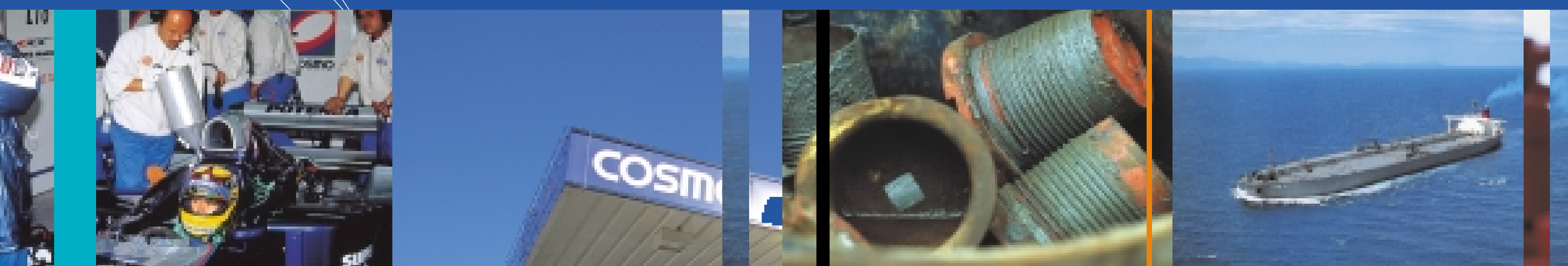
COSMO OIL

Marketing, Exploration and Production, Refining, Distribution, Gas and Power

ANNUAL REPORT 2001

YEAR ENDED MARCH 31, 2001



ESTABLISHED IN ITS CURRENT FORM THROUGH THE 1986 MERGER OF THREE OIL COMPANIES, COSMO OIL CO., LIMITED, IS AN INTEGRATED PETROLEUM COMPANY ENGAGED IN ACTIVITIES RANGING FROM CRUDE OIL PRODUCTION TO THE REFINING AND MARKETING OF PETROLEUM PRODUCTS. THE COSMO OIL GROUP CURRENTLY COMPRISES 152 SUBSIDIARIES AND AFFILIATES. CONSOLIDATED NET SALES AMOUNTED TO ¥1.85 TRILLION (US$14.89 BILLION) IN THE FISCAL YEAR ENDED MARCH 31, 2001.

COSMO OIL MEETS A HIGHER SHARE OF ITS CRUDE-OIL NEEDS WITH ITS OWN RESERVES THAN ANY OTHER JAPAN-BASED REFINER, OPERATES REFINERIES IN JAPAN'S THREE LARGEST METROPOLITAN REGIONS AS WELL AS SHIKOKU, AND CONDUCTS MARKETING ACTIVITIES THROUGH A DOMESTIC NETWORK OF 416 DEALERS AND 5,600 SERVICE STATIONS. THE COMPANY ENGAGES IN A WIDE RANGE OF R&D WORK AIMED AT CREATING HIGH-QUALITY PRODUCTS AS WELL AS TECHNOLOGIES THAT HELP RESPOND TO ENVIRONMENTAL PROTECTION CONCERNS AND DIVERSE CUSTOMER NEEDS.

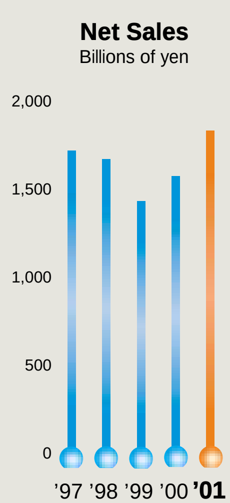
IN LINE WITH ITS MEDIUM-TERM BUSINESS PLANS, COSMO OIL HAS SUSTAINED STRENUOUS EFFORTS TO RESPOND TO CHANGING CONDITIONS, STRENGTHEN ITS COMPETITIVENESS, AND BECOME A MORE COMPREHENSIVE ENERGY COMPANY. THE COMPANY HAS ACCELERATED THE IMPLEMENTATION OF MAJOR REFORM INITIATIVES IN ITS MARKETING, SOURCING, LOGISTICS, AND ADMINISTRATIVE SUPPORT OPERATIONS THAT ENTAIL THE REEVALUATION AND RATIONALIZATION OF EXISTING SYSTEMS, THE CONSOLIDATION OF FUNCTIONS, AND THE PROMOTION OF SYMBIOTIC RELATIONSHIPS.

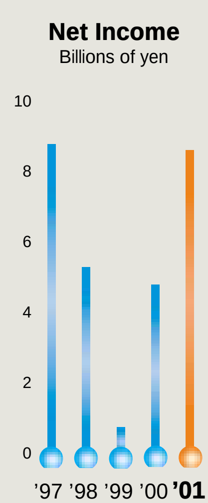
FINANCIAL AND OPERATING HIGHLIGHTS

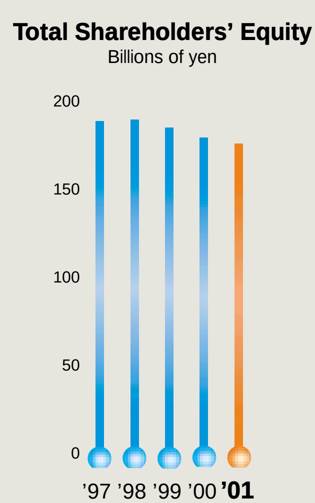
COSMO OIL COMPANY, LIMITED and Its Consolidated Subsidiaries
Years ended March 31, 1999, 2000 and 2001

	Millions of yen			Thousands of U.S. dollars (Note)
	1999	2000	2001	2001
For the year:				
Net sales	¥1,443,457	¥1,584,678	¥1,845,842	$14,885,823
Operating income	22,860	16,665	36,582	295,016
Net income	839	4,841	8,674	69,952
At year-end:				
Total shareholders' equity	186,496	180,386	177,773	1,433,653
Total assets	1,229,285	1,295,693	1,319,960	10,644,839
	Yen			U.S. dollars (Note)
Per common share:				
Net income	¥ 1.33	¥ 7.76	¥ 13.81	$ 0.11
Cash dividends	6.00	6.00	6.00	0.05

Note: U.S. dollar figures are translated from yen, for convenience only, at the rate of ¥124 to US$1, the approximate rate of exchange at March 31, 2001.







A MESSAGE FROM THE MANAGEMENT

Keiichiro Okabe

Chairman and Chief Executive Officer

Fiscal 2001 Operating Environment and Performance

Conditions in the Japanese economy remained harsh during fiscal 2001, ended March 31, 2001. The sustained expansion of principal economies in North America, Europe, and Asia boosted Japanese exports, thereby exerting a positive influence on corporate profitability and capital investment. However, record levels of unemployment and the persistent slackness of personal consumption were principal factors preventing Japan's economy from mustering an autonomous recovery. Against this backdrop, the overall domestic demand for petroleum products remained approximately the same as in the previous fiscal year, although the strength of demand for gasoline, kerosene, and other principal products—with the exception of diesel fuel—increased.

Despite successive production increases by OPEC, crude oil prices continued to rise. In October 2000, Dubai crude prices surpassed $30 per barrel and attained their highest levels since the Gulf War. These prices then fell to close to $20 per barrel in December and subsequently rose to approximately $23 per barrel, where they remained through the end of the fiscal year.

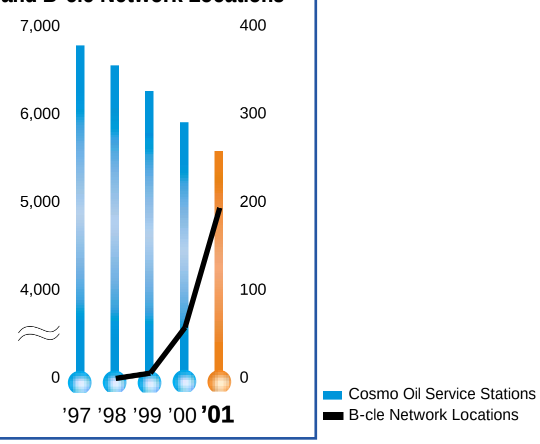
Reflecting the recovery trend in the Japanese economy, the yen-dollar exchange rate was relatively stable for the first eight months of the fiscal year, rising only slightly, from the ¥104-¥105 range in April to roughly ¥108 in November. From December, the lack of a solid base for Japan's economic recovery and renewed attention to the debt problem of Japanese financial institutions caused the yen to depreciate, and the yen-dollar exchange rate ended the period in the ¥123-¥124 range.

Regarding Japanese petroleum product markets, measures were taken to link production levels to demand and thereby improve the supply-demand balance. Although petroleum product prices trended upward against the backdrop of surging crude oil prices, marketers generally found it impossible to increase selling prices for industrial-use fuels and other petroleum products sufficiently to compensate for the rise in their crude oil procurement prices.

Amid this operating environment, Cosmo Oil Co., Ltd., continued concertedly working to rationalize and increase the efficiency of its corporate base while strengthening its competitiveness with regard to marketing, logistics, financial, and other types of operations. Based on the comprehensive business tie-up that was begun during the previous fiscal year, Cosmo Oil and Nippon Mitsubishi Oil Co. (NMOC) continued to take cooperative measures to reduce costs related to oil procurement, refining, distribution, and lubricant oils. These measures generated clear-cut benefits.

In marketing operations, Cosmo Oil worked to correct outmoded transactional practices through the introduction of a system for setting prices in line with market conditions as well as reforming its marketing promotion systems. The Company's

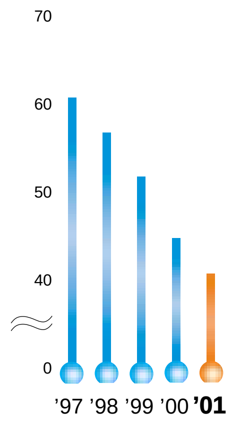
Number of Cosmo Oil Service Stations and B-cle Network Locations



increased marketing efficiency enabled it to conduct effective marketing operations in line with its strategic goals. With the objective of boosting competitiveness, Cosmo Oil proceeded decisively with the merger and consolidation of affiliated service stations in which it has an investment. It also strove to boost the competitiveness of each Cosmo service station and, thereby, strengthen the financial condition of affiliated service station operators by proactively considering the establishment of additional self-service facilities, energetically working to increase the number of Best Car Life Entertainment (B-cle) Car Care Convenience stores, enhancing the services available to holders of Cosmo The Card credit cards, and otherwise endeavoring to increase the number of cardholders. In March 2001, the Company revamped the marketing organization of its branches and proceeded with the building of a more flexible and dynamically responsive marketing system.

Regarding the procurement of crude oil and petroleum products, Cosmo Oil worked to continue flexibly responding to fluctuations in the supply-demand environment, secure stable supplies of crude oil, and trim related procurement costs. In November 2000, the Company and NMOC established a joint venture, Nippon Global Tanker Co., Ltd., which is taking measures to minimize crude oil transport costs. Aiming to enhance competitiveness by further increasing the efficiency of its refining system, Cosmo Oil proceeded with a project that seeks to trim refining costs ¥700 per kiloliter while maintaining highly safe operations and increasing the ability of the refining system to quickly and flexibly respond to fluctuations in supply-demand conditions.

Number of Cosmo Oil Storage Depots

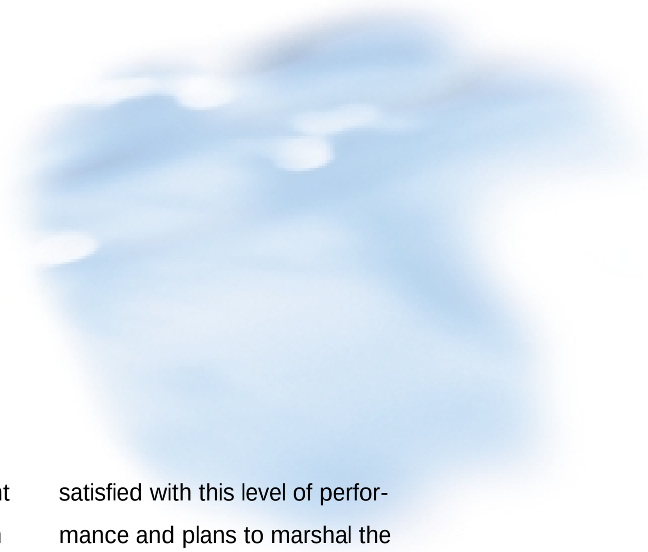


To reduce distribution costs, the Company took such steps as those to increase the share of shipments made directly from refineries to service stations, broaden the scope of its integrated planned delivery system, and raise the capacity utilization rates of its tanker trucks and domestic tanker vessels.

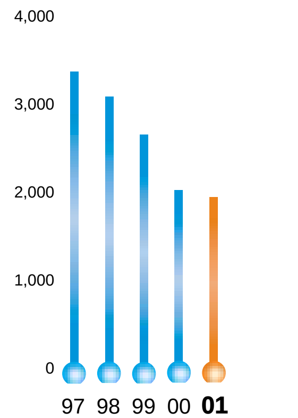
Cosmo Oil maintained oil development programs in the Middle East and elsewhere aimed at augmenting its own oil reserves and increasing the geographical diversity of those reserves. In February 2001, the Company successfully completed the drilling of an exploratory well off the northwest shore of Australia.

To bolster its financial position, Cosmo Oil procured low-cost funds through the issuance of ¥10.0 billion in unsecured bonds as well as by securitizing and liquidating service station assets. Such measures enabled the Company to reduce its interest-bearing debt by ¥86.1 billion from the end of the previous fiscal year.

To diversify its operations, Cosmo Oil is undertaking a variety of new businesses. Besides business related to Internet-based commerce and home-care operations, the Company is proactively developing businesses involving the development of fuel cells that use petroleum fuels, the use of thermal power plants to generate electricity for sale to local



Number of Cosmo Oil Employees



power companies, and the marketing of liquefied natural gas (LNG). In January 2001, the Company began constructing a power plant adjacent to the Yokkaichi Refinery. Construction is proceeding according to the original schedule, and plans call for the wholesaling of power from that facility to begin in 2003.

