second quarter. In the network business as well, we hear that device procurement will normalize sometime around the summer. As a result, the first quarter will be harsh, but we expect to see results from summer onward.

(Questioner No.6)

Q1: What has been the approximate size of your expenses and investments related to human resources, including hiring, over the past three to five years? And how are you analyzing the resulting effects? If you further advance your human capital in the Medium-Term Management Plan, around how much do you intend to invest, and what kind of return do you want to generate?

A1: Our turnover rate (of employees leaving on their own) is around 3%, but turnover of younger employees has been an issue over the past few years, so we have been conscious of the need to work toward improving engagement. We have not been significantly increasing the number of employees involved in hiring, but around 80 to 90 employees who handle onboarding after hiring are in human resources development-related departments that conduct training and related activities. This is a large allocation of people even compared to other companies in the industry. The in-house infrastructure is in place, including both online and on-site. We are creating the environments to provide growth opportunities to young people with high potential.

Q2: It seems that requests for disclosures have been increasing, and that originality is needed. What kind of return is expected for what scale of human resources-related investment? Going forward, is it safe to say that the scale of your investment in human resources among total investments will grow?

A2: The amount of our investments in human resources is disclosed in our ESG Databook. In FY March 2022 it was just under 4 billion yen. We are not considering any sudden increases to this amount. For skill transfer-related training during the pandemic, we were able to save costs by moving the sessions online. There will also likely be some changes due to larger employee numbers going forward, but we do not plan to continuously increase human resources investments. We will think things through as we ascertain the effects. As requirements for disclosures are also increasing, we are discussing

internally what would be the most useful way to aggregate for disclosures. In our case, we have excellent organizations in place on the headquarters side including our HR Department and Human Resources Development Department. Since we also have HRM organizations within each division that attentively provide business-specialized learning and organize trainings aligned with the organizational culture, we would also like to aggregate and disclose the costs and other expenditures related to these organizations in an appropriate manner.

(Questioner No.7)

Q1: What is your aim for overseas expansion in 2030 and beyond?

A1: In both consulting and IT, new management concepts, technologies, and business models often come from North America. Since Japan is our home turf, our business will be focused on Japan for the time being. However, we believe that global perspectives will become essential to maintaining and increasing competitive strength in Japan as well. We are not sure when it will happen, but once global business accounts for 30-40% of our consolidated sales, we should also have representatives from overseas businesses on our board and among our executives, taking part in the discussions. Our business will probably not be able to get stronger without progress in that type of diversity. Ultimately, I believe our management will need to be more global. However, we will not be bringing over experts from overseas to serve as outside directors. We also have a feel for how things are overseas through the companies we invest in. For our overseas managers, we want them to discuss matters from the overseas perspective after understanding NRI's management as part of the NRI Group. Proper management must also be implemented overseas in order to have meaningful, diverse discussions. We have consulting, application development, IT infrastructure solutions, and operations functions in Japan, and the strength of our business model is in upstream. We would like to employ the same model overseas. In Australia, we acquired multiple companies and assembled a lineup of businesses. Though we have laid the groundwork to create the same operating model as in Japan, we still need to spend time improving the level of the management. In North America, we acquired one company with strength in operations and infrastructure. We would like to add the functions we lack via acquisitions as we did in Australia, based on the foundation of the application development function we had since before the acquisitions. In order to grow overseas, we thought there were no options other than Australia or North America if you consider that these are regions with countries where domestic demand is growing. We decided

that if we were to invest, we should focus on these two regions. Also, since we also have the vulnerability of performance being impacted by changes in the external environment, we aim to formidably reinforce the existing business infrastructure.

Q2: In overseas IT markets, I understand there are no system integrators that offer a complete range of services. Do you aim to establish such a presence?

A2: In North America, what Japan's system integrators handle is handled by companies in-house. When large-scale system modifications are performed at large client companies, IT vendors with vast pools of human resources deploy people to support the user departments. That type of business is possible with large clients, but companies in Tier 2 and smaller do not have the organizations to handle things in-house. They contract the work to outside vendors. For example, when these companies want to move infrastructure to the cloud and contract a third-party vendor for what remains on-premises in combination with infrastructure operations, or when the user department develops a customer contact point application and wants to contract a third-party vendor for everything from design thinking to implementation, the scale might be small but Core BTS has the functionality to handle these. We will expand the regional coverage and delivery domain of this concept through additional acquisitions. We will move forward one step at a time while being mindful of M&A risk, . The environments and markets of Japan and the US are structurally different, but we understand there are market segments where we can apply business models that are our strengths in Japan.

(Questioner No.8)

Q1: Regarding your financial policy, what is your approach to overseas M&A and treasury stock buybacks?

A1: Basically, we carry around two months' worth of sales as immediate working capital. Since we have 100-200 billion yen per year in cash flow, we decide the size and timing of our share buybacks in each separate instance. The logic is not that we buy back treasury stock if we conduct no M&A.

Q2: Is my understanding correct that your attitude toward M&A overseas has neither become more cautious nor more proactive?

A2: Conducting large-scale M&A while our existing business is unstable would exhaust our financial strength. I do not imagine that we will engage in M&A on such a massive scale during the three years of this Medium-Term Management Plan.

(Questioner No.9)

Q1: How much potential is there in modernization of IT resources over a long-term timeline?

And on what type of timeline will the effects appear in the Medium-Term Management Plan, on what scale? How are you able to check on the progress of that from the outside?

A1: What we are most optimistic about during this Medium-Term Management Plan is modernization of existing IT resources. We have been working on this since last year, and the effects have been significant in terms of development volume reduced. There should be effects this year, next year, and the year after. Development frameworks are an activity we have been working on for a long time. Since our current development frameworks have been around for some time, we will use new tools to fine-tune them. As for usage of AI, we have completed Step 1. Now for Step 2, we will fully engage in efforts such as automatic generation of scripts and test cases. Then, Step 3 will be to make these general-purpose and get them to the level that we can use them internally. We want to get these to Step 3 during the current Medium-Term Management Plan. If we can successfully improve productivity, it will impact our P&L. The effects will more likely appear in the next Medium-Term Management Plan rather than the current one.