

Earnings Presentation Q&A for Q3 of the Fiscal Year
Ending March 31, 2021

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Location: Live audio streamed from NEC Headquarters, Tokyo

Presenter: Takayuki Morita, Representative Director, Senior Executive Vice President and CFO

Questioner A

Q: There were no changes to the full-year forecasts, but looking at progress in the respective segments, there have been significant changes. What are each of the segments going to do in Q4 to increase earnings?

A: In the Public Infrastructure Business, we believe we will achieve the annual forecast as IT system installations, including projects for central government ministries and agencies, and the GIGA school project, will be recorded in Q4. The Network Services Business started shipping Central Units (CU) for 5G base stations in large volumes around December last year. The forecast for Q4 is to be fully operational and to have growth through steady shipments related to 5G, so the Network Services Business is also projected to achieve forecast. The Enterprise Business has returned to a year-on-year increase in orders received since October last year, and sales began recovering compared to the previous fiscal year in December. However, this doesn't mean we can rest on our laurels. We believe that there are risks in the Global Business, but these are within a scope that can be managed throughout the whole NEC Group. The toughest will be the Public Solutions Business. Orders received have been gradually recovering each quarter, and sales from a project related to systems for hospitals and local governments are expected in Q4, so we believe there is a recovery trend.

Q: Am I correct in understanding that even if the Public Solutions Business fails to meet its goals, the Network Services Business is making good progress, so the Company as a whole will achieve its full year forecasts?

A: As of the end of Q3, we believe that our full year forecasts will be achieved as 9 months results was about ¥9.0 billion higher than our internal plan, though progress was different by segment. The likelihood of achieving targets is higher now than it was at the end of Q2.

Q: Does that mean that the situation has been gradually improving since December?

A: We have seen improvements every month since about October. We need to

be careful about the ongoing third wave of COVID-19, but as we learn how to manage COVID-19, we believe we can minimize its impact.

Questioner B

Q: In Q3, the impact of COVID-19 has been lessened to about half of what it was in Q2. Which is more settled, Japan or international markets?

A: From a profit aspect, cost-cutting has had a significant short-term effect on our international business, and in the midst of the COVID-19 pandemic, where sales have been tough, profits have rebounded and emerged positive. Added to that, there have been domains only marginally affected by COVID-19, such as the Submarine Systems business and software business for Service Provider, which have moved forward firmly as planned. Operating profit/loss in the Global Business in Q3 was almost unaffected by COVID-19, but we need to look carefully at the top-line impact from next fiscal year onward.

Meanwhile, domestically, cost-cutting has absorbed half the impact of COVID-19, but we predict it will take some time for the top line to bounce back. We are taking on all sorts of initiatives to meet New Normal demand and providing customers with unprecedented solutions, such as the case with airports in Hawaii. We will begin with demonstration testing, connecting this to results and then start contributing to financial results from next fiscal year.

Q: Please tell us about trends by business sector in the Enterprise Business environment.

A: Impact on the financial sector has been comparatively minor, and there is a tendency toward continued investment in modernization and digital transformation (DX).

In the manufacturing sector, investment was restrained at a very early stage, but the automotive and machinery manufacturing fields have picked up and projects that had been suspended or frozen have resumed.

The outlook for hotels, leisure and the like is uncertain as conditions remain severe for retail and transport. We expect restrained investment in transport-related areas to continue through next fiscal year and onward. On the other hand, there has been lively consideration for digital investment for the future in these areas.

Q: Has the increased investment in the financial and manufacturing sectors been in the DX area?

A: Much is DX-related. And among that, it has been for modernization of

existing systems with DX in mind. In short, there are an extremely large number of projects accompanying DX.

Q: How much impact has been made by the M&A of Avaloq Group AG, which will contribute to results from Q4? How do you view things like EBITDA?

A: About 70–80% of the Avaloq Group is solid business, so it has had relatively slight impact from COVID-19. It will contribute to results from Q4 of fiscal 2020, and we expect it to record 25% of its annual sales, about ¥15.0–16.0 billion, and 10% of adjusted operating profit. We are in the middle of PMI right now, and would like to secure EBITDA of about 20%. Since announcing the acquisition of Avaloq Group, we have received many inquiries from customers inside and outside of Japan. There is powerful interest in digitalization among customers from financial institutions, and we feel the wealth management field holds potential. We are taking action to generate synergies especially in Asia and Japan, where NEC has competitive capabilities.

Questioner C

Q: In regard to 5G, do you see that the U.K. is a link to the world as a base for global business expansion?

A: The U.K. government's stance and the relationship between the U.K. and Japanese governments are supportive for NEC, and we are able to take part in 5G verification in the U.K. in a good way. Four U.K. operators will take part simultaneously and verify things like connections. Normally, each company would act alone, but backing from both countries' governments has allowed it to move forward in this way, so we have great expectations. However, this is not just for the U.K., we also want to develop business in other areas, including Europe and the U.S.

