Summary Translation of Question & Answer Session at
FY 2023 Second Quarter Financial Results Briefing for Analysts

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Presenter: Takeshi Isobe, SEVP & CFO

Questioner A

Q1: Were there any special factors that made adjusted operating profit for Service Solutions in the second quarter so large? Also, please tell us your outlook for the second half.

A1: There were not any special factors in particular. The biggest factor was the impact of higher revenue. In addition, the initiatives that we have been continuing to pursue, such as efforts to improve profitability, have improved our gross margin by 1.3 percentage points. As for our outlook for the second half, the level of our backlog of orders in Japan, including orders for fiscal 2024, is 12% higher than last year's level, so we believe the revenue trend in the second half will also be solid. Our profit target for Service Solutions is quite high, but we believe that we can fully achieve it.

Q2: Are you anticipating significant demand in the future stemming from the government's promotion of digitalization? If you have any ideas about specific amounts, both for now and for next year, please let us know.

A2: For government ministries and agencies, as well as local governments and municipalities, we are clearly seeing initiatives to promote digitalization and standardization. We view that our role at Fujitsu is to respond to that demand with reliability, and we want to put together the right organization to sufficiently handle that. In terms of amounts for specific industries or sectors, I have to decline to give you a clear answer.

Questioner B

Q1: The improvement in profitability of Service Solutions in the Japan region is fairly remarkable. I think it is an improvement that cannot be explained just by the impact of higher revenue. What was the reason why the improvement in profitability accelerated in the second quarter? Does it also include the impact of price increases that you mentioned at the beginning of the fiscal year?

A1: In the Japan region, on a continuing operations basis, the increase in revenue compared to the same period of the prior year was roughly 12%, amounting to roughly 60.0 billion yen more. With 60 billion yen in higher revenue, because the gross margin in our Services business in Japan is around 35%, it generates an increase in operating profit of around 20-22 billion yen. In addition, if we consider that the revenue base for the Japan region in the first half was 570 billion yen, we can say that an improvement in the gross margin of roughly 1.5 percentage points also generates an improvement in operating profit of roughly 10 billion yen. In addition, holding down the level of unprofitable projects also made a positive contribution. Moreover, by fully emphasizing the value we deliver, we are also working to raise the pricing of our services. We can also say that, to a certain extent, higher revenue from Fujitsu Uvance contributed to the improvement in profitability. On the other hand, our personnel costs in the Japan region this fiscal year have been increased by a fairly significant degree, and the impact of higher pricing for our services was just barely enough to cover these higher costs. Accordingly, we do not have the sense that raising the pricing of our services caused a significant improvement in our profitability. What is significantly contributing to improvements in profitability is the expansion in revenue and operating profit, which enables us to maintain a sound level of profitability. We have been promoting the use of offshoring, and our improvements in the offshore usage ratio still have a long way to go. When our offshore usage ratio rises, that means we are also making progress on standardization, and when we make progress on standardization, profitability also goes up. That accounts for about 1.0-1.5 percentage points of the improvement in profitability.

Q2: Compared to the same period in the previous year, please tell us how much your operating profits increased because of the lower level of unprofitable projects. Also, do you think you can continue the same trends in raising the offshore usage ratio in the second half?

A2: I will refrain from mentioning what the absolute amount of the unprofitable projects is, but the impact of holding them to a low level was a positive contribution of several billions of yen. In our briefing materials, the offshore usage ratio is referred to as the Japan Global Gateway usage ratio, and it was 34% for the first half of fiscal 2023. Our ultimate goal is to bring it up to 45% in fiscal 2025. To achieve this, our plans call for slightly raising it some more in the second half. If we are able to do that, we think we can achieve a further improvement in our high profitability.

Q3: Please tell us what progress you have made in your share buybacks. I have a feeling that, for whatever reason, you have made absolutely no progress so far. Less than six months remain before the end of the fiscal year, but what are your thoughts about this issue? Today you made an announcement about an absorption-type merger with a subsidiary, but now that you have made that announcement, can you move forward with share buybacks?

A3: Our intention is to move forward with share buybacks. It is not the case that we paused because we needed a large sum of cash to make an acquisition or some other similar reason. We are moving ahead with initiatives designed to change the structure of our business, including deals relating to our non-core business. Please understand that the reason we have not made progress on share buybacks is because our work on those kinds of deals and reforming our structure have taken priority. We are taking a flexible approach to shareholder returns, and especially share buybacks, after considering such factors as the status of our need for funds. We have made absolutely no changes to the scale of shareholder returns we intend to provide as stated in the capital allocation policy of our Medium-Term Management Plan. As to what level we will implement in any given year, however, please understand that there can be a certain amount of variation in the level from year to year based on circumstances at any given time.

