Question & Answer

Questioner 1

Q&A Session 1

Q: I would like to ask three questions. First are orders in North America. You explained that there has been a slight delay in investment decisions, but if we calculate Q2, we see that orders have decreased by about 20% on a local currency basis.

I understand that you are saying that quality is better than quantity and that you do not pursue quantity unnecessarily, but how much uncertainty has emerged in terms of changes from three months ago, and whether this situation will continue in the future or whether the negative margin will shrink in Q3 and Q4 now that we have some more projects in sight. Could you give us your outlook for this?

A: As we have already explained, wining of orders in the North American market has been delayed due to the uncertainties in the market and the somewhat cautious approach of companies to investment.

We had a large project in Q1 that was pushed back to July, and although we received the order for that item, the order for the item scheduled for Q2 has been pushed back, so we are still behind schedule.

In North America, we place great importance on profit margins and purposely forego orders with low profit margins. Still, regarding the actual orders we have received, there has been an increase in consulting and digitalization projects with gross margins exceeding 30%. As for the pipeline, I mentioned in the previous Q1 that we have a solid pipeline, which is still quite strong at this stage. At this stage, we are continuing to accumulate a considerable amount of money.

Therefore, there is a delay due to the uncertain market conditions, but this does not mean that we are completely out of the orders, and we will continue to hold on to what we can get in the pipeline and keep it under control. We believe that there is a possibility of recovery if market conditions return to normal.

However, regarding the Q3 and Q4, we are confident that we will achieve this in the medium to long term, as we have a pipeline. We are determined to do our best and strengthen sales force and other various measures, but the situation may continue to be challenging.

Q: So, the pipeline itself is not gone, but because of delays in decision-making, there is a delay in orders, so there are some delays compared to the plan for the full year, but how much can you recover from that and how much can you reduce the downturn in terms of profitability, is that how you see the progress as of H1 of the fiscal year?

A: Yes, that's right. We still experience a periodic lag. Compared to last year, the pipeline for system renewal projects that we have undertaken has increased by approximately 50% YoY. In addition, several large projects are expected to be awarded. Moreover, the pipeline for projects in which we have a very high probability of receiving orders has increased by about 20%, so although it is a challenging target, we are working to achieve it in H2 of the fiscal year.

Q&A Session 2

Q: The second point is on page 23 of the investment and financial strategy mentioned earlier. You mentioned the refinancing to fixed interest rates in the lower part of the page and the use of yen carry. You mentioned the specific scope of application on a yen basis, but it seems that the coverage ratio is still not that large in terms of the total debt.

I wonder if you could comment on how long it will take to increase the coverage rate, or how you will implement these two measures toward that final goal, to the extent possible at this time.

A: First, let me explain a little more about these two measures. As you can see on page 23 of the company presentation material, the one refinanced to a fixed rate is a variable rate that was converted to a fixed rate. The interest rate has been reduced by approximately 1%. Since we started this in July, it has reduced interest expenses by about JPY1 billion or so in FY2023.

The effect of interest rate reduction on yen carry is approximately 5%. This measure has the effect of reducing interest by about JPY2.5 billion this fiscal year or about JPY5 billion for the full year.

We will continue to consider how much of this kind of mechanism should be introduced while keeping a close eye on the situation. We would like to receive many opinions from our shareholders and investors while we continue to consider the best balance between saving actual cash flow and taking foreign exchange risk in the case of yen carry; in addition, we further review various issues.

Q&A Session 3

Q: The third and final point is the domestic business. In the Public and Social Infrastructure area, you explained that profits increased in H1 due to eliminating unprofitable projects. Still, the profit level did not change much between Q1 and Q2. Could you please explain this?

A: First, in the Q2 results, we recorded a loss of JPY3.8 billion in an unprofitable project in the Public and Social Infrastructure area. I think the profit margin reflects that. We posted a loss of JPY5.8 billion in unprofitable projects on a consolidated basis.

Q: So, I think you were saying that some additional funds were added in Q4 of last fiscal year and that the final cutover would probably be at the end of September, but now that the final cutover has been made, is it my understanding that this is the end?

