# Q&A Regarding Financial Results for the Fiscal Year Ended March 31, 2023

Date/Time: April 28, 2023 16:00-17:00 JST
Location: Live audio streamed from NEC Headquarters, Tokyo
Presenter: Takayuki Morita, President and CEO (Representative Director)
Osamu Fujikawa, Executive Vice President and CFO (Representative Director)

**Questioner A**

*Q:*

*Results for FY23/3 significantly outperformed the Company's previous forecast announced in January. What was the positive factor there? Also, what are your thoughts regarding continuity going forward?*

A:

The domestic IT business performed strongly. Orders for IT services in FY23/3 increased 9% year on year, with an increase of 7% in the fourth quarter by itself. The backlog of orders at the start of FY24/3 was also up from the previous year, and there is no sense of business conditions having deteriorated at this point. When consulting with our customers, for example, they are not talking about curbing investment. However, our forecast for FY24/3 is a conservative one, as we are mindful of macroeconomic risks.

*Q:*

*Adjusted operating profit for the Enterprise segment in particular was higher than company forecasts. Could you explain the factors behind this?*

A:

In addition to expansion in sales, results were buoyed by our efforts to increase profitability, such as productivity and quality improvements in the system integration (SI) business. Orders also recovered swiftly from drops caused by COVID-19 and remained brisk. We also won large orders in businesses for finance and retail/services in FY23/3.

*Q:*

*What is the status of your business for SMEs?*

A:

In addition to raising the prices of common products such as servers in January, fourth quarter shipments increased, which contributed to an increase in profit.

*Q:*
*Earnings in the Network Services Business were lower than Company forecasts for FY23/3. However, in your plan for FY24/3, you expect to see operating profit increase by ¥17.9 billion year on year. What are the factors that will drive this significant improvement in earnings?*
A:
In FY23/3 we recorded around ¥17.0 billion in one-off costs, such as strategic projects for 5G business abroad and streamlining of assets, which will not be recorded in FY24/3. In addition, we expect a dramatic improvement in profit and loss for FY24/3 through appropriate control of strategic expenses and optimizing the cost structure of 5G business abroad.

**Questioner B**

*Q:*
*Please explain the forecast for the 5G business both inside and outside of Japan.*
A:
Sales for 5G business abroad were around ¥10.0 billion in FY23/3. In FY24/3, we are expecting this to nearly double. In Japan, sales are expected to decrease, partly due to the impact of investment restraint among telecom carriers. For the 5G business overall, sales in FY24/3 are expected to be about level with that of FY23/3 at ¥85.0 billion.
*Q:*
*For the Network Services Business overall, you are forecasting sales growth for FY24/3. In which areas will sales grow?*
A:
We are planning for sales growth in fixed wired networks and IT services.
*Q:*
*The Tokyo Stock Exchange requires listed companies whose PBR falls below one to formulate and disclose improvement measures. What kind of response are you planning to make?*
A:
We are always discussing how we can increase our value in the capital markets, regardless of whether there is a request or not. We recognize that a PBR lower than one means that the market evaluates the company as being unable to produce earnings that exceed the cost of capital. Once the viability of achieving our earnings forecast for FY24/3 and the Mid-term Management Plan becomes apparent, I think that we can expect an appropriate evaluation from the market. From FY24/3, we change our reportable segments, and it will be important to provide clearer explanations to

stakeholders and to continue faithfully to deliver on our promises by doing what we say we will. Business opportunities for NEC are abundant, and we believe that we should be increasing corporate value through active investment.

**Questioner C**

*Q:*

*The gap between the current state and the FY26/3 targets for core digital transformation (DX) and global 5G under the Mid-term Management Plan seems rather large. How do you plan to achieve growth going forward?*

A:

The target market for core DX is the entire IT market in Japan. NEC has set a target of expanding sales in the domestic IT business from ¥1.3 trillion in FY21/3 to ¥1.6 trillion in FY26/3. Important points include how much we can provide the NEC Digital Platform, which is our common platform, and how many large projects we can capture through consulting in conjunction with subsidiary ABeam Consulting, Ltd. Moreover, we aim to capture new business opportunities by expanding digital IDs and modernization that utilize biometric authentication technologies and so forth, as well as managed services by NEC Security, Ltd., which was launched in April.

