**July 31, 2020**

**Earnings Presentation Q&A for Q1 of the Fiscal Year Ending March 31, 2021**

Date/Time: July 31, 2020, 16:30–17:30 JST
Location: NEC Headquarters Building, Tokyo
Presenter: Takayuki Morita, Representative Director, Senior Executive Vice President and CFO

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**Questioner A**

Q. Please talk about your evaluation of Q1 results compared to the initial plan. Although the full-year forecasts remain unchanged and there is a plan to increase profit, Q1 adjusted operating profit decreased by around ¥13 billion year-on-year. How will you recover from Q2 onward?

A. In Q1, the COVID-19 impact accounted for around ¥30.0 to ¥35.0 billion of the year-on-year decrease in revenue of around ¥60.0 to ¥70.0 billion. The other factors, which accounted for about half of the decrease, were expected, such as large projects and business PC-related factors. In terms of the operating profit, COVID-19 had a negative impact of around ¥17.0 billion, and the impact of losses due to lower utilization at Japan Aviation Electronics Industry, Ltd. and the Public Infrastructure was over ¥7 billion.

Regarding the full year, we had initially envisaged a negative impact from COVID-19 on our revenues of around 5% to 6%, or ¥150.0 to ¥180.0 billion and about ¥50.0 billion on operating profit. This view has not changed. We have stated that we planned to recover around half of this impact through cost control, and half through capturing new demand. In cost controls, we made efficiency gains of around ¥7.0 to ¥8.0 billion in Q1, and we believe it is possible to reduce costs over the
full year by around ¥25.0 to 30.0 billion. For the remaining half, we need to secure profits of around ¥20.0 to 25.0 billion from expanding sales of new solutions for the new normal and acquiring projects through the government’s supplementary budgets, etc. There are some areas of uncertainty, but we are making every effort to achieve those figures. Meanwhile, we are examining contingency measures for the risks involved in achieving this on a companywide basis, as demonstrated in the recent sale of shares of Showa Optronics Co., Ltd. By carrying out these measures, we believe we can achieve our forecasts for adjusted operating profit of ¥165.0 billion in FY2020 ending March 2021.

Q. With regard to 5G trends, you mentioned that you are aiming to attain a market share of around 20% through a capital alliance with NTT. What kind of contribution to profit increase are you expecting from international sales expansion over the coming two to three years? Also, so far you have collaborated with Samsung to promote RU. Will this partnership with NTT mean that NEC will promote CU? Could you talk about this together with your strategy for sales expansion outside of Japan?

A. Various aspects of 5G are unclear, including the timing. However, we will continue working on our goal of attaining a 20% share of the global market. The open RAN market is currently being formed, and we expect around 40% of the entire market to change to an open-related one from 2025 to 2030. This open-related market covers two areas: the all cloud native area as seen with the complete virtualization of Rakuten Mobile, and the area including dedicated hardware through joint development with NTT. Currently, we are receiving inquiries from all areas around the world, and we have been proceeding in business talks. So, we expect to be able to present the results related to open RAN in the near future. On the other hand, we expect trial projects to continue initially.

Our partnership with Samsung, joint development with NTT, and the
RCP concept by Rakuten Mobile each represent a different business model. Over the medium term, we are looking at using our joint development with NTT to provide open RAN, and high performance, highly reliable hardware and software as a set. In the RCP model, with the end-to-end provision by Rakuten Mobile, we will provide not only RU and the 5G core network, but also part of the OSS/BSS. We may also provide it in the form of network as a service. We will pioneer the global market for this kind of comprehensive model.

**Questioner B**

*Q. I would like to ask about the Global segment. What kind of factors have caused changes from the full-year forecast announced in May before the segment changes? Also, could you explain about the impact of market deterioration in Q1 performance, and how you plan to improve profits from Q2 onward?*

A. The changes in full-year forecasts are due to the reorganization of certain businesses. Also, the Q1 performance for the Global segment reflects downward pressure on operating profit from a significant impact of a deterioration in the display market. In addition, there have been delays in progress in the wireless solutions business and the organic area of Safer Cities, and we think this creates a risk of around ¥10.0 billion against the full-year forecast.

*Q. Could you tell us about the situation with KMD and NPS in the Safer Cities business?*

A. NPS is performing very solidly, and this fiscal year it is on track to perform as expected, or slightly better. KMD has seen a contraction in profits, which was factored into the initial forecast due to the expected winding up of some of its businesses. We have seen a slight impact from market deterioration; but we have a plan to recover, and the company is performing solidly, so we are not greatly concerned.
Q. Orders are declining sharply for Public Solutions and Enterprise segments. On the other hand, you have explained that there is no change in your earnings forecast. In achieving the sales plan for this fiscal year, when and how do you expect orders to turn positive again, given their current trend. Could you break it down by segment?