Q4: If the reason why you cannot implement any share buybacks is because you have prioritized the types of deals you mentioned, and if you cannot foresee at the present time how quickly you will be able to complete those deals, am I correct to assume that there is greater risk that you will not be able to implement share buybacks by the end of this fiscal year?

A4: I think that possibility always exists. I have not said anything about Fujitsu making a specific acquisition, but, as I have said in the past, if there was a need for funds just for an example, we may need to rethink such issues as the timing of share buybacks. One thing I can say is that there has been absolutely no change to our current policy of generating 600 billion yen in shareholder returns, as stated in our Medium-Term Management Plan. While considering such issues as structural reforms and a variety of restructuring measures, it is our intention to also want to implement stable buybacks, but please understand that there is a need to implement them within the bounds of what is permissible in consideration of the need for funds and the issue of insider information.

Questioner C

Q1: For Hardware Solutions, please tell us about increases or decreases in operating profit performance in system products and network products in the second quarter and what your outlook is for the second half.

A1: Compared to the previous year, the performance in system products is very solid. Partly that is because this fiscal year we do not have the problem of chip shortages, but against a backdrop of rising demand for spending on IT, demand in the second quarter was very strong. By contrast, revenue from network products in the first half dropped 35% from the first half of last year, to an extremely severe level. This was partly because revenue levels in the previous year were high, but the leading cause is because demand has weakened both in Japan and in North America. We see these trends for both businesses continuing in the second half. From the outset we projected that operating profit for Hardware Solutions for the full year would be sharply lower than in the previous year, and that the operating profit margin would drop from 9.9% in the previous year to 8.7% this year. The main reason is the network business. Since demand in the network business is weak, some would suggest that we restrain development expenditures. Because development lead times in this business are long, however, we are continuing to invest in the business, such as in the development of energy-saving networks.

Q2: In the network business, has there been any change in demand compared to three months ago?

A2: Our understanding is that, compared to our original projections, demand is slightly weaker.

Q3: You mentioned that the Private Enterprise Business and Mobility segments were the drivers behind higher orders in Japan, but I think market conditions in the manufacturing industry and the mobility field are not good. Is there a risk that market conditions could deteriorate? Or, for the Private Enterprise Business segment, is it your view that spending on IT will continue because DX investments are less influenced by market conditions?

A3: In the Private Enterprise Business segment, demand is strong, mainly among large customers, and the trend of our business performance with those customers has been extremely solid. If there is a major change in the external environment, those trends could change, but demand in the Private Enterprise Business segment is strong, driven by the keywords of digitalization, DX, and sustainability, and we do not think these basic trends will change in the second half.

Questioner D

Q1: Your orders are exceedingly strong, but is there a risk that you will be unable to grow revenue further than this due to capacity constraints, such as engineering resources?

A1: We are always concerned about resource shortages and are working hard to recruit talent. We are particularly concerned about having enough engineers who are well-versed in areas such as SAP and ServiceNow. In addition to various recruitment efforts, we are also reskilling internal personnel, such as our human resources and accounting employees, and training them to become engineers. On the other hand, I would like for you to understand that our delivery capacity in Japan is very large, and we are not taking on orders to the point where we will be unable to provide our services. That is why, in order to further expand revenue, we are working to increase the ratio of our offshoring work and increase Fujitsu Uvance's revenue, which consists of standardized offerings.

Q2: ***The adjusted operating loss for Intersegment Eliminations and Corporate was 48.5 billion yen in the first half of fiscal 2023. Taking into consideration that your full-year financial forecast for fiscal 2023 shows an adjusted operating loss of 74.0 billion yen for the segment, you are forecasting that the absolute value of the segment's losses will decrease significantly in the second half of the fiscal year compared to the first. What is the probability of this happening?***

A2: I understand that the losses in the Intersegment Eliminations and Corporate segment in the first half were large. Results in the Intersegment Eliminations and Corporate segment are burdened by heavy investments in medium-term advanced R&D, such as AI, quantum computing, and CPU development for next-generation data centers, as well as the OneFujitsu Program, which is our internal enterprise resource planning program. Regarding the balance between the first half and second half of fiscal 2023, the ratio of money used for investments will be less in the second half of the year.

