

January 30, 2009

## Fiscal 2008 Third-Quarter Earnings Presentation Q&A

- : Question
- : NEC's answer
- Third quarter: October to December
- Fourth quarter: January to March

### Questioner A

•Does NEC plan to overhaul NEC TOKIN's business portfolio after its business restructuring has been completed?

→The primary objective of NEC's injection of capital into NEC TOKIN and its conversion into a wholly owned subsidiary is to stabilize its management base and restore profitability.

→Plans for NEC TOKIN after it becomes a wholly owned subsidiary will be determined taking into account market conditions at that time. Currently, market conditions are shifting dramatically at a breakneck pace. Therefore, our first priority is to stabilize NEC TOKIN's management base before making our next move. We intend to withdraw from rectangular-type rechargeable batteries and reed switches as early as possible.

→Meanwhile, the car battery business offers strong prospects for the future. In this field, NEC TOKIN and NEC will work as one to develop business.

•What is your timeframe for reducing your workforce by 20,000 employees?

→The 20,000 job cuts include personnel reductions at NEC TOKIN (450 employees through early retirement in Japan and 9,000 employees through downsizing overseas).

## **Questioner B**

•What is your outlook for market conditions heading into the next fiscal year? Do you have any particular concerns? For example, could the relatively healthy IT/Network Solutions business weaken in fiscal 2009? Could the Mobile Terminals and Electron Devices businesses, which both struggled in fiscal 2008, deteriorate further going forward?

→We have yet to formulate next fiscal year's budget. However, in the fourth quarter of fiscal 2008, we expect Electron Devices-related fields to see a significant downturn. The auto, digital home appliance and PC-related fields account for a significant portion of NEC's business. In response to worsening market conditions since around November and December 2008, manufacturers in these fields have continued to pare back production in order to reduce distribution inventories. There are no prospects for improvement in production in the fourth quarter of fiscal 2008. Orders may pick up again in the first quarter of fiscal 2009, but are unlikely to return to previous levels considering demand for end products. Having said that, the fourth quarter has been abnormal in many respects, and so we do not expect the current level of demand to persist into the third and fourth quarters of fiscal 2009. In Semiconductors, we will strive to ensure that profitability can be maintained even with net sales of ¥500 billion (cf. fiscal 2008 forecast is ¥550 billion).

→Regarding the Mobile Terminals business, the Japanese mobile handset market is expected to contract by approximately 30% in fiscal 2008, but I don't anticipate any more large declines going forward. Therefore, the issues we must now face are how to enhance our product appeal and how to expand our market share. In consumer PCs, with more netbooks and other small PC models on the market, NEC projects sales in fiscal 2008 to increase year on year. Meanwhile, there has been a sharp drop-off in business PC orders and shipments from the end of 2008. Therefore, we must expect the business PC market to remain soft in fiscal 2009, and to see further declines in consumer PCs prices. Overall, we don't expect consumer PC shipments to fall too much, but business PC shipments will probably decline considerably. Looking beyond the current economic malaise, however, NEC aims to shore up its performance as much as

possible by bringing to market PCs based on innovative concepts. In this context, we are considering the launch of new products such as a mobile-PC hybrid product next fiscal year.

→In communications systems, we don't foresee a large drop in telecom carrier business sales, but one of our concerns is the impact of the yen's appreciation. In fiscal 2009, the yen is unlikely to appreciate as sharply as it did in fiscal 2008, from ¥120 to ¥90 against the U.S. dollar. Hopefully, it seems we can assume that the yen will remain at the current level next fiscal year. The Network Systems business for enterprises has already contracted by around 10% year on year in fiscal 2008 and is projected to shrink a little more in fiscal 2009. However, we expect this business field to attract attention because it offers many effective solutions for enhancing the productivity of white-collar workers.

→In fiscal 2008, the IT-related business (IT Services/SI and IT Products areas) did not contract too much. However, sales to local/small and medium-sized enterprise customers have begun weakening in year-on-year terms since the end of 2008. In fiscal 2009, we are projecting a double-digit decrease in sales to these customers. Some large manufacturing-sector enterprises have suspended or cancelled IT investments, but this trend does not necessarily apply to all companies. Generally, upgrade and maintenance for existing systems accounts for approximately 70% of IT investment, while new projects account for the remaining 30%. Because the IT investments needed to develop new services are essential, we don't expect any large decrease in investment. For instance, NEC is investing around ¥40 billion in IT in order to make the entire organization more "visible." We will also tackle operational issues such as responding to in-progress construction standards. Contrary to expectations, we should see enterprises step up investments designed to enhance their competitiveness.

•What is your approach to reducing variable expenses as part of earnings structure reforms?

→Reducing variable expenses is challenging in the face of increasingly fierce competition and falling prices. However, we believe that any

improvement in the variable expenses ratio is crucial to restoring profitability. In the process of analyzing our overall cost structure, we will closely examine the effectiveness of both fixed and variable expenses. In any case, we intend to alter our spending on variable expenses.

•What overall direction do you foresee for the Semiconductors business going forward?

