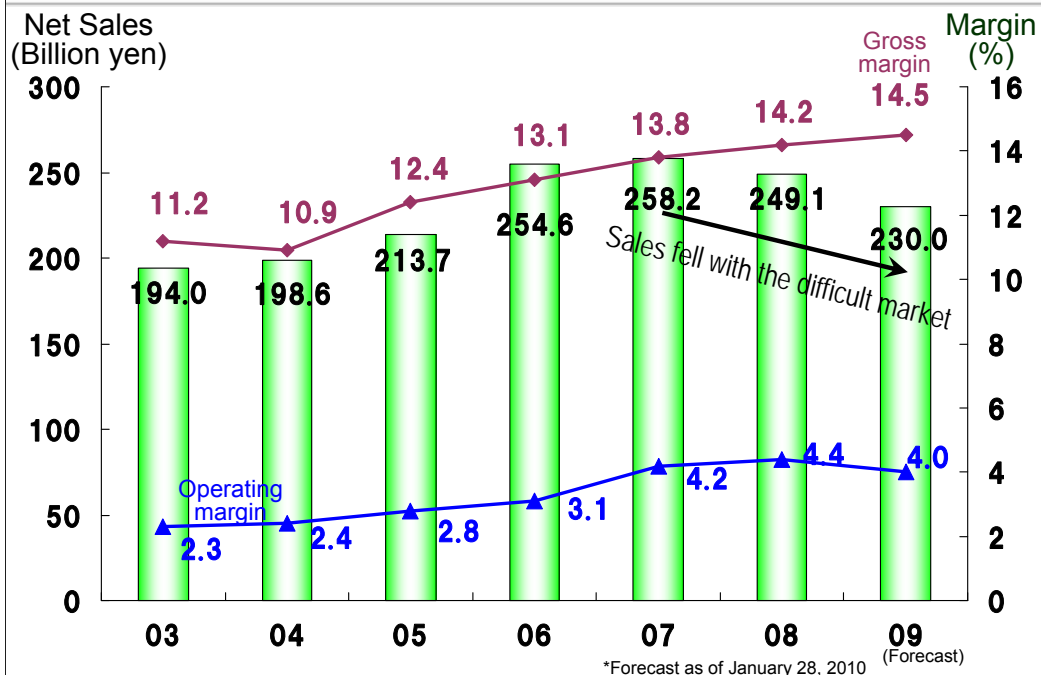


Management Innovation AC-I⁺ Activity

February 17, 2010
Masahiko Yamamoto, President
NEC Networks & System Integration Corporation

As explained in the financial results briefing, we are currently focusing on the Company-wide AC-I+ Activity (All Cost & Management Innovation Plus). Today, I would like to provide a summary of this activity and talk about its direction.

Performance Trends of NEC NW&SI



Before I do that, please let me review the performance trends of the Company in recent years.

Looking back on the trends from FY2003 to FY2009, the gross margin and the operating margin in FY2003 and FY2004 were both low, with the gross margin at 10% to 11%, and the operating margin just over 2%. The operating margin held steady, but the gross margin, which is the basis of the operating margin, worsened during the period. Sales did not grow.

Start of Management Innovation

Two issues before FY2004

- Weak profitability
- Low sales growth

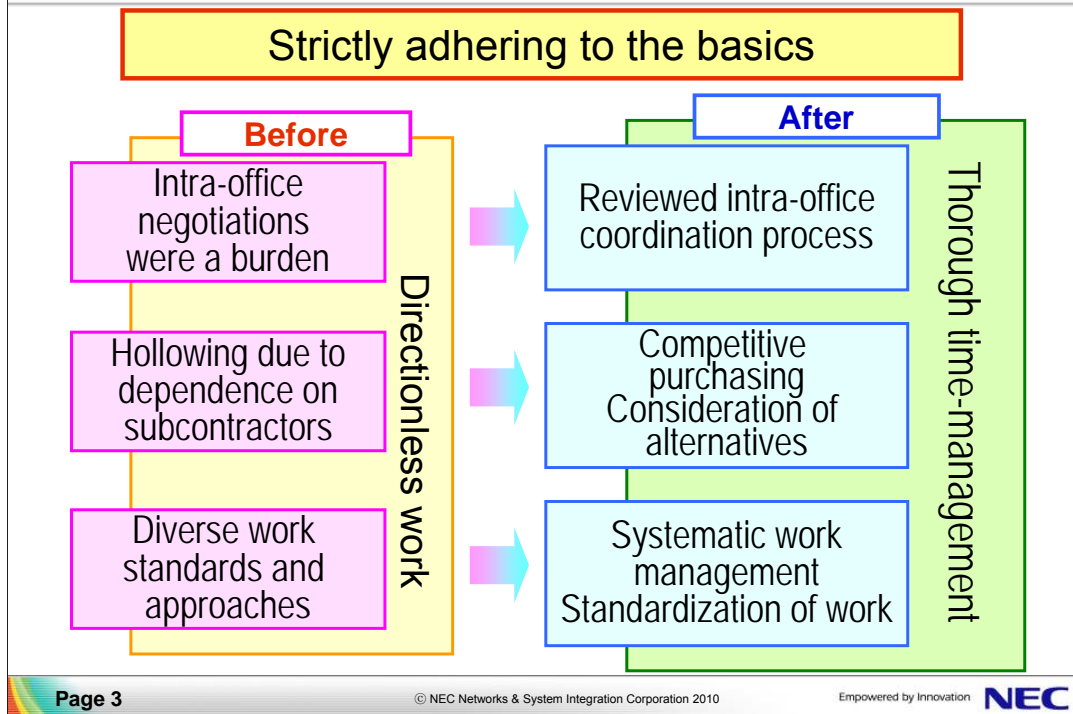


Started management innovation to overturn the status quo in FY2004 with the name of:

