

(Tokyo-30th November, 2023)

Nomura Research Institute, Ltd.

Q&A from Small Meeting for Institutional Investors

Part 1

(Questioner No.1)

Q1: The Financial Services Agency's Progress Report for Enhancing Asset Management Business in Japan which you touched on in the second quarter financial results briefings Q&A session recognizes the problem of double-check calculation to calculate the net asset value of investment trusts. What future impact will this have on NRI's earnings, and what communication have you had about this with the Financial Services Agency?

A1: There are two problems—one is double-check calculation, and the other is oligopolization by providing packages on open sales networks. Double-check calculation has been a conventional practice for a long time, but if single-party calculation is introduced, we will certainly comply. We will be paying close attention to future discussions about how this will officially be done. It would have some impact on earnings if the users of our calculation system decrease, but that would only comprise a modest portion of the whole. We will discuss this with clients throughout the industry.

(Questioner No. 2)

Q1: It was a surprise to learn that Ms. Yanagisawa will be taking over as CEO. This still seems to be a fresh development, but what message or thoughts do you have on the appointment of the new CEO?

A1: I would like to explain about the background behind this development. We are a company with an Audit & Supervisory Board, and we also have a voluntary Nomination Committee comprised of a majority of independent directors. For around two years, this committee had been discussing the next members of our leadership ("next cabinet members") as opposed to the president individually. New cabinet members were selected as a result of these discussions, and the new leadership team was established in April 2023. Ms. Yanagisawa has been in charge of a corporate department since before the next cabinet was formed, and she was part of the teams that handled the formulation of the long-

term management vision and Medium-Term Management Plan. Since April, Ms. Yanagisawa has exercised the most leadership in team-building among our new corporate officers. She was chosen for her leadership and her personable disposition.

Q2: I would like to ask about the positioning of your US business. I understand that you will be dedicating efforts to PMI in this Medium-Term Plan. NTT Data had been ahead at business in the US, but they are now struggling. Based on the struggles NRI is also having, what is your thinking at this point in time?

A2: Indeed, we are struggling in the US. We grew our business in Australia to around 70 to 80 billion yen in sales by the seventh year after acquisition. Australia is now also slumping, but that is attributable to curtailed IT investment due to high interest rates and the change of government. ASG, which is the predecessor of NRI Australia, has strength in public sector business, so they are heavily impacted. In North America, we are trying to create a company with a full lineup of services like in Australia, through Core BTS which we acquired. Core BTS originally started off in the network business. Since no major business growth had been expected in networks, they acquired four cloud companies with the intention of growing their cloud business with a focus on Microsoft Azure. This was before being acquired by NRI. At the time of the acquisition by NRI, they were considering cross-selling cloud business to their client base in networks. However, sales in cloud and sales in networks require different skill sets, so they realized that cross-selling would be difficult. For that reason, we worked until January 2023 on overhauling their sales organization. We bolstered their sales organization by appointing a Chief Revenue Officer (CRO) and also changing the area managers in three locations. We are also conducting training for their sales representatives. However, curtailed IT investment due to high interest rates is even harsher in the US than in Australia. The current situation is that we have an organization in place that is capable of producing sales results once the economy recovers. In the current Medium-Term Plan, we are prioritizing Core BTS's function as a core company. We will consider large-scale M&A in the next Medium-Term Plan.

Q3: Eventually, there will probably be a recovery in the external environment, including interest rates. Is there any change to your belief that the US is a market you should engage?

A3: There is no change.

(Questioner No. 3)

Q1: Your high margins in the domestic industrial IT solutions segment are stable. Could there be any potential upside in profitability from efforts such as modularization initiatives or making shared online services more prevalent? Could industrial IT be positioned as a driver for raising the profit margin of the group as a whole to 18% and 20% in FY March 2026 and FY March 2031?

