

## A Message from Management

We would like to begin our message in this year's annual report by expressing our deep appreciation to shareholders for their continued loyal support of our business activities.

Since commencing operations in 1905, Osaka Gas Co., Ltd. has fulfilled its crucial mission as a public utility supplying gas to the Kansai region while undertaking operations based on its "service first" corporate policy.

At present, Osaka Gas provides approximately 6.5 million customers in Osaka, Kyoto, and four surrounding prefectures with safe and reliable supplies of natural gas. While supplying natural gas—an environment-friendly fossil fuel that is abundantly available—we seek to maximize our corporate value through our involvement in a diverse range of business activities in both the upstream and downstream sectors of the energy field. These extensive activities encompass investment in natural gas production projects, ownership of a liquefied natural gas (LNG) carrier fleet, diversification into heat and power supply businesses, and participation in the liquefied petroleum gas (LPG) business as well as gas equipment sales. Moreover, we are also drawing on our management resources to carry out business activities in a broad array of other fields. For example, we are utilizing cryogenic energy from LNG to manufacture frozen foods as well as industrial gases. Osaka Gas is also active in housing, information and engineering-related businesses. Through these activities the Osaka Gas Group is playing a leading role in creating a better living environment and fostering the development of regional communities. At present, over 120 companies comprise the Osaka Gas Group, and the Group's consolidated annual sales exceed ¥970 billion.

### Long-Term Vision and Medium-Term Action Plan

In accordance with its "Vision 2010" long-term management guidelines, the Company will carry out "value-creation management" as a basic philosophy shared by the entire Osaka Gas Group. Under its Medium-Term Action Plan (from fiscal 2001 through 2003), which is the first step in realizing Vision 2010, to carry out value-creation management, Osaka Gas has promulgated goals it set for raising the Group's value for customers, shareholders, and society. Specifically, customer value goals have been set for gas rate levels, the diversification of rate options, and standards of service and safety. Shareholder value enhancement targets are based on

#### Shareholder Value Enhancement Targets under the Medium-Term Action Plan

##### 1. Income before income taxes

Consolidated (25-company basis): At least ¥75 billion in fiscal 2003

Non-Consolidated: At least ¥65 billion in fiscal 2003

##### 2. Net income

Consolidated: At least ¥40 billion in fiscal 2003

Non-Consolidated: At least ¥35 billion in fiscal 2003

##### 3. ROE

At least 9.0% at both the consolidated and non-consolidated levels in fiscal 2003

##### 4. ROA

At least 3.5% at both the consolidated and non-consolidated levels in fiscal 2003

##### 5. Free cash flows

Positive at both the consolidated and non-consolidated levels in fiscal 2001, and increasing thereafter

Note: Targets are as of February 2000 when the plan was formulated.



*(Left) Shin-ichiro Ryoki, Chairman (Right) Akio Nomura, President*

performance indicators, including income before income taxes, net income, ROE, ROA, and free cash flows. Social value goals encompass environmental behavior, social contribution, information disclosure, and compliance.

### **Achieving Goals of Medium-Term Action Plan Ahead of Schedule, and Management Plan for Fiscal 2003**

Our medium-term action plan has gotten off to a smooth start, and we are ahead of schedule for achieving the targets of the plan. In fiscal 2002, the second year of the plan, we implemented measures for allowing us to attain targets for fiscal 2003, the last year of the plan, one year earlier than planned. Despite a harsh environment that included an increasingly severe slump in consumption and higher-than-normal temperatures in winter, we have nearly attained our initial targets.

To maintain our price competitiveness amid intensifying competition among various types of energy due to ongoing deregulation and to pass on cost savings to our customers, in March 2003 we implemented a rate reduction that averaged 5.04%. Also, to redistribute profits to shareholders, in fiscal 2002 we retired 60 million shares of Company stock and also increased cash dividends per share by ¥1 to ¥6 per share.

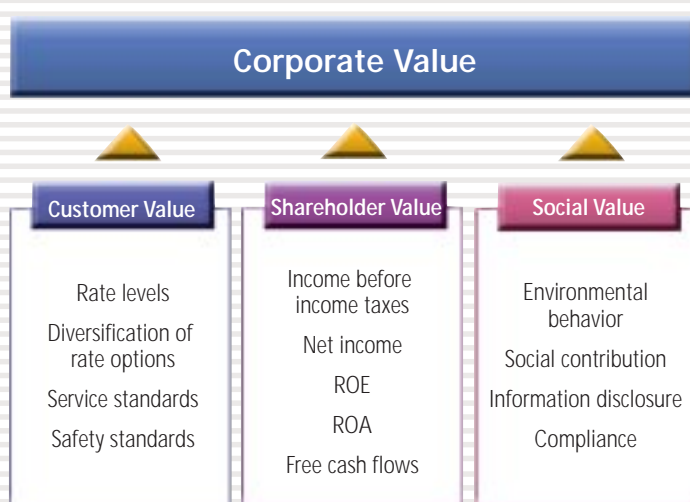
Our management policy in the current fiscal year focuses on achieving significant increases in our overall competitiveness, including those in price and non-price-related areas, to prevail amid an intensifying market competition, and to upgrade and expand our energy business. We will also strengthen our “federal management” system (quasi-holding company system) through the full-fledged introduction of shareholder’s value added (SVA), with each Group company posting a profit in terms of SVA.