“All Cost & Management Innovation (AC-I)”

To reverse this situation, the former president Yukihiro Baba introduced a series of management innovations named All Cost & Management Innovation, or AC-I Activity. Mr. Kihara, then senior executive vice president, was appointed to lead the activity.

Early Stages of AC-I (1st Phase)



When the AC-I Activity began, the basics were not in place in processes. For example, intra-office negotiations were time-consuming. There was a hollowing-out of the Company as a result of leaving operations up to subcontractors, with diverse work standards and approaches depending on individuals. I believe that these tendencies were seen not only in the Company but in Japanese companies in general, during a period in which manufacturing was transferred to China and domestic manufacturing was in collapse.

We then got back to the basics. We reviewed the intra-office coordination process. To correct the dependence on subcontractors, we developed rules on competitive purchasing and the consideration of alternatives and bolstered the sourcing capability of the supplies division, which actually did the sourcing. We also shared the expertise of individuals and promoted systematic work management and the sharing and standardization of work. We eradicated directionless work through comprehensive time management. We strictly adhered to the basics in a top-down approach, based on the firm belief of the then management.

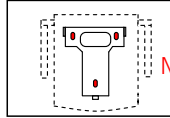
An Example of Onsite Ingenuity

Labor reduction by antenna mount creation

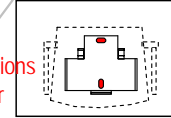
● Problem

Variations in antenna shapes among different types prevented the use of same antenna mounts

(Old type)



(New type)



Need to change mounts

Numbers & locations of holes differ

● Solution

● Previously

Locations for holes are changed

Drill on walls for new mount
Fix the old drill holes afterwards

Work needed to be done on weekends due to drill sound
Support worker for drilling on steps required

● New way

Holes in the same location can be used with a supplementary mount

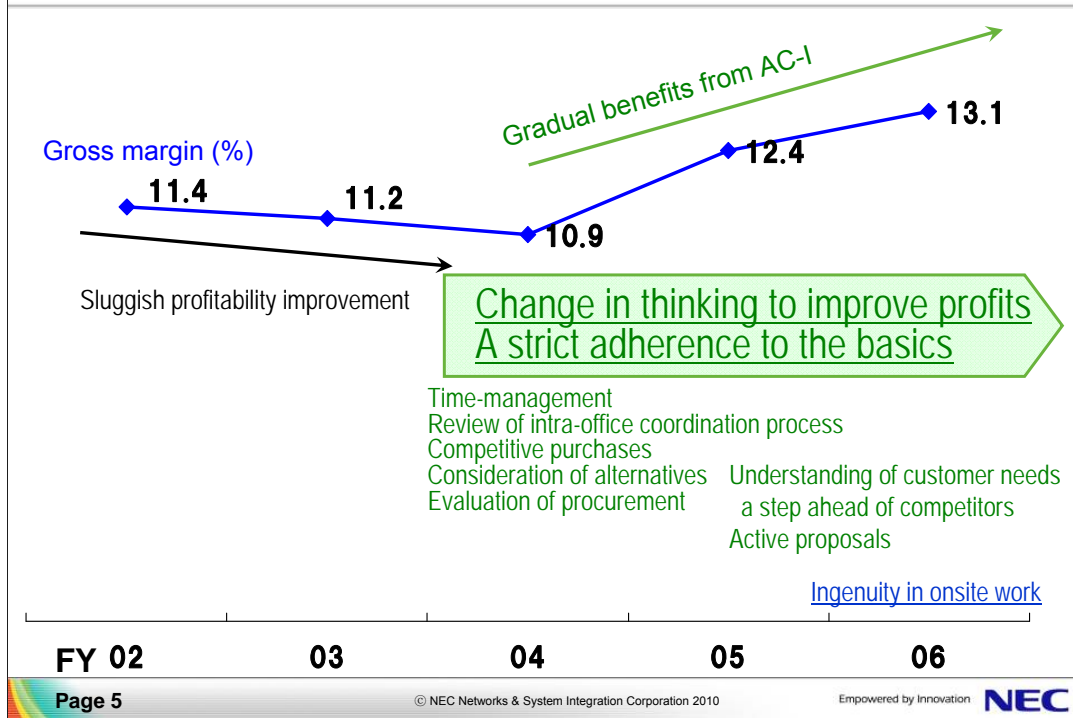
No drilling work
Weekday work

Reduction of workers
Efficient schedule

Supplementary mount

While returning to the basics, we recommended a number of onsite innovations, in stages. Let me introduce an example of that. As shown in the slides, there were old and new types of PHS antenna mounts, and each type had holes in different positions. Consequently, each time a PHS antenna was installed, we drilled holes in the wall, roof, and ceiling. We then invented a supplementary mount to make drilling holes unnecessary and improve work efficiency. As in this example, onsite innovations gradually emerged.

