A Conversation with President Hirofumi Shibano

# Progress Toward Our Vision

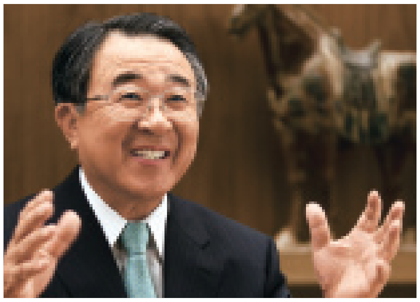
The Osaka Gas Group has finished the first year of Design 2008, the medium-term management plan of the Osaka Gas Group. The plan covers the period from the year ended March 2007 to the year ending March 2009.

The Osaka Gas Group will reap the fruits of further investments for growth made during the period of this plan, with the start of a major-scale electricity retail business in the year ending March 2010 using large electric power generation facilities, for example. Thus, the Osaka Gas Group will develop as a corporate group as it enters into an era of continued growth in the second century of its operations.

Q & A

## Q1

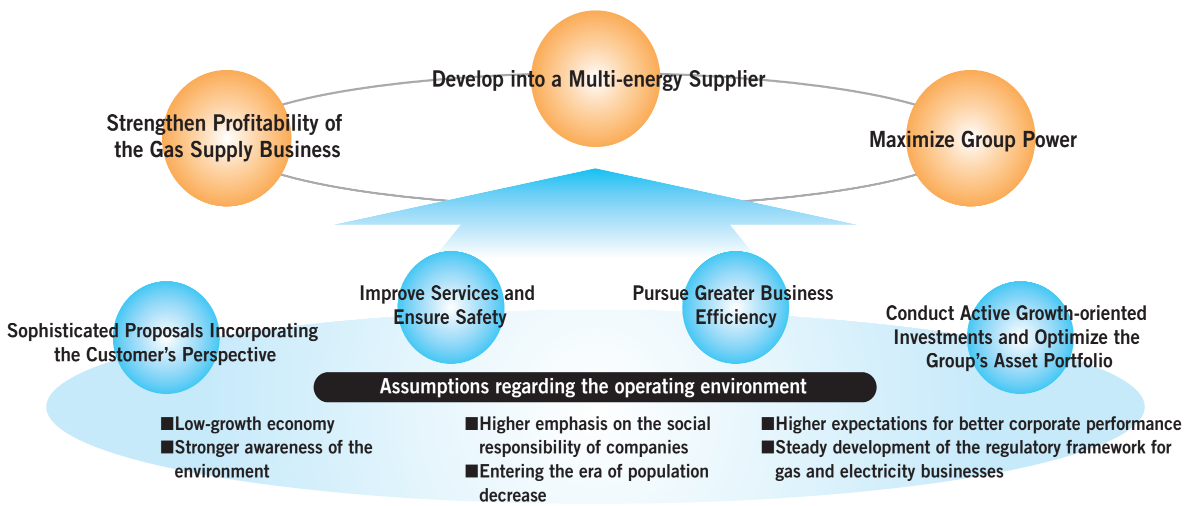
### What are your basic thoughts on Design 2008, the medium-term business plan that runs from fiscal 2007 through fiscal 2009?



From the viewpoint of management, we see these three years as a developmental period. Amid intensifying competition, we need to focus on growth-oriented investment in such projects as the Semboku Natural Gas Power Plant to establish the basis of a multi-energy supply business.

We also intend to surmount the competition in the gas supply business by bolstering our earning power. The key here is even greater management efficiency, with all of our efforts premised on offering innovative solutions tailored to our customers and improving services and assuring safety. We will also entrench our identity as a multi-energy supplier by further enhancing our Group strength through an aggressive growth-oriented investment strategy and the optimization of the Group's asset portfolio.

**Basic Overview of Medium-Term Business Plan (Fiscal 2007 to Fiscal 2009)**




## Q2

### What is this medium-term business plan's growth strategy?

Osaka Gas will continue to be an energy company based on natural gas, and our gas supply business will continue to be our major source of earnings. Considering the trend of lower growth of the economy of the Kansai region, the falling birth rate, and intensifying competition, however, there is a risk that concentrating only on the gas supply business could lower our chances of achieving sustained growth.

For Osaka Gas to achieve sustainable growth, we have to continually enhance our competitiveness in the gas supply business. Other urgent tasks required for sustained growth include our evolution into a multi-energy supplier by building new core businesses, such as full-scale development of the electric power business, geographic expansion of our energy business, and enlarging operations in advantageous non-energy fields. Design 2008 calls for growth-oriented investments totaling ¥256.0 billion. Including returns on previous growth-oriented investments, we are aiming to reach consolidated ordinary profit of ¥100.0 billion by the end of our current medium-term business plan.