A1: When we formulated the previous long-term management vision V2022, I was personally involved in strategic planning for industrial IT. We had a lower profit margin in industrial IT than in financial IT at the time, but that is significantly changing. The first change was gaining the ability to use the public cloud. Costs mount when building servers on-premises, but using the public cloud made it possible to build them in shorter time frames, and efficiency improved. The second change was bringing in larger clients. For instance, we are focusing on acquiring clients with sales of over 5 billion yen, or 10 billion yen. The third is, as you mentioned about modularization, our efforts in production innovation such as breaking down components (DiPcore). Shared online services cannot easily be created in industrial IT since there are no common regulations that apply to each company like there are in the finance industry. However, we worked on improving productivity through efforts such as breaking down functions common in the companies' e-commerce sites into components. Our profit margin improved as these efforts added up, but there is still room for additional upside going forward. There is particularly high potential for making larger clients out of companies with whom we have established joint ventures and clients whose senior management we have social relationships with.

Q2: Is it possible to secure earnings as a generative AI services provider in Japan's IT industry? Outside of Japan, generative AI is installed in SaaS and offered as a standard product like SAP's Joule. In Japan, SaaS vendors have little financial resources, and the business model is labor intensive with systems integrators handling work in contracted development arrangements.

A2: Multi-vendor is a characteristic of NRI. I do not believe that we will be creating generative AI in-house. OpenAI used to be the only option, but now the choices are growing. We will make good use of existing generative AI. At NRI, we use generative AI in two ways. One is to leverage generative AI that contributes to our clients' businesses. Clients are having trouble figuring out how to utilize generative AI. As such, it is important to have consulting capabilities to ascertain how generative AI can be leveraged to transform clients' businesses. We are actually receiving quite a large number of inquiries. Another

way that we use generative AI is to improve productivity internally. As we announced in the first half financial results briefings, we are working on improving the productivity of our test processes and coding. In some cases, we have even reduced man-hours of test processes by 50%. The key lies in how quickly you can find something for which the effects can be bolstered. The effects of the productivity improvements are sizeable. We anticipate productivity improvements in areas such as unit testing of downstream processes which we are outsourcing.

Q3: Will it no longer be necessary to think up solutions together with clients in consulting as those clients gain proficiency with generative AI?

A3: Here is an example from the education industry. At NRI, we understand what kind of data those clients have. For example, marking writing compositions takes them the most time. We realized that large effects could be achieved from having generative AI take over that marking work, and the managers were highly appreciative. Since there are many different types of writing compositions, we could not simply create something once and be done as you would with normal work systems. We end up providing ongoing support for updates to new content.

(Questioner No. 4)

Q1: What is the status of Planit, and how might it be deployed in Japan?

A1: Testing processes consume lots of man-hours. Planit does business in outsourcing for companies' test processes. Some people think that this work could be replaced by generative AI, but the key point is planning what perspective to perform the testing from. Not everything can be done by training generative AI. Planit and the Japan side will be exchanging information while moving forward.

(Questioner No. 5)

Q1: Cisco downwardly revised their guidance in their financial results. Is the North American business environment worsening more than NRI had anticipated?

A1: Indeed, IT investment is being curtailed, and the environment is harsh enough to require staff downsizing. We hear the situation is harsh even for larger companies than Core BTS. However, Core BTS also had internal factors. The slump from the end of 2022 through 2023 was tough, but their profit margin one year ago was around 5%.

Q2: Regarding generative AI, it was explained in a seminar at the Nomura Investment Forum that a telecom operator is leading Japan with its own proprietary LLM (large language model) and is using it in business. In a small meeting for another telecom operator, it was mentioned that there are business opportunities for generative AI such as usage in call centers. Is there anything you should be thinking about in terms of competition or alignment between NRI and telecom operators for generative AI? There seems to be no discussion about generative AI between NRI and the telecom operators you have close relationships with.

A2: In the evolution of generative AI, there is a movement toward being able to do various things through universality (versatility) and higher performance, and also a movement toward more compactness and specialization. Some people are likely pursuing more universality and higher performance, but at NRI we want to focus on usage of more compact, specialized generative AI by doing well at combining the necessary elements. Something more general-purpose like OpenAI's that produces answers no matter what you throw at it will end up with high CPU usage. As for our relationships with individual clients, I would prefer to refrain from making any comments at this time.

