

## **Q&A session at the small meeting for analysts (November 9, 2022)**

### Questioner 1

#### Question 1

I understand that the gross margin ratio in the second quarter declined even after excluding a loss from an unprofitable project. Please explain the background of the decline?

#### Answer 1

One reason for this is a decline in reaction to the strong performance in the previous year, when the Public & Social Infrastructure Segment had a large-scale project with high profits. While the operating income of the Public & Social Infrastructure Segment in the second quarter fell about 10 billion yen year-on-year, this decrease includes a loss of about 7 billion yen due to the occurrence of an unprofitable project and a decline of around 2 billion yen in reaction to a large-scale, high-profit project in the previous year.

#### Question 2

While your Company had a high-profit project in the first half of the previous fiscal year, you say that the profitability in the same period of this fiscal year was at a normal level when excluding the effects of an unprofitable project. Can I assume that a similar tendency will continue in the second half of this fiscal year?

#### Answer 2

As a characteristic of the second half of the previous fiscal year, the selling, general, and administrative expenses significantly increased due to such reasons as up-front investments made in the fourth quarter, which caused the operating income to decrease. Considering this, we would like to control those expenses in the second half of this fiscal year. Since the gross margin ratios of overseas businesses have been improving mainly in North America due to an increasing number of digital projects and other reasons, we believe that we will be able to maintain a certain level.

## Questioner 2

### Question 1

As for an unprofitable project that arose in this fiscal year, I understand that the current phase will be completed within this fiscal year while I wonder if the whole project will continue in the next fiscal year and beyond. In addition, I understand that, in this project, you successfully made switching from a rival company in the public sector division. Please explain why you were able to receive the order for the project.

### Answer 1

We are scheduled to start the service for this project before the end of this fiscal year.

We won a bid for the project, and we believe that our bidding price and technologies were highly recognized. The project is to renew the foundation of the customer's information system, and we contracted the project in the anticipation that we would be able to further expand the business in the future based on the renewed foundation.

### Question 2

I would like to ask about tax rates you have to pay during the Medium-term Management Plan period after the business combination with NTT Ltd. My understanding is that tax rates NTT Ltd. has to pay are high partly because it does not use the consolidated taxation system. When do you expect will the tax rates become ordinary levels?

### Answer 2

At the moment, we have not been able to aggregate profits and losses between countries with deficits and those with high profits. However, we are currently reviewing low-profit countries and businesses and working to adjust the tax rates we have to pay to certain levels. Given the estimates on the progress of overseas business integration, this is likely to be achieved in the latter part of the Medium-term Management Plan period.

### Questioner 3

#### Question 1

An operating income disclosed as a reference in the full-year forecast for this fiscal year is 236 billion yen that includes the business combination with NTT Ltd. and 222 billion yen that does not include the effects of the business combination. Based on these figures, I understand that the difference of 14 billion yen is NTT Ltd.'s operating income in the second half of this fiscal year. On the other hand, the full-year forecast released by NTT expects an operating income of 35 billion yen, 25 billion yen of which is in the second half. Could you provide an additional explanation about the difference?

#### Answer 1

The operating income of NTT Ltd. for the second half of this fiscal year is expected at 25 billion yen and about 14 billion yen, which remains after deducting about 11 billion yen including the PMI cost for the business combination, is expected to contribute to the results in the second half of this fiscal year. Meanwhile, NTT Ltd.'s operating income for the first half of this fiscal year is slightly lower than the plan; hence, we will make efforts to ensure the operating income of at least 25 billion yen specified in the plan by regaining strength in the second half, although the overseas business environment is uncertain.

#### Question 2

I recognize that NTT Ltd.'s full-year sales plan has progressed without a problem but do you expect a decline due to internal sales when consolidation takes place?

#### Answer 2

We do not expect much decline. Although the sales of some communications devices are sluggish, the overall sales of NTT Ltd. are strong and steadily increasing. For that reason, we think the plan will be achieved.