As a result of these management initiatives, Cosmo Oil succeeded in boosting its total fuel sales volume 0.2% from the level in the previous fiscal year, to 44,324 thousand kiloliters, as a decline in sales of diesel fuel was offset by increases in sales of such other fuels as gasoline and kerosene. Reflecting rises in sales volumes as well as in procurement and selling prices, total net sales of the parent company surged 13.8%, to ¥1,605.8 billion. Despite the Company's progress in cost-cutting programs, such factors as the difficulty of quickly adjusting selling prices to completely offset rises in procurement prices caused recurring income and non-consolidated net income to amount to ¥12.9 billion and ¥5.2 billion, respectively. Management is by no means satisfied with this level of performance and plans to marshal the Company's resources to mount an even more vigorous push to obtain highly ambitious performance targets during the current fiscal year.

The Company disbursed interim cash dividends at a rate of ¥3.00 per share, and year-end dividends are scheduled to be paid out at the same rate. Thus, the total value of dividends applicable to fiscal 2001 is scheduled to be ¥6.00 per share, the same level as in the previous fiscal year.

June 2001

Keiichiro Okabe
Chairman and
Chief Executive Officer

At the end of fiscal 2001, Cosmo Oil announced the following fundamental principles regarding safety and environmental protection. These principles are being rigorously adhered to by all companies in the Cosmo Oil Group.

Fundamental Safety Principles

Cosmo Oil has made sustaining and realizing progress in safety and safe operations a top management objective. At facilities that handle such hazardous materials as flammable materials and pressurized gases, rigorous measures will be taken to ensure the safety of all employees, other people involved with work processes, and local residents as well as to ensure a harmonious coexistence with local communities.

Fundamental Environmental Protection Principles

Cosmo Oil has made protecting the environment a top management objective. The Company will strive to contribute to society by minimizing the environmental impact of all its activities and by utilizing the technological capabilities it has developed over many years to promote progress in environmental protection technologies.

Trends in Cosmo Oil's Operating Environment

Although the Japanese economy is expected to benefit from the government's emergency economic countermeasures and the promotion of structural reforms, the trend of decline in Japan's nominal GDP has continued, and the deceleration of economic growth in the United States has been accompanied by a slackening in the capital investment of Japanese manufacturing industries. Thus, there is cause for considerable concern regarding future trends in the Japanese economy.

Meanwhile, Japan's oil industry is undergoing a major restructuring. Each company in the industry is expected to further accelerate its efficiency-boosting programs and must respond to various challenges, such as a shrinkage in profit margins, increases in the rigor of quality and environmental protection standards, and fluctuations in crude oil prices. Members of the Japanese oil industry can thus expect to face an increasingly severe operating environment.

Rationalization Results—¥150 Billion of Cost Reductions over the Five Years Ended March 31, 2001

Since fiscal 1997, a period in which the full-scale deregulation of the oil industry was accompanied by the harshness of the operating environment, Cosmo Oil has made strenuous efforts to strengthen its capabilities through a rationalization program that places principal emphasis on establishing a Cosmo Oil network that is the strongest such network in terms of cost-competitiveness and that attracts and inspires loyalty on the part of customers.

To strengthen cost-competitiveness, Cosmo Oil cut its annual costs approximately ¥150 billion over the five years ended March 31, 2001. Each of the Company's service stations and affiliated service station operators has also proceeded with cost-cutting programs. Great improvement has been achieved in improving the NAVI index—which objectively measures a service station's earning power and the added value of Company-owned and affiliated service stations—and the Cosmo Oil Group has increased its overall cost-competitiveness to one of the highest levels in the Japanese oil industry.

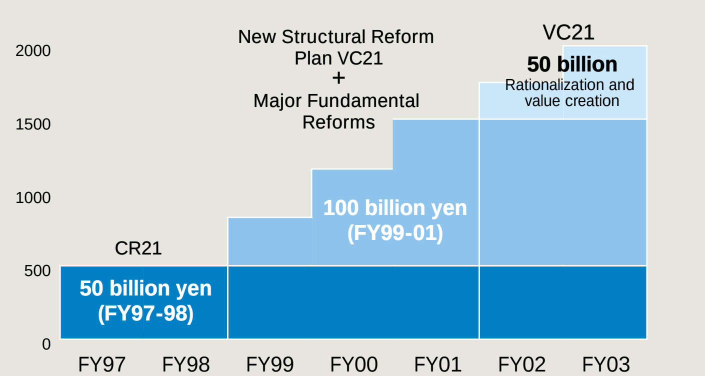
Cosmo Oil is sustaining its rationalization drive. During the two years ending March 31, 2003, the Company intends to cut its annual costs approximately ¥50 billion through such measures as collaboration with NMOC and steps to increase the efficiency of affiliated companies. Thus, combined with previous accomplishments, the Company intends to have implemented rationalization measures that reduce its annual costs a total of approximately ¥200 billion by the end of VC21, its current two-year management plan.

Aiming to Be the Number One Company in Six Respects

Anticipating that its operating environment will present it with still harsher competitive challenges, Cosmo Oil has drafted VC21 with an eye to providing the management vision and strategies needed to confidently face those challenges.

In addition to sustaining the cost-cutting measures of previous management plans, VC21 goes a step further in prescribing steps to differentiate Cosmo Oil more clearly from Cosmo's competitors and to build competitive strengths that are clearly superior to those of competing companies. Aiming to make its network one that attracts and inspires

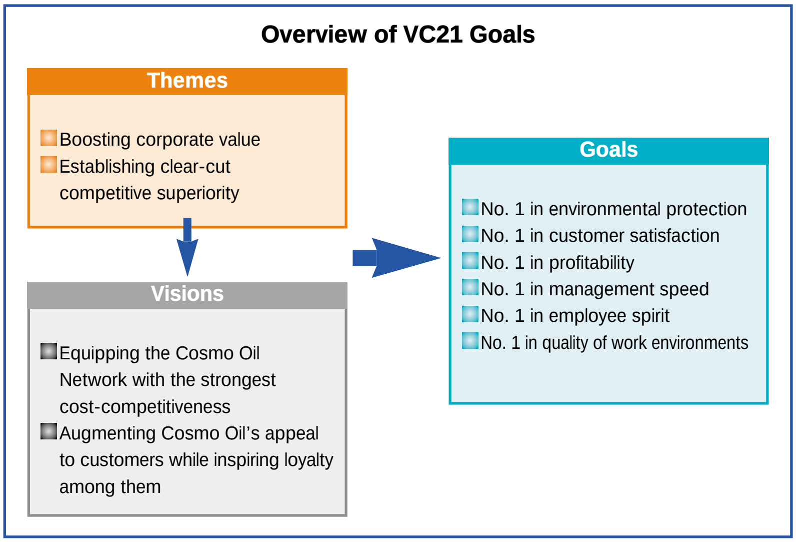
Rationalization Performance and Targets
Billions of yen



strong loyalty on the part of customers, the Company is placing primary emphasis on boosting the added value generated throughout its operations.

VC21 calls for Cosmo Oil to be the number one company in its industry in the six following ways.

- No. 1 in environmental protection: Cosmo Oil will meet and surpass the growing expectations of global society in this regard as a means of displaying excellent corporate citizenship and boosting its competitiveness.
- No. 1 in customer satisfaction: Cosmo Oil will further increase the emphasis on customer satisfaction that is a traditional part of its corporate culture.
- No. 1 in profitability: Cosmo Oil will relentlessly pursue the goals of equipping itself with superior cost-competitiveness, marketing capabilities, and risk management systems.
- No. 1 in management speed: Cosmo Oil will strategically utilize superior information resources and technologies so that it can make the best management decisions more quickly.
- No. 1 in employee spirit: Cosmo Oil will promote employees' efforts to constantly upgrade their skills and to enthusiastically contribute to the Company's success through participation in value-creating groups.
- No. 1 in quality of work environments: Cosmo Oil will utilize personnel systems that ensure that employee contributions are appropriately recognized.



Regarding overall consolidated performance, by the end of March 2003 VC21 calls for Cosmo Oil to boost its return on equity and equity ratio to 10% and 20%, respectively, while reducing interest-bearing debt as a share of total assets to 40%.

Strong Emphasis on Added Value in Marketing Operations

Because augmenting Cosmo Oil's appeal to customers while inspiring loyalty among them is one of VC21's two principal visions, the plan devotes great attention to the Company's marketing operations. VC21 calls for Cosmo Oil to further differentiate itself from competing companies by more fully leveraging its unique strengths.

The Company independently manages its Cosmo The Card credit card system. Approximately 2.4 million Cosmo The Card credit cards have been issued over the years, of which a large number, almost 70%, are still active. This system and cardholder base represent important corporate strengths. Cardholders can avail themselves of such optional services as bonus point accumulation based on the value of nonfuel purchases at service stations as well as the oil industry's only electronic toll collection service. In the future, Cosmo Oil intends to work hard to further increase the convenience of its card services and thereby expand its cardholder base. The Company is also striving to meet its clientele's needs for "total car care" centers that offer a comprehensive range of services, including the performance of maintenance and mandatory vehicle inspections. To achieve this, Cosmo Oil is expanding its nationwide network of B-cle CAR CARE Convenience outlets at service stations while supporting the efforts of affiliated service stations to enhance their service quality by assigning a greater number of its personnel to work as supervisors for affiliated service stations. Cosmo Oil is utilizing the Internet to augment its two-way communications with affiliated service station operators, particularly with respect to such knowledge-management methods as those involving the sharing of information on marketing success stories.

Maximizing Value Creation in Operations of All Divisions and Group Companies

Cosmo Oil is already one of the top Japanese oil companies in terms of the cost-competitiveness of its refining operations, and plans call for the Company to further integrate its refining and marketing systems and better leverage the strengths of those systems through sophisticated supply-demand management systems that promote a rise in the added value of refining operations. At the same time, the Company is augmenting its programs aimed at ensuring environmental protection and harmonious relations with communities near its facilities through the development and utilization of improved technologies for reducing the environmental impact of operations and ensuring operational safety.

As it is also intent on becoming a top company in the industry with respect to distribution efficiency, Cosmo Oil has accelerated its timetable for rationalizing its distribution network. Targets originally scheduled for attainment in March 2003 are now expected to be reached by March 2002.

Structural reforms are progressively being implemented in finance, personnel, general affairs, accounting, and other administrative departments. In particular, Cosmo Oil has slimmed its balance sheet ¥93.0 billion over the past 2 years and is aiming to increase this aggregate sum to ¥200.0 billion. To realize the remaining ¥107.0 billion in reductions, the Company is continuing to take such measures as boosting the liquidity of accounts receivable and disposing of underutilized assets. Other important means of rationalizing and boosting added value throughout the Company include the introduction of Companywide knowledge-management systems and the promotion of management transparency and efficiency using SAP, an enterprise resource planning package and comprehensive accounting system that was introduced in April 2000.

Cosmo Oil is introducing more rigorous Group management systems that require, in principle, that all loss-making companies expeditiously begin generating a profit. These systems and another system for the permanent reassignment of parent company employees to Group companies are designed to ensure the appropriate assignment of profit-generation responsibilities as well as provide a clear-cut basis for increasing the efficiency of capital allocation.

Becoming a Comprehensive Energy Company

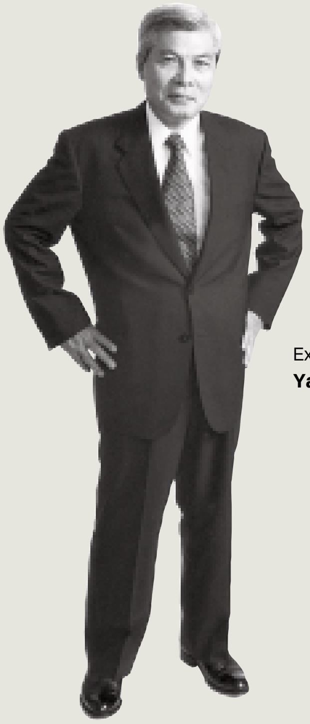
Cosmo Oil has begun full-scale efforts to build a solid base as a comprehensive energy company, with particular attention to expanding the Company’s electric power generation and natural gas operations. Regarding electric power, Cosmo Oil has a comprehensive operational scope because it supplies equipment for small- and large-scale dispersed generation needs as well as direct power generation and supply operations as an independent power producer (IPP). The Company has already begun taking concrete steps to establish natural gas operations that are facilitated by the recent relaxation of related regulations.

Creative Destruction

Cosmo Oil is determined to proceed with the steps required to reform its operations and attain its strategic goals. Accordingly, it will not flinch from the need to decisively eliminate existing systems and operations when such destruction is necessary to create the optimal systems and operations that are the defining characteristics of corporate groups with clear-cut competitive superiority in their industries. The Cosmo Oil Group is firmly resolved to follow through with its plans to transform itself.

BOARD OF DIRECTORS AND AUDITORS

Chairman and
Chief Executive Officer
Keiichiro Okabe



Executive Vice President
Yaichi Kimura

Chairman and
Chief Executive Officer
Keiichiro Okabe*

Executive Vice President
Yaichi Kimura*

Managing Directors
Masaaki Takeda
Masaru Mori
Masaaki Takeuchi
Takefumi Uchida
Yasuyo Kobuchi

Directors
Kiyoto Kudama
Yoshiyuki Yuasa
Makoto Kobayashi
Kazuhisa Tamura
Keizo Morikawa
Yasuo Sakata
Masahide Furuzone
Kenji Hosaka
Yoshihisa Matsumiya

Standing Auditors
Keizo Nishimura
Yoshitomi Ebisuya**
Takeo Yamamoto
Susumu Eda

Auditor
Hajime Miyamoto**

*Representative Director
**Independent Auditor

(As of June 28, 2001)

Marketing

Marketing Strategy

Of all the restructuring that Cosmo Oil has undertaken since the deregulation of Japan's oil industry, the Company has spent the most energy on restructuring its marketing operations. Moreover, the Company has devoted great attention to reforming its service station distribution operations, thoroughly cutting costs, and developing new markets.