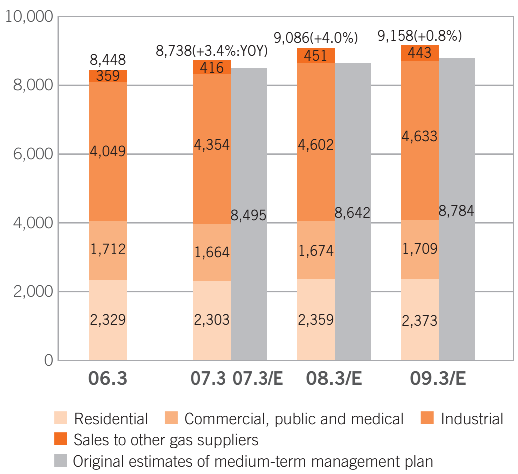
Attaining this profit goal will allow us to restrict the growth in our interest-bearing debt and continue to maintain a strong financial position as well as providing the funds needed to invest in further growth. By reaping the benefits of those investments, we will create a growth cycle that will be the basis for maintaining sustained expansion throughout our second century.

## Q3 What does the future hold for the core gas supply business?

The gas supply business will remain the core of our multi-energy supply business. Together with our Group companies and external business partners, we will address the various needs of our customers based on five core principles. We will propose solutions supported by technological and engineering prowess developed over many years. We will offer comfortable, convenient, safe and energy-efficient gas systems. We will make our rate schedule easier to use. The Group will supply customers with a wide range of products, including electricity, LPG, security services and Internet services, combined with a strong capability for providing services and proposing innovative solutions. We will thoroughly utilize our infrastructure assets, including pipeline networks, to serve customer needs. Additionally, we will find ways to cope with the population decrease in the Kansai region and the intense competition in the energy sector, all with the aim of achieving sustainable growth in our gas sales.

**Actual Gas Sales Volume and Outlook (Non-consolidated)**

(Million m³)



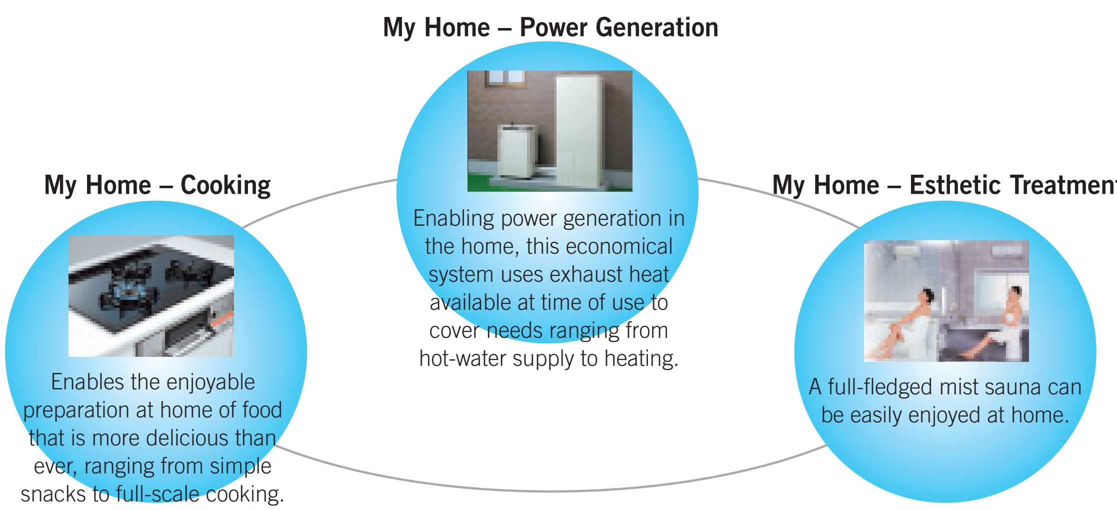
## Q4

**What is the future of gas sales in the domestic sector considering such factors as the falling population and the push for all-electric energy systems?**

Amid intensifying competition with all-electric systems for households, we are taking steps to get customers to recognize the advantages of gas and gas appliances. We are attracting customers by making sophisticated and innovative proposals that fully comprehend their needs. Our solutions include home-use power generation using ECOWILL, which is a residential-use gas cogeneration system, the mist sauna and advanced cooking appliances. Through these actions, we are promoting the increased proliferation and usage of products that are not only economical and environment-friendly, but also offer users upgraded lifestyles in terms of comfort, convenience, and safety.