AC-I Activity (1st Phase)



Reflecting the attitude of sticking to the basics and establishing an awareness of profits through the AC-I Activity, the gross margin improved gradually after FY2004, when the activity began.

Results & Limits of the AC-I 1st Phase

Thorough adherence to basics enforced by senior management

Result 1: Profitability improvement (reduction of profit drain)
(cost cutting commitment throughout the company)

Result 2: Commitment to improving onsite work
(Ingenuity in methods, devices and working process)

But → Independent improvements will not lead to big results

Advance to systematic activity with stronger management

**to AC-I 2nd Phase
(AC-I⁺ activity)**

I believe the improvement in gross margin is attributable to a Company-wide commitment to cost cutting by adhering to the basics in the AC-I Activity, especially to the curbing of expenses. Costs stemming from operations left to subcontractors that could have been done internally and costs for corrections caused by poor arrangements were slashed. Reducing waste in the broad sense of the word brought improvements in profitability. Meanwhile, the AC-I Activity boosted improvements by bottom-up approaches such as onsite work and small-group activities.

However, although bottom-up activities enable reductions in waste, they have limits. Considering that we would not be able to advance further with bottom-up activities alone, we sought to make the AC-I Activity a larger reform involving management two years after I became president. That was the beginning of the second phase of the AC-I Activity.

To AC-I 2nd Phase (AC-I⁺)

To systemize voluntary onsite improvements for the company-wide stream

- To establish a PDCA cycle in each division
 - From one-shot improvements to continuous & organized improvement activities toward a target led by the heads of divisions
 - Promoting continuous improvement through innovation by senior management, such as the preparation of business infrastructure
- To create a company-wide organization and mechanism to support AC-I

*PDCA Cycle: A management cycle of "Plan-Do-Check-Act-Plan-Do-...")

The second phase began in 2007 and developed in earnest as Company-wide activities from 2008. We sought to systemize voluntary onsite improvements from the first phase into a Company-wide trend and to substantially change the Company's system and approaches to operations. To that end, we established a PDCA cycle in each division and changed the management method, which had tended to depend on bottom-up approaches. We encouraged continuous and organized improvement activities to achieve our targets, instead of one-shot improvements, appointing the heads of divisions to lead the activities. Meanwhile, we sought to promote continuous improvements through the top-down development of business infrastructure and bolstered the creation of a Company-wide organization and mechanism to advance the reform.

The limits of bottom-up activities are a challenge that the NEC Group faced when it introduced value engineering (VE) and zero defect (ZD) activities in the 20th century. Although bottom-up activities produced some results, they did not develop further. We reflect on the lack of initiative by the president, officers, and the heads of divisions to incorporate bottom-up activities into management from their perspectives. Based on this reflection, we changed the AC-I Activity in the second phase and included not only bottom-up activities but also top-down activities.

Three Pillars of AC-I

AC-I = All Cost & **Management** Innovation

- Through elimination of waste
- Expansion of added value
- Construction of a large, strong stream



No.1 cost competitiveness/SG&A efficiency
No.1 quality/TAT

No.1 customer satisfaction

In the phase 1, sticking to the basics was the key. In AC-I+, we are emphasizing the active participation of management and we are focusing on the complete elimination of waste, expansion of added value, and creation of a large, strong, and managed stream across the board. As a result, we aim to achieve number-one customer satisfaction through number-one cost competitiveness, SG&A efficiency, and quality and turnaround time.

We improved the bottom line, or the gross margin, in the first phase. In contrast, reinforcing the growth dynamic in the top line is our major goal in the second phase. Bolstering our growth potential is an important management target for the Company, and we need to clearly seek that in the AC-I Activity. To that end, the important point is, I believe, to develop the AC-I Activity into activities designed to deliver top customer satisfaction. I would like to use the AC-I Activity to enhance our growth potential.

Three Pillars of AC-I (2)

1. Comprehensive elimination of waste

- Improvements in work efficiency with stronger time management
- Daily improvement of work preparation and processes
- Comprehensive review of waste cost, space, etc.

2. Expansion of added value

- Absorption of added value (= money) draining from the company
- Creation of new value

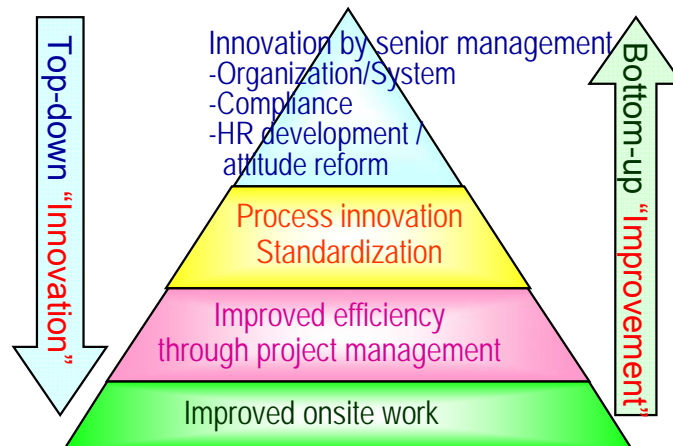
Of the three pillars of AC-I, the thorough elimination of waste, the first pillar, means bolstering time management, enhancing work efficiency, and improving work arrangements and procedures on a day-to-day basis. We are comprehensively reviewing unnecessary costs and space.