The drop in persistently high crude oil prices in December 2000 enhanced Cosmo Oil's profitability to a certain extent during the latter half of fiscal 2001, but a severe winnowing out in the oil industry due to intensified competition is still considered inevitable. To ensure that it can succeed in that competition, the Company is emphasizing two strategies. First, Cosmo Oil is liquidating unprofitable service stations and increasing the NAVI index level that service stations must attain through additional rationalization measures. Second, the Company is leveraging the power of its brand name to the maximum possible extent as it implements new strategies for augmenting the added value of service stations.

Cosmo Oil is the only company in the Japanese oil industry that manages its own credit card system. At the end of fiscal 2001, the Company had issued an aggregate total of approximately 2.4 million Cosmo The Card credit cards, of which roughly 1.6 million are still active. Cosmo Oil's card services are an extremely effective means of strengthening the loyalty of its best customers, and they thus represent an important asset of the Company.

Begun in summer 2000, the Cosmo Mileage system allows cardholders to accumulate points when they purchase nonfuel products at service stations and then use the points to obtain discounts on fuel charges. In July 2000, the system was renamed Cosmo Gasoline Mileage and its scope was broadened to allow the award of mileage points for goods sold via the Company's web site. By offering this type of new service, the Company has increased the convenience of its cards and promoted a rise in new card issuance as well as in the profitability of its service stations.

Proactively Entering the Car-Care Market

In response to the increasingly diverse needs of motorists, Cosmo Oil has increased the number of its self-service stations to 23 while expanding its nationwide network of B-cle Car Care Convenience stores, which have broadened the scope of their services to include vehicle maintenance services and the performance of mandatory vehicle inspections. The existing B-cle service stations have enjoyed strong support from customers throughout Japan and recorded excellent profitability and fuel sales volumes. In light of this, the Company plans to

$$\text{NAVI index} = \frac{\text{Service station direct expenses} - \text{Gross profits excluding auto fuel (Kerosene gross profit + Value-added services and products' gross profit)}}{\text{Auto fuel (Gasoline + Light oil) sales volume}}$$

Notes: The NAVI index numerically measures the competitive strength of service stations.
A smaller NAVI index means a competitively stronger service station.

$$\text{Corporate NAVI index} = \frac{\text{Corporate overhead costs} - \text{Gross operating profit excluding service station business}}{\text{Auto fuel (Gasoline + Light oil) sales volume at directly operated stations}}$$

Notes: The corporate NAVI index numerically measures contribution or burden by revenue and expenditure, excluding service station business, on a service station auto fuel margin basis.
A smaller corporate NAVI index means a competitively stronger corporate organization.

further expand its B-cle network during fiscal 2002 through the establishment of an additional 20 core B-cle facilities and 100 satellite B-cle facilities.

Cosmo Oil's "supervisors" are management consultants that specialize in support programs for improving the management of affiliated service station operators and their service stations. These staff members have proved highly useful, and the Company will increase their number to approximately 100 during fiscal 2002.

To promote two-way communication between Cosmo Oil and service stations, the Company began using the Internet-based Cosmo On-Line service in fall 2000. The service has proved an invaluable means of implementing such knowledge-management programs as those aimed at disseminating information about successful new marketing methods throughout the Group.

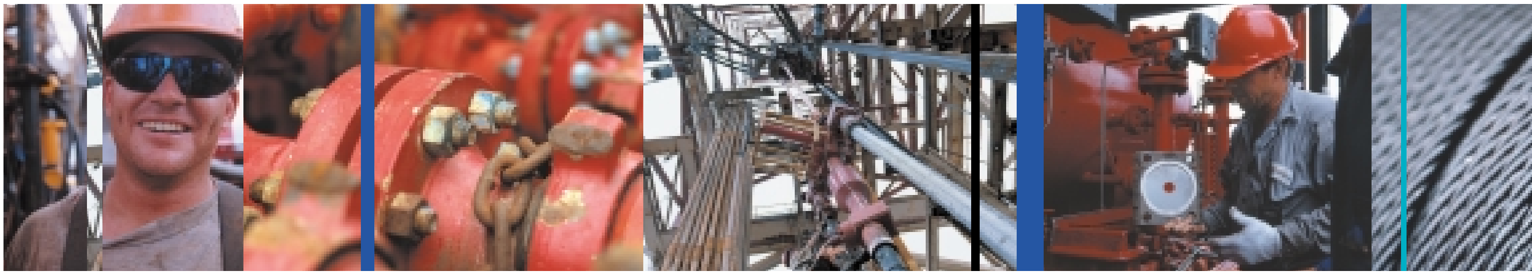
In addition, the Cosmo Oil web site is being expanded to include various features for Cosmo The Card credit card holders, such as The Card.com and B-cle.com. These appealing features are expected to reinforce the efforts of service stations to issue cards and boost profitability.

Transaction Methods and Proactive Service Station Management Methods

One reason that Cosmo Oil and affiliates' service stations can focus all their energies on augmenting their added value is the Company's April 2000 move to predetermine, or formulize the calculation of, selling prices at service stations as well as increase the diversity of service stations' payment schemes. This move, which was the first such in the industry, eliminated traditional Japanese transactional practices that had become outmoded and replaced those practices with new systems that clearly indicate the performance goals of each service station operator and, thereby, promote progress in management reforms. The more diverse payment schemes are facilitating the Company's efforts to shrink the outstanding period of its accounts receivable, thereby strengthening its financial position.

Cosmo Oil's head office, branches, and Company-owned and affiliated service stations are simultaneously working to better address customer needs, and their roles and capabilities are clearly differentiated to maximize the efficiency of their collaboration. In this way, Cosmo Oil is striving to effectively marshal all of its resources to increase the Group's overall value and maximize profitability. The Company's strategy places strong emphasis on building a solid marketing base that will facilitate the attainment of its goal—being the industry's top company with regard to customer satisfaction and profitability.

Best Car Life Entertainment (B-cle) Car Care Convenience facilities offer a broad range of products and services.



Exploration and Production

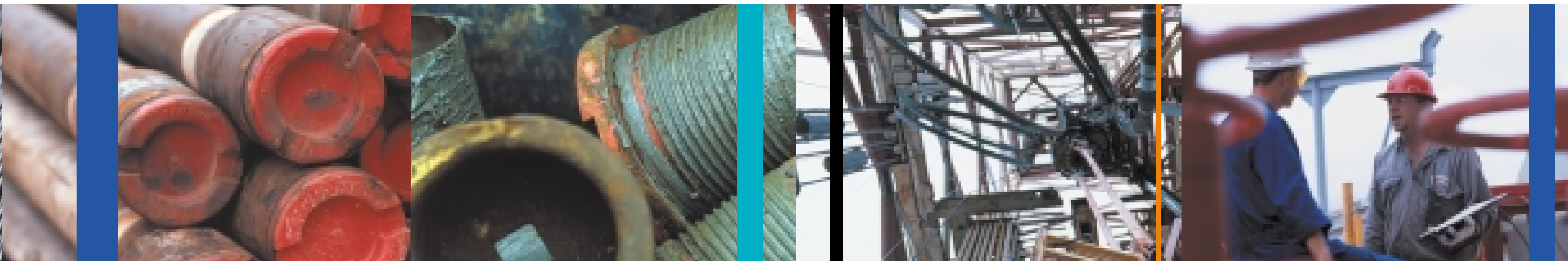
Overseas oil development activities are an extremely important means of obtaining stable energy sources for Japan in light of the country's negligible crude oil reserves, and Cosmo Oil has actively engaged in such activities since the 1960s. By sending many Japanese staff overseas to participate in exploration and development operations, particularly in the Middle East, the Company has accumulated a wealth of direct experience while building solid ties of mutual trust with crude oil exporting countries. The Company is distinctive in this regard, having been considerably more active in overseas oil development operations than other Japanese oil companies.

This platform is the center of operations in a Cosmo Oil block of the Timor Sea off Australia.

Steadily Increasing Production in the Middle East

For more than 30 years, Cosmo Oil has undertaken oil exploration, development, and production operations in Abu Dhabi and Qatar. In these countries, the Company works through a subsidiary—the Abu Dhabi Oil Co., Ltd. (ADOC), in which the Company has a 51.1% share—and two affiliates: Mubarraz Oil Co., Ltd. (MOCO), in which it has a 20.3% direct equity stake as well as indirect investments made through ADOC and other companies, and United Petroleum Development Co., Ltd. (UPD), in which the Company has a 13.3% share.

Currently, ADOC and MOCO produce approximately 30,000



barrels of crude oil per day. They are successfully developing additional oil wells, and it is expected that stable production will be maintained. Substantial investment in environmental protection measures has been undertaken at the companies' oil fields since 1999, and a facility completed in May 2000 is used to inject all the natural gas generated during production and processing activities back into the oil strata rather than releasing it into the atmosphere. The companies are also installing zero flaring equipment and wastewater processing facilities, and the bulk of related work was completed in early 2001. These new types of oil field facilities for helping protect the global environment have been highly evaluated in the Middle East.

UPD's oil development operations are continuing to produce a stable yield of approximately 20,000 barrels of crude oil per day, and the installation of equipment for protecting the environment through the reinjection of natural gas at the sites of UPD's operations is currently under consideration.

Cosmo Oil is the largest private-sector investor in Qatar Petroleum Development Co., Ltd. (QPD), having a 38.44% equity stake in that company, which has completed exploratory drilling in a new oil field offshore Qatar and begun the final stage of assessment surveys.

Initiating Full-Scale Production Offshore Australia

Cosmo Oil has exploration permits for a block in the Timor Sea off the northwest shore of Australia. Cosmo Oil Ashmore Ltd., in which Cosmo Oil has a 51% shareholding, drilled two exploratory wells that confirmed the presence of oil in 1997, and a third exploratory well confirmed the presence of oil in February 2001. Commercial production in those locations is expected to provide approximately 30,000 barrels of crude oil per day. Preparations for the drilling of two additional exploratory wells is scheduled to begin during 2001. The Timor Sea block is expected to be highly profitable, as all the reserves in the block are ultralight crude oil, the production efficiency of the field is high, and the tax system of Australia is considerably more advantageous than those of Middle Eastern countries.

Oil development operations offer oil companies an important means of hedging risks due to crude oil price fluctuations, and Cosmo Oil's oil development operations were an important factor contributing to the Company's consolidated performance in fiscal 2001 amid rising crude oil prices. In the future, the Company plans to prudently and proactively proceed with the expansion of its oil development operations, using cash flows generated by upstream operations.

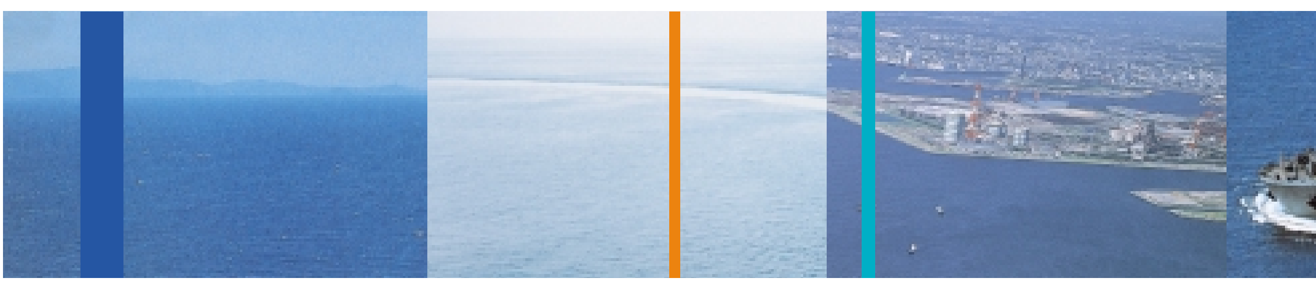
Rapidly Adjusting Supplies in Line with Demand Trends

Since 1997, when Japanese petroleum product exports were deregulated, Cosmo Oil has installed a growing number of facilities in preparation for producing petroleum products for export. During the latter half of fiscal 2001, such factors as the economic recovery in Asia and improving conditions in overseas petroleum product markets led the Company to slightly modify its supply-demand management system, which had previously focused exclusively on the domestic market. The more proactive new system aims to increase capacity utilization rates, reduce product imports, and boost exports. As a result, Cosmo Oil exported diesel fuel, gasoline, heavy fuel oil C, and other products to such countries as Korea, Taiwan, and Australia. The total volume of exports amounted to 600,000 kiloliters, up from 30,000 kiloliters in fiscal 2000. These exports included both shipments based on long-term contracts that lock in stable profits and spot shipments that were carefully timed to help maintain appropriate capacity utilization rates despite fluctuations in the domestic supply-demand balance. In the future, the Company intends to continue proactively exporting petroleum products in line with trends in overseas market prices and the balance of domestic supply and demand.

Integrating Refining and Marketing Operations to Optimize Supply-Demand Management

Cosmo Oil's system for the complete integration of refining and marketing operations greatly facilitates the implementation of the Company's strategy of maintaining levels of production, imports, and exports that are optimized in light of domestic demand trends. The Company is unique among Japanese oil companies in its ability to identify changes in domestic demand in a timely manner and rapidly fine-tune

Refining



its production levels in response to those changes. In autumn 1999, Cosmo Oil began using its computerized New Demand-Supply System, which quickly processes large volumes of data and has enabled the Company to increase the precision of its production-optimization adjustments.

