

Medium-Term Business Vision

“EPOCH 2010: Conquer the Change, Pioneer the Future”

Showa Shell is aiming for sustainable growth by responding to a changing business environment and moving quickly to execute strategies.

Q The economic climate as a whole changed tremendously in 2008. What was the year like for Showa Shell Sekiyu's oil business?

A In 2008, we worked hard to cope with the dramatic changes in our business environment. Crude oil price at first climbed relentlessly to a historic high by midyear, only to decline suddenly by the end of the year. The extent to which these massive short-term movements in crude oil prices would be accurately reflected to the market in product costs emerged as the year's biggest issue. In our accounts for financial year 2008, we posted a net loss of 16.2 billion yen. This primarily stemmed from applying the weighted-average method for inventory valuation. Consequently, when crude oil prices suddenly dropped in the second half of the year, our inventory value remained much higher than market prices, which caused the cost of sales to rise. If

we exclude this inventory valuation effect, in other words, if we look only on a Current Cost of Supply (CCS) basis, ordinary income actually rose slightly compared with that of the previous financial year.

Losses also arose from the fact that the rise in crude oil costs could not be fully reflected in sales prices. Nevertheless, we worked to enhance stable operation of our refineries, strengthen retail sales, and boost exports.

Q What is your perception of these market changes?

A There is a structural decline in demand for fuel oil. Fuel consumption is also decreasing, reflecting a move away from cars triggered by high gasoline prices and a growing consciousness among drivers of saving fuel. In Japan, demand from industry is also receding due to weak economic conditions. At the



Jun Arai
President and Representative Director

A handwritten signature in black ink, appearing to read 'Jun Arai', positioned below the printed name and title.

same time, the shift to natural gas and other types of fuel is gradually gaining ground in step with increased environmental awareness.

In this climate, Japan's oil products market is becoming increasingly globalized. Along with more vigorous product exports, the price differential between domestic and international oil products is becoming narrower.

The changes we see are not temporary. Rather, we recognize that the structural changes in our business environment are actually signs of a paradigm shift. To help Showa Shell respond swiftly to these structural changes, we have formulated a new growth strategy from a medium-term perspective, called "EPOCH 2010: Conquer the Change, Pioneer the Future." "EPOCH 2010" expresses our commitment to conquer the significantly changing epoch (era) by working together with members of the Showa Shell Group including employees, dealers and business partners with a new management team in the pursuit of achieving sustainable development.

Q What can you tell us about medium-term management issues and growth strategies for the oil business?

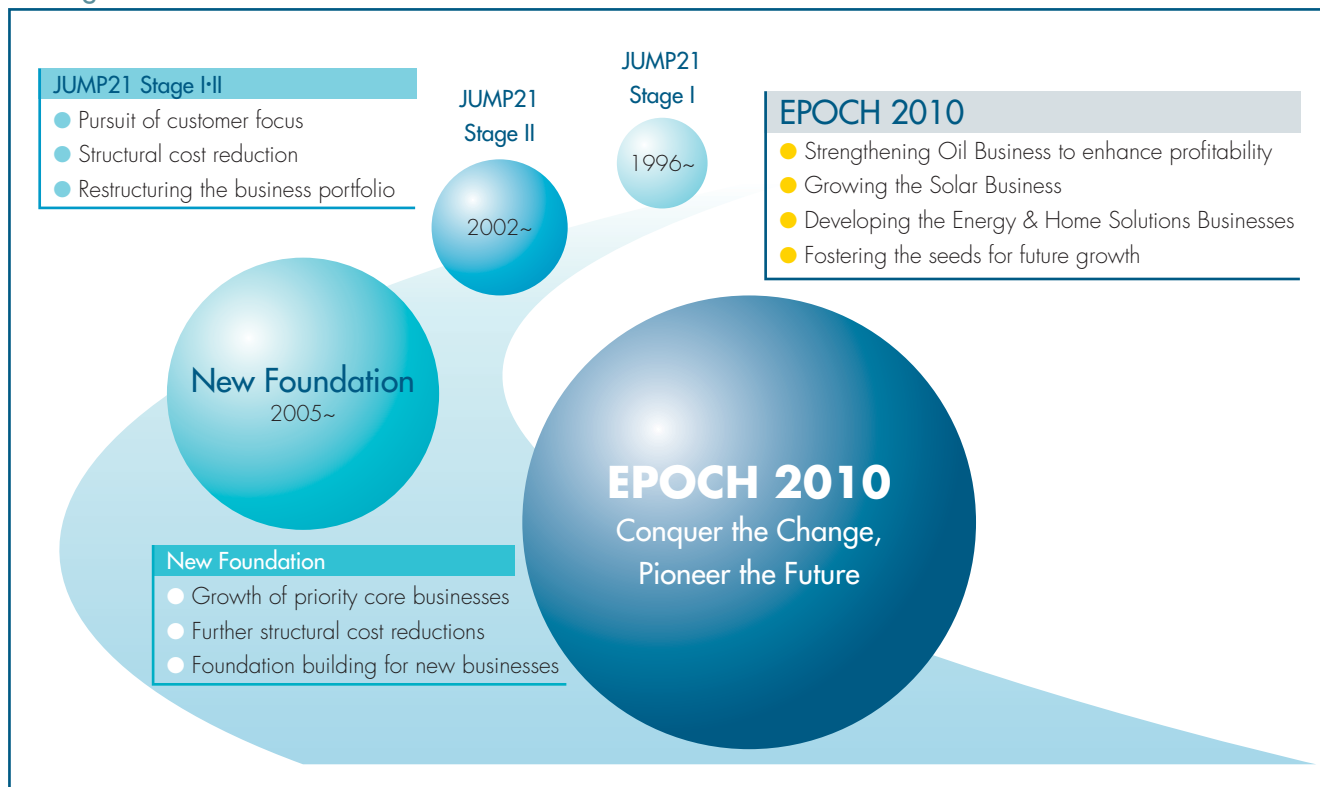
A We will continue to enhance the profitability of this business as a core operation. Measures to expand our customer base will be essential to realize the Company's sustainable growth.