The second pillar is the expansion of added value. We are absorbing money, or added value, which is draining from the Company and thereby increasing the ratio of added value. In other words, we are creating new value.

Three Pillars of AC-I (3)

3. Construction of a large, strong stream

Construction of stream in both top-down and bottom-up directions

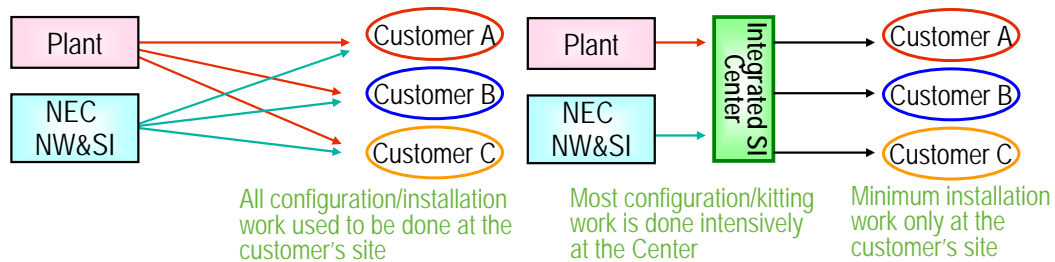


The third pillar is the construction of a large, strong stream. To create the stream, we need to promote not only bottom-up proposals for improvement but also top-down innovation and create more innovative reform, something that I see as the responsibility of management.

Mechanism for Organized Improvement (Integrated SI Center)

A paradigm shift from an onsite completion approach to a Integrated SI Center work system

- Improving working efficiency by minimizing onsite work
- Standardizing quality with an intensive work system

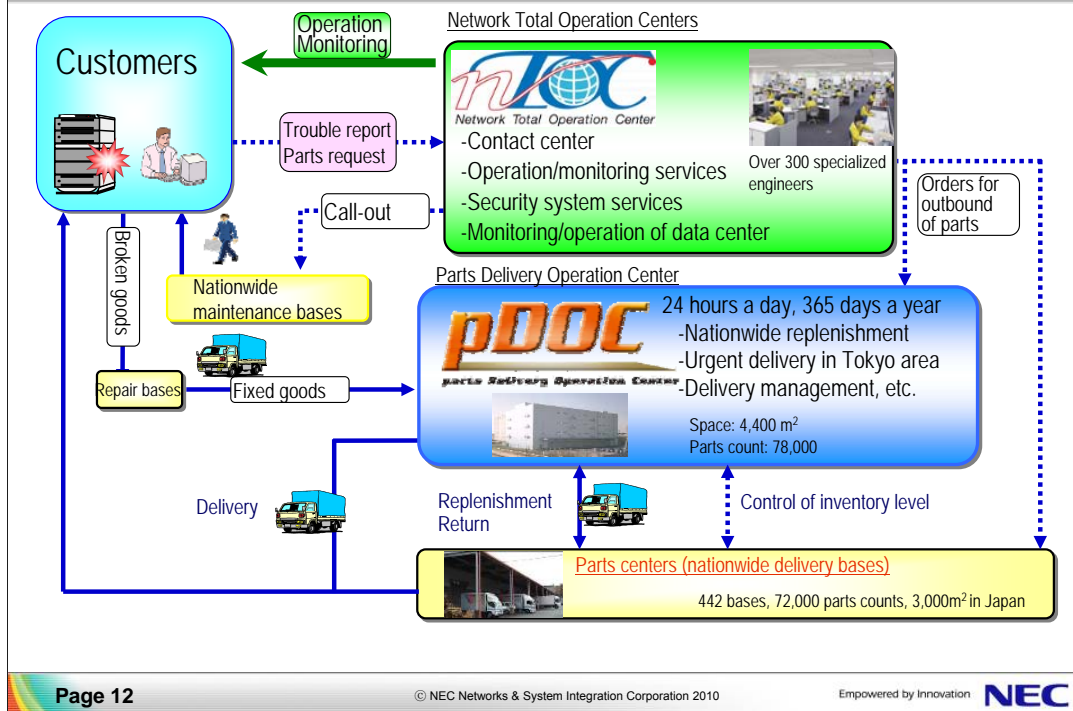


Production innovation at the Integrated SI Center as a plant Ingenuity/improvement of workbenches, returnable box and tools

