Company Presentation for the Fiscal Year Ended March 31, 2024

Question & Answer

Questioner 1

Q&A Session 1

Q: Regarding overseas EBITA results on page 8 of the presentation material, you said it is actually higher in EMEA/LATAM after adding back the one-time costs like integration costs. What about NTT Ltd.? I guess the gain from the sale of the data center was posted in Q4 of FY2023, but could you tell me the approximate amount?

A: For NTT Ltd., as the YoY increase in business combination costs was JPY4.6 billion, the actual EBITA is higher by that amount. For the capital gain of data center transaction, we recorded JPY15.6 billion in Q4 of FY2023. In Q4 of FY2022, there was a one-time gain of JPY8.5 billion associated with a long-term lease contract at NTT Ltd., so YoY change is about JPY7 billion.

Q: It means, even excluding such one-time factors like capital gains or expenses, NTT Ltd. has enjoyed profit growth in Q4 of FY2023. Therefore, their underlying operations are recovering. Is it correct?

A: It is safe to say that its fundamental performance is getting better.

Q&A Session 2

Q: Do you expect any capital gains on data center sales for FY2024?

A: For FY2024, we have not factored in the gains on data center sales.

Q: I see. The second point is your forecast for financial expenses. I think it was JPY88 billion in FY2023, but the yen is weakening further. As the assumed exchange rate is JPY138, financial expenses could become bigger when you calculate with the actual exchange rate. How much financial expenses have been factored in FY2024, and what measures are being taken to reduce them?

A: For finance income and expenses, etc. of FY2024, our plan is to expect a net expense of JPY81 billion. It will be about JPY20 billion decrease, compared to the net expense of JPY60.9 billion in FY2023. For initiatives in FY2024, as shown on the page 28 of the presentation material, we are looking to promote reduction of financial expenses by fixing the portion of interest-bearing debt currently being borrowed at floating rates and taking advantage of the yield curve inversion.

In addition, when raising funds for new investments, we will consider various factors such as due date, payment terms, environment, and currency to reduce our sensitivity to the market rate fluctuation. By the way, we are considering securitization of data center assets aiming for FY2025.

Q&A Session 3

Q: I'd like to hear your view again on the ownership of data center (DC) business.

I think that your company should not own the facility-based DC business. Divesting it should benefit both NTT DATA and NTT Corporation.

You are an IT service provider, and with such a balance sheet-intensive business, it has been negatively affecting your business in the past one and half years or so, I guess. You mention edge-to-cloud services, but it may not be widely understood yet in the market. I also wonder if the NTT DATA Group really has to have 55% stake of NTT Ltd. to conduct DC services.

So, I think it would be a win-win situation for both NTT DATA Group and NTT Corporation, if NTT Corporation, which has a lot of facility businesses, could handle the DC business, and NTT DATA Group works with them as a collaboration partner.

As NTT DATA Group, do you intend to return the DC business to NTT Corporation or review the capital structure? Your new segment structure that started from FY2024 seems like you are carving out the DC business, so I am hoping that you are thinking about that. Please share your thoughts on the ideal state of DC ownership.

A: I think it requires continuous deliberation. DC business of NTT Ltd. was consolidated into NTT DATA Group in October 2022, and we are not thinking of divesting and returning the DC business to NTT Corporation.

Our domestic DC service is mostly provided in combination with system integration service. However, in overseas, our DC service is not as widely penetrated unlike Japan where many clients use our data centers in combination with consultation or system integration services. Therefore, we intend to increase such bundle-type of services. As you pointed out, we are having some difficulties with financial soundness, but we are conducting the business also in collaboration with NTT Corporation, who is our joint venture partner.

Q: I understand. That's all.

Questioner 2

Q&A Session 1

Q: In the past briefing, you said business combination costs would be in the range of JPY10 billion to JPY20 billion in FY2024, but according to the page 22 of the presentation material, now you increased it to JPY30 billion. Could you tell me the reason for this? Also please tell me the amount of synergy you are expecting and its timing of realization.

A: For business combination costs, we indicated JPY10 billion to JPY20 billion for FY2024 and FY2025, but we changed it this time to JPY30 billion for FY2024 because we aim to accelerate the spending with the peak in FY2024, so that we can enjoy the fruit of the business combination earlier. The effects are already being seen little by little. We are expecting a synergy of JPY30 billion in FY2025.

