

## TO OUR SHAREHOLDERS

### Business Performance in the Fiscal Year Ended December 2007

Consolidated sales for the fiscal year ended December 2007 increased 5.5% on the previous year to 3,826 yen billion. A difficult business environment prevailed as domestic oil demand continued to decline and product prices climbed due to sharp rises in crude oil prices. While our sales volume of kerosene and fuel oil fell, we took in measures to boost sales by meeting customers' needs and we increased our market share of gasoline sales as well as our sales volume by 3% year-on-year. In the area of profit, inventory valuation effects were significant, and consolidated operating income rose to 88.8 yen billion, an increase of 19.5% in comparison with the previous year. Moreover, consolidated ordinary income rose to 92.7 yen billion mainly due to an improvement of 2 yen billion in gains/losses on foreign exchange translations. Inventory valuation effects excluded, crude oil price increases that could not be passed on to retail prices had a significant effect on worsening our margin and the consolidated operating income on a current cost of supply basis (CCS basis) fell 14.3 yen billion from the previous term to 40.3 yen billion and consolidated ordinary income on a CCS basis fell 13.8 yen billion from the previous term to 44.2 yen billion. Furthermore, there was a year-on-year decrease of 104 yen billion in sales in the international trading business due to the transfer of this business, which sells oil products and other products, and is subject to consolidation in the Shell Group from August. However, the business is structured so that earnings will be stably recovered as business licensing fees, and the change will have little effect on overall Showa Shell earnings.

The Showa Shell Group posted net extraordinary losses of 14.1 yen billion for the term. Despite gains on asset sales accompanying the disposal of idle assets, losses accompanying the disposal of assets, including oil storage facilities, at affiliates and impairment losses accompanying a contraction in the power business of our consolidated subsidiary On-site Power brought extraordinary items to a net loss. As a result of the above, consolidated net income for the year under review came to 43.7 yen billion, down by 5.4% from the previous year.

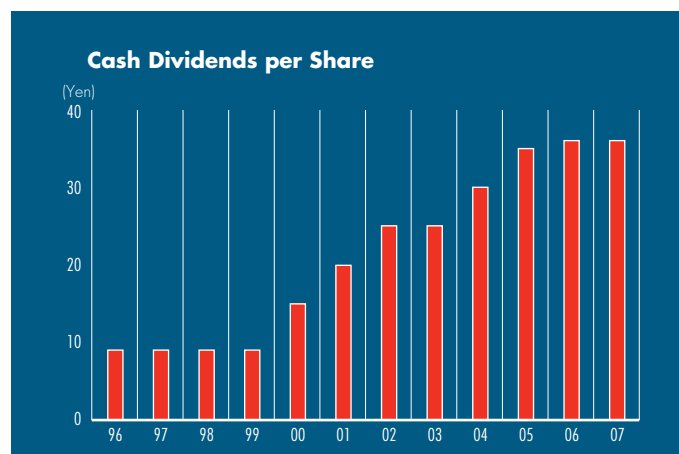
### Enhancing Shareholder Value

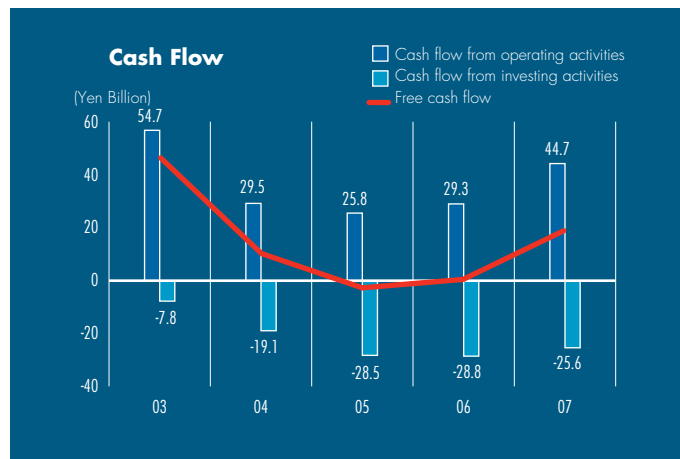
Demand for oil in the domestic market is expected to fall due to factors such as improvement in fuel efficiency, energy savings, and a switch to alternative energies. However, we at Showa Shell have our sights set on a course of growth which includes diversification in other energy areas apart from the oil business in addition to our existing oil product sales business in Japan and overseas. On this basis, we plan to optimize our corporate value through mid-term to long-term growth. To achieve this, we will direct our resources to expanding our retail sales channels and to new businesses such as CIS solar powered cells. We also plan to allocate resources to growth investments to expand our export facilities and enhance the reliability of our refineries.