- Further gains in work efficiency and quality

The Integrated SI Center is a concrete example of our efforts. In improvement activities at sites where IP telephony systems are installed, calls for reviewing the workflow increased, and the head of the division took the lead in making a specific change. Most of the work for building network systems was done at customer sites. Highly skilled system engineers and technicians carried in, set up, and installed equipment, and also conducted testing at each customer's site. Since the time of the delivery of equipment was unclear, engineers and technicians sometimes wasted time, waiting for the arrival of equipment. Supervisors at each site had the discretion to confirm basic arrangements, schedules, and work procedures, and the confirmation was not sufficient. In this situation there were errors and quality incidents. The Integrated SI Center is likened to the building of a house. There are very few carpenters seen on construction sites. Parts are made from housing materials at plants and are fit together at building sites. In the past, skilled carpenters cut and shaved wood on site, which was time-consuming and costly. However, with work at construction sites reduced, efficiency in the building of houses has been improving recently. We established the Integrated SI Center to realize the same idea. We are maximizing the transfer of work from customers' sites to the center. In so doing, we are eliminating waste and quality problems. We are checking work at the center or carrying out remote checking from the center. Naturally we have shortened work period and minimized customer inconvenience. As a result, customer satisfaction increased significantly.

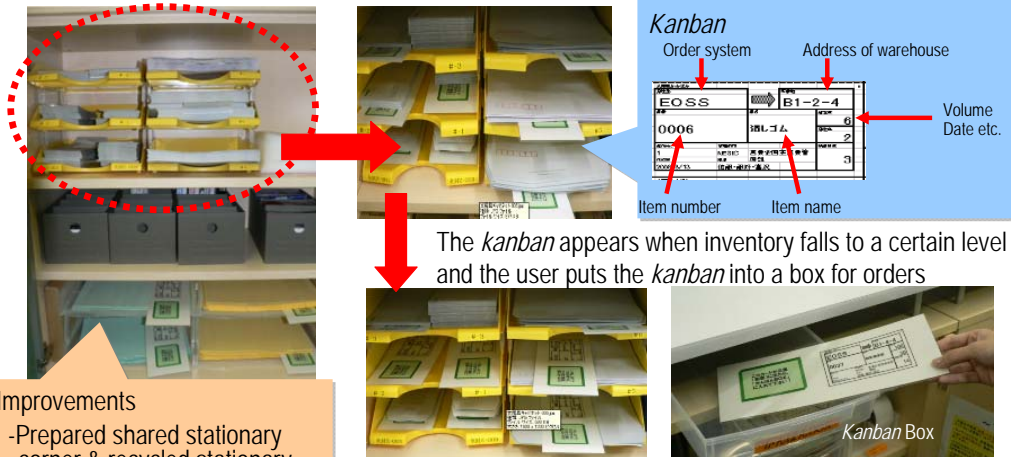
Mechanism for Organized Improvement (Service Business Platforms)



Another specific example of the AC-I Activity is in the service business. We have amalgamated our warehouses for equipment for maintenance and spare parts into one, and have set up a center called the Parts Delivery Operation Center (pDOC) for delivering maintenance equipment and spare parts. As a preliminary step, we also consolidated system operation functions such as call centers, which received calls from customers about the occurrence of trouble, and monitoring centers, which monitored the status of systems, and have established Network Total Operation Centers (nTOC). By establishing a common base for the monitoring function and troubleshooting function in our network, we have created a “large stream” of consolidated support services for customers. This is the second example of our AC-I Activity.

Example of Onsite Ingenuity (From single shot to continuous activity)

The *kanban* system of stationary



Improvements

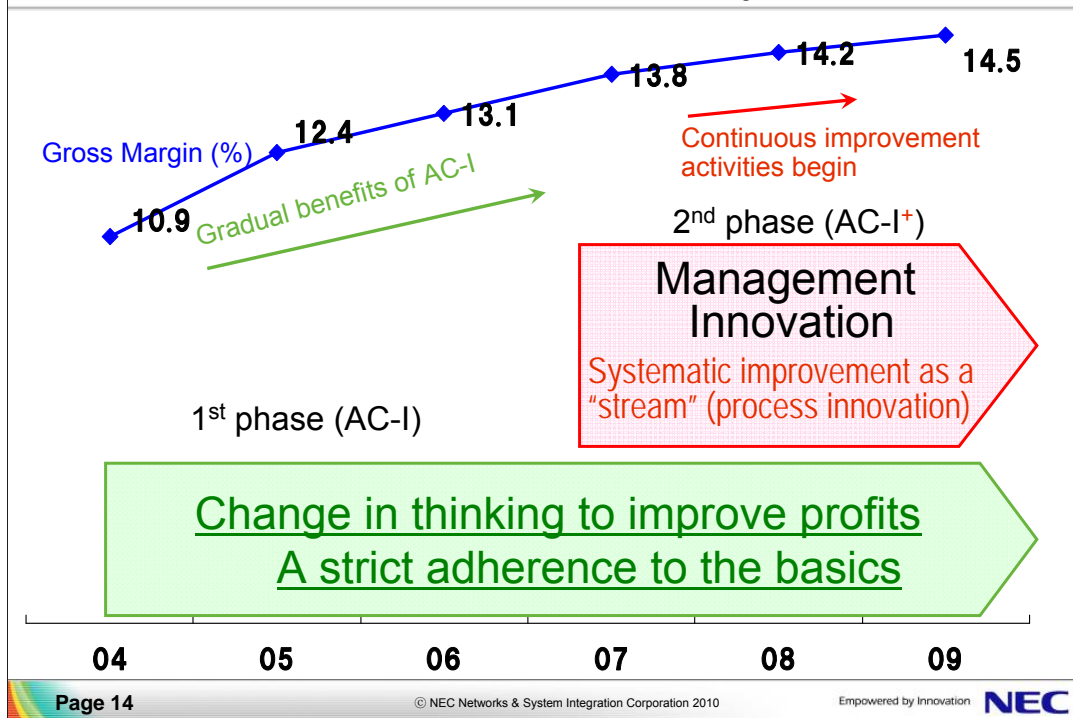
- Prepared shared stationary corner & recycled stationary corner
- Ingenuity for storage
- Reviewed inventory volume, etc.