#### Question 3

As for the non-operating profit and loss and extraordinary gain and loss/corporate tax, etc. of NTT Ltd., my understanding is that there was a transient increase factor in the first quarter. I would like to know if there was anything noteworthy in the second quarter as well as the forecast for the second half of this fiscal year.

#### Answer 3

There was no transient factor worthy of special mention in the second quarter, and we do not expect anything extraordinary to occur in the second half of this fiscal year. However, the effects of rising interest rates are a cause of concern and we will closely look at the situation.

#### Question 4

I would like to confirm how much debt will increase due to the business combination with NTT Ltd. Are you planning to disclose the balance sheet?

#### Answer 4

We plan to disclose a postconsolidation balance sheet when we release financial results for the third quarter of 2022.

#### Question 5

In the second quarter, the results of the Overseas Segment are disclosed as a reference by separating North America and the EMEA & LATAM region. Please describe your image on how to disclose NTT Ltd.'s results in the third quarter and after. NTT has so far disclosed NTT Ltd.'s business results by putting it in the category of high value-added services, etc. I would like to ask whether the categorization will be changed or not.

#### Answer 5

We plan to disclose the results of the Overseas Segment by dividing it into three categories of North America, EMEA & LATAM, and NTT Ltd. Moreover, we are currently discussing the disclosure of NTT Ltd.'s results by category such as high value-added services.

#### Questioner 4

##### Question 1

I want to know the number of projects that constitute the loss of about 7 billion yen from unprofitable projects.

##### Answer 1

One project in the public sector division constitutes the most part of the loss.

##### Question 2

When did you receive the order for the project? May I ask if the customer is one of main government ministries and agencies, or if the project is a cross-ministry project?

##### Answer 2

Please allow me to refrain from giving more details than that the project is related to the public sector.

## Questioner 5

### Question 1

Could you provide the numbers on the balance sheet to create business forecasts? I also would like to know the amounts of assets to be included in the balance sheet such as an image about the depreciation of capital investment of NTT Ltd.

### Answer 1

I cannot give specific numbers but the amount of capital investment is expected to slightly increase from the previous fiscal year.

### Question 2

Concerning the PMI cost for the business combination with NTT Ltd., I would like to know your action plan for the next six to 12 months, what the cost will be used for, and when synergies emerge, among other issues.

### Answer 2

The new structure started on October 1, and leaders from NTT DATA's overseas regional headquarters office and NTT Ltd. have just begun discussions for the future. From here on, they are going to discuss a business plan for the next fiscal year, and I assure you that the next fiscal year is the first year of our full transformation.

Since we had been different companies so far, we expect short-term synergies such as cross-selling to each other's customers to emerge in the next fiscal year, whereas we will spend money on measures that require a certain amount of cost and time, such as IT integration, from around the second half of the next fiscal year and work to achieve synergies by fiscal 2025.

### Question 3

Do you mean that the PMI cost, which was said to be around 10 to 20 billion yen a year, will not reach that level in the next fiscal year?

### Answer 3

We will determine the size of the PMI cost while preparing a business plan for the next fiscal year.

#### Question 4

While NTT Ltd.'s operating income in the first half of this fiscal year was lower than the plan, please explain a concrete action plan for the second half of this fiscal year to achieve the full-year forecast.

#### Answer 4

We believe we should prioritize the solid implementation of the structural reform that has been carried out within NTT Ltd. over PMI for the business combination with NTT Ltd. Out of the planned annual structural reform cost of 38 billion yen, around 17 billion yen has been spent in the first half of the year. Thus, the top priority is to implement the reform as planned during the remaining period and improve the efficiency of the company.

As for PMI for the business combination with NTT Ltd., we will start with measures to produce solid returns, such as cooperating in cross-selling and creating common offerings, before launching a large-scale structural reform.

#### Question 5

Regarding the cost for NTT Ltd.'s structural reform, you expect that NTT DATA's profit-and-loss statement will be affected by the remaining amount of about 21 billion yen after deducting the amount spent in the first half from the planned annual amount. Is the estimate included in the forecast you have disclosed?