Further Boosting Efficiency of High-Value-Adding Refining Facilities

Cosmo Oil operates four refineries—the Chiba, Yokkaichi, Sakai, and Sakaide refineries—all of which are optimally situated adjacent to major consuming regions. The Company anticipates that all of these facilities will continue to play important roles in maintaining a balance between domestic demand and production in the future.

A distinctive characteristic of all four of Cosmo Oil's refineries is that their ratios of direct desulphurization capacity to atmospheric distillation capacity are higher than the national average. As a result, during fiscal 2001 the refineries were able to add a relatively large amount of value to the crude oil they processed by achieving a 47.3% yield of the four principal middle distillates—kerosene, diesel fuel, jet fuel, and fuel oil A—significantly above the industry average of 45.5%.

To further boost their international competitiveness, the four refineries are engaged in a project with the goal of trimming refining costs ¥700 per kiloliter by the end of 2003. The attainment rate for this goal was approximately 70% in fiscal 2001, and plans call for boosting the rate to roughly 80% during fiscal 2002. The implementation of the project is proceeding smoothly through the reduction of personnel, maintenance, and other costs while maintaining safe operations.

During the first 18 months of Cosmo Oil's comprehensive tie-up with NMOC, the partners began their collaboration with barter transactions of such items as products and basic materials, imported products, and products for export. The scope and scale of cooperation has been steadily expanded to include such activities as joint imports of crude oil, entrusted crude oil processing, and the exchange of certain petrochemicals. Currently, the partners are devising a system for optimizing production operations through the integrated operation of all 12 of their refineries, and this system promises to generate considerable additional benefits for both companies.

Distribution

Cosmo Oil's refineries are located in a well-balanced network that covers four regions—the Tokyo metropolitan area, the Chukyo region surrounding Nagoya, the Kansai region centered on Osaka, and the Seto Inland Sea area centered on Shikoku—and the Company's distribution departments have undertaken bold rationalization measures since the mid-1990s, aimed at making the most of the strengths of the refining network. In fiscal 2001, those measures enabled approximately ¥3.0 billion in cost reductions. Another long-term project has the objective of using product-barter arrangements to increase the share of tank truck shipments that proceed directly from refineries to service stations without passing through transshipment depots. As a result, in fiscal 2001 the number of transshipment depots was reduced from 46 to 41, and the share of direct tank truck shipments surpassed 50%.

Boosting Efficiency with Planned Delivery Schedules and New Order Placement System

Currently, Cosmo Oil's principal tool for boosting distribution efficiency is a system for planning deliveries of fuels to service stations. Previously, affiliated service stations submitted orders for their estimated fuel requirements and tank trucks were dispatched to fill individual orders. The new system projects the volumes of fuels required by service stations based on point-of-sale data and then automatically plans delivery schedules. The number of service stations covered by this system was increased from 810 to 1,300 during fiscal 2001, and plans call for the number to reach 2,700 during fiscal 2002. The system has boosted efficiency by raising tank truck capacity utilization rates in terms of the number of trucks in operation as well as in terms of the amount of each truck's utilized carrying capacity. The Company has also endeavored to increase the number of shipments that are unloaded outside of service stations' operating hours without the attendance of service station employees, and thereby expects to be able to reduce the number of its own tank trucks from 570 to 470. Moreover, by shifting order placements from Cosmo Oil's independently developed CORASII on-line network to the Internet-based Cosmo On-Line system, the Company anticipates that it will be able to reduce system-related capital investment as well as operating and maintenance costs, and the staff of the Company's order center is scheduled to be reduced from 48 people in fiscal 2000 to 38 in fiscal 2002.

Steady Rise in Efficiency through Cooperation with NMOC

Cosmo Oil is also increasing its distribution efficiency through moves taken as part of its comprehensive tie-up with NMOC. Primarily through the cooperative use of refineries and transshipment depots that enables the elimination of certain transshipment depots, rationalization moves are being implemented that are expected to reduce costs ¥10.0 billion from fiscal 2000 through fiscal 2003.

Trucks are dispatched at night, following highly efficient product shipment plans.

A micro-gas turbine unit is undergoing performance evaluation testing at the Sakaide Refinery

Gas and Power

Cosmo Oil is proceeding with a variety of measures in line with its goal of developing into a comprehensive energy company. Currently, the Company is devoting particular attention to expanding its presence in electric power generation and natural gas markets, which are growing at more rapid rates following deregulation measures. Cosmo Oil has a comprehensive operational scope in electric power, as it supplies equipment for small- and large-scale dispersed generation needs and is beginning large-scale power supply operations as an IPP. In all these operations, the Company is developing new sources of demand for its petroleum fuel products as it markets generating equipment and electric power.

Cosmo Oil's dispersed generation products offer superior economy and energy efficiency. The Company's smallest-scale product in this field is a petroleum-fueled fuel cell cogeneration system for residential use. A pilot model fueled with butane gas was completed during fiscal 2001, and the Company is conducting R&D related to the commercial development of models fueled with naphtha and kerosene. Cosmo Oil is already marketing a kerosene-fueled heat pump air-conditioning system that provides stores and other small-scale businesses with cool and hot air as well as hot water. Another of the Company's new electric power generation systems, a micro-gas turbine, is currently undergoing performance evaluation testing.

Cosmo Oil has steadily increased its sales of cogeneration systems for such large-scale customers as office buildings, hotels, and hospitals. The Company has also begun heat and electric power supply operations. In these operations, the Company undertakes the construction, operation, and maintenance of on-site generating facilities at customers' buildings and plants and sells heat and power to the customers, who can benefit from lower power costs without having to make capital investments or operate the facilities themselves.

Regarding large-scale power generation, Cosmo Oil is preparing to begin IPP operations supplying power to the Chubu Electric Power Co., Inc. Having completed an environmental impact assessment, the Company has begun constructing a power generation plant at a site adjacent to the Yokkaichi Refinery, in Yokkaichi City, Mie Prefecture.

Cosmo Oil is responding proactively to opportunities presented by the deregulation measures related to natural gas marketing business. The Company participated in the establishment of LNG Chubu, in cooperation with Chubu Electric Power and Iwatani International Corp., and the joint venture is aiming to record annual net sales of ¥100 million in fiscal 2002 and ¥1 billion in fiscal 2006.

Cosmo Oil has also cooperated with Kansai Electric Power Company, Limited, Iwatani International, and Ube Industries, Ltd., to found Sakai LNG Corp., which plans to begin operating an LNG base in 2005. The Company is participating in a pilot plant project to test the commercial viability of the newly developed gas-to-liquid technology for the conversion of natural gas into a liquid, establishing compressed natural gas facilities at service stations, and otherwise responding to the potentials of new energy sources.

While contributing to the utilization of "clean energy" and developing new markets for petroleum resources, Cosmo Oil is maximizing the utility of its distribution systems and promoting its evolution into a comprehensive energy company.

Besides improving technologies related to petroleum fuels, oil refining, and catalysts over many years, Cosmo Oil's R&D departments have undertaken work related to biotechnologies and are strongly emphasizing programs for responding to environmental issues.

Regarding oil refining, Japan has reduced the maximum permissible amount of sulfur in diesel fuel from 500 ppm to 50 ppm, and Cosmo Oil is responding to this by developing a catalyst that is highly effective in removing sulfur from diesel fuel. This catalyst simplifies desulfurization by helping chemically transform difficult-to-remove sulfur compounds, and the Company is developing it with attention to such innovative concepts as those associated with catalyst-pore optimization. The Company is also using other petroleum fuel technologies to ensure that the desulfurized diesel fuel offers excellent performance despite the decrease in the sulfur particles that work as lubricants.

A large volume of catalysts are used in oil refining, and Cosmo Oil is seeking to extend the usable life spans of catalysts and thereby reduce the volume of catalysts that are disposed of. The Company has developed a catalyst for its indirect desulfurization units that can be used for four years before replacement, and this catalyst is already in use in its indirect desulfurization units. The Company has also created a technology that doubles the usable life span of catalysts used in fluid catalytic cracking units, and it is currently considering beginning their commercial use.

Cosmo Oil is actively developing fuel cells that have attracted considerable attention due to their great potential as an environment-friendly, second-generation energy technology. The Company has completed a prototype fuel cell system that employs a highly sophisticated technology—one which generates hydrogen from petroleum fuels.

At its refineries, Cosmo Oil is implementing programs to greatly reduce the volume of waste products that are discharged. Sludge from wastewater treatment units accounts for the majority of the refineries' waste product volume, and the Company has succeeded in developing a technology capable of reducing the volume of such sludge to zero. Plans call for the demonstration testing of the new technology at refineries during fiscal 2002.

Regarding soil contaminated with oil and other substances, Cosmo Oil is progressing with the development of technologies for detecting the pattern and volume of contamination and for inexpensively and efficiently purifying the soil using microorganisms.

In other fields, Cosmo Oil has developed a microorganism fermentation method for the industrial-scale manufacture of 5-aminolevulinic acid, a bioactive substance that can reduce atmospheric carbon dioxide by accelerating the growth of vegetation and can be used in optical therapeutic methods for treating cancer.

Cosmo Oil Lubricants Co., Ltd., a wholly owned subsidiary, conducts research to enable the continual enhancement of its LIO line of high-performance engine oils. During fiscal 2001, that company began marketing the New Lios Series of high-performance, fuel-saving engine oils that respond to the latest safety level standards of the American Petroleum Institute. Cosmo Oil Lubricants is emphasizing the development of lubricant oils that are easily broken down by microorganisms in water and soil as well as chlorine-free lubricant oils that help prevent the generation of dioxins. It has already begun marketing such products, which have been highly evaluated by customers.

ENVIRONMENTAL PROTECTION

Being a company involved with the supply of energy, Cosmo Oil believes that issues related to the protection of regional and global environments are among its most important management concerns.

In 1993, Cosmo Oil established its internal Global Environment Committee to provide comprehensive guidance for environmental protection activities Companywide. The committee has worked to contribute to society by promoting reductions in the environmental impact of the Company's refining, distribution, and service station operations; developing environmental protection-related technologies; and undertaking other initiatives. The committee has steadily promoted Companywide environmental programs and conducted annual follow-ups to confirm progress in those programs.

All four Cosmo Oil refineries have received ISO 14001 certification and are proactively operating their certified environmental management systems. The facilities are reducing the levels of SO*x*, NO*x*, and other pollutants generated during refining processes and are fully compliant with the regulatory standards of their regions.

Regarding industrial waste, the Japanese oil industry has set itself the "reduce, reuse, recycle" goal of reducing the volume of industrial waste that is ultimately disposed of to 67% of the 1990 level by 2010. Cosmo Oil has progressed rapidly toward this objective, and the volume of its industrial waste during fiscal 2001 was only 70% of the fiscal 1991 level.

Cosmo Oil has also proactively worked to conserve energy. The Chiba, Yokkaichi, and Sakai refineries are equipped with highly energy-efficient cogeneration facilities that are helping prevent global warming. The share of the electric power needs of the Company's refineries that is met with self-generated power has reached 77%, and plans call for further boosting this share. Moreover, the Company has taken thorough energy conservation measures at its refineries through careful attention to the precise optimization of refining facility management. In recognition of this, the Sakaide Refinery was given a special award from Japan's Energy Agency during fiscal 2001.

Employees at each Cosmo Oil refinery and transshipment terminal have been given training and encouragement to be extremely rigorous in their safety-management activities related to the unloading of seaborne and land-borne shipments. The Company has also equipped its facilities with such environmental protection equipment as that for recovering vapor emitted during the loading of tank trucks and oil fences for the prevention of water pollution.

Cosmo Oil's service stations are thorough in their activities aimed at preventing water and noise pollution as well as in consistently using industrial waste management manifests to ensure proper waste disposal. Careful attention has been given to maximizing the environmental friendliness of service station operations, from safety training for employees to introducing uniforms made from recycled materials.

More detailed information on Cosmo Oil's environmental protection activities during fiscal 2001 is scheduled to be made public in the form of the Company's second environmental brochure.

Exhaust gas processing units have been installed to control discharges of NO*x* generated during oil refining processes.

COMMUNITY INVOLVEMENT

The happy faces at the Cosmo Waku Waku Camp 2000 summer camp program are a result of the staff's painstaking preparations.

The Cosmo Christmas Concert is held each year.

The proceeds from the Cosmo Christmas Concert were donated to refugees via the Miyakejima Disaster Support Center.

Aiming to be an excellent corporate citizen, Cosmo Oil works to make a broad range of contributions to society through cooperation with residents of local communities, non-governmental organizations, and other companies. The Company's fundamental policy is to proactively engage in long-term social contribution programs regardless of trends in its performance, to undertake innovative social contribution programs, and to encourage the participation of its employees in such programs.