Competitiveness throughout our supply chain from procurement through to sales is vital to maintain and reinforce the profitability of this business. However, given the structural changes in product demand that we currently see, we recognize that the strategic responses in our product supply and sales segment will be more critical than ever before.

> Response in Product Supply Segment

In product supply divisions, key issues to examine going forward are the effective utilization of existing refining facilities, and devising facilities to produce high-value-added products to be refined from low-priced crude oil. Meanwhile, pursuing production that is optimally matched to changing demand means ensuring operational flexibility. We will continue efforts to minimize lost earnings due to equipment trouble and work to enhance energy efficiency.

Aiming for Sustainable Growth



> Response in Sales Segment

In the sales segment to date, we have worked to upgrade and expand our service station network, as we focused on the retail sector based on “Dealerism”—our approach emphasizing our relationship with dealers. However, given declining domestic demand, raising the effectiveness of this network will be more vital now than ever before. While continuing the shift to self-service stations and the development of new service stations, we will also enact structural initiatives that will ultimately improve competitiveness on a per-station basis.

In sales of fuel oil, lubricants and other products for industrial users, we expect structural changes in industry in the coming years to bring changes in the needs of client companies. By supplying products with high added value in terms of environmental performance, energy efficiency and other benefits, we hope to satisfy customers and improve profits. From this standpoint, we will need to strengthen activities in our R&D divisions.

> Response in Product Exports

Product exports will also be indispensable to maintaining efficient refinery operations amid declining domestic demand, and we will export flexibly responding to international markets.

In 2008, we boosted our export facilities to double our export capacity. Moreover, we are gaining access to markets worldwide by utilizing the Shell Group’s global trading network, one of the largest trading networks in the world.

Q Next-generation CIS solar business is gaining a great deal of attention. What is your vision for this business?

A We completed a second plant in Miyazaki Prefecture, built as a follow-up to the stable production framework we established earlier with our first plant in the same prefecture. Also, we have conducted sales of solar modules, mostly in Europe, and they have been very well received. We believe we have succeeded in meeting customer needs by offering products of outstanding quality. In addition to an electric power buyback (feed-in tariff) system largely promoted in Europe, a variety of initiatives are also being formulated here in Japan, including the revival in 2009 of a subsidy scheme for installing solar power generation systems. In parallel, attention is turning to the expansion of future investments and grants for renewable energy in the United States as part of the “Green New Deal” legislation. This trend will likely accelerate efforts to put mechanisms in place for further promoting the spread of solar powered cells in Japan and abroad. A key issue for Showa Shell will be improving cost competitiveness and rapidly expanding business scale at the same time.

> Improving Cost Competitiveness

Next-generation CIS solar powered cells offer cost advantages in manufacturing processes and raw materials. Nevertheless, lowering the production costs per panel through further improvements in cost efficiency and reducing the initial investment required for plant facilities are critical to raising the global market profile of these products. For this reason, in March 2009, we established a research center in Atsugi, Kanagawa Prefecture dedicated to solar powered cells, where we have begun developing technologies for improving cost competitiveness, productivity, and conversion efficiency.



> Business Scale Expansion

Achieving business expansion at an early stage is another issue that must be addressed. We recognize that building a highly competitive supply chain such as early establishment of a mass production framework, achieving optimal market access, and ensuring a good distribution network is a key point in making this business successful.



Given the structural changes in the business environment, how do you intend to allocate management resources?



> Approach to Future Growth Investments

The management team has spent a great deal of time discussing the best method of allocating management resources to achieve sustainable growth. It will still be several years before business scale expansion in next-generation CIS solar business delivers earnings that can be channeled into the next round of investment. Therefore, in the short term, we must work extensively to raise efficiency in our oil business, devising structural reforms to increase profitability even further.

Over the medium- and long-term, our goal is to have a business framework underpinned by both the oil and next-generation CIS solar businesses, with both contributing to earnings. Taking changes in the business environment into account, our policy is to optimally allocate cash flows from both operations in ways that further promote their respective growth.

> Human Resource Allocation

We are enacting a new strategy for human resource allocation. In addition to appropriate allocation in oil operations, we opted in April 2009 to set up a new solar

business center as a more autonomous business entity to accelerate future business development.

> Optimal Asset Utilization

We will re-examine the best approaches for optimally utilizing our assets. In house, we set up a new Real Estate Business Division charged with reviewing real estate utilization company-wide.

For the low carbon society of the future, the products and services offered by Showa Shell will certainly grow more diverse. We are working on elements of the social infrastructure of a low-carbon society, such as our next-generation CIS solar cells, quick-charging equipment for electric vehicles, and stationary fuel cells. Going forward, we will examine specifically how we will combine these developments with Show Shell's assets and in what way we will deliver them to meet the needs of society.



What is your policy on returning profits to shareholders?



By expanding the next-generation CIS solar business, and carrying out aggressive growth investments to sustain and expand the customer base in our oil business, we are aiming for sustainable growth that will maximize our corporate value. We will strive to manage future cash flows from the business so as to maintain payment of a stable dividend at an attractive level to our shareholders, while ensuring we have the funds necessary for investment and strengthening our financial position. The ongoing understanding and support of our shareholders will be vital to this policy going forward.

Strategies in the Medium-Term Business Vision