Q&A Session 2

Q: On page 24 of the presentation material, you changed the net sales target to JPY4.7 trillion for the final year of the medium-term management plan, including the effect of integration of NTT Ltd. However, you did not change the 10% consolidated operating profit margin. Does it mean you are confident?

As NTT Ltd. is cost-heavy for this year with sizeable upfront investment as they are in the growth phase, I don't think they can improve the profit margin so quickly. Based on the forecast for FY2024, it requires JPY134 billion profit growth in one year. I would like to know the logic behind achieving 10% operating profit margin in that scenario.

A: For net sales, we expect around 5.3% growth at this point in the period of FY2023 through FY2025 excluding the FX impact. We don't think it is unrealistic.

As for the profit, we think it is more challenging compared to the net sales, but we expect to see the synergy from business combination. In addition, business combination cost itself will decrease, while we are expecting profit increase from sales growth. Besides, M&As are one of our options to grow the net sales, which will also contribute to profit. We are also hoping to see the effects of securitization of data centers using REIT to be implemented as a way to maintain financial soundness.

Q: But it still seems that JPY134 billion profit increase is too big. I would like to know the approximate amount of each contributing factors such as topline effect and profitability improvement in Japan. Also, I think M&As won't have that much positive impact on the profit, as they accompany some cost outflow, but what do you think?

A: The 10% margin is based on the adjusted operating profit. We are targeting around a bit more than JPY440 billion in operating profit before adjustments in FY2025. We generated about JPY10 billion level of business combination synergy in FY2023 via cross-selling and full-stack services by NTT Ltd. and each region, and for FY2024, we expect a bit above JPY15 billion. In FY2025, we are aiming to generate about JPY40 billion in synergy (about JPY30 billion after netting the one-time costs). Through this and business growth, as well as organic growth via M&As, we aim to achieve 10% adjusted OP margin.

Q: I understand. That's all.

Questioner 3

Q&A Session 1

Q: The new orders received on page eight of the presentation material increased in Q4 for both North America and EMEA/LATAM, partly due to currency effects, I guess. Could you give us some qualitative and quantitative assessment on this? How do you view the market environment? I would also like to know if there are any large projects in the pipeline. Please elaborate on the background of overseas order growth.

A: EMEA/LATAM are performing very well. However, net sales in North America were down JPY7.6 billion YoY. This includes a positive impact of JPY37.3 billion from foreign exchange rates, meaning an actual decrease was around JPY45 billion. In North America, clients were very cautious about future growth until around Q2 of FY2023 and were holding back on IT investment, but orders have been increasing since around Q3 of FY2023. In Q4, orders increased as we won orders worth approximately JPY140 billion, although it's partly due to the currency effect.

The reason behind the revenue decrease in North America is that we have been focusing on profitability in the past couple of years in the region, and in some cases we intentionally give up low-profitability traditional projects upon contract renewal. Therefore, on an annual basis, sales in the health care, financial, and other fields have decreased by about JPY50 billion in relation to the existing projects. We have been working to replace this with new high-value-added consulting and digital projects, but the challenge is that we have to accelerate our efforts more. So, starting April 2024, we established two organizations to promote growth strategies: one is a team to accelerate the digital business in North America, and the other is for existing clients, to propose the use of cutting-edge technologies one and half years before their contract renewal dates.

Through these initiatives, we will pursue growth accompanied by quality in North America.

Q: Thank you. The new orders received in North America from January to March increased by about JPY25 billion, partly due to the currency effect, I guess. Is this increase the result of an emphasis on profit margins, or thanks to the projects in the digital domain? Or are they increasing because you had a large project?

A: We are receiving orders for digital projects. We also have a solid pipeline of digital projects, but the challenge is that we have not been able to accelerate to the point where we can offset the negative impact of existing projects.

Q: I understand.

Q&A Session 2

Q: Regarding the FY2024 operating profit guidance for Japan on page 20 of the presentation material, you are planning to increase the total operating profit of the three businesses in Japan by JPY21.9 billion. Meanwhile, operating profit for Japan Segment is expected to increase by JPY6.3 billion. Why those two numbers have a huge gap?

Also, how will you steer the effort in FY2025, the final year of the medium-term management plan? To achieve OP level of JPY400 billion, the businesses in Japan should serve as a driver. Will your upfront investment start to bear fruit from FY2025? What is your outlook?

