

CFO Message



Osamu Fujikawa

Corporate Executive Vice President and CFO
(Representative Executive Officer), Member of the Board

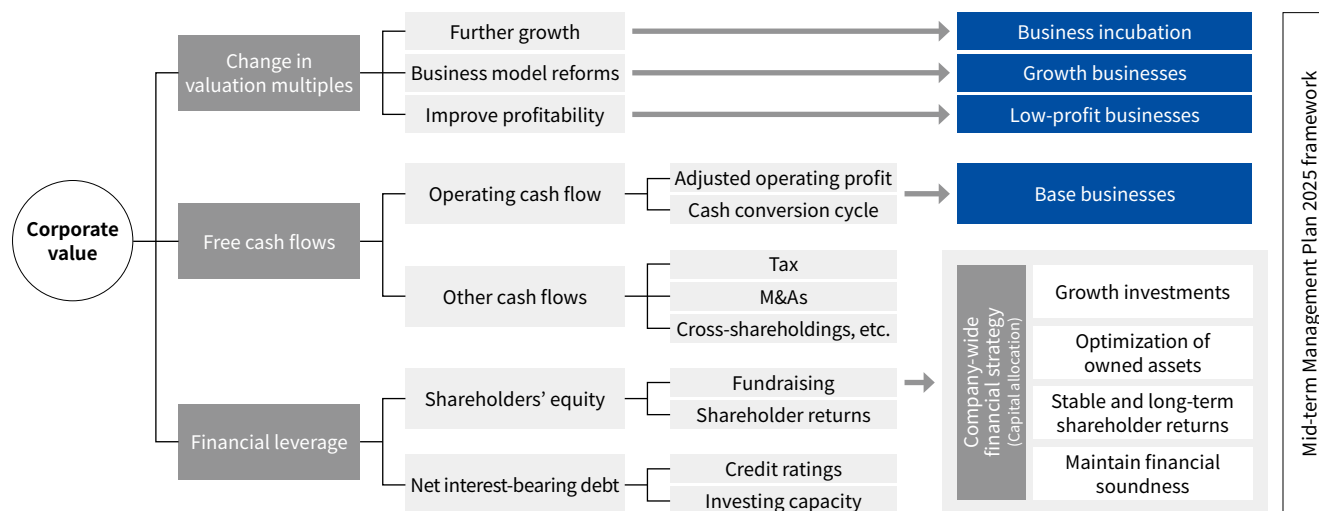
Completion of the Third Year of Mid-term Management Plan 2025

Three years have already passed since my appointment as CFO, and I have now entered my fourth year of tenure. Mid-term Management Plan 2025, which we announced in May 2021, has already passed its halfway point and is now in its final stages. Looking back at fiscal 2024, the third year of the plan, revenue and non-GAAP operating profit exceeded our initial forecasts, due in part to the continued strong performance of our domestic IT services business and growth in our national security business. For fiscal 2025, we are projecting revenue of ¥3,370.0 billion and non-GAAP operating profit of ¥255.0 billion. Revenue is expected to decrease by 3.1%, mainly due to Japan Aviation Electronics Industry, Ltd. no longer being a consolidated subsidiary, but we expect both the IT Services and Social Infrastructure businesses to see an increase in revenue, as the Company plans to take advantage of the continued strong demand in the domestic IT services and aerospace and national security domains to firmly seize business

opportunities. We will also continue to work on improving profitability, and plan to achieve a year-on-year increase in non-GAAP operating profit of ¥27.4 billion. At around double the fiscal 2021 level, the target of ¥300.0 billion in non-GAAP operating profit set forth in Mid-term Management Plan 2025 initially appeared to be a rather challenging hurdle, but we are now starting to see a path to achieving it.

While revenue and non-GAAP operating profit are important indicators, we also need to improve our valuation multiples, generate stable free cash flows, and optimize financial leverage if we are to achieve our ultimate goal of enhancing corporate value. As a framework for achieving the goals set forth in Mid-term Management Plan 2025, we have set a target level of corporate value to be achieved by the end of fiscal 2026, the final year of Mid-term Management Plan 2025, and are working to achieve this by creating a road map and setting clear milestones in a logic tree, which we incorporate into our action plan and review on a regular basis. In the next section, I will focus on the activities I am responsible for as CFO as we work to achieve our target level of corporate value.