Support for Miyakejima Refugees

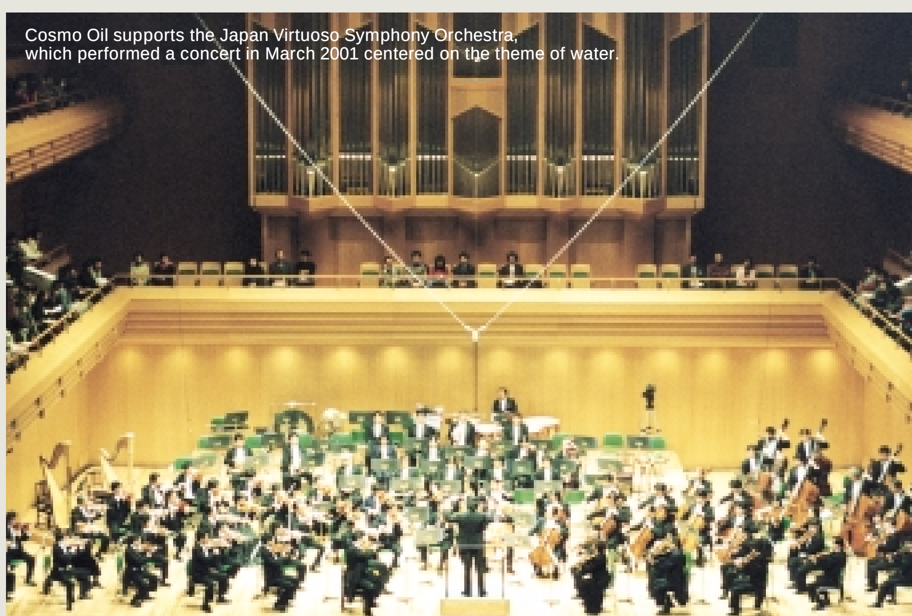
During fiscal 2001, Cosmo Oil provided support for residents of Miyakejima, an island in metropolitan Tokyo, who have had to flee their residences due to volcanic eruptions. In December 2000, Cosmo Oil cooperated with other companies to organize the Cosmo Christmas Concert—for charity—in the lobby of the Company's head office building. The majority of those performing in the concert were Cosmo Oil employees, and a large number of the Company's officers and employees participated in fund-raising efforts. The proceeds from the concert were donated to refugees via the Miyakejima Disaster Support Center. In addition, many Cosmo Oil employees participated in a get-together event with refugees, at which the Company presented the refugees with Cosmo Oil calendars.

Proactive Sponsorship of Cultural Activities

As one of its programs for supporting cultural activities, Cosmo Oil has provided support for the Japan Virtuoso Symphony Orchestra since 1995, and such support was again rendered for that orchestra's concert held in March 2001. From 2001, the concert has focused on nature themes, in line with the Company's emphasis on environmental protection. In December 2000, the Company invited children attending a foster home school and primary schools in Tokyo's Minato Ward to attend the Cosmo Charity Concert, an event managed by employee volunteers.

Broad Range of Contributions to Automotive Society

Since 1993, Cosmo Oil has organized Cosmo Waku Waku Camp, a summer camp program for children orphaned due to traffic accidents that is operated by volunteers from among the Company's employees. In fiscal 2001, 45 children were invited to have fun while learning the importance of respect for nature and other aspects of social responsibility. The head office, branches, and refineries also actively undertake activities geared toward their local communities, including area cleanup campaigns and the hosting of sports events.



Cosmo Oil supports the Japan Virtuoso Symphony Orchestra, which performed a concert in March 2001 centered on the theme of water.

FINANCIAL SECTION

COSMO OIL COMPANY, LIMITED and Its Consolidated Subsidiaries
March 31

	Millions of yen					Thousands of U.S. dollars (Note)
	1997	1998	1999	2000	2001	2001
For the year:						
Net sales	¥1,729,495	¥1,680,478	¥1,443,457	¥1,584,678	¥1,845,842	$14,885,823
Operating income	35,409	27,901	22,860	16,665	36,582	295,016
Net income	8,839	5,340	839	4,841	8,674	69,952
At year-end:						
Total shareholders' equity	189,790	190,716	186,496	179,536	177,773	1,433,653
Total assets	1,287,172	1,277,022	1,229,285	1,294,843	1,319,960	10,644,839
	Yen					U.S. dollars (Note)
Per common share:						
Net income	¥ 13.99	¥ 8.45	¥ 1.33	¥ 7.76	¥ 13.81	$ 0.11
Cash dividends	8.00	8.00	6.00	6.00	6.00	0.05
Ratios:						
Operating profit margin (%)	2.0	1.7	1.6	1.1	2.0	
Return on equity (%)	4.7	2.8	0.4	2.7	4.9	
Return on assets (%)	0.7	0.4	0.1	0.4	0.7	
Interest coverage ratio (times)	1.8	1.5	1.4	1.0	2.1	
Dividend payout ratio (%)*	69.74	98.95	51.67	98.29	72.56	

Note: U.S. dollar figures are translated from yen, for convenience only, at the rate of ¥124 to US$1, the approximate rate of exchange at March 31, 2001.
* Dividend payout ratio is calculated on a non-consolidated basis.

Net Sales

Consolidated net sales increased 16.5% from the previous fiscal year, or ¥261.2 billion, to ¥1,845.8 billion (US$14,885.8 million). The principal reasons for the rise in consolidated net sales were the growth in selling prices in the oil business segment and the decision to include an additional seven subsidiaries within the scope of consolidation in light of the increasing importance of consolidated accounting practices. In the cases of eight of the nine consolidated subsidiaries that were removed from the scope of consolidation, the removal was only nominal due to mergers that created new consolidated subsidiaries, and there was thus no effect on consolidated net sales.

Petroleum—Trends in oil prices, currency exchange rates, and the Japanese economy caused domestic gasoline prices to bottom out and begin rising. Overall, however, the rise in crude oil prices was not completely reflected in price rises for petroleum fuels, particularly in the case of industrial-use fuels. Overall domestic demand for petroleum fuels was almost unchanged from the previous year, although consumption levels were higher for gasoline and three of the four principal middle distillates, with diesel fuel being the exception. As a result, Cosmo Oil's Petroleum business segment accounted for ¥1,766.5 billion in net sales, up 15.9%, or ¥242.8 billion. This corresponded to 95.7% of consolidated net sales, down 0.5 percentage point from the previous fiscal year.

Real Estate—Although the Company continued with a program to expedite the disposal of real estate assets for sale that was begun in the previous year, net sales for the real estate segment declined 15.1% year-on-year, or ¥1.0 billion, to ¥5.4 billion. This corresponded to 0.3% of consolidated net sales, down 0.1 percentage point from the previous fiscal year.

Other—The principal components of the other business segment are engineering and leasing businesses. Net sales for this segment advanced 35.5% year-on-year, or ¥19.4 billion, to ¥74.0 billion. This corresponded to 4.0% of consolidated net sales, up 0.6 percentage point from the previous fiscal year

Costs, Expenses, and Earnings

On a consolidated basis, the cost of sales increased 16.6% from the previous fiscal year, or ¥237.1 billion, to ¥1,664.8 billion (US$13,425.5 million). This rise was 0.1 percentage point greater than that in net sales, causing the ratio of cost of sales to net sales to grow 0.1 percentage point, to 90.2%. This reflected a change in the inventory valuation method employed by the Company. Inventories were previously valued at cost based on the last-in, first-out (LIFO) method but, beginning from the period under review, have been valued at original cost based on the gross average cost method (GACM) with the goal of making the book value of inventories more appropriately reflect fluctuations in crude oil prices. Together with Groupwide cost-reduction measures and a lowering of yen-denominated crude oil procurement costs—due to a rise in the average value of the yen vis-à-vis the U.S. dollar during the fiscal year—the change partially offset the effects of the surge in crude oil prices and the Company's inability to fully adjust selling prices for refined petroleum products in line with the rise in crude oil procurement costs.

Selling, general and administrative (SG&A) expenses edged up 2.9%, or ¥4.1 billion, to ¥144.5 billion (US$1,165.3 million). Although Groupwide rationalization and cost-cutting measures enabled large drops in shipping costs, the cost of work contracted out, and general expenses, SG&A expenses were pushed upward due to the general expenses of newly consolidated subsidiaries, particularly personnel expenses. Another factor boosting SG&A expenses was a rise in retirement allowance expenses due to the adoption of new consolidated accounting methods related to retirement allowances. However, the ratio of SG&A expenses to net sales declined 1.1 percentage points, to 7.8%.

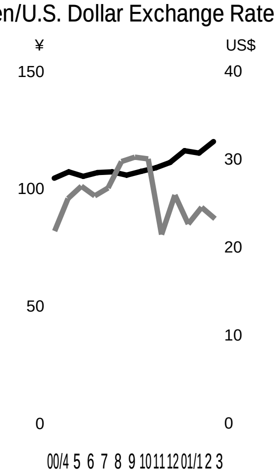
As a result of the rise in net sales, the change in the inventory evaluation method, measures taken to restrain the rise in the cost of sales, and the limited rise in SG&A expenses, operating income surged 119.5%, or ¥19.9 billion, to ¥36.6 billion (US$295.0 million). The ratio of operating income to net sales increased 0.9 percentage point, to 2.0%.

Petroleum—Groupwide rationalization and cost-cutting measures, the previously described change in inventory valuation methodology, higher selling prices in oil development operations, and other factors combined to raise operating income 227.7%, or ¥24.7 billion, to ¥35.5 billion.

Real Estate—Despite the Company's continued efforts to expedite the disposal of real estate for sale, a decrease in net sales, deteriorating market conditions, and other factors caused operating income to drop 50.2%, or ¥2.3 billion, to ¥2.3 billion.

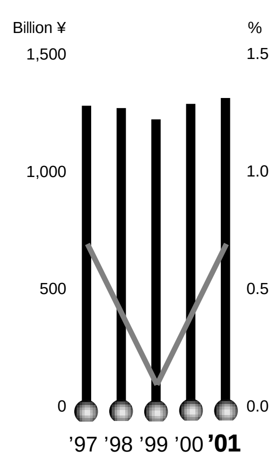
Other—Although net sales grew considerably, the other business segment recorded an operating loss of ¥0.4 billion.

Crude Oil Price and Yen/U.S. Dollar Exchange Rate



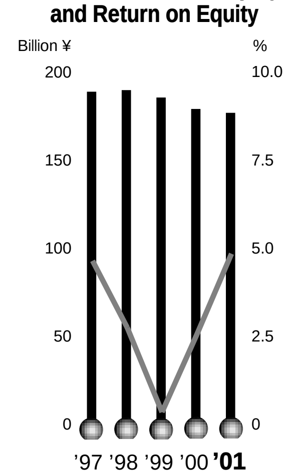
Yen/U.S. Dollar Exchange Rate (Left scale)
Crude Oil Price per Barrel (Right scale)

Total Assets and Return on Assets



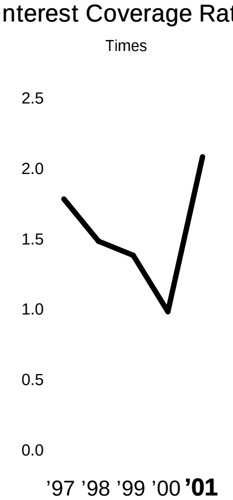
Total Assets (Left scale)
ROA (Right scale)

Total Shareholders' Equity and Return on Equity



Total Shareholders' Equity (Left scale)
ROE (Right scale)

Interest Coverage Ratio



Other expenses, net, surged ¥10.8 billion year-on-year, to ¥14.1 billion (US$113.9 million). Negative factors included a ¥6.8 billion decrease in net gain on sale of disposal of property, plant and equipment, to ¥7.0 billion; a ¥2.2 billion decrease in exchange gain, to ¥1.3 billion, due to yen depreciation; and a ¥6.0 billion loss on sale of marketable securities, compared to a ¥7.1 billion gain in the previous fiscal year.

Positive factors included a ¥1.6 billion improvement in the net value of interest and dividend items, to an expense of ¥15.2 billion; the lack of special severance payments for early retired employees, which amounted to ¥7.0 billion in the previous year; and a ¥2.4 billion improvement in equity in (losses) earnings of affiliates, from a loss of ¥1.8 billion in the previous fiscal year to a gain of ¥0.6 billion, which reflected the addition of new companies accounted for by the equity method as well as an improvement in the performance of affiliates.

As a result, income before income taxes and minority interests totaled ¥22.5 billion (US$181.1 million), up 68.7%, or ¥9.1 billion, and net income surged 79.2%, or ¥3.8 billion, to ¥8.7 billion (US$70.0 million). The principal reason why the rate of increase in net income exceeded that in income before income taxes and minority interests was that the tax burden after application of tax effect accounting dropped, from 61.0% to 56.4%.

Diluted net income per share grew ¥5.85, to ¥13.53 (US$0.11).

Financial Position

In light of the severity of the operating environment, the Company has worked to increase the efficiency of total capital employed by endeavoring to restrain growth in assets and reduce the level of interest-bearing debt. However, total assets edged up 1.9% from the previous fiscal year-end, or ¥25.1 billion, to ¥1,320.0 billion (US$10,644.8 million), due to several factors, including the addition of the assets of seven subsidiaries newly brought within the scope of consolidation.

Total current assets grew ¥16.0 billion year-on-year, to ¥631.0 billion (US$5,088.3 million). This was principally the result of a ¥32.3 billion rise, to ¥248.3 billion, in notes and accounts receivable, trade that reflected the rise in net sales as well as the subsidiaries newly brought within the scope of consolidation and an increase in inventories of ¥26.7 billion, to ¥190.2 billion, reflecting the change from the LIFO to the GACM valuation methodology as well as an actual rise in inventory levels. Cash and deposits increased ¥3.3 billion, to ¥54.2 billion, principally reflecting the rise in net sales. Other current assets grew ¥14.9 billion, to ¥103.3 billion. Partially offsetting the rises in the aforementioned items was a ¥61.5 billion drop in marketable securities, to ¥35.8 billion, which reflected the transfer of ¥50.9 billion of securities from marketable securities to the investment securities item due to a change in investment objective.

Payments for purchases of property, plant and equipment amounted to ¥19.6 billion (US$158.3 million) on a cash-flow basis. The principal targets of investment were renewal projects at refineries. Although the value of property, plant and equipment was boosted due to the existing assets of newly consolidated subsidiaries, the increase in capital investment was exceeded by the increase in depreciation, and, thus, net property, plant and equipment fell ¥4.9 billion, to ¥535.1 billion (US$4,315.5 million).

Other assets were increased ¥50.9 billion by the previously mentioned transfer of securities from the marketable securities item to the investments in unconsolidated subsidiaries, affiliates, and securities item, but the sale of ¥33.5 billion in trust assets and other factors restrained the rise in other assets, which grew ¥14.1 billion, to ¥153.9 billion (US$1,241.0 million).