A. Regarding the recovery trend in earnings going forward, the first thing to note is that the backlog of orders in each area at the moment is basically maintaining the same level as last year. Therefore, we think that there is a risk to our sales going forward with regard to our order trend going forward. In the Public Solutions segment, we expect to incorporate the supplementary budgets, mainly in Q4. Demand from GIGA School has already started. Furthermore, in the Enterprise segment and also in the Public Solutions segment we have started to promote our new-normal solutions, including digital workplaces in Q1. Depending partly on the progress in Q2, we are planning to realize a certain scale in this business in the second half onward. However, in the Enterprise segment there are some sectors that have adverse conditions forecast, such as apparel, certain areas of logistics, and public transport. Therefore, we recognize there may be a risk of sales decreasing overall. Orders in the Public Infrastructure and Network Services segments have been strong and we expect them to increase continuously.

Q. The Public Infrastructure and Network Services segments continue to show a strong trend. Could you comment on your outlook for the Global segment, including your expectations for acquiring 5G projects in the U.K.?

A. Even if 5G projects in the U.K. and the U.S. do materialize in this fiscal year, they are only going to be trial projects, and we expect their
contribution to earnings to be small. We expect our submarine cable projects to be strong in this fiscal year. On the other hand, in the Public Infrastructure segment, we are expecting additional orders related to the supplementary budget, mainly for the central government. Second and third supplementary budgets are planned, and we are also making various proposals. With this in mind, we think that orders will materialize from Q3 onward, followed by sales in Q4.

**Questioner D**

Q. The 5G base-station related business appears to be seeing an increase in inquiries; but has there been any impact from COVID-19 on this? Also, in global markets there are moves to exclude a certain vendor. Will this assist NEC?

A. COVID-19 hasn’t had much of an impact on network related demand. Inquiry activity is picking up, and we are steadily advancing in Japan and international markets. Meanwhile, that certain vendor has been conducting business all over the world. Our view on this is that a lack of options in the telecommunications industry itself is driving demand for new options. There is a demand for an increase in providing vendors, such as Rakuten Mobile’s completely virtualized network running on cloud native and the O-RAN promoted by NTT and others. If O-RAN can spread in this way, then we think we will see our opportunities expand.

**Questioner E**

Q. Breaking down the factors behind the decrease in orders in Q1 results by segment, these seem to include a decrease in hardware, such as PC demand. If you have figures excluding the impact of hardware, could you share those?

A. The recent reorganization and change in reporting segment was carried out with the aim of providing everything to the customer,
including hardware. Therefore, I hope you will understand that we cannot present those figures.

**Q. Orders in the Public Solutions and Enterprise segments have fallen sharply. Is the decrease in PC demand that started last year a factor in this?**

A. The decline in PC demand from last year is a factor. In particular, with PCs we prepared new products for Q2, so we encountered difficulty in supplying products during Q1.

**Questioner F**

**Q. On page 15 of the financial results presentation materials, what is the year-on-year change in orders companywide?**

A. The year-on-year change companywide was a decrease of 5%.

**Q. How does the situation look for private-sector IT investment having bottomed out and now starting to build momentum again?**

A. We have seen some differences between sectors. In the financial sector and the telecommunications carriers, investment has been relatively solid. In the manufacturing sector, investment was curbed at quite an early point, but it looks as though the trend may have bottomed out in Q1 and will gradually improve from now. We think orders in the logistics and services sector will be the slowest to recover.

**Questioner G**

**Q. Based on your Q1 results, how has the impact of COVID-19 changed compared with three months ago?**

A. The impact from COVID-19 hasn’t really caused much of a deviation
from what we expected three months ago. Sales in Q1 decreased by around 10% year-on-year, considering the initial stage of people refraining from going out and that we are in a transition stage to a new normal, there is little change to our estimate of 5% to 6% risk to sales over the full year. There was a negative impact from COVID-19 in Q1 of ¥17.5 billion on operating profit, but around ¥7.0 billion of this was due to the impact of operation capacity issues, and by recovering operation capacity we expect to recover this over the full year. Assuming a risk to profit of between ¥40.0 and ¥50.0 billion over the full year, we believe we can eliminate this risk by taking various measures. Through cost control, we can make improvements of between ¥7.0 and ¥8.0 billion per quarter, which enables us to eliminate half of the risk. Also, by incorporating new business such as demand associated with the new normal, if we can secure a contribution to profit of between ¥20.0 and ¥30.0 billion, then we will be at the level where we can achieve our initial forecasts. The situation is still uncertain, but the impacts and countermeasures for them are becoming clearer now than they were three months ago, so we aim to continue to watch the situation through to the end of the first half.

Q. How has IT demand changed compared to three months ago? No doubt there has been some assistance from demand related to the new normal. But on the other hand, there is a growing sense that business conditions are slowing down. How has your outlook for the next three years or so changed compared to three months ago?

A. Compared to our previous views on IT investment, our view on DX investment has changed. We believe this is the most important area for companies to strengthen their competitive advantages. For this fiscal year, there may be a tendency to wait and see, looking carefully at scale and timing. From next fiscal year onward, our outlook is for solid growth in demand.