Among other efforts to comprehensively meet the needs of customers, Osaka Gas offers I-rusu, an Internet-based home security service.

**Promotion of the Proliferation of the MYHOME 3 Culture**




## Q5

**How is the surge in crude oil prices affecting gas sales in non-residential gas fields, including the industrial and commercial sectors?**

The purchase price of LNG based on long-term contracts is linked to the price of crude oil. However, when crude oil prices rise sharply, comparable price increases are moderated by agreement with the sellers. Consequently, natural gas prices offer a comparative advantage in phases of surging crude oil prices. Additionally, customers enjoy environmental benefits of natural gas compared with other petroleum-based fuels. Against this backdrop, gas sales to the non-residential sector have increased markedly in recent years.

We plan to achieve sustained growth in our energy businesses by differentiating ourselves in the market through our proven record in sophisticated natural gas utilization technologies. We also will apply our “Only One Business Model,” which offers individual customers an optimum energy solution. To provide that solution, the model combines multi-energy supplies of natural gas, electricity, liquefied petroleum gas (LPG), and others; an Eco Wave energy service utilizing advanced financial management technologies; and an energy management service featuring IT-enabled remote monitoring systems.

## Q6 What is the impetus for the Group’s activities in the multi-energy supply business, especially electric power?

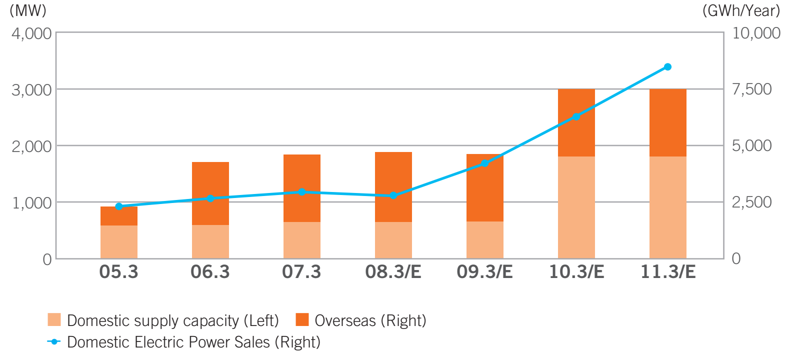
As a Group, we believe that the gas supply business alone will be insufficient to meet our stakeholders’ expectations of growth in corporate value under the current economic conditions in Japan. For that reason, we are aiming to create a multi-energy supply business, including electricity, to drive the Group’s future growth.

We have amassed a great deal of know-how about the energy industry through our sales of gas and gas appliance systems over the years. This knowledge means we are able to provide full-line consulting services to our customers regarding all their energy needs, including electricity. Moreover, we intend to own highly competitive electric power generation facilities in the future. Combining competitive electricity supply with our gas facilities will enable us to provide customers with comprehensive energy services, affording the Osaka Gas Group a competitive advantage in the energy sector. We view this as our main strength in the energy business.

Against this backdrop, we are pushing ahead with full-scale development of the electricity business as shown below. In conjunction with this full-fledged development of the electricity retail business, we will offer customers the best energy mix for their needs: gas, electricity generated by gas cogeneration systems, or electricity. In this way, we will accelerate a dual approach to growth based on the gas supply and electric power businesses.

We envisage the scale of our overall electricity business around 2010 to be approximately 1,800 megawatts in the domestic IPP and generation business, or about 3,000 megawatts when combined with other overseas IPP capacity. Our annual electricity sales in the domestic market will be about 8,500 million kWh, yielding an ordinary profit of ¥10 billion.

**Projected Electric Power Procurement and Sales Volume**



## Q7

### How is the multi-energy business envisioned in terms of business fields?

There are two main fields. One field is areas that will contribute to the medium to long-term growth of our domestic energy business, such as the domestic electricity retail business or expansion of our natural gas business. The other field comprises overseas independent power producers (IPPs) or upstream interests in energy development that could be expected to quickly contribute to consolidated profits.

Irrespective of domestic or overseas, decision-making regarding investment is based on uniform criteria. Also, investment in overseas targets is focused on ensuring stable cashflow and controlling risks. In acquiring interest in gas/oil assets, our shareholding is limited to minority interest. For overseas IPPs, risks are constrained through long-term contracts.