Excluding minority interests, total liabilities edged up 2.5%, or ¥27.1 billion, to ¥1,120.9 billion (US$9,039.9 million). Despite the Company's accelerated progress in reducing interest-bearing debt, operating liabilities and other liabilities increased primarily due to growth in procurement expenses that stemmed from business expansion and a rise in accrued excise tax for oil product and other taxes that reflected the prolongation of the relevant payment period.

Interest-bearing debt fell ¥76.9 billion, to ¥610.7 billion (US$4,924.9 million). This principally reflected the repayment of long-term borrowings and the redemption of convertible bonds, which together totaled ¥83.3 billion on a cash flow basis. This reduction was partially offset by the existing interest-bearing debt of newly consolidated subsidiaries.

Operating liabilities and other liabilities were up ¥104.0 billion, to ¥510.3 billion (US$4,115.0 million). This principally reflected a ¥44.8 billion increase in notes and accounts payable, trade that stemmed from business expansion and the existing liabilities of newly consolidated subsidiaries and a ¥31.9 billion rise in income, excise and other taxes payable that resulted from the shift into the start of fiscal 2002 of the payment date for excise tax for oil products and other taxes for the period under review. Other liabilities grew ¥26.0 billion, primarily due to a rise in deferred tax liabilities.

Total shareholders' equity declined ¥1.8 billion, to ¥177.8 billion (US$1,433.7 million), and the rise in total liabilities caused the equity ratio to decrease 0.4 percentage point, to 13.5%. Despite the rise in net income, the decline in total shareholders' equity reflected a drop in consolidated retained earnings due to the ¥2.0 billion cumulative effect of adopting deferred income tax accounting.

Cash Flows

Free cash flow increased greatly during the year, although most of this cash flow was used to reduce the balance of interest-bearing debt. Thus, cash and cash equivalents at the of year increased only ¥1.8 billion during the year under review and amounted to ¥97.8 billion (US$788.6 million) at March 31, 2001. This includes ¥1.5 billion of additional cash stemming from the consolidation of additional subsidiaries as well as ¥0.7 billion of additional cash stemming from the merger of consolidated subsidiaries.

Net cash provided by operating activities amounted to ¥58.8 billion (US$474.4 million), a ¥101.5 billion change from the net cash outflow of ¥42.7 billion in the previous year. Cash inflow from income before income taxes and minority interests was ¥22.5 billion. After adjustment for depreciation and other non-cash items and the deduction of tax payments, cash inflow amounted to ¥39.4 billion, ¥30.1 billion more than in the previous year. This reflected the relatively high level of income before income taxes and minority interests, the considerable value of such non-cash items as asset write-downs, and the absence of special severance payments for early retired employees in the period under review.

Cash inflow attributable to changes in operating and other assets and liabilities amounted to ¥19.5 billion (US$156.9 million), a ¥71.4 billion change from the net cash outflow of ¥52.0 billion in the previous year. This principally reflected a ¥78.6 billion reduction in the funding burden related to accrued excise tax for oil product and other taxes that reflected the timing of the tax payment dates for the period under review as well as the previous fiscal year.

Net cash provided by investing activities amounted to ¥27.3 billion (US$220.5 million), up from ¥13.5 billion in the previous year. This primarily reflected the ¥42.0 billion in cash inflow from the disposal of trust assets, which was partially offset by ¥8.5 billion in cash outflow from an increase in payment for capital investments. Net payment for other items amounted to ¥6.3 billion.

As a result of the above items, free cash flow during the period amounted to ¥86.2 billion, an improvement of ¥115.3 billion from the previous year. This free cash flow provided ample resources for considerably reducing the level of the Company's interest-bearing debt.

Net cash used in financing activities totaled ¥87.2 billion (US$703.5 million), primarily due to the previously mentioned reduction of interest-bearing debt, and this figure represents a change of ¥118.5 billion from the previous year, when financing activities generated ¥31.3 billion of net cash inflow. Changes in short- and long-term interest-bearing debt caused a net cash outflow of ¥83.3 billion. This reflected net reductions of ¥48.2 billion and ¥44.6 billion in short- and long-term interest-bearing loans and in convertible bonds, respectively, which were partially offset by the issuance of ¥10.0 billion in straight bonds.

CONSOLIDATED BALANCE SHEETS

COSMO OIL COMPANY, LIMITED and Its Consolidated Subsidiaries
March 31, 2000 and 2001

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2000	2001	2001
ASSETS:			
Current assets:			
Cash and deposits (Note 5)	¥ 50,855	¥ 54,157	$ 436,750
Marketable securities (Note 9)	97,285	35,817	288,847
Notes and accounts receivable, trade (Note 3)	216,059	248,326	2,002,629
Less allowance for doubtful accounts	(1,134)	(834)	(6,726)
	214,925	247,492	1,995,903
Inventories (Note 4)	163,503	190,186	1,533,758
Other current assets (Note 12)	88,424	103,298	833,048
Total current assets	614,992	630,950	5,088,306
Property, plant and equipment (Note 6):			
Land	326,214	323,163	2,606,153
Buildings and structures	352,779	369,738	2,981,758
Machinery and equipment	301,853	319,494	2,576,565
Construction in progress	15,366	15,213	122,686
	996,212	1,027,608	8,287,162
Less accumulated depreciation	(456,143)	(492,488)	(3,971,677)
Net property, plant and equipment	540,069	535,120	4,315,485
Other assets:			
Investments in unconsolidated subsidiaries, affiliates and securities (Notes 6 and 9)	48,831	95,637	771,266
Long-term loans receivable	10,325	8,826	71,177
Other (Note 12)	80,626	49,427	398,605
Total other assets	139,782	153,890	1,241,048
Total assets	¥1,294,843	¥1,319,960	$10,644,839

The accompanying notes are an integral part of these statements.

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2000	2001	2001
LIABILITIES AND SHAREHOLDERS' EQUITY:			
Current liabilities:			
Short-term loans and current maturities of long-term debt (Note 6)	¥ 289,643	¥ 237,067	$ 1,911,831
Notes and accounts payable, trade (Note 3)	183,751	228,563	1,843,250
Income, excise and other taxes payable	84,098	116,042	935,823
Accrued expenses and other current liabilities (Note 12)	101,474	120,884	974,871
Total current liabilities	658,966	702,556	5,665,775
Long-term debt, less current maturities (Note 6)	397,920	373,619	3,013,056
Retirement and severance benefits	3,968	3,612	29,129
Other long-term liabilities (Note 12)	32,991	41,157	331,911
Minority interests	21,462	21,243	171,315
Contingencies (Note 8)			
Shareholders' equity:			
Common stock, par value ¥50 per share			
Authorized–1,700,000,000 shares;			
Issued–631,705,087 shares	51,887	51,887	418,444
Additional paid-in capital	34,092	34,092	274,935
Retained earnings	94,883	92,848	748,774
Foreign currency translation adjustments	(850)	(693)	(5,589)
Less treasury stock, at cost (Note 6)	(476)	(361)	(2,911)
Total shareholders' equity	179,536	177,773	1,433,653
	¥1,294,843	¥1,319,960	$10,644,839

CONSOLIDATED STATEMENTS OF INCOME

COSMO OIL COMPANY, LIMITED and Its Consolidated Subsidiaries
Years ended March 31, 1999, 2000 and 2001

	Millions of yen			Thousands of U.S. dollars (Note 1)
	1999	2000	2001	2001
Net sales (Note 13)	¥1,443,457	¥1,584,678	¥1,845,842	$14,885,823
Cost of sales	1,265,443	1,427,640	1,664,757	13,425,460
Gross profit	178,014	157,038	181,085	1,460,363
Selling, general and administrative expenses	155,154	140,373	144,503	1,165,347
Operating income (Note 13)	22,860	16,665	36,582	295,016
Other income (expenses):				
Interest and dividend income	2,177	2,171	3,445	27,782
Interest expense (Note 6)	(18,488)	(18,991)	(18,692)	(150,741)
Foreign currency exchange gain, net	2,629	3,502	1,347	10,863
Net gain on sale and disposal of property, plant and equipment	5,125	13,819	7,024	56,645
Equity in (losses) earnings of affiliates	(1,406)	(1,798)	555	4,476
Write-down of marketable securities and investments in securities	(2,238)	(2,312)	(2,536)	(20,452)
Gain on sale of marketable securities	—	7,063	—	—
Loss on sale of investment securities	—	—	(6,044)	(48,742)
Special severance payments for early retired employees	(6,080)	(6,956)	—	—
Other, net	(228)	150	779	6,282
	(18,509)	(3,352)	(14,122)	(113,887)
Income before income taxes and minority interests	4,351	13,313	22,460	181,129
Income taxes:				
Current	3,269	4,379	8,245	66,492
Deferred (Note 12)	—	3,745	4,430	35,726
	3,269	8,124	12,675	102,218
Income before minority interests	1,082	5,189	9,785	78,911
Minority interests	(243)	(348)	(1,111)	(8,959)
Net income	¥ 839	¥ 4,841	¥ 8,674	$ 69,952

	Yen			U.S. dollars (Note 1)
Amounts per share of common stock:				
Net income	¥ 1.33	¥ 7.76	¥ 13.81	$ 0.11
Diluted net income	—	7.68	13.53	0.11
Cash dividends	6.00	6.00	6.00	0.05

The accompanying notes are an integral part of these statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

COSMO OIL COMPANY, LIMITED and Its Consolidated Subsidiaries
Years ended March 31, 1999, 2000 and 2001

	Number of shares of common stock (Thousands)	Millions of yen				
		Common stock	Additional paid-in capital	Retained earnings	Foreign currency translation adjustments	Treasury stock
Balance at March 31, 1998	631,705	¥51,887	¥34,092	¥104,737	¥ —	¥ —
Net income for the year	—	—	—	839	—	—
Cash dividends paid	—	—	—	(5,054)	—	—
Bonuses to directors and corporate auditors	—	—	—	(100)	—	—
Increase resulting from decrease in consolidated subsidiaries	—	—	—	95	—	—
Balance at March 31, 1999	631,705	51,887	34,092	100,517	—	—
Net income for the year	—	—	—	4,841	—	—
Cash dividends paid	—	—	—	(3,742)	—	—
Bonuses to directors and corporate auditors	—	—	—	(26)	—	—
Cumulative effect of adopting deferred income tax accounting	—	—	—	955	—	—
Increase resulting from increase in consolidated subsidiaries	—	—	—	2,710	—	(476)
Decrease resulting from increase in affiliates on equity method	—	—	—	(3,751)	—	—
Decrease resulting from decrease in affiliates on equity method	—	—	—	(972)	—	—
Decrease resulting from mergers	—	—	—	(5,649)	—	—
Balance at March 31, 2000	631,705	51,887	34,092	94,883	—	(476)
Net income for the year	—	—	—	8,674	—	—
Adjustments from translation of foreign currency financial statements	—	—	—	—	(693)	—
Cash dividends paid	—	—	—	(3,779)	—	—
Bonuses to directors and corporate auditors	—	—	—	(8)	—	—
Cumulative effect of adopting deferred income tax accounting	—	—	—	(1,982)	—	—
Decrease resulting from increase in consolidated subsidiaries	—	—	—	(30)	—	(106)
Decrease resulting from increase in affiliates on equity method	—	—	—	(522)	—	—
Decrease resulting from mergers	—	—	—	(4,388)	—	—
Sales of treasury stock	—	—	—	—	—	221
Balance at March 31, 2001	631,705	¥51,887	¥34,092	¥ 92,848	¥(693)	¥(361)

	Thousands of U.S. dollars (Note 1)				
	Common stock	Additional paid-in capital	Retained earnings	Foreign currency translation adjustments	Treasury stock
Balance at March 31, 2000	$418,444	$274,935	$765,185	$ —	$(3,838)
Net income for the year	—	—	69,952	—	—
Adjustments from translation of foreign currency financial statements	—	—	—	(5,589)	—
Cash dividends paid	—	—	(30,476)	—	—
Bonuses to directors and corporate auditors	—	—	(64)	—	—
Cumulative effect of adopting deferred income tax accounting	—	—	(15,984)	—	—
Decrease resulting from increase in consolidated subsidiaries	—	—	(242)	—	(855)
Decrease resulting from increase in affiliates on equity method	—	—	(4,210)	—	—
Decrease resulting from mergers	—	—	(35,387)	—	—
Sales of treasury stock	—	—	—	—	1,782
Balance at March 31, 2001	$418,444	$274,935	$748,774	$(5,589)	$(2,911)

The accompanying notes are an integral part of these statements.

CONSOLIDATED STATEMENT OF CASH FLOWS (1999)

COSMO OIL COMPANY, LIMITED and Its Consolidated Subsidiaries
Year ended March 31, 1999

	Millions of yen
	1999
Cash flows from operating activities:	
Net income	¥ 839
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation	21,773
Gain on disposals of property, plant and equipment	(5,125)
Write-down of marketable and investment securities	2,238
Gain on redemption of convertible bonds	(1,199)
Loss on collectible accounts receivable	974
Effect of decrease of consolidated subsidiaries	(289)
Bonuses to directors and statutory auditors	(100)
Decrease in other assets	2,221
Increase in retirement and severance benefits	84
Equity in losses of affiliates	1,406
Decrease in minority interests	(459)
Other, net	18
Net decrease in current assets:	
Notes and accounts receivable	4,274
Inventories	10,410
Other current assets	6,242
Net decrease in current liabilities:	
Notes and accounts payable	(7,009)
Income, excise and other taxes payable	(5,655)
Accrued expenses and other current liabilities	(16,790)
Increase in other long-term liabilities	3,865
Net cash provided by operating activities	17,718
Cash flows from investing activities:	
Purchases of property, plant and equipment	(31,325)
Proceeds from disposals of property, plant and equipment	17,945
Increase in marketable securities	(753)
Increase in investments in unconsolidated subsidiaries, affiliates and securities	(5,099)
Decrease in long-term loans receivable	1,426
Net cash used in investing activities	(17,806)
Cash flows from financing activities:	
Proceeds from long-term loans payable	67,716
Repayments on long-term loans payable	(47,839)
Decrease in short-term loans	(29,415)
Cash dividends paid	(5,054)
Net cash used in financing activities	(14,592)
Net decrease in cash	(14,680)
Cash at beginning of year	52,034
Cash at end of year	¥37,354

The accompanying notes are an integral part of this statement.