Logic Tree for Improving Corporate Value



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Measures to Improve Profitability of Low-profit Businesses

To increase profits, I believe that it is important to improve the profitability of base businesses in parallel with the development of growth businesses, and, as CFO, I am taking a hands-on approach to monitoring the improvement of particularly low-profit businesses. Businesses that do not meet the set hurdle rate are defined as low-profit businesses. I am working with the relevant business units to identify structural issues related to profitability and formulate improvement plans, and I regularly monitor the progress of these initiatives. At the start of Mid-term Management Plan 2025, there were 16 businesses defined as low-profit businesses, but the number has been reduced to nine as of the end of fiscal 2024, and the profitability of the remaining businesses has also steadily improved. Of the nine businesses that have successfully exited the group of monitored low-profit businesses, the mobile backhaul business was chosen to be integrated with a partner company. While considering options such as this, we will continue our activities to turn around low-profit businesses by the end of fiscal 2026 as planned. Meanwhile, to prevent high- and

medium-profit businesses from becoming low-profit businesses, we will work to improve profit margins on a permanent basis through early detection and improvement of businesses that may present issues when carrying out the annual budget.

Improving Capital Efficiency

To increase free cash flows, it is important to improve capital efficiency as well as increase profits.

One approach we have taken to this end is to shorten our cash conversion cycle (CCC). In fiscal 2023, we took strategic measures including increasing inventory in response to business conditions such as component shortages, but by the end of fiscal 2024, we had almost normalized our operations. Having experienced these changes in the business environment, we have resumed activities to improve asset efficiency that are in line with current business conditions. In particular, as we work to address the vulnerability of supply chains that was brought to the fore by the COVID-19 pandemic, we are strengthening measures to ensure thorough management of working capital, as well as preparing for potential future risks by promoting closer collaboration between related departments such as sales,

manufacturing, and procurement. We are also engaging in ongoing efforts to promote the creation of cash by converting assets into cash, while taking steps to eliminate cross-shareholdings and examining the significance of continuing to hold real estate.

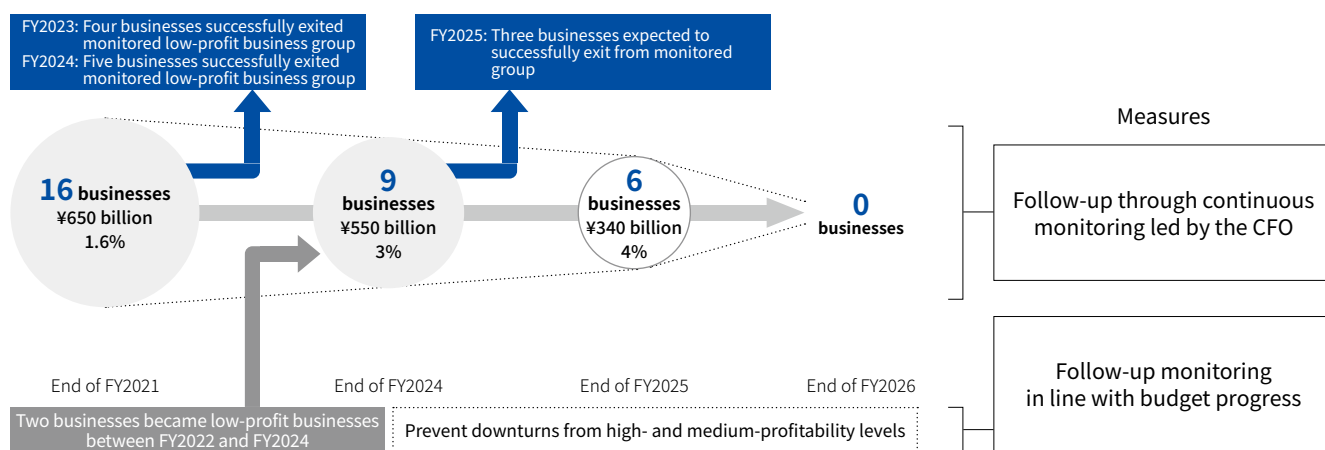
We recognize that ROIC should exceed the weighted average cost of capital (WACC) level expected by the capital markets, and have set a target of 6.5% for fiscal 2026 (7.0% if no M&As are implemented). We will first thoroughly ensure that we meet this standard, and then work to improve upon it while ensuring consistency with our management strategies, such as our competitive environment and M&As.

Capital Allocation

Through the measures I have mentioned, we aim to generate ¥1.3 trillion in operating cash flow over the five-year period from fiscal 2022 to fiscal 2026. Our policy is to retain the cash generated as surplus funds for investments in areas that will become growth drivers in the future, as opportunities arise aimed at increasing corporate value while prioritizing stable dividends and maintaining financial soundness. We will use the level of financial soundness currently evaluated by credit rating agencies as a guideline to be maintained over the medium term. Our basic policy regarding dividends is to steadily increase them. In the dynamic ICT market, there is an abundance of investment opportunities for business expansion. We will maximize returns to our shareholders by translating these investment opportunities into increased earnings, and through capital gains from increased corporate value and stable dividends. We will also make flexible decisions regarding acquisition of treasury stock, considering factors such as growth investment plans and the level of surplus funds.

