

NEC IR Day 2024 IT Services Business Q&A

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Presenters: IT Services Business:
Kazuhiro Sakai, Corporate Senior Executive Vice President and Co-COO
(Executive Officer)
BluStellar:
Toshifumi Yoshizaki, Corporate Senior Executive Vice President and CDO
(Executive Officer)
DGDF (Digital Government / Digital Finance):
Tomoki Kubo, Corporate Senior Vice President (Executive Officer) and
President of DGDF Business Unit

Questioner A

Q:

Could you please discuss the share of BluStellar and hardware within the IT Services Business? Additionally, is hardware included in BluStellar?

A:

The IT Services Business is forecast to generate ¥2 trillion of revenue in FY26/3. Of this amount, domestic IT revenue is forecast to be ¥1.69 trillion. Hardware is projected to account for around one-third of the total, while software and services are projected to account for around two-thirds. In addition, hardware is not included in BluStellar. BluStellar is expected to contribute ¥428.8 billion to domestic IT revenue.

Questioner B

Q:

Does your conservative outlook for BluStellar restrict the growth rate to this level? If BluStellar can achieve even higher profitability, I believe that this will drive the IT Services Business' profitability as a whole.

A:

BluStellar is now on a growth trajectory as a result of reforms undertaken over the past five years. Additionally, BluStellar's adjusted operating margin forecast of 11.4% in FY26/3 is still in progress. We are confident that BluStellar's profitability can be increased further by shifting to high-margin products, creating offerings, and standardizing platforms. Given that the current profit targets for domestic IT services are not particularly high, we aim to make further improvements. The profitability levels are low due to differences in the profitability of hardware and SI services. Although we have no intention of leaving the hardware business, we must carefully consider how we will transform hardware into high-

margin products, and look closely at the parts of our portfolio that should be revised. Therefore, we believe that in the next Mid-Term Management Plan, we should organize and tackle these issues, conduct benchmarking, and aim to achieve high standards, even within the IT industry.

Questioner C

Q:

Will NEC be able to take the lead in controlling the profit improvement measures for BluStellar products? Could you please discuss whether there is any possibility of exceeding your forecast?

A:

Because the profitability improvement measures include controlling development expenses and other costs, NEC's self-reliant efforts can accomplish many things. We will also reduce the cost ratio by shifting from man-hour pricing to added-value pricing, in addition to improving automation and productivity through modeling and pattern recognition. Currently, we believe that our targets are sufficiently achievable.

Q:

Would it be correct to assume that as customers' infrastructure shifts to SaaS and cloud, you will naturally achieve your target ratios for BluStellar and offerings?

A:

It is inconceivable that all customers who are currently operating legacy infrastructure will continue to do so. Therefore, we expect that the ratio for these customers will continue to rise. Furthermore, we will work to boost efficiency by actively deploying AI to in-house SI processes. We have found that productivity will increase by 20% to 30% depending on the process. There are also cost improvement benefits, and these efforts can lead to increases in prices per project. We are confident that there is scope to make significant improvements and that our processes will undergo major changes.

Questioner D

Q:

The profit level of BluStellar products is equivalent to that of domestic IT services overall. While BluStellar products are a growth driver, the plan does not seem capable of raising the overall profit level of domestic IT services. Is this because the products are still in the development stage? Could you please also discuss your level of investment in BluStellar?

A:

Because BluStellar includes investment, it initially posted a loss in FY22/3 when its revenue was low. The period until 2022 was an investment phase. In this phase, efforts were made to build a common platform and establish offerings. In FY24/3 and beyond, we have continued to make investments while growing revenue and transitioning to an investment recovery

phase. We are investing roughly the same amount every year, so our cost ratio will decrease as revenue increases, and profitability will continue to increase even further. Furthermore, BluStellar's high-margin offerings still account for only around half of the portfolio, and we have the potential to grow that share to 60% to 70% of the portfolio.

Questioner E

Q:

Around what share of projects are man-hour-priced projects? How specifically do you set the price of value-priced projects?

A:

The share of business negotiations for value-priced projects remains low. However, this share, which was nearly non-existent a few years ago, is now approaching 20%. For man-hour pricing projects, pricing is based on the number of people working each month. In contrast, value-priced projects are priced using two methods: one based on the value of the delivered project and the other based on the economic gain for the customer. The latter method is more complex and still has a low share, although cases using the former method have been gradually increasing.

As NEC's SI productivity improves, man-hours and costs will both decrease. If projects are priced based on value delivered, revenue will remain stable and not decrease. Part of the cost reduction can contribute to our profit, and if part of the remaining cost reduction is returned to the customer, both parties will benefit. This will enhance our market competitiveness and expand our target markets, allowing us to increase our profits.

Furthermore, revenue will grow as work volume per person increases. Modeling is crucial for improving productivity and is a measure that will enable us to focus on improving profitability.

Q:

Could you please discuss the composition ratio and targets of service-type businesses providing cloud and SaaS services that can generate recurring revenue and high profitability?

A:

I believe that around 40% of our high-margin products are in cloud-related domains. We expect that further progress on the adoption of cloud services by customers will provide us with an opportunity to increase our overall profitability.

Questioner F

Q:

In FY26/3, the adjusted operating margin is forecast to be 10.9% for domestic IT services and 11.6% for international IT services. International IT services are thus expected to be more profitable. Is this because international IT services are highly profitable due to their specialization in SaaS, whereas domestic IT services have a low adjusted operating profit

margin as a result of BluStellar's substantial development investment burden? Additionally, will you expand BluStellar internationally?

A:

International IT services do not include any hardware, while domestic IT services include hardware. Excluding hardware, domestic IT services have higher profitability than international IT services.

With international IT services, we are working under a policy of concentrating more on SaaS-type business, as part of efforts to streamline operations. That said, international IT services are profitable not simply because of their status as a SaaS-type business. By increasing the efficiency of infrastructure and operations, we aim to go beyond 12% and achieve an even higher level of profitability.

In addition, we are considering expanding BluStellar internationally. We are currently focusing on the domestic market due to the high growth rate in Japan. However, it is common for products and services to cross national borders, which is why we are exploring the possibility of growing BluStellar through global expansion.

Questioner G

Q:

The profitability of BluStellar products has improved significantly over the last three years. Will this improvement trend continue in 2025 and beyond?

A:

In the future, we believe that we will make significant progress in improving SI man-hours through the use of AI. ABeam Consulting Ltd. conducts highly profitable consulting globally, primarily in Asia and Europe. Therefore, we see potential for growth, including possible synergies with ABeam Consulting.