

(Tokyo-30th November, 2023)

Nomura Research Institute, Ltd.

Q&A from Small Meeting for Institutional Investors

Part 2

(Questioner No. 1)

Q1: Your domestic business is currently performing well. How much of the current growth pace can you sustain?

A1: We are achieving revenue and profit growth across all segments. Business in consulting is strong in public sector PMO projects and DX consulting. For IT solutions business, we had large numbers of projects in non-face-to-face, contactless, and e-commerce, and in increasing logistics efficiency during the three years of the pandemic. Even since the pandemic subsided, the momentum behind IT utilization has not changed. Japan has also been behind other countries in IT utilization, and managers consider this an ongoing issue.

Momentum is also building for changing front-end systems. At the same time, the back-end systems that support front-end are having issues with being old and having poor connectivity or otherwise holding back future business expansion, so there is also movement toward modernizing those. Demand is rising for both front-end and back-end, and we believe this situation will continue for a while.

Having both consulting and IT solutions enables us to meet clients' expectations for IT utilization. We also have the capabilities and solutions to create both high-difficulty mechanisms for front-end and large-scale mechanisms for core systems, which puts us in a very favorable position.

Q2: Japan's IT industry has issues such as personnel shortages and surging labor costs, but demand is also robust. What does NRI think about passing on surging labor costs and the cost of securing personnel headcount to clients?

A2: Since our compensation levels are high (relative to other companies), we are not in a situation where we cannot secure enough human resources without paying more. Our compensation is configured for annual salary increases in correlation with improvements in company performance. Monthly salary raises and promotions can be awarded based

on capability. We determine bonuses according to added value and operating profit growth rate per person. Our framework enables employees to also reap benefits from the company's continuous growth.

Currently, we are hiring around 450 new graduates, and we plan to hire around 500 in the final year of the Medium-Term Plan in FY 2025. Until now our focus has been on new graduate hires, but now we are also bolstering our mid-career hiring for immediate contributors.

Q3: What types of companies do your mid-career hires come from?

A3: They come from various companies, but many of them are in the same industry as us. Some also come from the IT departments of business companies.

(Questioner No. 2)

Q1: What is the impact of generative AI on NRI's business? Please share your comments in terms of both the status of demand and inquiries from clients and also its utilization for your own processes.

A1: Consulting demand for how to use generative AI is increasing. We think of its application for clients in three separate phases. Phase 1 is simple work that clients themselves can do. Currently we have entered phase 2, and there is significant demand for using generative AI to make call center, help desk, and other such operations more efficient. Then in phase 3, we would like to create AI-based management information systems. At this current stage, phase 2 is our main focus.

We are also working on using generative AI to improve NRI's own development productivity. In the development process, the most labor-intensive parts are development and testing processes. In the first stage, we utilize AI in testing processes and then work on automating program generation via AI.

(Questioner No. 3)

Q1: Will technological advancements in generative AI result in less need to outsource?

A1: Generative AI should be able to replace the majority of downstream processes. However, that does not mean that our business partners' work will disappear. They can expand the breadth of the work they handle and increase their workloads by shifting to more upstream processes. We hope that our business partners will work on shifting toward

more upstream processes, and that we can build the age of generative AI together.

(Questioner No. 4)

Q1: Since Japan has been behind other countries in the shift to DX, investment that started in front-end is now shifting to back-end. Is it that front-end caught up and attention has now shifted to back-end? Or is it that both front-end and back-end are still behind?

A1: The framework of front-end is not something that you build once and are done with. It must undergo changes along with the growth of the business, so work arises on a regular basis. On the other hand, back-end is cyclical once it has been built. Currently there is demand for both.

(Questioner No. 5)

Q1: Does anything look promising in business with public offices and government agencies, such as dealing with e-invoicing?

A1: There is a certain level of demand for work related to e-invoicing, and the release has already happened. There will likely be an increasing shift to electronic going forward. NISA will also be under a new scheme starting next year. The new NISA is a mechanism that encourages investing, so an increase in transactions is anticipated. We expect this to have an impact on our sales. In Japan, there will probably be more work making IT more sophisticated in line with tax reforms and system reforms.

Additionally, we are devoting effort to working on “My Number” cards. This is not for the government’s system itself. Rather, we are working on shared online services for financial institutions and others who use that system.

(Questioner No. 6)

Q1: Failures occurred in the government administrative services system that uses My Number and in the Zengin System. Is there any risk of something similar happening to NRI?

A1: We offer a wide variety of shared online services. Among these, our THE STAR system for securities back office supports social infrastructure by processing half of the transactions and managing half the brokerage accounts on the Tokyo Stock Exchange. Since the impact is enormous if a failure occurs, we are always monitoring projects in

the Quality Management Department that I oversee so that failures do not happen. We have accumulated decades of experience preventing failures such as these from occurring.