## Q8

### What is the reason for expanding the upstream natural gas business?

In the international LNG market, we expect the supply-demand balance to remain tight. Consequently, we plan to secure a stable supply of LNG for the Osaka Gas Group and reduce our LNG procurement costs, as well as use our accumulated know-how and networking assets to expand earnings. We will achieve this by proactively entering upstream businesses.

In our gas and oil production businesses, we are pushing ahead with preparations to commercialize the operations of the Greater Sunrise Gas Field and other fields in which we have acquired interests. We will also continue to seek proactive development, including participation in LNG projects. These investments will contribute to stabilizing our supply, to natural hedging of our risks by achieving a balance between our upstream and downstream businesses, and to growth in consolidated profits.

## Q9

### What are your thoughts on the future of the non-gas/non-energy businesses?

In the past, we have developed non-gas businesses in various fields closely related to our gas business. We are now proceeding with evaluation of those non-gas businesses in terms of degrees of synergy, their SVA*, contribution to consolidated profits, autonomy, competitiveness, and market growth potential. Based on this assessment, we are selecting and focusing on appropriate strategies for each segment, such as market exit, divestiture, and integration with another company.

* SVA (Shareholders' Value Added) = net income before interest and income taxes – corporate taxes – cost of capital

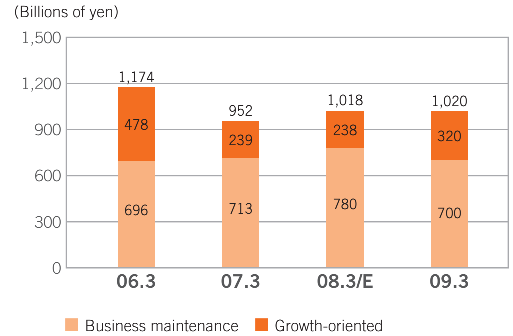
In our LPG and real estate businesses, we look to take maximum advantage of synergies with the energy business in pursuing growth. We will make our IT and chemical products and carbon materials businesses fully autonomous to enable them to pursue business outside the Group and contribute to increased consolidated profits.

# Q10

## What is the outlook for the level of capital expenditures going forward?

Capital expenditures not earmarked for growth-oriented investments but for regular maintenance of business are allocated to active configuration of our pipeline infrastructure and preventative maintenance in such areas as increasing competitive trading, reducing indirect costs in constructing pipelines by utilizing IT, and increasing applications for the non-excavation method. During the business plan, we will undertake capital expenditures of ¥70.0 billion each fiscal year. Since we additionally plan on making growth-oriented investments of ¥30.0 billion per year, total capital expenditures will be about ¥100.0 billion annually for the duration of the plan.

**Projected Capital Expenditures (Consolidated)**




Fiscal 2008 forecasts were announced in March 2007; fiscal 2009 forecasts will be announced in October 2005.

# Q11

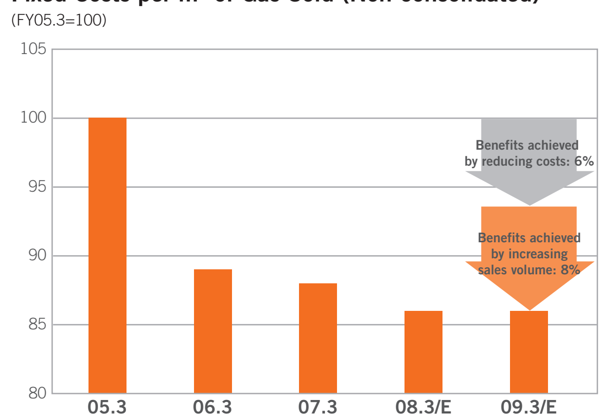
## How are cost reductions to be sustained?

We are aiming to reduce our fixed costs per sale of one cubic meter of gas in fiscal 2009 by 14% from the level recorded in fiscal 2005.

(Fixed costs = Labor costs + overhead costs + costs of capital, etc.)

To achieve this goal, we will redouble our efforts to cut costs through such measures as decreasing the labor force and labor costs, reducing capital investments, and improving the productivity of periodical safety inspections and billing and other tasks. We will also cut gas meter delivery costs using supply chain management and reduce information system maintenance and management costs.

**Fixed Costs per m³ of Gas Sold (Non-consolidated)**



# Q12

## How will free cash flow be applied?

Free cash flow and additional borrowing within a range that sustains financial health are applied to aggressive growth-oriented investments.