(Questioner No. 6)

Q1: You mentioned that Core BTS has pivoted to cloud business since growth is not expected in conventional network business. Will investment return to the network business, or is there room for even further downsizing there?

A1: The network business will not vanish. There is cyclical demand to address aging networks. The shortage of semiconductors for procurement has subsided, and we can now record revenues. Once demand settles down, investment to address aging networks should return. We will capture cyclical demand while maintaining the current organizations in place. We would like to significantly grow our cloud business.

(Questioner No. 7)

Q1: There have been some concerning articles about consulting business in Japan. One article was about foreign-owned companies freezing their regular pay raises. The other was about downsizing due to capacity utilization falling to around 60%, although there are probably many individual factors involved. How does NRI see the business climate?

A1: Currently, we have not had any discussions about operations slumping in consulting. Our order volume was somewhat lower year-on-year during the three months of the second quarter, but there has been no change in the business climate and business in the public sector and DX consulting has been strong, so our high rate of operations has continued. Even if other companies are in such a situation, the competition to attract talent is ongoing. We have no concerns about any macroeconomic factors, either.

(Questioner No. 8)

Q1: There have been numerous cases of overseas M&A by Japanese IT companies not working out well. I think there is some sort of problem. Situations where a company produces losses and downsizes after being acquired are happening everywhere. Is NRI experiencing the same pattern? Will there be any lack of clarity over where responsibility lies with the new president taking over? At the board level, what is your perspective on overseas M&A?

A1: Other companies sometimes acquire large numbers of companies when expanding overseas. At NRI, we have been acquiring companies whose management is capable of future growth. Domestic growth will be our focus for the next five to 10 years, but overseas growth is essential as Japan's population will further decline over the longer term. Overseas growth is also necessary for acquiring new expertise and technologies. NRI has also done some downsizing after acquisitions, but if we do nothing, the losses grow and the acquired companies end up being let go. After doing what must be done, if that is still not enough then management will decide how to proceed. We also overcame a period of struggles in Australia and achieved growth. I cannot say what we will end up thinking when we look back on it later.

Q2: Is it a case of not being able to help what has already occurred, and just digging in?

A2: First was to decide as a company whether or not to expand overseas. Then, we narrowed our focus to industrialized countries where the population is growing and domestic demand is increasing. We narrowed down our candidate companies with the approach of targeting those who will meet their clients' needs similarly to NRI rather than whether or not they have certain products. However, Core BTS also had internal problems, so we handled those.

(Questioner No. 9)

Q1: This question is about your human resources strategy for Japan's "2025 Digital Cliff." NRI might have hiring advantages in terms of name recognition and compensation, but BayCurent and Simplex have raised their compensation, as have M&A intermediary companies. How will you deal with the risk of being unable to secure sufficient personnel leading up to 2025?

A1: Human resources are everything for an IT company, including for NRI. We are always thinking about how to hire and develop them. In terms of hiring, we plan to expand our new graduate hires to 500 in 2025, while still maintaining the quality level of our personnel. We are also putting out recruiting advertisements, doing promotions, and are engaged in various other efforts to hire outstanding university students.

(Questioner No. 10)

Q1: In North America, your profit margin has not really been able to increase. While we could say that you are taking action according to the market environment, your measures are proceeding slowly and it is concerning whether governance there is functioning. Have you changed from leaving things up to the local management to exercising more control?

A1: In our announcements until now, we have been saying that the next half-year will improve, yet that has not happened. In North America, we are thinking about sending over Japanese companies as clients and leveraging Core BTS's resources by teaming them up with NRI-ITSA. Some might think that NRI-ITSA should have been teamed up with Core BTS from the start, but it is fundamental for Core BTS to grow organically. We are taking measures according to changing circumstances.

Q2: Cisco claims that they had a large order backlog but not enough resources for implementation, and that final demand is there. What do you think about this?

A2: At Core BTS, they have been making progress at recording sales. They have been shuffling personnel in sales, but their engineers are in place.

(Questioner No. 11)

Q1: This question is about your mid-career hiring. Your focus had previously been on new graduate hires. How would you evaluate your retention rate for mid-career hires?