Despite market changes and heavy competition in the global 5G business, the trend toward openness and virtualization means the convergence of IT and networks will accelerate, and the importance of software will increase even further in the future. Internationally, we will leverage the strengths of NEC's subsidiary Netcracker Technology Corporation's high value-added network optimization and automation software products to drive business expansion with a focus on the software/services domain abroad. In Japan, we will shift our emphases to the software/services domain, mainly using the unrivalled capabilities of NEC's 5G core networks.

*Q:*

*Could you tell us about your initiatives on underperforming businesses?*

A:

At the start of the Mid-term Management Plan in FY21/3, there were 16 underperforming businesses that did not meet the set hurdle rate of an operating margin of 7%. Through intensive monitoring and improvement measures carried out under the supervision of top management, four of the businesses have cleared the 7% hurdle rate for two consecutive years—one in the Public Solutions Business, two in the Enterprise Business, and one in the Global Business. These will no longer be monitored from FY24/3. Aside from these, some of the other underperforming businesses are currently just one step away from clearing the hurdle rate.

For FY26/3, we believe that underperforming businesses will need an operating margin of at least 7%, and more than 10% for the company overall. We will map our pathway to achieve this and execute measures, but if we find it difficult to achieve both qualitative and quantitative targets, then we will take actions from an early stage. For example, in FY23/3, we transferred the stock of NEC Embedded Products, Ltd., and we will continue to take swift and appropriate action as necessary.

**Questioner D**

*Q:*

*Has there been any change in attitudes of telecom carriers abroad towards Open-RAN? With macroeconomic conditions becoming more adverse, how do you see capital investment trends among telecom carriers going forward?*

A:

Telecom carriers abroad are becoming more cautious regarding costs and investment, partly due to energy issues. However, we feel that willingness to implement new technologies such as Open-RAN remains high. We are making progress with verifications for the implementation of Open-RAN, however, large-scale commercial deployment will take time. In addition to the cost aspect, power consumption remains an issue for Open-RAN technology when compared to existing single-vendor proprietary solutions abroad, which has also discouraged telecom carriers' investment. To address this, we plan to proceed with the adoption of new semiconductor chips and design changes. Our policy is to proceed with the 5G business by carefully assessing technology and cost-performance aspects while emphasizing profitability.

*Q:*

*Why did the profit of Global Business increase significantly year-on-year in the fourth quarter in FY23/3? Also, what is the reason for your forecast of lower sales and higher profits in your plan for FY24/3?*

A:

In the fourth quarter, there was a contribution to higher profits from Netcracker and the submarine systems business, among others. In FY24/3, we are planning on increased profit following growth in sales of Digital Government/Digital Finance (DGDF). Netcracker and the submarine systems business both have strong global competitive advantages and are expected to continue growth going forward.

**Questioner E**

*Q:*

*Following Rakuten Symphony, NTT DOCOMO also announced a new brand, OREX, as a service platform for international 5G. What kind of relationship will NEC have with these kinds of partners?*

A:

For NEC, the ability to compete in foreign markets with partners such as Rakuten Symphony and NTT DOCOMO is extremely encouraging. However, it will take time for large-scale commercial projects to produce results, and their contributions to earnings in FY24/3 is expected to be minor.

**Questioner F**

*Q:*

*The adjustment for FY24/3 is forecast at ¥78.0 billion, an increase of ¥18.5 billion from FY23/3. What are the factors behind this forecast?*

A:

We are planning to increase expenses by approximately ¥10.0 billion for internal business infrastructure upgrades and investments for the future. Also, for the past two years, we have recorded intellectual property income, and plan to strengthen activities so that we can regularly generate such profit.