

November 14, 2007

## **First-half Earnings Presentation Q&A**

### **<Overall Business Performance>**

**Q** How have your full-year forecasts changed from your initial projections? What negative factors at present, such as exchange rate movements as the yen has been appreciating, could affect your full-year forecasts going forward?

**A** NEC's first-half earnings exceeded our initial forecast. However, after reviewing NEC's overall performance and considering uncertainties in our business environment, we decided to leave our full-year forecasts unchanged. Although individual segments and business areas performed slightly better or worse than expected, we have left our forecasts unchanged. Furthermore, of the approximate ¥20 billion in company-wide strategic costs included in "Others/Eliminations etc.", ¥10 billion for which the use has been determined has been reallocated to the IT/Network Solutions business.

Regarding the impact of exchange rate fluctuations on operating results, there will be almost no impact as long as there are no large, short-term changes. This is because NEC's transactions are split almost equally between foreign currency-denominated exports and imports. We also hedge foreign exchange risk. But we are concerned that exchange rate movements may dampen IT investment by our customers and have other negative consequences for the actual economy.

**Q** How much in free cash flows is NEC forecasting for the full year?

**A** We are projecting free cash flows of ¥80 billion, as per our initial forecast.

### **<Segment Performance>**

#### **IT/Network Solutions Business**

**Q** What is your full-year sales forecast in the IT/Network Solutions business?

**A** We are projecting a year-on-year increase of approximately 4% in the IT/Network Solutions business. Breaking this down, we expect IT Services/SI (Systems Integration) to achieve around 4% growth, IT Platforms' sales to be almost unchanged year on year, Network Systems to post an increase of roughly 7%, and Social Infrastructure sales to be almost on a par with the previous fiscal year. While some businesses are performing slightly worse and others slightly better than expected, we have not revised our initial forecasts.

**Q** NEC is forecasting operating income of ¥164 billion in the IT/Network Solutions business. How has this changed from your initial forecast?

**A** Around ¥10 billion in company-wide strategic expenses, where specific measures have been determined have been reallocated from "Others/Eliminations etc." to this segment. Our forecast has changed by this amount.

**Q** How is this ¥10 billion split between the first half and second half?

**A** Almost all of this ¥10 billion is expected to be recognized in the second half of the current fiscal year.

**Q** Sales in IT Services/SI grew around 6% year on year. Is this because sales that you expected to record in the second half of the fiscal year were recorded in the first half?

**A** No, the early recording of sales was not a factor behind growth in IT Services/SI. Rather, in the first half we saw steady growth in most areas, including the finance sector and central government.

**Q** Was the improved profitability in IT Services/SI in the first half due to the sales growth? Or was it attributable to cost cutting? Also, what is your outlook for the full year for profitability?

**A** Profitability improved in the first half due to enhancement of SI development processes as well as cost reductions achieved mainly by reducing underperforming projects. We haven't changed our full-year

forecast on account of uncertainties and other considerations, but we are determined to continue first-half activities to achieve further improvement in the second half of the current fiscal year.

**Q** By roughly how much have you managed to reduce underperforming projects in monetary terms in IT Services/SI?

A Various initiatives such as stricter project management and pre-screening of orders have produced results and we have already seen a decrease in large underperforming projects. We will endeavor to achieve a further reduction this fiscal year.

**Q** Profitability in IT Platforms in the first half was below your initial forecast. NEC cited a transitional period concerning large projects as a factor for this. But didn't you know that would be the case from the start of the year? Also, what is the outlook for the second half? Is there a risk that you could underperform again as in the first half?

A To a certain extent we knew at the start of the fiscal year that there would be a transitional period for replacement for projects in the first half. We had hoped to make up for this to some degree by reducing costs, promoting sales and taking other steps. In the end, though, we didn't reach our target for the first half. However, we expect to achieve our initial target for the second half set at the start of the fiscal year based on expectations for a large mainframe project and several other projects. Furthermore, through a sales expansion drive and other actions in the second half we hope to make up for the first-half shortfall as much as possible.

**Q** How is Network Systems performing?

A Sales grew by roughly 6% year on year in the first half. The main reason for this growth was a strong performance in overseas business, including sales of PASOLINK, an ultra-compact, point-to-point microwave wireless access system used mainly for connecting base stations, as well as sales of submarine cable systems. Despite this sales growth, operating income declined year on year as strong investment by telecommunications carriers in preparation for the start of MNP, or

Mobile Number Portability, ran its course. The demand this capital investment created had a large bearing on results in the previous fiscal year.

**Q** You appear to be projecting higher earnings for the full year in Network Systems. What do you expect to lift earnings?

**A** Our plans call for lower sales of mobile communications infrastructure in Japan to be offset by higher sales of PASOLINK and submarine cable systems. PASOLINK sales are growing sharply, while demand is robust for submarine cable systems, particularly in Asia and Oceania. We are selecting and winning orders for prime projects only.

### **Mobile/Personal Solutions Business**

**Q** The Mobile/Personal Solutions business recorded interim operating income of ¥8.1 billion. How does this break down in terms of Mobile Terminals and Personal Solutions? Also, what is your forecast for the second half of the fiscal year?

**A** Mobile Terminals and Personal Solutions were both profitable in the first half. Mobile Terminals focused on the domestic business in the first half and also trimmed costs through greater efficiency in development. As a result, it achieved its goal of becoming profitable in the first half. However, we have not revised our full-year outlook for this business as the effect of changes to sales system-related subsidies at telecommunications carriers is difficult to gauge and due to other uncertain factors. We aim to at least break even in Mobile Terminals in the second half, however, because our current goal is to ensure full-year profitability in this business.

**Q** Mobile Terminals may have turned a profit in the first half, but it is still not producing the level of earnings seen at peer companies. The PC market is also good at the moment, yet this hasn't translated into large profits. How do you see NEC's present level of earnings in this context?

**A** The first-half performance of the Mobile/Personal Solutions business, which includes mobile handsets and PCs, exceeded NEC's forecast.

There has been no change to our full-year forecasts, however, because the difference from our initial forecast would be small, in the order of several billion yen. Also there are uncertainties in the direction of our markets and other factors in the second half. Given that second-half shipments of PCs in Japan are expected to be higher than in the first half, we would not be satisfied with merely breaking even in this business.

### <Others>

**Q** How is NGN-related business progressing? Will the lowering of NTT's FTTH subscriber target change the NGN-centered growth scenario?

**A** The NGN construction business recorded sales of about ¥90 billion in the past fiscal year. Our plan is to more than double these sales to approximately ¥200 billion in the current fiscal year. First-half sales were in line with our plans.

We see wide-ranging business opportunities related to NGN. Besides putting in place NGN infrastructure, there are opportunities such as in providing NGN-based services. Consequently, there has been no change in our stance toward the prospects for NGN.

**Q** The NGN construction business generated sales of approximately ¥80 billion in the first half as you initially planned. But what developments are expected in the second half in terms of the roll out of commercial NGN services?

**A** NTT plans to roll out a commercial service from March next year. Because of the start of actual services in some regions, higher investment is expected. Based on this and the efforts of our sales force, we are continuing to target sales of ¥200 billion for the full year.

**Q** From when do you expect NGN development costs to decline?

**A** Business opportunities in NGN-related business such as NGN-based services are expected to continue for some time. For this reason, rather than suddenly becoming unnecessary, we believe that development

costs will still be necessary to a certain extent.

**Q** There have been various reports in the media about NEC Electronics Corporation. What is your stance as regards your equity interest in this company?

**A** Basically, our policy has not changed as regards our equity interest.