#### Answer 5

Yes, it is. The annual amount of 38 billion yen and the spending of about 17 billion yen in the first half are in line with the original plan.

## Questioner 6

### Question 1

I understand that NTT Ltd. should have an operating income of about 28 billion yen in the second half of this fiscal year in order to achieve an operating income of 35 billion yen set forth in the company's full-year forecast. Meanwhile, NTT DATA's plan for the second half expects NTT Ltd.'s operating income at about 14 billion yen. Could you explain the difference? Is the PMI cost included?

### Answer 1

When we created the plan, we estimated NTT Ltd.'s operating income in the second half at around 25 billion yen. However, we now expect a loss of about 11 billion yen in the second half due to costs such as the PMI cost including the cost for the latest deal and deducted the amount.

### Question 2

Let me confirm NTT Ltd.'s sales trend. As far as I know, the sales achieved year-on-year growth of 16% in the first quarter and 19% in the second quarter. I would like to know results that exclude the effects of foreign exchange rates.

### Answer 2

For the period from April 1 to September 30, 2022, the sales increased by about 90 billion yen from the same period of the previous fiscal year. Since the sales increase includes about 62 billion yen in gains from foreign exchange differences, when the effects of foreign exchange rates are excluded, the sales grew by about 28 billion yen year-on-year. Meanwhile, the sales increase of around 40 billion yen in the first quarter includes about 26 billion yen in gains from foreign exchange differences. Therefore, in the second quarter, the sales grew by about 50 billion yen, including the effects of foreign exchange rates worth about 36 billion yen.



## Questioner 7

### Question 1

Following the business combination with NTT Ltd., you set a goal of achieving an EBITA margin of 10% in fiscal 2025. Do you intend to gradually improve the EBITA margin? Or will it temporarily decline and then recover at a rapid pace toward the target year? Could you explain your view on this?

### Answer 1

The goals of operating income margin at 10% and overseas EBITA margin at 10% outlined in the Medium-term Management Plan do not consider transient costs such as structural reform costs, and we assume that an adjusted EBITA margin, which indicates the actual performance, will be improved gradually. The PMI cost for the business combination with NTT Ltd. is likely to reach a considerable amount in fiscal 2023 and fiscal 2024, and we will plan concrete measures and the amount of expenditure during the second half of this fiscal year.

### Question 2

NTT Ltd.'s structural reform cost is planned at about 38 billion yen. I would like to ask about the cost for the next fiscal year. Is there a possibility of more money to be spent on the structural reform than this fiscal year?

### Answer 2

The structural reform cost for the next fiscal year, even if it is implemented, is expected to be lower than that of this fiscal year.

## Questioner 8

### Question 1

My understanding is that strategic investment for the entire company will be increased by around 15 billion yen from the previous fiscal year. Please explain levels of strategic investment for the next fiscal year and beyond.

### Answer 1

We will consider the issue while preparing a business plan for the next fiscal year. Considering that we need to discuss how to enhance the competitiveness of NTT Ltd., I think we will make a strategic investment of a similar, or larger, size to that of this fiscal year at least.

### Question 2

In your plan, you will spend nearly 11 billion yen this fiscal year on PMI for the business combination with NTT Ltd. and for other purposes. While I think you have already spent a certain amount in the first half, I want to know the specific amount you have spent. Am I correct in assuming that there will be no change to the full-year plan?

### Answer 2

There is no change to the full-year spending of around 11 billion yen, and we spent about 1 billion yen in the first half of this fiscal year.

## Questioner 9

### Question 1

Apart from the PMI cost for the business combination with NTT Ltd., are there any other costs to strengthen NTT Ltd. as a company-wide strategic investment? In that case, I guess the total amount of strategic investment will be around 50 to 60 billion yen in the next fiscal year, given that you have announced that the next fiscal year's PMI cost will be around 10 to 20 billion yen and this fiscal year's strategic investment will be around 32 billion yen. Is my understanding correct?