A: First, the difference in operating profit between the total of the three businesses in Japan and the Japan Segment is worsening by JPY15.6 billion over FY2023. The reason for this is that we have released a new internal system for domestic companies, and the majority of this is the burden of amortization as well as maintenance and operation costs. In addition, some incremental cost for strategic investment and security countermeasure cost are also included. Please understand the difference is due to the increase of negative effect of these costs. In FY2025, amortization cost itself should remain unchanged and we expect the expenditure of the same amount, but maintenance and operation costs should be a bit lower than FY2024, as FY2025 will be the second year after implementation.

In terms of profits, we must of course increase profits in Japan toward FY2025. This is same for overseas. We intend to drive profit by topline growth.

Q&A Session 3

Q: About financial strategy on page 28 of the presentation material, you said financial expenses in FY2023 was JPY88 billion but how much are you planning for FY2024? You said for FY2025, you expect a rapid recovery of financial soundness such as net debt/EBITDA ratio because of the utilization of REIT. I would like to know specifically what kind of REIT it will be and if you are transferring almost all of your DCs to them, and what sort of impact it will have on your B/S and P/L.

A: In terms of financial income/expenses, etc. for FY2024 forecast, we are looking at a net expense of JPY81 billion.

The actual net debt/EBITDA ratio of FY2023 was 3.0 times, and for FY2024, as we have not incorporated any capital gains of DC sale into our business plan, the net debt/EBITDA ratio is expected to remain unchanged. As for the sharp recovery in FY2025, it is because we are thinking about leveraging REIT to securitize our DC assets.

Concerning the impact on P/L, it should have a similar impact as selling the data centers.

As for the impact on B/S, the investment in the data center that we are building now is funded both by our equity and debt components, but if we sell our equity interest in the DC asset or move it off from our balance sheet from the beginning, our debt will be reduced.

Q: Is it correct that it is almost a done deal to leverage REIT?

A: We are currently studying that approach, targeting to implement it within FY2025.

Q: I understand. As for the financial income/expenses, etc. for FY2024, you said it will be a net expense of JPY81 billion, which means you expect about JPY20 billion increase in financial expenses, is that correct?

A: You are correct.

Q: As someone mentioned earlier, data center business may not be something that you should be involved by using your P/L or B/S. Should NTT Group bear the cost, or does it have to be posted on the P/L of NTT DATA Group, which is an intermediate holding company? If it does, the financial expenses will go up again by JPY20 billion in FY2024. I think that is quite deficient in terms of strategy, don't you think? You probably need more drastic approach to reduce the financial expenses. Do you expect a significant recovery by transferring it to REIT? Should we wait for that?

A: As for financial income/expenses, etc., it will be a net expense of JPY81 billion, which is a deterioration of about JPY20 billion. Of which, about JPY4 billion is an increase of expense due to a loss on business withdrawal. In other words, the real net expense will deteriorate by about JPY16 billion, excluding the loss on business withdrawal.

About the securitization of DC assets including REIT utilization, it is not reflected in the FY2024 business plan. However, we aim to complete it in FY2025.

Q: I understand.

Questioner 4

Q&A Session 1

Q: Regarding the FY2024 guidance of the new orders received in Overseas Segment, it says that new orders received excluding DC business will be JPY2.67 trillion. How much will it be, if you include DC business? Should I expect the new orders received to be similar level as FY2023?

A: New orders received for data centers may deviate largely from the plan depending on the arrangements with clients, such as long-year contracts of more than 15 years, with the renewal cycle of two to three years or longer etc. Therefore, we think it would be better not to give specific figures for the new orders received for the DC business itself, so we decided to disclose the figures like this format.

We thought it would be easier for you to understand our current order situation if you look at the new orders received outside of the DC business. About the specific figure for the new orders received for DC business in FY2024, we would like to refrain from sharing it with you.

Q: I understand. That's all.

Questioner 5

Q&A Session 1

Q: Regarding the synergy from the business combination with NTT Ltd., you mentioned JPY40 billion in FY2025. I remember that you said it would be around JPY30 billion before. This means that you are seeing the accelerated effect of synergy compared to your previous forecast?

A: Through the full-stack services and cross-selling by NTT Ltd. and the former NTT DATA, new orders received have grown significantly, reaching JPY130 billion in FY2023. In addition, implementation, etc. of IT support services to global clients are trending very favorably. So, we are aiming for a synergy effect of JPY40 billion (about JPY30 billion after netting the one-time costs).

Q: Thank you. One more thing. You reclassified the Segments in FY2024. Why is Business Solutions only combined with the DC business?