(Questioner No. 7)

Q1: When do you conduct the impairment tests for your US subsidiaries?

A1: We are verifying that with accountants every quarter. The situation is not favorable, but we are reaching our planned numbers every time.

Q2: How are things in Australia?

A2: We have been doing business there for seven years while repeatedly conducting M&A. High interest rates are having an impact, but not as much as in the US. We are conducting impairment tests there in a similar manner, and there are no problems at this time.

(Questioner No. 8)

Q1: There was an announcement that the Australian government would reduce its reliance on consultants. Is that impacting NRI's business?

A1: We have been impacted by curtailed investment in consulting and IT resulting from the change of government there last year. However, their government will not be able to keep functioning with continued restriction on IT investment. Once things have gotten settled again, we anticipate that investment will return.

(Questioner No. 9)

Q1: Will you be accelerating your overseas M&A going forward under your new president?

A1: Our business base is established in Australia, so we do not plan on any large-scale M&A there. The country is massive, so we could conduct some smaller-scale M&A. In North America, we are doing business centered around Core BTS which we acquired two years ago. Currently, we have finished rebuilding their sales organization and making structural reforms, and our policy is to verify the results of these before considering subsequent M&A. We have already set out our policy to plug in any missing pieces through M&A during the next Medium-Term Plan without conducting any large M&A

during the current one, and our new president has the same mindset.

Q2: Are you considering entering Europe?

A2: We are not. If the country is not an advanced country with IT industry fueled by domestic demand due to a growing population, we will not be able to charge the appropriate prices. Only Australia and North America meet these criteria. North America is large in size and high in difficulty, so we first gained experience in Australia before entering North America.

(Questioner No.10)

Q1: What are the financial KPIs in your Medium-Term Plan?

A1: We raised our dividend payout ratio from 35% to 40%. We will also thoroughly maintain an ROE of over 20%.

Q2: Your ROE is currently already over 20%. Will you keep it steady for a while, or do you plan to continue increasing it? If it keeps rising, will it rise at the same pace as it has until now, or could there possibly be any factor that would speed up the increase?

A2: In the current Medium-Term Plan, we will reliably conduct treasury stock buybacks and keep ROE around the 20% level while managing business growth. As for ROE level in the next Medium-Term Plan, we will discuss that more going forward.

(Questioner No.11)

Q1: Please share more details about the problems in your overseas business. I understand that the environment is harsh. Could you particularly share the background behind why consulting is producing a loss?

A1: Our overseas consulting business primarily consists of supporting Japanese companies that have entered overseas markets. They operate on a small scale in locations throughout the world, and growth in South Asia and China slowed this year. In IT solutions-related business, Core BTS in North America originally started in the network business, but they had added cloud business by acquiring four companies through M&A in the past since no major business growth had been expected in networks. The M&A happened before being acquired by NRI, but the post-merger integration (PMI) did not go well, so we spent around six months overhauling their sales organization starting in January of this year.

(Questioner No.12)

Q1: You announced that there would be stronger collaboration between Core BTS and NRI-ITSA. What impact will that have on your North America strategy and sales going forward?

A1: The highest priority is organic growth for Core BTS. On the other hand, NRI-ITSA located in Dallas, Texas in the US operates on a small scale, mainly supporting the IT of Japanese companies. They need additional resources to expand their operations, so we teamed them up with Core BTS.

Q2: Which of the two companies will manage the collaborative business between Core BTS and NRI-ITSA?

A2: It will be the business of NRI-ITSA's clients, and NRI-ITSA will be mainly in charge with cooperation from Core BTS.

(Questioner No.13)

Q1: Why is your profit margin in industrial IT lower than in financial IT?

A1: Our domestic financial IT includes shared online services which achieves a high operating margin and also comprises a large proportion of that segment. On the other hand, systems in industrial IT are built individually, resulting in a low profit margin. Although it may still be lower than financial IT now, our profit margin in industrial IT has come a long way to reach the level it achieves now. The efforts we have made to increase the scale of our clients, utilize public cloud, and break down components in e-commerce front-end have contributed to that, along with productivity improvements. Due to the cumulative effect of these efforts, there are now even months in which our profit margin in industrial IT exceeds the margin in financial IT.

(Questioner No.14)

Q1: Could we expect further improvements in productivity from breaking down components in industrial IT? Or has it reached a plateau?

A1: There is further potential for breaking down components, so more productivity improvements could be expected. We will be producing one new component after another. It seems unlikely that we would run out of components to make.