CONSOLIDATED STATEMENTS OF CASH FLOWS (2000 AND 2001)

COSMO OIL COMPANY, LIMITED and Its Consolidated Subsidiaries
Years ended March 31, 2000 and 2001

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2000	2001	2001
Cash flows from operating activities:			
Income before income taxes and minority interests	¥13,313	¥22,460	$181,129
Adjustments to reconcile income before income taxes and minority interests to net cash used in operating activities:			
Depreciation and amortization	23,436	24,672	198,968
Amortization of consolidation goodwill	431	274	2,210
Decrease in allowance for doubtful accounts	(121)	(469)	(3,782)
Increase in valuation allowance for investments in securities	185	—	—
Decrease in retirement and severance benefits	(1,502)	(4,090)	(32,984)
Increase in liability for severance and retirement benefits	—	3,633	29,298
Increase (decrease) in provision for loss of loan guarantee	558	(558)	(4,500)
Interest and dividend income	(2,171)	(3,445)	(27,782)
Interest expense	18,991	18,692	150,742
Equity in earnings or losses of affiliates	1,798	(555)	(4,476)
Net gain on sale and of property, plant and equipment	(14,520)	(7,024)	(56,645)
Loss on sale of investment securities	—	6,044	48,742
Write-down of marketable securities and investments in securities	—	2,536	20,451
Special severance payments for early retired employees	6,956	—	—
Increase in notes and accounts receivable	(11,731)	(31,786)	(256,339)
Increase in inventories	(22,364)	(26,549)	(214,105)
Increase in notes and accounts payable	37,916	44,935	362,379
Increase in other current assets	(23,297)	(11,987)	(96,669)
Decrease (increase) in other current liabilities	(28,289)	49,650	400,403
Decrease (increase) in other long-term liabilities	(11,720)	645	5,202
Other, net	(3,188)	(4,062)	(32,758)
Subtotal	(15,317)	83,016	669,484
Interest and dividend received	2,008	2,743	22,121
Interest paid	(18,841)	(18,515)	(149,315)
Amount of special severance payments for early retired employees	(6,956)	—	—
Income taxes paid	(3,592)	(8,420)	(67,903)
Net cash (used in) provided by operating activities	(42,698)	58,824	474,387
Cash flows from investing activities:			
Payments for purchases of marketable securities	(16,708)	—	—
Proceeds from disposal of marketable securities	18,193	—	—
Payments for purchases of property, plant and equipment	(24,239)	(19,626)	(158,274)
Proceeds from disposal of property, plant and equipment	29,165	16,551	133,476
Proceeds from sale of settled property	—	42,000	338,709
Payments for purchases of investment in securities	(6,274)	(7,036)	(56,742)
Proceeds from sale of investment in securities	8,719	7,335	59,153
Increase in intangible assets and deferred charges	(1,950)	(1,923)	(15,508)
Proceeds from purchase of investment in newly consolidated subsidiaries	3,206	—	—
Proceeds from sale of investment in a consolidated subsidiary	—	915	7,379
Decrease in short-term loans	—	(609)	(4,911)
Payments for long-term loans	(2,319)	(3,916)	(31,581)
Proceeds from long-term loans receivable	6,091	4,554	36,726
Payments for investment money	—	(8,454)	(68,177)
Other, net	(346)	(2,443)	(19,702)
Net cash provided by investing activities	13,538	27,348	220,548
Cash flows from financing activities:			
Increase (decrease) in short-term loans	19,767	(16,627)	(134,089)
Repayments for commercial papers	(10,000)	—	—
Proceeds from long-term loans payable	61,516	4,905	39,557
Repayments for long-term loans payable	(48,999)	(36,947)	(297,959)
Proceeds from issuing straight bonds	55,000	10,000	80,645
Repayments of convertible bonds	(42,054)	(44,584)	(359,548)
Cash dividends paid	(3,742)	(3,777)	(30,460)
Other, net	(217)	(199)	(1,605)
Net cash provided by (used in) financing activities	31,271	(87,229)	(703,459)
Effect of exchange rate changes on cash and cash equivalents	(54)	588	4,742
Net increase (decrease) in cash and cash equivalents	2,057	(469)	(3,782)
Cash and cash equivalents at beginning of year (Note 5)	89,735	96,013	774,298
Cash and cash equivalents from newly consolidated subsidiaries	4,221	1,515	12,218
Cash and cash equivalents from mergers	—	729	5,879
Cash and cash equivalents at end of year (Note 5)	¥96,013	¥97,788	$788,613

The accompanying notes are an integral part of these statements.

COSMO OIL COMPANY, LIMITED and Its Consolidated Subsidiaries
Years ended March 31, 1999, 2000 and 2001

1 SUMMARY OF ACCOUNTING POLICIES

(1) Basis of presenting consolidated financial statements

Cosmo Oil Company, Limited, (the "Company") and its consolidated domestic subsidiaries maintain their accounts and records in accordance with the provisions set forth in the Japanese Commercial Code and the Securities and Exchange Law and in conformity with accounting principles and practices generally accepted in Japan, which are different from the accounting and disclosure requirements of International Accounting Standards. The accounts of overseas consolidated subsidiaries are based on their accounting records maintained in conformity with generally accepted accounting principles and practices prevailing in the respective countries of domicile.

The accompanying consolidated financial statements are a translation of the audited consolidated financial statements of the Company and its consolidated subsidiaries which were prepared in accordance with accounting principles and practices generally accepted in Japan from the accounts and records maintained by the Company and its consolidated subsidiaries and were filed with the appropriate Local Finance Bureau of the Ministry of Finance as required by the Securities and Exchange Law.

In preparing the accompanying consolidated financial statements, certain reclassifications have been made in the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan. The consolidated statements of cash flows for 1999 and shareholders' equity for 1999, 2000 and 2001 have been prepared for the purpose of inclusion in the consolidated financial statements although such statements were not required for domestic purposes and not filed with the regulatory authorities.

The translation of the Japanese yen amounts into U.S. dollars are included solely for the convenience of the reader, using the prevailing exchange rate at March 31, 2001, which was ¥124 to U.S.$1.00. The convenience translations should not be construed as representations that the Japanese yen amounts have been, could have been, or could in the future be, converted into U.S. dollars at this or any other rate of exchange.

(2) Reporting entity

The consolidated financial statements include the accounts of the Company and its significant subsidiaries. All significant intercompany transactions and account balances are eliminated in the consolidation.

Effective for the year ended March 31, 2000, all companies are required to consolidate all significant investees which are controlled through substantial ownership of majority voting rights or existence of certain conditions. Previously, only majority-owned companies were consolidated.

In the elimination of investments in subsidiaries, the assets and liabilities of the subsidiaries, including the portion attributable to minority shareholders, are recorded based on the fair value at the time the Company acquired control of the respective subsidiaries.

The excess of cost over net assets of subsidiaries acquired is amortized on a straight-line basis over a period of five years.

Investments in non-consolidated subsidiaries and affiliates of which the Company has the ability to exercise significant influence over operating and financial policies, are accounted for on the equity method. Prior to April 1, 1999, only investments in companies of which the Company owned 20% to 50% of the voting rights and had the ability to significantly influence over financial, operational or business policies were accounted for using the equity method. There was no effect of adopting the new accounting standard.

The numbers of consolidated subsidiaries and affiliates accounted for using the equity method at March 31, 1999, 2000 and 2001 were as follows:

	1999	2000	2001
Consolidated subsidiaries	18	22	20
Subsidiaries on equity method	—	—	12
Affiliates on equity method	3	3	3

Investments in unconsolidated subsidiaries and affiliates not accounted for using the equity method are carried at cost (adjusted for any substantial and non-recoverable decline in value). The effect on consolidated net income of not applying the equity method for these investments is not material in the aggregate.

(3) Statements of cash flows

In preparing the consolidated statements of cash flows for 2000 and 2001, cash on hand, readily-available deposits and short-term highly liquid investments with maturities of not exceeding three months at the time of purchase are considered to be cash and cash equivalents.

The Company prepared the 2000 and 2001 consolidated statements of cash flows as required by and in accordance with the "Standards for Preparation of Consolidated Cash Flow Statements, etc." effective from the year ended March 31, 2000. The 1999 consolidated statement of cash flows, which was voluntarily prepared for the purpose of inclusion in the consolidated financial statements in a form familiar to readers outside Japan has not been restated. Significant differences in the consolidated statements of cash flows for 2000, 2001 and previous year include the use of pretax income in 2000 and 2001 instead of net income and additional disclosure in cash flows from operating activities in 2000 and 2001 of interest expense, interest and dividend income, interest and dividend received and income taxes paid.

(4) Conversion of foreign currencies and translation of statements

Short-term receivables and payables denominated in foreign currencies are translated into Japanese yen at the year-end rates. Prior to April 1, 2000, long-term receivables and payables denominated in foreign currencies were translated at historical rates.

Effective April 1, 2000, the Company and its consolidated subsidiaries adopted the revised accounting standard for foreign currency translation, "Opinion Concerning Revision of Accounting Standard for Foreign Translation", issued by the Business Accounting Deliberation Council on October 22, 1999. Under the revised accounting standard, long-term receivables and payables denominated in foreign currencies are also translated into Japanese yen at the year-end rate.

As a result of adopting the new accounting standard for foreign currency translation, income before income taxes decreased by ¥2,661 million ($21,460 thousand).

Financial statements of consolidated overseas subsidiaries are translated into Japanese yen at the year-end rate, except that shareholders' equity accounts are translated at historical rates and income statement items resulting from transactions with the Company at the rates used by the Company.

Due to the adoption of the revised accounting standard, the Company and its domestic subsidiaries report foreign currency translation adjustments in the shareholders' equity. The prior year's amount, which was included in assets, has been reclassified to conform to the 2001 presentation.

(5) Allowance for doubtful accounts

Notes and accounts receivable, as well as loans and other receivable, are evaluated as to their collectibility. Effective April 1, 2000, new Japanese accounting standard for financial instruments was adopted in the year ended March 31, 2001, and the Company and its consolidated domestic subsidiaries provide allowance for doubtful accounts by estimating uncollectible amount with respect to certain identified doubtful receivables and by calculating amounts using the percentage of actual collection losses. Previously, allowance for doubtful accounts was provided at the maximum amount deductible under the Japanese tax laws plus certain uncollectable amounts.

As a result of adopting the new accounting standard for financial instruments operating income and income before income taxes increased by ¥3,234 million ($26,081 thousand).

(6) Marketable securities and investments in unconsolidated subsidiaries, affiliates and securities

Marketable securities, investments in unconsolidated subsidiaries, affiliates and other securities are primarily stated at cost determined by the moving-average method.

Prior to April 1, 2000, securities of the Company and its consolidated subsidiaries were stated at moving-average cost.

Effective April 1, 2000, the Companies adopted new Japanese accounting standard for financial instruments (“Opinion Concerning Establishment of Accounting Standard for Financial Instruments” issued by the Business Accounting Deliberation Council on January 22, 1999).

Upon applying the new accounting standard, all companies are required to examine the intent of holding each security and classify those securities as (a) securities held for trading purposes (b) debt securities intended to be held to maturity (hereafter, “held-to-maturity debt securities”), (c) equity securities issued by subsidiaries and affiliated companies, and (d) for all other securities that are not classified in any of the above categories (hereafter, “available-for-sale securities”).

Held-to-maturity debt securities are stated at amortized cost. Equity securities issued by subsidiaries and affiliated companies which are not consolidated or accounted for using the equity method, are stated at moving-average cost. Available-for-sale securities are stated at moving-average cost.

If the market value of held-to-maturity debt securities, equity securities issued by unconsolidated subsidiaries and affiliated companies, and available-for-sale securities, declines significantly, such securities are stated at fair market value and the difference between fair market value and the carrying amount is recognized as loss in the period of the decline. For equity securities with no available fair market value, if the net asset value of the investee decline significantly, such securities are required to be written down to the net asset value with the corresponding losses in the period of decline. In these cases, such fair market value or the net asset value will be the carrying amount of the securities at the beginning of next year.

Based on the examination of the intent of holding each security upon application of the new accounting standard on April 1, 2000, held-to-maturity debt securities and available-for-sale securities maturing within one year from the balance sheet date, which are similar to cash, are included in current assets, and other securities are included in investments and other assets. As a result, at April 1, 2000, securities in current assets decreased by ¥50,872 million ($410,258 thousand) and investment securities increased by the same amount compared with what would have been reported under the previous accounting policy.

(7) Inventories

Effective April 1, 2000, the Company changed its inventory costing method for finished products, semi-finished products and materials from the last-in, first-out method to the average method as discussed in Note 2.

In-transit inventory is stated at cost determined by the specific identification method.

(8) Property, plant and equipment and depreciation

Property, plant and equipment are stated at cost. Depreciation is computed primarily using the straight-line method over the estimated useful lives of the assets.

The cost and accumulated depreciation applicable to assets retired or otherwise disposed of are eliminated from the related accounts and the gain or loss on disposal is credited or charged to income.

Expenditures for new facilities and those that substantially increase the useful lives of existing property, plant and equipment are capitalized. Maintenance, repair and minor renewals are charged to income as incurred.

(9) Research and development costs

Research and development costs for the improvement of existing skills and technologies or the development of new skills and technologies, including basic research and fundamental development costs, are charged to operations in the period incurred.