A: The unprofitability that we have been discussing up until now has been the unprofitability of the development process. This time, we are seeing these things in the operating phase. However, we believe that we have made a sufficient estimate of the amount in the maintenance flow in the operating and maintenance phase, so we are working on the situation at this time with the hope that we can finish the process here.

M: I understand. Thank you very much. That is all.

Questioner 2

Q&A Session 1

Q: I would like to ask you about two major points. I think you gave us the figures for H1 for integration expenses and restructuring expenses, but I would like to know how much of these expenses were incurred in each segment in Q2.

A: As for the JPY3.4 billion for the integration in H1, the breakdown is JPY2.7 billion for EMEA and LATAM, the other half for North America and NTT Ltd., approximately JPY0.3 billion each.

A: JPY7 billion for structural reforms in EMEA and LATAM, of which JPY4.3 billion is planned to be spent during the year. Also, JPY9.2 billion out of the annual forecast of JPY19 billion has been spent in NTT Ltd.

Q: Next, about the progress in the disbursement of integration expenses, I think we have made progress of JPY3.4 billion in H1 against the annual plan of JPY19 billion. Looking at the progress rate alone, I think this number appears low, but I would like to know if this is just an assumed line or if there are any factors that may inhibit any cost expenditures.

A: Integration costs only amounted to JPY3.4 billion in H1, against an estimate of JPY19 billion for the full year. It was only JPY3 billion in Q1, and so we have posted only JPY400 million in the three months period of Q2. As stated in the presentation material, we promoted measures to strengthen sales collaboration in each global region and the integration of office corporations in the EMEA region.

Regarding the overall flow of activities, we are currently working toward the establishment of a system for new business operations in April, 2024. The members of the new system were decided in July, and the announcement was made in October. Now, the leaders of each region are taking responsibility for the formation of their respective regions.

To summarize, we plan to contribute JPY19 billion annually. However, we believe there is a strong possibility of higher expenses than the level of H1 of the current fiscal year.

As for the actual costs, the main items include how to establish a financial reporting process for the new unit that will start in April, how to create an IT environment to support this process, and how to proceed with the integration of offices at each of the major bases, the items required for such integration have all been submitted by each region and division. Therefore, I do not believe this expense will stop being paid out as content.

However, when the expenses are divided by fiscal year, it may happen that some will be paid out during the current fiscal year and some will be extended to next year, but we plan this expense to be contributed to the fund.

Q&A Session 2

Q: One last point. I would like to know your view on the North American margin. Even if you add back the several hundred million yen for the integration expenses, I think the EBITDA margin is trending slightly downward, so I would like to know the background.

As you mentioned at the beginning, I think it is because we have continued to focus on quality. Still, I would like to know if any factors are worsening the margin here as well, and whether it will recover in the future, and if so, what your outlook is.

A: In North America, there was a one-time gain in the previous fiscal year, leading to a decline of approximately JPY2.5 billion in the current fiscal year. In terms of the projects to be awarded, we are conscious of profit margins, so we have been foregoing projects with low-profit margins or not going for the next one, so sales themselves have declined slightly. Still, I hope you understand that the profit margin itself has not declined.

M: I understand.

Questioner 3

Q&A Session 1

Q: The first point is the financial cost. I would like to confirm the structure on page 23 of the company presentation material again. I understand that NTT Finance basically represents the financing of the NTT Group. Is NTT Finance not lending directly to NTT Ltd. but rather through NTT DATA Group Corporation, a holding company? I would like to ask you to confirm where the foreign exchange risk will come from.

A: Until now, for data center loans in foreign currencies, it has been common for NTT Finance to lend directly to NTT Ltd.

As just mentioned, in this scheme, we, NTT DATA Group Corporation, will first borrow from NTT Finance The loan is then sub-loaned to NTT Ltd., and the loan is made in US dollars. Therefore, NTT DATA Group Corporation will bear the foreign exchange risk.

Q: What is the reason for such a scheme? If you loan directly to NTT Ltd. from NTT Finance, I don't think the foreign exchange risk is looked at that severely. If it is a business company and the exchange rate risk is on the scale of your company, I think some people may not like it. Is there a reason for the change?