→Whatever the direction we aim for, we must first and foremost prioritize improving the cost structure so that operations produce no losses. In any event, the semiconductors market is contracting. Therefore, we are thinking seriously about the future course of the Semiconductors business, assuming that NEC Electronics' sales could fall to around ¥500 billion.

→We recognize that the economic downturn is gradually reshaping customer needs for system LSIs. For example, one customer asked us whether we could offer an efficient way for his entire company to unify design specifications for system LSIs, rather than having each division make separate requests as before. To satisfy these needs, we must provide consulting services from a broader point of view, encompassing not only mere LSI circuit design but also basic systems design and software architecture. We believe that NEC is better positioned to develop new business of this sort than companies that are simply semiconductor manufacturers because NEC has a strong grounding in IT/Network Solutions. We must transform our business model into one that views semiconductor chips as one piece of a comprehensive solution to the issues faced by customers. To do so, we must embrace the core perspective of first understanding these business issues faced by customers, and then ask ourselves how we can best solve them.

→We will begin by offering consulting services of this nature to customers facing many different business issues, and seek to expand these services into a new solutions business. We are considering ways to best transform our current business structure to achieve this goal. By no means do we believe that volume expansion holds the key to riding out the economic downturn. We need to determine our next move in line with a solutions-oriented strategy.

→In this sense, given the rapidly changing market conditions, we don't believe that we should determine our future direction now. Rather, we need to clearly gauge conditions after the economy settles down in order to ensure that we get our overall strategy right.

•In the latter half of fiscal 2009, I don't expect NEC to book lower sales and earnings as in the same period of fiscal 2008. In recent years, NEC has refrained from haphazardly expanding business overseas, and so any harm done by the global economic downturn should be relatively minor. In fact, considering the setbacks experienced by overseas communications equipment manufacturers, NEC may be better positioned to reap considerable business opportunities ahead. Although difficult conditions should persist into the first half of fiscal 2009, I suspect that the second half will not be as bad as you expect. Wouldn't you agree?

→We strongly wish that things play out according to your scenario, but we must maintain a conservative outlook at this time. Without being too optimistic about current uncertainties, we will take actions based on a conservative outlook, in order to steadily capture opportunities. Following the collapse of the IT bubble, NEC saw a considerable drop in the weight of its overseas business and it is currently in the process of improving that ratio. Although this small share of overseas business has kept our exposure to losses fairly low, our overseas business is still susceptible to the global economic downturn. Furthermore, the overseas businesses of our competitors have also suffered setbacks overseas, resulting in fiercer competition in Japan.

→We are neither optimistic nor by any means pessimistic about the future. Considering the plight of communications equipment manufacturers doing business with Western communications carriers, NEC's carrier business remains in a relatively strong position.

### **Questioner C**

•What is your revised forecast for consolidated free cash flow for fiscal 2008?

→Our revised forecast for consolidated free cash flow for fiscal 2008 is negative ¥190 billion. We aim to restore profitability and positive free cash flow as soon as possible.

•What is the point of converting NEC TOKIN into a wholly owned subsidiary given NEC's focus on the IT/Network Solutions business?

→Recently, companies of all kinds have been focusing on the environmental and energy fields. In the near future, a new era of electric vehicles should arrive. At that time, we expect applications for automotive semiconductors to grow by leaps and bounds. In addition, the uptake of home-use batteries could lead to the use of many more electronic devices in the home. Because battery technologies could open up new markets in these kinds of ways, we believe that the environmental field has the potential to become a key engine behind our future businesses. For this reason, NEC has positioned the environmental and energy field, including car batteries, as a core business, and will develop operations in this field as a centerpiece of its new business portfolio. NEC is currently ahead of competitors in terms of car battery technologies. Nonetheless, NEC is working on many fronts to develop next-generation batteries at its research laboratories. Going forward, NEC will advance R&D initiatives in the battery business while striving to be a leader in the battery market.

•The U.S. Obama administration has recently announced plans to invest US\$6 billion in broadband infrastructure. Could you please comment on the current status of LTE(\*1)-related business and NEC's business opportunities ahead?

→Our Next Generation Network (NGN)-related business in Japan is progressing steadily, and sales are largely on target. Various overseas countries are stepping up efforts to convert their communications infrastructure into fiber optical networks. Because network infrastructure investments are one means of providing an economic stimulus in times of recession, we believe that NEC will enjoy significant opportunities in many different areas. Going forward, it is difficult to foresee what kinds of

economic stimulus measures may be implemented by various countries. However, we will strategically concentrate development resources in this area, targeting the potential benefits that can be expected.

NEC is a world leader in LTE development. Through an alliance with Alcatel Lucent, we plan to deliver devices to NTT DOCOMO, Inc. and U.S.-based Verizon Communications Inc. We see sizable opportunities in LTE, WiMAX(\*2), femtocells (\*3) and other businesses because they represent an effective means of building broadband access infrastructure.

\*1 LTE: Long Term Evolution: a high-speed 3G standard also referred to as “3.9G” and “Super 3G.”

\*2 WiMAX: a wireless standard that has been approved for standardization by the IEEE 802.16 Committee as a broadband wireless access system that enables “last one mile” access.

\*3 Femtocells: compact wireless base stations for home use.