### Answer 1

As for the PMI cost, we assume the organizational integration between NTT Ltd. and NTT DATA's overseas business segments and IT integration. Conversely, strategic investment is part of efforts to create offerings, develop personnel, and strengthen consulting capabilities to strengthen competitiveness, so I would like you to see strategic investment as a separate initiative.

Regarding strategic investment, we will closely examine and discuss each measure and decide the amount of investment while preparing a business plan for the next fiscal year. If the level of strategic investment in the next fiscal year's plan is similar to that of this fiscal year and the PMI cost comes close to the upper limit, the total will be around 52 billion yen. This amount is within the scope of our expectations.

### Question 2

I think that the PMI cost is a cost related to the Overseas Segment. Am I correct?

### Answer 2

Yes, you are. The updates on the PMI cost will be provided in every quarterly financial statement.

## Questioner 10

### Question 1

In recent years, new technologies have been emerging continuously while customer companies are facing a shortage of engineers. That's my understanding of the trend of the industry. While I think you will work to prevent unprofitable projects from occurring in the future, what points do you see as the risk of projects becoming unprofitable?

### Answer 1

We have been trying to prevent unprofitable projects from occurring, aiming to contain the total loss from unprofitable projects to 0.3% to 0.5% of consolidated net sales. However, we had a large loss of about 7 billion yen lately, so we are currently promoting measures to prevent this from occurring again across the Company.

Unprofitable projects have occurred not only in Japan but also in other countries. Especially in overseas countries, we see fixed-price contracts as a risk. Moreover, it tends to be a high risk both at home and abroad to accept projects that require the retention of existing system specifications. With these in mind, we try to minimize risks when signing a contract.

In Japan, we have a relatively increasing number of projects that are not so large and are implemented in cooperation with customers based on SES contracts not on fixed-price contracts. As the number of such projects will increase, the number of large-scale projects based on fixed-price contracts will decrease proportionally. In that sense, the risks of respective projects will become lower than that before.

### Question 2

I would like to ask about risk management standards regarding overseas projects. Just like in Japan, do you currently have a system to require the reporting to top management in light of certain standards, among other requirements?

### Answer 2

We are taking similar measures in overseas countries. Project management offices in respective countries and regions monitor the status of each project involving a certain amount of money and certain risks regularly, and the headquarters office also monitors them as needed.

### Question 3

I want to know specific positive changes in NTT DATA's overseas businesses that have appeared as a result of the structural transformation you have implemented so far, if there are any.

### Answer 3

In North America, we have completed the structural transformation aimed at bringing about changes to achieve a digital shift and enhancing digital talent. At the moment, we set relatively strict standards to decide whether or not to continue to accept low-profit projects in traditional fields, while trying to increase the number of projects in which we can use digital talent acquired through the structural transformation, M&As, and other means. Because of these efforts, the profitability ratio has been steadily increasing more than the growth rate of sales.

In the EMEA & LATAM region, we have built comprehensive competitiveness over the past 2 years and the number of new orders received and sales have grown steadily. Considering a surge in labor costs, we must further increase the profitability ratio. Even so, we have been able to receive orders for good projects lately. For these reasons, we think we have made smooth progress toward achieving an adjusted EBITA margin of 10%.

### Question 4

I think surging labor costs can be passed on to prices to a certain extent thanks to the strong IT demand. I would like to ask about your future plan.

### Answer 4

Seeing the results for the latest first and second quarters, we have been able to certainly pass the increased costs on to prices. However, in case we find investors less willing to invest in the IT sector due to the concerns about a recession, a risk factor is how much cost we can pass on to customers. Hence, we will continue to closely watch the situation of the cost ratio.

## Questioner 11

### Question 1

I would like to confirm the performance-based operating income excluding structural reform and other transient costs in NTT Ltd.'s full-year plan for this fiscal year. In my understanding, it is about 86 billion yen. Am I correct?