Effects

Efficient clerical work, less space for inventory, etc.

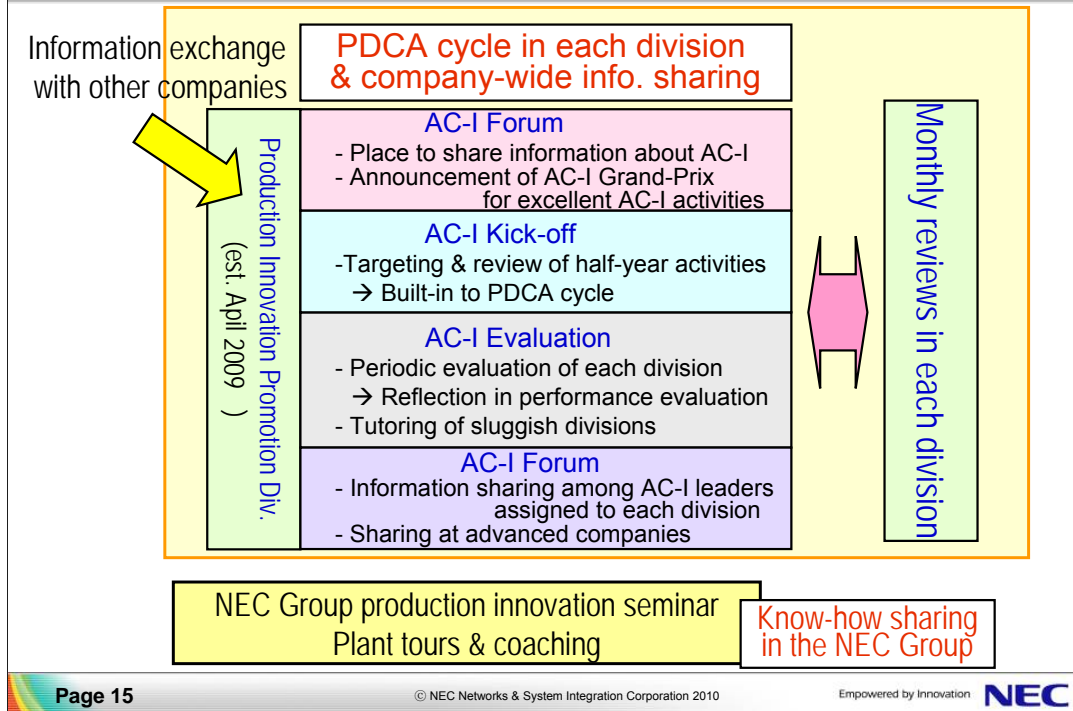
We are emphasizing the participation of all members in the AC-I Activity. Office workers are undertaking their own onsite innovations. For example, we have applied the *kanban* system to office supplies, previously dispersed, to organize them. Although the effect of the application has not been large in terms of money, I would like to emphasize that office workers, who were not involved in improvement activities, have begun to participate in the activities.