A1: We had previously been focused on developing new graduates, but we are now

bolstering our mid-career hiring to bring aboard more personnel who can contribute immediately. Our voluntary turnover rate is around 3%, and mid-career hires comprise a larger proportion of that than the overall average for the company. Some mid-career hires are not averse to leaving. Among our 250 office and department heads, the ratios of those originally hired as new graduates and those promoted from among mid-career hires are around the same. Promotions depend on capability, and those who fit in and get established at NRI move up.

Q2: Are you fully satisfied with the retention rate and performance of your mid-career hires?

A2: Our hiring fundamentally focuses on new graduates, but we also need mid-career hires in order to add immediate contributors.

(Questioner No. 1 2)

Q1: For your approach to domestic price increases, do you have a table of unit prices based on which you offer discounts and estimates? And did you revise the table this year? Many other companies are revising their unit price tables.

A1: The rising energy costs due to high crude oil prices and increased overseas cloud usage fees due to the weak yen have been passed on to clients. NRI has a standardized profit margin approach, but our prices are decided according to whether we are providing added value that our clients recognize. We strive to generate added value rather than to lower prices when facing competition. For example, since added value is not high in reworking core systems by itself, we propose added value that will be convincing to clients who are struggling with the move to DX.

Q2: The rising energy costs last year have entered a correction this year. Since other companies are also raising their prices, do you think it will be an environment conducive to price increases next year also?

A2: The key lies in how much we can improve productivity. We are projecting an operating margin of 20% or higher as our numerical outlook for the year 2030, and this will be achieved through higher added value proposals and productivity improvements. Other companies point to labor costs, but our approach at NRI is to distribute our results as a company among our employees. Returns to employees are determined according to a calculation formula using amount of added value per person and profit per person, and our average salary has been increasing as a result.

(Questioner No. 1 3)

Q1: Will you raise your standard profit margin going forward?

A1: Ultimately, our standard profit margin is nothing more than a standard. The idea is to propose added value that meets or exceeds our standard profit margin. We do not simply make proposals by adding our standard profit margin to the cost. Our proposals always have a balance of cost versus added value and function in mind.

Q2: With your overseas business at the stage of making a turnaround, will you also apply the standard profit margin approach overseas?

A2: At this point in time, I cannot say. We will probably need to exercise more ingenuity to be able to provide high added value. Our profit margin in Australia based on actual performance is around 10%. With the current state going forward, we could probably project that no higher than 15%. Various efforts need to be made, including to improve productivity.

(Questioner No. 1 4)

Q1: Your disclosure materials show that stable revenue sources account for about 60% of total revenue. Around what level do you aim for this to be in 2030?

A1: The ratio of our ongoing business will continue forward at the same level of around 60%, and we consider that to be an appropriate level. We must try to do new things, and those are influenced by the economy. Balancing new efforts with ongoing business, we will maintain the level of around 60%. When high-profit-margin financial IT comprised 60-70% of sales by segment in the past, our profit margin in industrial IT was low. When past financial crises occurred, our performance suffered because financial IT comprised a larger proportion of our business. Based on that experience, we worked on structuring ourselves to generate profit even in the face of a financial crisis and increased the proportion of industrial IT. We will likely have much more resilience than before when the next financial crisis hits.

(Questioner No. 1 5)

Q1: Around what level of profit margin are you targeting in North America long term? The competitive environment in North America is different from Australia. Can you produce a two-digit profit margin in North America? If it cannot go any higher than around 5%, is

there any sense in devoting resources there?

A1: In Australia, we are targeting a profit margin of around 15% in 2025. In North America we are currently breaking even, and we want to be able to achieve a high-single-digit profit margin by the end of FY 2025. We will consider margins beyond that in the next Medium-Term Plan, but I would like to be able to reach 10%.

Q2: What is the difference in profit margins between Australia and North America attributable to?

A2: It is due to the differences in capabilities owned and business scope. In Australia, we plugged in the pieces that were missing. We acquired the functions of managed services and systems consulting through M&A. We are lacking capabilities in upstream processes in North America, which might be why our growth there is weaker than in Australia.