A: The simple answer is that we want to control the exchange risk ourselves. If we take it as NTT Ltd., as we are taking on the risk in terms of currency valuation, we have to think about how much, when and what to do. We are also thinking about how to control it.

Therefore, in the end, we are looking at what kind of P&L and balance sheet we will have on a consolidated basis for the NTT DATA Group and considering where we can best control this. That is separate from the fact that we do not see any issues with taking risks with the NTT DATA Group.

Q: At the time of financing at NTT Finance, do you have any thoughts of rolling over in US dollars?

A: In the end, if we borrow in yen and lend in US dollars, in the case of a normal loan, the P&L will be hit first, and that portion will damage our net assets.

There is a proposal that NTT Finance takes a foreign exchange risk, but we think it would be better to use NTT DATA Group since we have more capacity in terms of net assets; thus, we are proceeding with our decision.

Q: I would like to ask a little more about the yen carry. President of NTT mentioned that there is an effect of 5% more yen carry at the NTT IR Day. The fact that USD650 million was converted in one month suggests that the conversion pace is quite fast. Was this only in October, and has it stopped since November?

You mentioned earlier that you are listening to various opinions, but how are you starting to control financial expenses in the end? As shown in the PL, financial expenses for H1 of the fiscal year are just under JPY38 billion, but I think some of this will increase due to new debt. How large do you want the JPY38 billion to be, and what is your basic policy regarding new borrowing? What do you consider to be the default procurement method for new debt issuance and borrowing?

A: In October, we refinanced USD650 million of loans into yen. For this fiscal year, we have not done anything to be implemented after that so far. As of now, this is all we have done.

A: Additionally, the basic concept of new debt is that we would like to determine it according to what the asset side is like, but if we assume that there will be no long-term holding or off-balancing for the time being and considering that it will take several years from the actual construction until the facility is ready, we would like to start with a fixed rate of return, thus, the fixed rate is the basic approach.

As for the level of financing costs, this is still under consideration, and I do not have a clear idea of what level we aim towards. As mentioned earlier, we are going to consider and decide on the balance between saving cash and taking foreign exchange risks.

Q&A Session 2

Q: Secondly, it has been one year since the integration of NTT Ltd. and is the current pace in line with the plan? How many milestones are you at now, and where are you trying to target to settle the integration to some extent? I would like to confirm the integration costs for the next fiscal year and beyond and where structural reform costs may be involved, but I would like to know where they will peak and decrease.

A: We are working on various initiatives that we believe are important in preparation for the integration of the former NTT DATA group and the NTT Ltd. group from April next year. In terms of costs, there will be office consolidation, the cost of developing an IT environment, and so on. We expect integration costs to peak in FY2024.

Regarding synergies from the integration, we expect to generate 30 billion yen in synergies in FY2025 from an increase in operating income due to higher sales.

Looking at NTT Ltd.'s income and expenditure on a non-consolidated basis, I feel that we are moving toward an improvement trend as a whole. Therefore, I think we need to accelerate this trend further.

M: I understand.

Questioner 4

Q&A Session 1

Participant [Q]: The first question is on North America. I would like to know a little bit more about the nature of the decrease in orders this time. I think the impact on recurring revenue will vary depending on whether there is a decrease in systems development or IT outsourcing.

Looking at the industry as a whole, I get the impression that many of your competitors are seeing a large decrease in orders for IT outsourcing that leads to recurring revenue, so could you please tell us qualitatively where your company's 20% decrease in orders on a local currency basis is coming from?

A: If you look at Q2, there was a decrease in ITO and system development.

Q: With the decline in recurring income and interest rates rising beyond the end of March this year, I think the risk of impairment has increased. If there is anything you can comment on, please share your thoughts on your company's direction in this area.

A: The fact that interest rates are rising means that inflation is rising, so I think one of the key points for each project is whether or not we can pass on the cost to customers in the form of prices, etc., and whether or not we are earning a proper return on our investment. As far as we have heard, there are some cases where there are no issues, and the gross profit margin and actual profit of projects are solid, so qualitatively speaking, I am aware that there are no such issues.