### Answer 1

An adjusted operating income is about 73 billion yen, calculated by adding the structural reform cost of about 38 billion yen to the full-year operating income forecast of 35 billion yen. PPA depreciation costs and other costs are added to the adjusted operating income and an adjusted EBITA calculated based on it is about 86 billion yen, as you know.

### Question 2

There were no modifications to NTT Ltd.'s full-year plan. Am I correct in understanding that that is because the results were sluggish due to the difficulty in procuring equipment and other reasons, despite the contribution of positive effects of foreign exchange rates?

### Answer 2

The sales of communications equipment declined while we recognize that the increased sales of high value-added services, especially data center-related services, make up for the sales decline.

### Question 3

The operating income of NTT Ltd. for the second quarter alone did not even reach 1 billion yen. Is that correct?

### Answer 3

Yes, it is. As you know, the operating income for the period from April 1 to September 30, 2022, was 6.4 billion yen and that for the first quarter alone was 6.2 billion yen. Given these, your understanding of the operating income for the second quarter alone is correct.

#### Question 4

In the process to improve an adjusted EBITA margin in a phased manner to achieve 10% in fiscal 2025, how will NTT Ltd.'s structural reform cost be disclosed in the next fiscal year and beyond? Will the total cost be disclosed as a structural reform cost for the entire NTT DATA?

#### Answer 4

If any costs are corresponding to this fiscal year's costs for NTT Ltd.'s structural reform after the next fiscal year, such costs would be explained as part of costs for our Company's overseas businesses because the combination has already been completed.

#### Question 5

After the next fiscal year, NTT Ltd.'s structural reform cost will be reduced while this fiscal year's planned PMI cost will reach around 10 to 20 billion yen a year. Is my understanding correct?

#### Answer 5

Yes, it is. NTT Ltd.'s structural reform cost will be lower than about 38 billion yen for this fiscal year.

#### Question 6

Regarding the unprofitable project, I remember that you had received an order for a project to renew another company's building system in the past but the project ended up unprofitable due to insufficient understanding of the existing system's structure. I wonder the latest unprofitable project occurred due to the similar reason.

#### Answer 6

The latest unprofitable project is not as operationally complex as the past one you mentioned, and most of the loss from the latest unprofitable project was due to the cost required for a migration of the foundation system. Thus, the nature of those two projects is different.

#### Question 7

Let me confirm the real reason for that surge in costs and measures you will take to address the issue. You say that the performance related to the foundation was poor, but it seems to me that the improvement of the performance of the foundation itself is outside the scope of NTT DATA's business. Did the addition of hardware or other factors cause an increase in cost?

#### Answer 7

The issue of the latest unprofitable project was a poorer-than-expected performance of a tool used to migrate the huge volume of data with complex file structures from the on-premise environment to a cloud foundation. This is not only because we needed operations to improve the tool while negotiating with the product's vendor but also because the labor costs increased to secure the necessary personnel during a new period added due to a change in a release plan.



## Questioner 12

### Question 1

Is there anything that I should keep in mind about the improvement of treatment at NTT Group, which was announced to the press on the other day?

### Answer 1

The improvement of treatment covers the entire NTT Group, and NTT DATA also will take measures for that. Nevertheless, we expect the financial effects of the measures to be minor.

### Question 2

Concerning the results of NTT Ltd. for the first half of this fiscal year, please explain the structural reform cost and its investment effects.

### Answer 2

The structural reform costs about 4 billion yen in the first quarter and about 13 billion yen in the second quarter; therefore, about 17 billion yen has been spent on the structural reform for the period from April 1 to September 30, 2022. In the previous fiscal year, of 44 billion yen spent a year, approximately one-fourth was used in the first half of that year.

The structural reform is estimated to have produced effects worth about 1 billion yen for the first and second quarters, respectively. The effects of the structural reform last year are believed to be about 17 billion yen in the first half of that year in total. In total, the structural reform has produced effects totaling about 19 billion yen in the first half of this fiscal year. The previous year's structural reform generated effects of about 5 billion yen in the first half of the previous fiscal year.