Q3: ***Did the strong financial results for the second quarter exceed your internal expectations? Or were they in line with your assessments? Also, please share with us your assessments for the second half of fiscal 2023 as well.***

A3: We are progressing in line with our forecast. The growth in orders will slow down slightly in the second half of the fiscal year, but this is a pull-back from the strong amount of orders we received in the second half of the previous fiscal year. Orders from major enterprise customers in the second half of the year are forecasted to vary by business area and include some areas that we forecast will do even better than the favorable amount that we received the previous fiscal year, but our overall feeling is that orders will gradually weaken. On the other hand, for revenue growth in the second half of the fiscal year, the orders that piled up through the end of the first half of the year will be converted into revenue. That's why we forecast that, at the very least, our current momentum will not weaken in the second half of the year. It may not reach several billions of yen, but we anticipate a revenue increase of 8-9%.

Questioner E

Q1: ***Please explain the reason behind the change in adjusted operating profit for Service Solutions shown on slide 8. The slide shows an improvement in profitability of 19.3 billion yen, but could you please break down the reason behind the change a bit further? In particular, please tell us how both the financial impact of increased personnel expenses and price increases are factored into this amount. Also, how much of a financial impact do you anticipate the increase in personnel expenses will have on your consolidated profit and loss for fiscal 2023?***

A1: Increased personnel expenses will have a negative impact of 20.0-30.0 billion yen on our consolidated operating profit in fiscal 2023, primarily in Japan. Consequently, this had a negative impact of 10.0-15.0 billion yen in the first half of the year. Of course, the financial impact of the increased personnel expenses is spread across each segment, but in terms of personnel composition, Service Solutions will be the most affected. On the other hand, I would like for you to understand that, as I mentioned earlier, in the first half of the fiscal year, there was an increase in profit because we raised prices, and that level of higher profit essentially offset these higher personnel expenses. Due to this, I would like for you to understand that the majority of the 19.3 billion yen figure was achieved by improving profitability through our usual activities, such as utilizing our Global Delivery Centers, which are our offshoring locations, and curbing unprofitable projects.

Q2: ***I have a question about your shareholder returns. You previously mentioned that the amount of shareholder returns could increase or decrease from year to year. You are planning to return 60.0 billion yen to shareholders based on your total cash flow over the next three years, but what progress have you made toward doing so to date, and what do you anticipate going forward? Including the downward revision of your free cash flow for fiscal 2023, are you currently in-line with your expectations?***

A2: We factored in the risk that Shinko Electric may fall short of our previous projections into our operating profit forecast. In accordance with this, we have also revised our free cash flow downward. So in that sense, it was not in line with our expectations. As I just mentioned, in the first half of the fiscal year, Shinko Electric's operating profit was several billions of yen short of what we expected, and that, of course, had a negative impact on our cash flow. On the other hand, besides this, the cash flows generated from Service Solutions and Hardware Solutions are progressing in line with our expectations. Revenue is also solidly expending and as there have been no special changes in our business structure that would change the speed at which we can collect revenue, our working capital is improving. We believe that Device Solutions, despite its recent downward revision, will have a solid recovery in the long term. In that sense, we do not believe this will cause a significant enough impact to change the cash flow that is the basis of our three-year capital allocation plan. Due to this, if you exclude the delayed recovery of Device Solutions, then we are currently in line with our expectations.

<u>Questioner F</u>

Q1: In the first half, the operating loss posted in Intersegment Eliminations and Corporate, at 48.5 billion yen, was quite large, but are you still projecting a loss of 74.0 billion yen for the full year?

A1: In the first half, we made large investments in such areas as the OneFujitsu Program, so the pattern of spending was slightly unbalanced with the second half. On top of that, because revenue was strong, our consolidation adjustments were large, and the balance of inventory assets has been growing from the previous year, so unrealized gains and losses in the first half were slightly higher. There will be an improvement in unrealized gains and losses in the second half, so we expect the operating loss for Intersegment Eliminations and Corporate to be 74.0 billion yen, as projected.

Q2: For Service Solutions, you did not change your full-year forecast. Is that because that was your determination after reviewing current conditions, such as the status of orders, or is the reason you did not change it because the outlook is not yet clear?

A2: It is the former reason. After thoroughly considering the performance of Service Solutions, we felt we could fully meet our forecast. On the other hand, Device Solutions is an area in which demand is hard to read, but we revised our forecast down by the amount actual volumes have fallen, and it is now at a level that we can achieve.