Q&A Session 2

Q: The second major point is related to NTT Ltd. Since your company has been consolidated from H2 of last year, I think we can see the movement of the same period last year in your company. Still, as far as this sense of level in H1 is concerned, it appears that the EBITDA forecast for H2 is quite a bit less simple.

What I would like to ask you is, first of all, what kind of progress has been made in terms of profit and loss for H2 against the full-year plan. Secondly, regarding demand for data centers, I think the actual situation is still favorable because, excluding the impact of the transfer of operations, there has been an increase of billions of yen. Since you mentioned earlier that the situation in North America is difficult, could you give us your final comments on sales and EBITA?

A: First of all, I would like to show you the status of EBITDA for Limited. H1 of this fiscal year was consolidated from the current fiscal year, so we are only showing EBITDA of JPY25.6 billion. Still, the level of EBITDA of NTT Ltd. in the previous fiscal year was before consolidation, and compared to that, H1 of this fiscal year showed an increase of JPY12.4 billion YoY.

An EBITDA of JPY53.4 billion is required in H2 to reach the forecast of JPY79 billion, which represents an increase of JPY13.6 billion YoY. Therefore, I would not go so far as to say that the achievement of the plan is easy, but we believe that the level of increase from JPY12.4 billion in H1 to JPY13.6 billion in H2 is sufficiently high to achieve the plan.

In terms of each of our businesses, we are missing the Hong Kong and China businesses from NTT Ltd., which used to be included in the count in the previous fiscal year. Considering the impact of the data center business transfer to Hong Kong, which amounted to approximately JPY13 billion, sales for H1 actually increased by approximately JPY13 billion YoY.

As mentioned earlier, IT demand in North America is very conservative. Still, in the data center business, demand for orders is extremely high, and we are proceeding at full capacity to meet clients' needs. In this regard, we are not worried about the data center business.

Q: Thank you very much. If you have the figures, could you provide us with the amount of the effect of the exchange rate boost on sales in NTT Ltd.?

A: The foreign exchange effect was JPY27 billion in H1.

M: I understand.

Questioner 5

Q&A Session 1

Q: I would like to ask you three quick questions. The first point is regarding the unprofitability. Please tell us about the JPY3.8 billion out of the JPY5.8 billion. Is this for one project, and where did the other JPY2 billion come from, and what is the outlook for the future?

A: The JPY5.8 billion mentioned earlier, JPY3.8 billion, is the loss recorded by one company. Other than that, there are a little loss in Japan and some losses in overseas projects. Basically, there are no major losses, but several hundred-million-yen losses.

Q: The remaining JPY2 billion, there is a really small amount in Japan, and then overseas, which is this?

A: Overseas, both companies in North America and Europe are experiencing some expenses.

As for unprofitable business, there are some items that we will take on as a challenge to some extent, so we expect a certain amount to be generated. We will try to control the overall amount.

Q: I see. In relation to the Zengin-Net case, do you have any cost pressure factors factored in here, or do you have any forecasts for H2?

A: We are currently working together with Zengin-Net to confirm the measures to be taken to deal with the situation in earnest and to dig deeper to prevent a recurrence. First, we will prioritize this, and then we will discuss the matter with Zengin-Net. At this point, there is nothing we can say for sure about the impact on our business performance for the current fiscal year.

Q&A Session 2

Q: Secondly, you mentioned that the EBITDA margin in North America has been declining and that it was a one-time profit last year, and in Q2 it was 5.3%, down from 6.4%. Could you please reiterate this point again?

A: Regarding North America, as pointed out, there was a transient in Q2 of last fiscal year. If we look only at the Q2 accounting period, you are right, but we are now working to improve profits for the entire year in North America. We expect to see an improvement for H2.

Q: Thank you very much. In H2, the profit margin on the pipeline projects themselves is good, so I am not sure if the overall profit will improve once the top line comes out, but is it correct to say that a recovery trend can be seen?

A: Yes.

Q&A Session 3

Q: The third and final point is that large orders have been received from central government agencies in Japan. I think some types of orders will not increase revenues because of renewal projects, while some new orders will really expand.