A: In FY2024, we have changed to a new structure for our overseas business, and we have divided it into five Units, three of which are by region: the North America, the EMEA/LATAM, and the APAC. The other two Units are the global businesses across the regions: one is the Unit in charge of data center network etc., and the other is the Business Solutions, a Unit that operates SAP business.

On our financial results presentations for FY2024, we will combine the Business Solutions and the Global Technology and Solution Services that include data centers.

Q: I understand your treatment.

Questioner 6

Q&A Session 1

Q: EBITDA margin for the DC business was higher than the plan in FY2023, but is expected to return to 30+% level in FY2024. Why are you targeting the lower margin, and also, how you see the margin to evolve in mid- to long term horizon?

A: The EBITDA margin of 45% in FY2023 includes the gain on the sale of the data center. On the other hand, for FY2024, we do not expect any such gains. Therefore, we expect it to return to the level around 40%. We will use this as a baseline but intend to improve it where possible.

Q: What are the underlying drivers of the margin improvement besides selling the assets?

A: The more data centers we have, the percentage of HQ cost will become lower. In addition, we believe we can cut costs by consolidating global operations.

Q: I understand very well.

Questioner 7

Q&A Session 1

Q: I have a question about the tax rate. Net profit was significantly lower than expected in FY2023, and I think the impact of the tax rate was probably about 10 percentage points higher than expected.

It appears that you assume the tax rate at around 40% for FY2024 as well, so please remind me of the background of tax rate deviation from your initial forecast. It is largely driven by the netting of P&L. Do you expect the situation to become quickly normalized in FY2025? Any thoughts on the outlook?

A: As for FY2023, there was an increase in tax expenses. As a result, the tax burden rate has risen. The reason is mainly due to the increase in tax expenses at overseas subsidiaries, including NTT Ltd. As we explained in the past, some of our overseas subsidiaries have incurred losses due to increased financial burdens. The fact that future taxable income is not expected means that there is a potential increase in tax expense.

In addition, there were some special events in Q4 of FY2023, that is, there were several companies where the deferred tax assets were reversed for accounting purposes as the recoverability of planned amount has become a point of contention.

In addition, there was some impact from the cases in which foreign tax credits could not be applied to tax payments arising from the inter-group transactions among overseas group companies. As a result, tax expenses were higher in Q4 of FY2023.

We have set the tax rate for FY2024 considering the actual rates for FY2023, but we are also concerned about the high tax burden. We intend to proceed with measures to reduce tax burden, such as the reduction of interest expenses and withdrawal from low-profit businesses, including reduction of the number of subsidiaries.

Q: I understand. Thank you.

Questioner 8

Q&A Session 1

Q: On pages 27 and 28 of the presentation material, it says the actual investment for DC was JPY390.5 billion in FY2023, and you expect the similar level in FY2024. Is it safe to understand that it is because of solid demand? The resulting financial soundness on the graph is that the absolute net debt amount is not decreasing. This is also probably a different trend from the guidance one year ago, but should I take it as a positive sign?

Lastly, you decided to utilize REIT, among various options. Will the transaction primarily take place in the US? In terms of debt reduction, now that the market is favorable, you are pivoting to defer the action, which could hamper the progress of medium-term management plan? I don't think it's all bad news, but could you share your insights on this?

A: First, the investment in DC for FY2023 was JPY390.5 billion. One of the reasons why it was bigger than the initial plan is the impact of the foreign exchange rates. It turned out that the actual rate was JPY144 against the assumed rate of JPY130.

The other reason is that there was a data center we originally anticipated to build with a partner, but in the end, we had to build it ourselves, and therefore we had to make a larger capital investment than we assumed.

The investment amount for FY2024 is planned to be slightly lower compared to FY2023, but as the demand for data centers continues to be strong, we are going to consider revisions to the plan based on demand trends.

As for the net debt/EBITDA ratio, we explained in FY2023 that we would securitize the DC assets every year. However, we have not incorporated any capital gains of DC assets for the FY2024 plan. Therefore, we expect the net debt/EBITDA ratio to stay flat. In FY2025, we hope to complete the REIT conversion and regain financial soundness.

Q: To enjoy tax benefit, do you see high probability of forming a REIT in the US?

A: We are still in the process of considering the specifics. The specific regions and scale of the deal will be discussed from now on, so I would like to refrain from going into details.

Q: Thank you very much. That's all.