**Targets and results for principal management indicators (figures in parentheses are non-consolidated)** Unit: ¥100 million, %

	Result for fiscal 2001	Target for fiscal 2002	Result for fiscal 2002	Target for fiscal 2003
Income before income taxes	¥638 (539)	¥720 (610)	¥759 (703)	¥650 (540)
Net income	360 (329)	430 (385)	394 (376)	380 (330)
ROE	8.0% (8.2%)	8.7% (9.0%)	8.4% (9.2%)	7.9% (7.8%)
ROA	2.9% (3.2%)	3.2% (3.5%)	3.1% (3.6%)	2.9% (3.0%)
Free cash flows	405 (372)	450 (335)	706 (673)	260 (215)
SVA	111 (123)	—	131 (157)	114 (118)

Notes: 1. Free cash flows = cash flows from operating activities – capital expenditures (operating profit after tax + depreciation expenses and other non-cash expenses)  
 2. The number of consolidated subsidiaries was 35 in fiscal 2001. The target for the number of consolidated subsidiaries in fiscal 2002 was 42, and the actual number was 43. The target for the number of consolidated subsidiaries in fiscal 2003 is 54.

**Osaka Gas Vision 2010 — Value Creation on Three Levels**



**SVA (Shareholder's Value Added)**

This indicator was introduced on a trial basis in fiscal 2002. Performance evaluations for organizations and groups within Osaka Gas were stated using SVA instead of operating income. SVA is calculated by subtracting creditors' and shareholders' anticipated returns on capital invested from after-tax operating income. It therefore represents the value added for shareholders. SVA is calculated using the weighted average cost of capital (WACC), which reflects the risk-adjusted anticipated rate of return. This means that shareholders' value added for each activity can be monitored more accurately, providing information that can be used to support a strategy of business selection and concentration.

$$SVA = NOPAT - (\text{interest-bearing liabilities} + \text{shareholders' equity}) \times WACC$$

NOPAT (Net operating profit after taxes) = Before-tax income before deduction of interest paid x (1 – effective tax rate)

**The Strengths of the Osaka Gas Group**

Amid a dramatically evolving business milieu, the Osaka Gas Group's strengths can be classified into the three areas outlined below. Utilizing these strengths, Osaka Gas aims to become a corporate group that is the first-choice of customers and investors in the energy industry, where competition is expected to intensify.

**1. Outstanding Financial Structure and Abundant Cash Flows**

Osaka Gas boasts a conspicuously low reliance on interest-bearing debt and has a high shareholders' equity ratio vis-à-vis other companies in the Japanese energy sector, particularly public utilities. This factor, coupled with a projected abundance of free cash flows over the medium term, will solidly position the Company to undertake forward investment in sectors such as the electric power business and overseas energy projects.

**2. Strong Bonds of Trust with Customers and Ability to Respond Accurately to Customer Needs through Solution Marketing**

Thanks to its advanced proposal-based solution marketing capabilities and high-level engineering and

maintenance capabilities, Osaka Gas is firmly positioned to respond accurately to customer needs. In addition the Osaka Gas Group has forged strong bonds of trust with its customers over many years.

### 3. Group Companies Achieving Growth

The companies comprising the Osaka Gas Group recorded net sales of ¥380.3 billion and income before income taxes of ¥15.2 billion in fiscal 2002 (according to a simple total of the results for all Group companies), which highlights the continued steady growth of these companies. The Osaka Group initially diversified into fields that offered significant synergies with its gas business. Today, an increasing number of Group companies are utilizing their core competencies in their respective industrial sectors. Osaka Gas has achieved greater diversification than any other energy-related company in Japan. Since embarking on diversification 20 years ago, Osaka Gas has also accumulated a wealth of knowledge and expertise as well as cultivated outstanding human resources, which are also an important Group strength. With an eye to the future, Osaka Gas will emphasize “selection and concentration” to utilize its core competencies, mainly through its core companies in each business field, thus raising its presence in these fields.


### In Closing: Meeting the Challenges Ahead

A principal issue in energy fields is the so-called “3E” challenge—achieving a balance among sustainable economic growth, environmental protection, and energy security. In electric power and gas businesses, deregulation and regulatory reforms are progressing with the aims of improving efficiency by encouraging competition and creating an open market environment where information is transparent. These changes are fueling a host of trends, chief among these an influx of new companies into the energy sector and the diversification of existing energy suppliers into other energy industries. Traditionally, the energy sector has been divided into separate industries, including electric power, gas, and heat. Today, however, these industries are merging to form a single energy market.

Players in this new market must go beyond merely supplying one form of energy. Instead, they must offer a one-stop energy-supply service, namely efficient integrated energy supply systems that optimally combine various types of energy. At the same, there are expectations that the creation of comprehensive energy-supply systems will contribute to environment protection, enhance urban functions, and create pleasant living spaces.

Osaka Gas aims to raise management ability and respond more flexibly to changes in the business environment. By doing so, we seek to realize a one-stop energy-supply service, establish a competitive advantage in terms of costs, efficiency, and consideration of the environment, and become a corporate group that is the first choice of customers.

We look forward to your continuing support.



*Shin-ichiro Ryoki, Chairman*



*Akio Nomura, President*