A: Large orders are for renewal projects. So, I think we will be able to land the order in a way that we can calculate to some extent, as we have been working on it as an existing project.

Q: As for new orders, there may be an increase in revenue in the future, but it will not be large, or is it not something that will have a positive impact on business performance?

A: It is a large project that will significantly affect our business performance, and, it will affect not only this year but also next year and beyond.

Q: Is this an integrated service, or is it a SI rather than the old data communication service, and can it be considered a project that will have an effect on sales and increase revenues for two or three years?

A: Yes, that's right. This is a very large project for SI, so it is a project that will increase sales in the next few years.

M: I understand.

Questioner 6

Q&A Session 1

Q: I would like to ask a question. I would like to ask you about the tax rate. I think that NTT Ltd. was affected by the deficit, but the tax rate in Q1 was about 45%, but in Q2, the tax rate worsened further to 47% or 48%. Including H2, how much should we expect the tax rate to be? Also, if the Company will be profitable in the next fiscal year, I would like to know how you see the tax rate in the future.

A: Regarding the tax rate, it is difficult to foresee. As you pointed out, in Q2, some of our limited subsidiaries are in the red. They cannot be expected to have taxable income in the future, so financial expenses have increased significantly. The plan is to improve the future situation and review low-profit businesses, including withdrawing from them.

M: I understand.

Q&A Session 2

Q: I would like to ask you to comment on financial improvement and progress toward meeting your profit targets. For example, with profit, the progress under operating income in H1 is not as good as in previous years. I understand it is mainly overseas, but can anything be done? You talked a lot about North America; for example, is there room to slightly curb integration costs, or is it something that is difficult to deal with?

Also, on the financial side, if I remember correctly, you are planning to reduce debt by JPY150 billion to JPY200 billion this fiscal year. Still, there is no concrete progress on the off-balancing of the data centers, so could you give us an update?

A: First of all, regarding profit improvement, as you just pointed out, orders, sales, and profits in North America have been struggling compared to the previous year as a whole. In terms of profit, we are determined to achieve our target for the current fiscal year, and we have been promoting efficiency improvement for some time now, aiming to strengthen such cost control measures in North America further to secure profits.

In Europe, sales and orders are also very strong, but we need to work a little harder on the profit side. Here, business integration and structural reforms are underway in some areas, and excluding those areas, substantial profit improvement has been achieved in some areas. So, I think that the main focus is to improve the profit from the actual orders received by further enhancing the digital projects. This concludes our efforts to improve profits in our overseas business.

In terms of financial improvement, I think that a debt reduction on the scale of JPY150-200 billion would be challenging to implement in FY2023 as it were large, but there is no change in the direction of firmly promoting the off-balancing of our data centers. As I have explained in various presentations, there is a growing need to expand our data center business as the demand for AI has emerged.

In reality, however, it is not possible to spend an unlimited amount of money, so it is essential that we make firm progress with the off-balancing that we have been working on for some time. We classify our assets as core assets and non-core assets, and we are making a firm selection of which properties to sell this fiscal year, next fiscal year, and the fiscal year after that. We are currently in the process of screening properties for sale in H2 of this fiscal year as well.

In addition, the method of sale will not be limited to the usual sale or negotiated sale. Still, we are also considering introducing a method in which bids are made to multiple parties. Although it may take some time, we are considering introducing a REIT-like method.

Q: Just one follow-up question. Your comments on the profit and loss situation in the US and Europe were very helpful. Still, the purpose of my question was to ask how the situation is for achieving profit on a company-wide basis, so I was wondering if you could comment on the overall picture, such as whether the domestic situation is progressing well enough to surpass the situation in Japan, or on the integration costs you mentioned earlier?

A: As mentioned earlier, the overseas business is progressing well, and the domestic business is generally progressing well, as you can see from the results for Q2 of this fiscal year. However, we believe that we need to work a little harder in the overall market.

Also, in comparison with the previous year, the previous year saw the posting of several billion yen in unprofitability at the end of the fiscal year. Still, we do not plan to do so this fiscal year. That is all.