Achieving Data-driven Management

We are working to revamp our core systems to enable them to serve as a management infrastructure that will allow us to digitally grasp the progress and effects of initiatives like those



Note: Figures in circles refer to the number of target businesses monitored by the CFO, and include the total revenues and adjusted profit margin of the targeted businesses.

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I have discussed so far, as well as the impact of changes in the business environment, and to respond flexibly and promptly to these changes. Because NEC works with a variety of products whose characteristics differ from business to business, there had been no unified Company-wide system for the process from sales negotiations to contracts and orders. To address this issue, we have standardized data by establishing Company-wide criteria for products and pricing and standardizing processes. This has enabled us to share information to the entire Company that had previously only been visible within individual business units. The first iteration of the new system for sharing information was launched in May 2023, with all other releases expected to be made by the end of fiscal 2026. We are beginning to see results emerge through the use of this system sooner than expected. For example, it is now possible to instantly view detailed data on the actual status of operations, enabling us to immediately identify issues and implement appropriate countermeasures. The system then enables us to grasp the progress of countermeasures whenever necessary in the form of data, making data-driven management possible. Importantly, this means that an environment has been created in which everyone from top-level management to the relevant personnel can view, make decisions, and take action based on the same shared data. By further strengthening internal systems and human resource development to make the most of this visualized information, we hope to utilize the data in a more advanced manner going forward.

Non-financial Strategies Linked to Corporate Value

Positioning non-financial strategies as an important foundation for sustainable growth, NEC not only discloses non-financial information in response to requests from external parties but also aims to utilize non-financial information for the sustainable enhancement of corporate value by further clarifying the link between non-financial strategies and financial aspects of the Company. In addition to working to reduce capital cost over the medium to long term from a risk

management perspective, we will leverage the know-how we have developed through our in-house efforts to address issues such as climate change and information security to propose solutions to our customers, leading to expanded business opportunities and increased free cash flows. We are also working to further advance and apply causal analysis of indicators of corporate value and non-financial data and initiatives. One such example is our analysis of correlations between corporate value indicators and our “transformation of people and culture” initiative. To achieve the target employee engagement score of 50% set forth in Mid-term Management Plan 2025, we have identified measures that are expected to have a particularly significant impact on each organization, and are narrowing down our focus areas and working to improve our initiatives with efficiency and effectiveness as key themes. By using the data we have gathered in this way, we are incorporating non-financial indicators into data-driven management, leading to more advanced managerial practices.

In July 2024, NEC issued a sustainability-linked bond via a public offering in the domestic corporate bond market. The issuance of the bond is an example of NEC using financing to show its strong commitment to one of its material issues (Fundamental Materiality), “Environmental Action with a Particular Focus on Climate Change (Decarbonization).” The SDGs-based financing initiatives are the NEC Group’s Purpose put into practice, and they provide a way for us to engage in dialogue and co-creation with a variety of stakeholders related to our management of sustainability initiatives.

Final Remarks

I have been striving to do my part in achieving the goals of Mid-term Management Plan 2025 for the past three years since becoming CFO, but looking back, my appointment came at a time when the Company was under exceptional operating conditions due to the COVID-19 pandemic. Since then, the Company has faced further changes in the business environment, such as

a shortage of components and a sharp depreciation of the yen, and I have been compelled to make management decisions to minimize the impact of such external factors. From this experience, I have learned that while it is important to be able to prepare countermeasures for anticipated risks, it is also important to have a system in place to quickly grasp changes and swiftly implement countermeasures, given the likelihood that unexpected or greater-than-expected risks may occur. In other words, I have come to believe that the ability to respond resiliently to changes is crucial. I mentioned earlier that we are beginning to see a path to achieving the adjusted operating profit target set forth in Mid-term Management Plan 2025, but geopolitical risks, abnormal weather events, and other factors mean that the business landscape remains uncertain. We will swiftly identify signs of change and, while making full use of our long-cultivated ability to respond, we will fully commit to achieving the targets of Mid-term Management Plan 2025.

From fiscal 2025, we have decided to calculate and disclose segment performance by properly allocating Company-wide expenses, which were previously shown as adjustments, to each segment. We believe that this will make it easier for investors to make comparisons between NEC and other companies, help us to gain a more accurate understanding of the state of operations within the Company, and be particularly effective in expediting efforts to improve profitability. Since taking office, I have made changes to the way NEC discloses information, including reorganizing the Company’s business segments into IT Services and Social Infrastructure and introducing the disclosure of non-GAAP profit. Both changes were implemented after receiving suggestions in my discussions with investors. Our aim is not just to disclose information in a way that is easy to understand but also to share management issues with our stakeholders and use this to improve the quality of management within the Company. I will continue to actively engage in dialogue and discussion with our stakeholders and will work to improve NEC’s corporate value while sincerely taking on board the content of these discussions. I would like to ask for your continued support and honest feedback.