Current Status of AC-I⁺ Activity

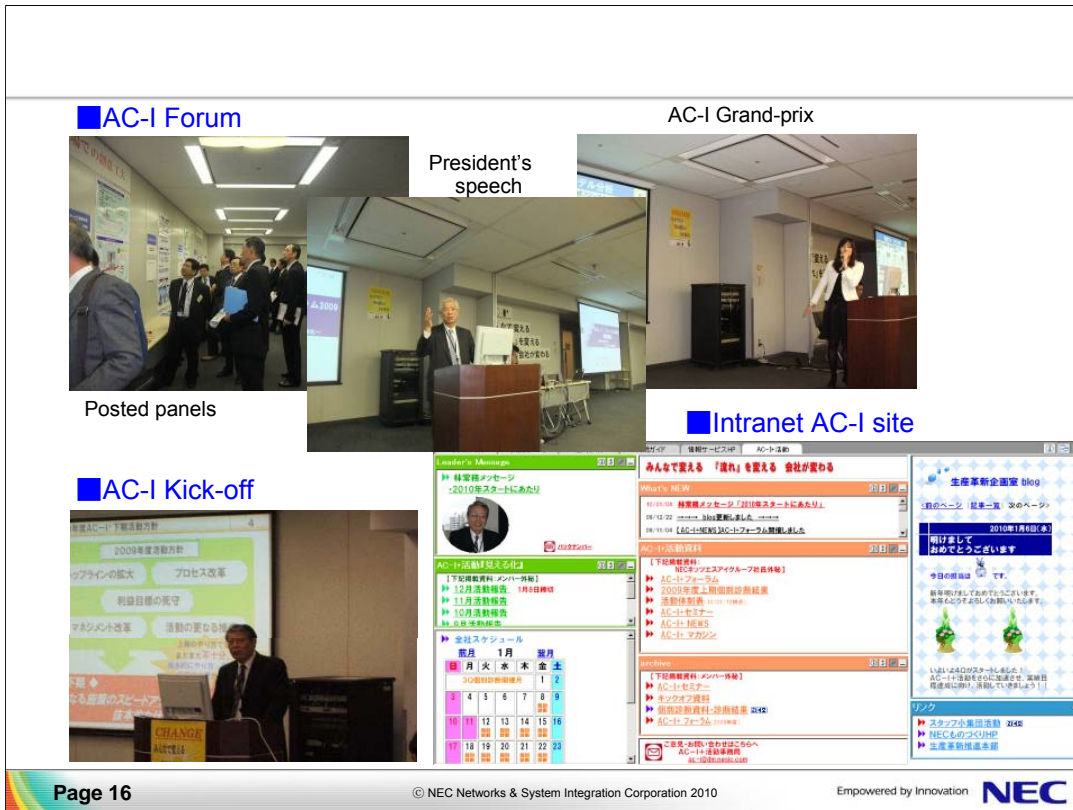


These efforts are the factors in the continuous improvement of the gross margin from FY2005 to FY2007.

Support System for AC-I⁺

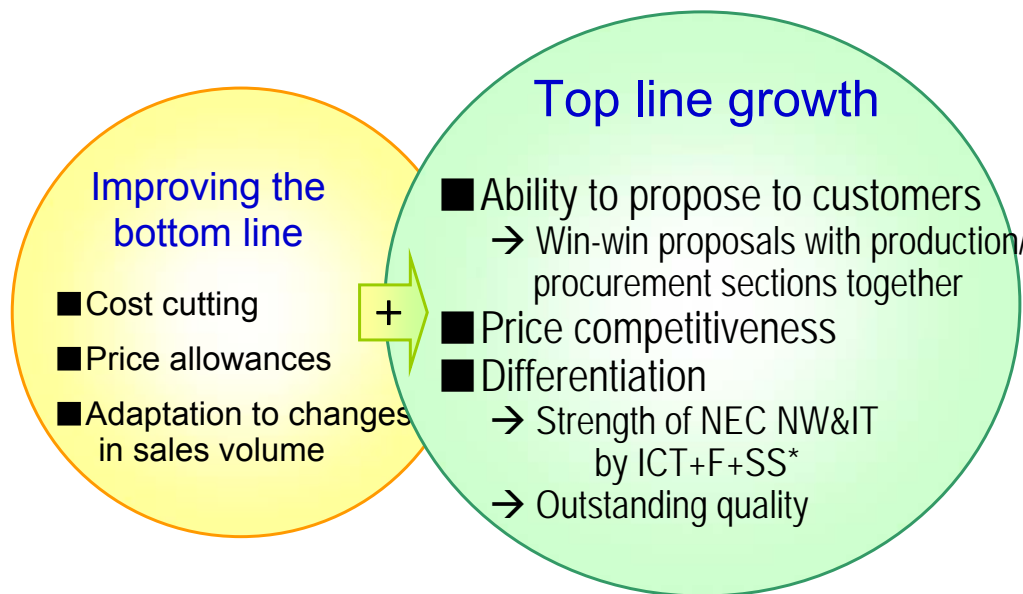


To bolster the Company-wide system, we established a Production Innovation Promotion Division in April 2009 as the driving force of the AC-I Activity. Each division reviews the progress of the AC-I Activity every month. The Production Innovation Promotion Division not only supports the reviews by each division but also promotes Company-wide activities including AC-I Forum, Kick-off, Evaluation, and Seminar. Another important role of the Production Innovation Promotion Division is to promote activities in collaboration with production innovation activities by the NEC Group. The Company members visit NEC plants to study their production innovation approaches. NEC members visit us to study our approaches. Through coordination within the Group, the scope of production innovation activities of the NEC Group has expanded.



These photos show activities in the Company. I always express my views to employees at AC-I Forums. The picture at the lower left shows Senior Vice President Yasuo Hayashi, who controls the AC-I Activity, giving a pep talk. The photo at the upper right shows another employee giving a presentation about her experience.