Q: There are difficulties in the business environment in regard to 5G and submarine systems about economy and security, but what are your thoughts about geopolitical risks? What is the significance of forging ahead with these businesses from the standpoint of medium- to long-term profits and growth?

A: The submarine systems business contributes significantly to national security and global telecommunications networks need submarine cables systems. Networks, cables and logistics are key to developing the submarine cable systems, but few companies around the world possess all of these. In Asia, NEC is overwhelmingly strong. This market brings in a scale of around ¥200.0–250.0 billion per year, demand is expected to continue growing and we are confident of our competitive capabilities. We believe this business is sufficiently capable of maintaining a 30% global share and producing an adjusted operating profit margin exceeding 10%. We want to make a social

contribution that has global competitiveness.

Questioner D

Q: At Q2 financial announcement in October last year, you saw risks relating to operating profit of ¥150.0 billion, but can you tell us the latest full-year forecasts excluding asset sales?

A: When announcing the Q2 results, I said that we would need to add about ¥10.0 billion in the adjusted operating profit with demand related to New Normal, but at the moment, we outperformed our internal 9 month plan by ¥9.0 billion. During Q3 only, we believe we were able to add about ¥25.0 billion in footing due to orders received, full-scale shipments of 5G base stations, Global Business results and special countermeasures.

Q: Regarding the Global Business, adjusted operating profit made a significant turnaround to emerge positive in Q3. I'd heard until now that there was a risk of about ¥10.0 billion annually, so what changed and what business contributed to the improved profits?

A: There have been two positive factors. Profits have increased in the Service Provider business, particularly systems for operation management, billing, etc. by subsidiary NetCracker Technology Corporation, which has performed strongly until now and had especially high earnings in Q3. On top of that, profits have grown steadily in the submarine system business. However, the display business fell into the negative for the month of October before it was deconsolidated. The significant growth in Q3 was a positive and the sense of risk for the full year forecasts has improved slightly since the end of Q2, but we are still carefully considering matters such as the impact of COVID-19 internationally and investments for business expansion for the next fiscal year onward.

Q: Do you have any plans for additional measures such as structural reforms in Q4?

A: Looking ahead to the top line, we believe there is a necessity in some areas, such as optimizing the cost structure. To move forward in a better way from next fiscal year onward, we would like to take appropriate action while assessing conditions across the entire NEC Group.

Questioner E

Q: The Network Services Business performed strongly in Q3, with sales growing by ¥14.0–15.0 billion compared to Q2. Am I correct in understanding this is due to growth in 5G base stations? And will you aim for an even higher level in Q4 compared to Q3?

A: Yes. Central units (CU) for 5G base stations contributed, in addition to radio units (RU). We expect Q4 to be at a similar level as Q3 and for that strong performance to continue through the next fiscal year.

Q: Regarding the improvement of earnings in the Global Business, there was the positive surprise in Q3 of an increase in adjusted operating profits of ¥10.9 billion year on year. Will this improving trend continue?

A: In adjusted operating profit for Q3, profits were ¥2.0 billion for Safer Cities, ¥6.0 billion for Service Provider and ¥3.0 billion for the Submarine Systems. On the other hand, there were minor losses in the Wireless Backhaul, Display and Energy businesses. Recording a profit of about ¥2.0 billion for the sale of the Display business was a one-off factor in Q3.

There were some major projects in Q3, but we were able to secure solid profitability in Service Provider and Submarine Systems business as well as manage unprofitable businesses.

Questioner F

Q: NEC is a corporate sponsor of the Tokyo Olympic and Paralympic Games, and according to opinion polls and such, concerns are being raised about them being held in July. Do you see the Games being held at all? Is the Company receiving sufficient benefits for being a corporate sponsor?

A: There is still hope for holding the Olympics and Paralympics under safe conditions, and we are cooperating as best we can. As a corporate sponsor, we are involved in the technologies and system developments connected to the safe and secure hosting of the events, such as security, remote services and measures to control the spread of disease, so we believe there are benefits in terms of technology progress and business development.

Questioner G

Q: Are there any plans to post one-off profits in Q4?

A: We are not planning to record profits from special countermeasures in Q4.

Q: Regarding the figures outlining the impact of the spread of COVID-19 on page 18 of the presentation materials, why are there gradual reductions in cost-cutting and capturing New Normal demand? Furthermore, if you're considering negative impacts will carry over into next fiscal year, there are concerns that the New Normal demand you are able to capture may not fully counteract it, but what's your outlook?

A: Strict management will be applied to cost-cutting, aiming for a reduction of about ¥20.0 billion, excluding the scaling back businesses. Moreover, as sales have increased more than expected in the Public Infrastructure and Network Services Businesses, there has also been an increase in selling expenses in line with the increased sales.

Regarding capturing New Normal demand, we are not including PCs required for simple remote work. The increase in demand includes, for example, countermeasures for infection, enhancement of network environments for remote work and business related to education in response to COVID-19. There was a gradual recovery in profits on an essential business basis that excluded special factors in Q1 and Q2 and an increase in profits year on year in Q3. We believe that we have been able to build a sound business structure against the COVID-19 pandemic.