Our basic thoughts on growth-oriented investments are:

(1) Investments should be in accordance with either of our two management strategies: expansion of our multi-energy supplier business or concentrated and selective investments in non-energy businesses,

(2) Investments should be in fields where the Group can leverage its strengths and where markets have growth potential, and

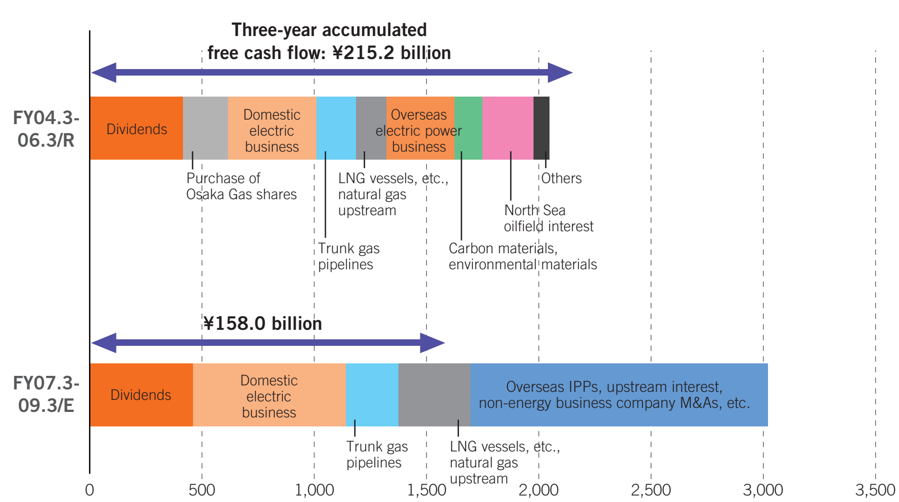
(3) Investments should be able to contribute to consolidated profits substantially and as quickly as possible.

The investments that will contribute to the growth of our domestic energy business in the medium to long term include investments in the domestic electric power business, in trunk pipelines, in the geographic expansion of the natural gas business, and in LNG vessels. Through these investments we plan to expand the scope of the Osaka Gas Group's core energy business. Likely candidates to contribute quickly to consolidated profits include earnings-oriented investments in overseas IPPs and upstream interests. At the same time, we will actively invest in promising non-energy businesses, accelerating our concentrated and selective investment strategy.

Based on this framework, detailed application (growth-oriented investment categories) of consolidated free cash flow over the three years of fiscal 2007 to fiscal 2009 is as follows:

**Free Cash Flow Application During Fiscal 2007 to Fiscal 2009**

(Billions of yen)




FCF= Cash flow from opening activities – payments for capital investments
Capital investments do not include investments for growth.
Growth investment items include both capital investment items and investment-and-loan items.

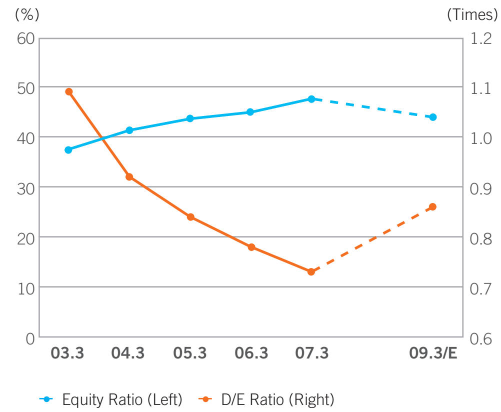
Q13

## What is the company's approach to optimizing the capital structure?

We continually are looking at what overall composition of debt and equity will maximize our capital efficiency. Currently, we believe that an equity ratio of about 40% and a debt-to-equity ratio of approximately one give us a capital structure that maximizes capital efficiency for each of our stakeholders.

Since our current capital structure almost matches these targets, we believe it is possible to increase debt somewhat along with the growth in equity provided by retained earnings while maintaining our sound financial position.

**Equity Ratio and Debt-to-Equity (D/E) Ratio (Consolidated)**




Q14

## What is management's policy on the acquisition of treasury stock?

In the past, we have regularly used buybacks of our shares as one method of returning profits to shareholders by boosting earnings per share.

During the period of the current medium-term business plan, however, given the expected lower growth rate of our gas business, our priority in application of our free cash flow will be investments for corporate growth. For that reason, we will continue to consider the acquisition and retirement of treasury stock always with a view to improving the EPS and ROE, but it will be done flexibly on condition that growth-oriented investments have been made first and that there is sufficient cash flow.

**Acquisition of Treasury Stock**