Moving Forward with AC-I⁺ (The top-line)

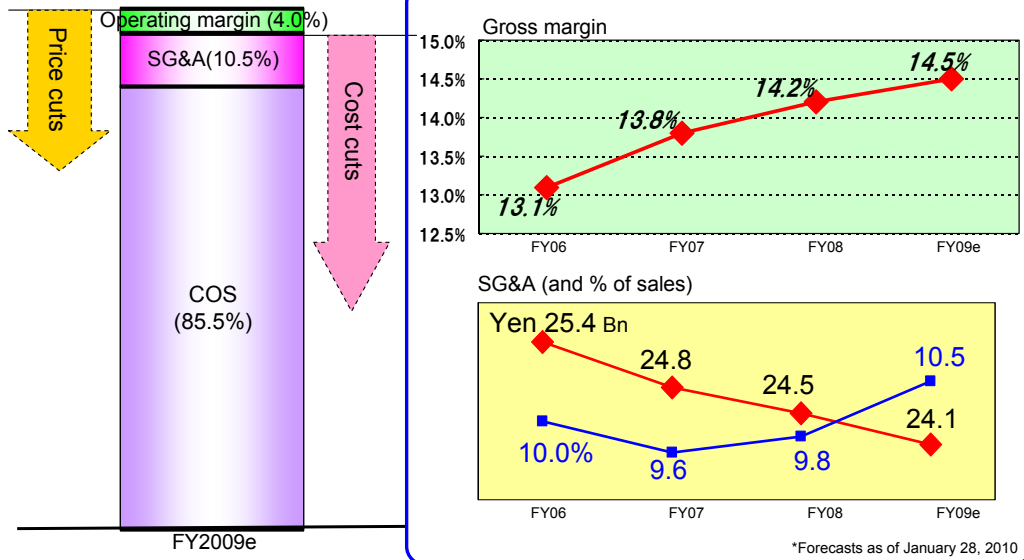


*F: Facility, SS: Support Services

As I have described, we have instilled the AC-I Activity as DNA into the core of the operations of the Company. I believe that awareness of the activity has spread to a considerable degree within the Company. We position the AC-I Activity, which was initially intended to boost the bottom line, as the driving force for the expansion of the top line, or the growth of the Company. Through the AC-I Activity, we will improve our business processes and will enhance our competitiveness by bolstering customer-oriented sales activities through stronger ties with customers, improving our ability to make proposals, sharpening our price competitiveness, and differentiating ourselves from our competitors.

Moving Forward with AC-I⁺ (Total cost reduction)

Total cost reduction with SG&A from gross margin improvement

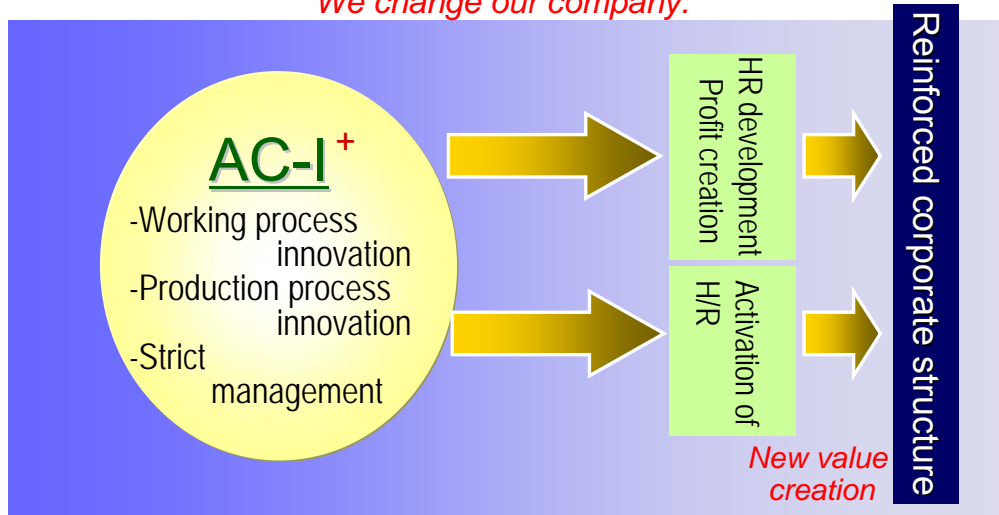


To improve earnings, we are seeking to reduce total costs, including selling, general and administrative expenses, as well as to improve the gross margin. Although the ratio of SG&A to sales will worsen in the current fiscal year, reflecting a fall in net sales, the amount of SG&A has been declining steadily. We will reduce it further.

Ultimately

AC-I for the DNA of NEC NW&SI

Our motto is: *"We all change. We change the stream.
We change our company."*



I hope to bolster the Company's strength by developing human resources, creating profits, and invigorating human resources through the AC-I Activity. We need to create new businesses, while developing our existing operations. To that end, the invigoration of human resources, by which I mean getting more out of people in the Company, is also important in addition to seeking human resources outside the Company. I would like to make the AC-I Activity the key to the strengthening of our corporate structure, for instance by developing our human resources so that we improve our ability to execute business.

Cautionary Statement

The results forecasts contained in this document are future estimates and are thus inclusive of risks and uncertainties since they are not based on definite facts. Please be aware that a variety of factors could cause actual results to differ materially from those projected. Major factors influencing actual results include the economic climate and social trends surrounding the business of the Group, changes in consumer preferences concerning the systems and services offered by the Group, as well as pressure to lower prices and the ability to succeed in an increasingly competitive market.

Factors affecting results are not limited to those described above.

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