Our fundamental policy for returning profits to shareholders is to pay stable and attractive dividends taking into consideration factors such as business conditions, our financial position, and trends in the financial markets. For the fiscal year under review we have decided to pay year end dividends of 18 yen per share, making total annual dividends 36 yen when including interim dividends.

### Compliance and Corporate Social Responsibility

Considering the large responsibility to society companies have, we consider compliance and HSSE (health, safety, security, and environment) to be top priorities in our management. To improve transparency and efficiency in our management, we are building an internal control system with built-in check functions. Unfortunately, serious incidents





\*Free cash flow=Cash flow from operating activities+Cash flow from investing activities

involving quality problems occurred at service stations in 2006. After carefully reviewing these incidents, we decided to redouble our efforts at providing our customers with the best quality possible. Under the slogan "Quality First 2007" we set 2007 as the period for systematically establishing quality systems through promotion of the Initiative for Establishing an Accident-free System and Quality Improvement Initiative. In quality improvement, we deployed a Quality First 2007 campaign focusing on the identification of latent risks at every stage of the supply chain from production to sales, and the resolution of problems. We are also continuing our efforts during 2008 under the slogan "Safety and Quality First 2008." As measures to improve safety, we will promote special efforts in the following four areas as priority tasks for 2008: (1) strengthen human error prevention measures, (2) conduct thorough training for staff in affiliated companies, partner companies, and staff, (3) promote the thorough use of appropriate safety apparatus, and (4) reinforce accident prevention measures for trucks, sales personnel cars, and work cars. In addition, as two quality improvement tasks during 2008 we will: (1) continue to resolve issues in each division and engage in quality maintenance activities based on the PDCA (plan, do, check, act) cycle and, (2) promote product safety courses.

Moreover, as a company that views corporate social responsibility very seriously, we do not stop at providing society with a stable source of energy. We hold a range of activities such as the Showa Shell Environment Photo Contest, and the Project for Reforestation of the Mt. Fuji. Together with the Integrated Research System for Sustainability Science (IR3S), an educational-industrial collaborative organization, we also launched the "Energy Sustainability Forum" to investigate and develop sustainable energy strategies. Furthermore, we continue our efforts to expand our line of eco-friendly products and services such as our CIS solar powered cells "Solacis" and "Shell Eco Toyu."

## Tasks in 2008

To achieve our goals, we will continue to push forward with our efforts to strengthen our business. In procurement we will continue to promote optimal and flexible purchasing through cooperation with the Shell Group and Saudi Aramco. In production and supply, we will raise refinery utilization through stable and efficient operation and increase production volume of high value-added products. In domestic distribution, we will make efforts to strengthen competitiveness by enhancing the efficiency of our distribution network through the joint use of oil depots with other oil companies. At the same time, we will also continue to make efforts to boost sales by promoting self-service stations and accelerating the opening of new types of service stations in order to realize our growth strategy of customer expansion. In exports, we will focus on profitability and devote efforts to increase earnings opportunities that effectively utilize our international network by integrating operations with the Shell Group. In other businesses, we will direct our efforts to increasing business competitiveness aimed at growth in various areas. In the CIS solar powered cells business we will establish a sound business base at an early stage including the construction of a second plant for CIS solar powered cells. We will enter the paraxylene sector through a joint venture and in the LP gas business we will integrate our import operations with Sumitomo Corporation and establish a holding company under which the LP gas sales subsidiaries of both companies will be placed.

We at Showa Shell Sekiyu appreciate the understanding of our shareholders as we move ahead with these initiatives and we look forward to receiving your continued support in the future.

Haruyuki Niimi  
Chairman and Representative Director

Shigeya Kato  
Vice Chairman and Representative Director

Yasuo Murayama  
President and Representative Director