The Company and its consolidated subsidiaries amortize software for its own using the straight-line method over the estimated useful lives (five years).

(10) Retirement and severance benefits and pension costs

Effective April 1, 2000, the Company adopted new accounting standard, “Opinion on Setting Accounting Standard for Employees’ Severance and Pension Benefits”, issued by the Business Accounting Deliberation Council on June 16,1998 (the “New Accounting Standard”).

Under the New Accounting Standard, liabilities and expenses for severance and retirement benefits are determined based on the amounts actuarially calculated using certain assumptions.

The Company and its consolidated subsidiaries provided allowance for employees’ severance and retirement benefits at March 31, 2001 based on the estimated amounts of projected benefit obligation and the fair value of the plan assets at that date.

The net transition obligation amounting to ¥23,696 million ($191,097 thousand) will be recognized in expenses in equal amounts primarily over 5 years commencing with the year ended March 31, 2001. Actuarial gains and losses are recognized in expenses in equal amounts over 10 years, which is the average of the estimated remaining service lives, commencing with the following period.

As a result of the adoption of the New Accounting Standard, in the year ended March 31, 2001, severance and retirement benefit expenses decreased by ¥2,385 million ($19,234 thousand), operating income increased and income before income taxes increased by ¥2,363 million ($19,056 thousand), compared with what would have been recorded under the previous accounting standard.

(11) Finance leases

Finance leases except for those leases which the ownership of the leased assets is considered to be transferred to the lessee, are accounted for in the same manner as operating leases.

(12) Shareholders' equity

Under the Japanese Commercial Code, at least 50% of the issue price of new shares, with a minimum of the par value thereof, is required to be credited to common stock. The portion which is to be credited to common stock is determined by resolution of the Board of Directors. Proceeds in excess of the amounts credited to common stock are credited to additional paid-in capital.

Under the Code, certain amounts of retained earnings equal to at least 10% of cash dividends and bonuses to directors and corporate auditors are required to be set aside as a legal reserve until the reserve equals 25% of common stock. The reserve is not available for dividends but may be used to reduce a deficit by resolution of the shareholders or may be capitalized by resolution of the Board of Directors. The legal reserve is included in the retained earnings.

The maximum amount that the Company can distribute as dividends is calculated based on the unconsolidated financial statements of the Company and in accordance with the Japanese Commercial Code subject to certain covenants regarding convertible bonds (see Note 6).

(13) Issuance costs of corporate bonds

Issuance costs of corporate bonds are charged to income in the fiscal year incurred.

(14) Derivative transaction and hedge accounting

The new accounting standard for financial instruments, effective from the year ended March 31, 2001, requires companies to state derivative financial instruments at fair value and to recognize changes in the fair value as gains or losses unless derivative financial instruments are used for hedging purposes.

If derivative financial instruments are used as hedges and meet certain hedging criteria, the Company defers recognition of gains or losses resulting from changes in fair value of derivative financial instruments until the related losses or gains on the hedged items are recognized.

Also, if interest rate swap contracts are used as hedge and meet certain hedging criteria, the net amount to be paid or received under the interest rate swap contract is added to or deducted from the interest on the assets or liabilities for which the swap contract was executed.

(15) Income taxes

The Company provided income taxes at the amounts currently payable for the years ended March 31, 1999. Effective April 1, 1999, the Company adopted the new accounting standard, which recognizes tax effects of temporary differences between the financial statement basis and the tax basis of assets and liabilities. Under the new accounting standard, the provision for income taxes is computed based on the pretax income included in the consolidated statements of income. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences.

(16) Net income per share

Net income per share is computed based upon the weighted-average number of shares of common stock outstanding during the fiscal year.

Diluted net income per share was not disclosed for the year ended March 31, 1999 as net income per share, assuming all potential shares were converted, was not diluted for the year.

(17) Reclassifications

Certain prior year amounts have been reclassified to conform to the 2001 presentation.

These changes had no impact on previously reported results of operations or shareholders' equity.

2 CHANGES IN ACCOUNTING POLICY

Change in inventory costing method

Prior to April 1, 2000, the Company computed costs of inventories including finished products, semi-finished products, and raw materials, using original costs based on the last-in, first-out (LIFO) method. However as the Company's operating environment has recently featured large fluctuations in crude oil prices, the gap between the book value of inventories and the current market value of inventories tends to become larger. In addition, there has been the progressive shift to the use of current market price-based accounting, and the introduction of new standards for financial instruments, from the fiscal year. Therefore, effective April 1, 2000, the Company adopted the method of costing inventories using original costs based on the overall average price method.

As a result of the change, the balance of inventories at March 31, 2001, was increased by ¥13,566 million ($109,403 thousand), and operating income and income before income taxes and minority interests were increased by the same amounts. The effect of the change on segment information is described in Note 13.

3 EFFECT OF BANK HOLIDAY ON MARCH 31, 2001

As financial institutions in Japan were closed on March 31, 2001, amounts that would normally be settled on March 31, 2001 were collected or paid on the following business day, April 2, 2001. The effects of the settlements on April 2 instead of March 31 included the following:

Notes and accounts receivable, trade	Increased by approximately ¥394 million ($3,177 thousand)
Accounts payable, trade	Increased by approximately ¥ 10 million ($ 81 thousand)

4 INVENTORIES

Inventories at March 31, 2000 and 2001 were summarized as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2000	2001	2001
Finished products	¥ 36,633	¥ 44,284	$ 357,129
Semi-finished products	23,291	28,408	229,097
Materials—crude oil, auxiliary materials, etc.	27,853	44,674	360,274
Supplies—spare parts, etc.	7,849	3,735	30,121
In-transit crude oil and oil products	59,968	63,607	512,960
Land for sale	3,217	1,112	8,968
Others	4,692	4,366	35,209
Total	¥163,503	¥190,186	$1,533,758

5 NOTES TO THE CONSOLIDATED STATEMENTS OF CASH FLOWS

Cash and deposits and cash and cash equivalents

Reconciliation of cash and deposits in the consolidated balance sheets and cash and cash equivalents in the consolidated statements of cash flows at March 31, 2000 and 2001 were as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2000	2001	2001
Cash and deposits	¥50,855	¥54,157	$436,750
Add:			
Marketable securities	97,285	35,817	288,847
Other current assets (short-term loans receivable)	—	10,498	84,661
Less:			
Deposits with maturities exceeding three months	940	1,073	8,653
Stocks and bonds with maturities exceeding three months included in marketable securities above	51,187	1,611	12,992
Total	¥96,013	¥97,788	$788,613

6

SHORT-TERM LOANS AND LONG-TERM DEBT

Included in short-term loans at March 31, 2000 and 2001 were import bills payable and import financing bills payable to banks aggregating ¥3,037 million and ¥1,988 million ($16,032 thousand), respectively. These bills bear interest from 6.73% to 6.75% and from 5.50% to 5.75% per annum, respectively, and mature at various dates, mainly 45 days after issuance. The remaining short-term loans of ¥214,753 million and ¥200,271 million ($1,615,089 thousand), at March 31, 2000 and 2001, respectively, from banks bear interest from 0.10% to 2.20% and from 0.10% to 2.25% per annum, respectively. The banks have basic agreements with the Company and its consolidated subsidiaries to the effect that, with respect to all present or future loans with the banks, the Company and its consolidated subsidiaries shall provide collateral (including sums on deposit with such banks) or a guarantee immediately upon request from the banks and that any collateral furnished, pursuant to such agreement or otherwise, will be applicable to all indebtedness to the banks.

Short-term loans and current maturities of long-term debt at March 31, 2000 and 2001 consisted of the following:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2000	2001	2001
Short-term loans	¥217,790	¥202,259	$1,631,121
Current maturities of long-term debt	71,853	34,808	280,710
Total	¥289,643	¥237,067	$1,911,831

Long-term debt at March 31, 2000 and 2001 consisted of the following:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2000	2001	2001
Loans from banks, insurance companies and other financial institutions, secured, with interest at 0.9%–7.7% due serially through 2015	¥305,370	¥278,559	$2,246,443
4.4% unsecured convertible yen bonds due in 2001	44,535	—	—
1.1% unsecured convertible yen bonds due in 2005	19,868	19,868	160,225
2.8% unsecured straight yen bonds due in 2003	15,000	15,000	120,967
3.3% unsecured straight yen bonds due in 2007	10,000	10,000	80,644
3.15% unsecured straight yen bonds due in 2007	10,000	10,000	80,644
2.30% unsecured straight yen bonds due in 2002	10,000	10,000	80,644
2.72% unsecured straight yen bonds due in 2003	5,000	5,000	40,323
3.08% unsecured straight yen bonds due in 2004	5,000	5,000	40,323
3.50% unsecured straight yen bonds due in 2005	5,000	5,000	40,323
3.10% unsecured straight yen bonds due in 2005	5,000	5,000	40,323
2.34% unsecured straight yen bonds due in 2003	5,000	5,000	40,323
2.70% unsecured straight yen bonds due in 2004	5,000	5,000	40,323
3.00% unsecured straight yen bonds due in 2006	5,000	5,000	40,323
2.45% unsecured straight yen bonds due in 2004	5,000	5,000	40,323
2.83% unsecured straight yen bonds due in 2005	5,000	5,000	40,323
3.05% unsecured straight yen bonds due in 2006	5,000	5,000	40,323
2.86% unsecured straight yen bonds due in 2005	5,000	5,000	40,323
2.50% unsecured straight yen bonds due in 2004	—	5,000	40,323
2.84% unsecured straight yen bonds due in 2005	—	5,000	40,323
	469,773	408,427	3,293,766
Less current maturities	(71,853)	(34,808)	(280,710)
Total	¥397,920	¥373,619	$3,013,056

The aggregate annual maturities of long-term debt at March 31, 2001 were as follows:

Year ending March 31	Millions of yen	Thousands of U.S. dollars (Note 1)
2002	¥ 34,808	$ 280,710
2003	56,977	459,492
2004	95,538	770,468
2005	116,764	941,645
2006 and thereafter	104,339	841,443
	¥408,426	$3,293,758

The 4.4% unsecured convertible yen bonds in the original principal amount of ¥48,000 million were issued in October 1991. The Company fully redeemed the bonds from the market in this fiscal year.

The 1.1% unsecured convertible yen bonds in the original principal amount of ¥30,000 million were issued in March 1994. The bonds are subject to conversion currently at ¥877 ($7.07) for one share of the common stock of the Company from April 1, 1994 to March 30, 2005. At March 31, 2001, 22,653 thousand additional shares of common stock of the Company would have been issued upon full conversion at the current conversion price. The bonds may be redeemed, at the option of the Company, beginning April 1, 2001, in whole or in part at prices which range from 104% to 100% of the principal amount plus interest accrued. The Company redeemed a part of the bonds from the market in this fiscal year.

So long as the 1.1% bonds are outstanding, the cumulative amounts of payments of cash dividends must not exceed ¥7,300 million ($58,871 thousand) plus the Company's cumulative net income for the fiscal years following March 31, 1994.

Assets pledged as collateral primarily for short-term loans and long-term debt at March 31, 2001 were as follows:

Year ending March 31	Millions of yen	Thousands of U.S. dollars (Note 1)
Land	¥221,460	$1,785,968
Buildings and structures at net book value	42,988	346,677
Machinery and equipment at net book value	56,874	458,661
Investment in securities	3,249	26,202
Less treasury stock, at cost	25	202
	¥324,596	$2,617,710

7

LEASE TRANSACTIONS

A. Lessee leases

Leases payment of finance leases which do not transfer ownership of the leased assets to lessees for the years ended March 31, 1999, 2000 and 2001 were ¥747 million, ¥5,234 million and ¥5,012 million ($40,419 thousand), respectively.

Total lease commitment as of March 31, 1999, 2000 and 2001, inclusive of interest expense under such leases, were ¥1,471 million, ¥11,407 million and ¥10,641 million ($85,815 thousand), including ¥583 million, ¥4,706 million and ¥4,240 million ($34,194 thousand) due within one year. Included in the total lease commitment as of March 31, 2001 is commitment for sub-lease payment of ¥6,661 million ($53,718 thousand).

Equivalent of acquisition cost, accumulated depreciation and book value of leased properties for the years ended March 31, 2000 and 2001, were as follows:

	Millions of yen		
Year ended March 31, 2000	Machinery & vehicles	Other	Total
Acquisition cost	¥1,626	¥2,740	¥4,366
Accumulated depreciation	(974)	(1,665)	(2,639)
Net book value	¥ 652	¥1,075	¥1,727

	Millions of yen			Thousands of U.S. dollars (Note 1)		
Year ended March 31, 2001	Machinery & vehicles	Other	Total	Machinery & vehicles	Other	Total
Acquisition cost	¥3,174	¥7,497	¥10,671	$25,597	$60,460	$86,057
Accumulated depreciation	(1,761)	(4,930)	(6,691)	(14,202)	(39,758)	(53,960)
Net book value	¥1,413	¥2,567	¥3,980	$11,395	$20,702	$32,097

B. Lessor leases

Rental income from finance leases which do not transfer ownership of the leased assets to lessees and related depreciation for the year ended March 31, 2001 were ¥3,201 million ($25,815 thousand) and ¥12 million ($97 thousand), respectively.

Total lease commitment as of March 31, 2001, inclusive of interest income under such leases, were ¥7,010 million ($56,532 thousand), including ¥2,647 million ($21,347 thousand) due within one year. Included in the total lease commitment as of March 31, 2001 is commitment for sub-lease payment of ¥6,965 million ($56,169 thousand).

Acquisition cost, accumulated depreciation and book value of leased properties for the year ended March 31, 2000 and 2001, were as follows:

	Millions of yen
Year ended March 31, 2000	Machinery & equipment
Acquisition cost	¥1,942
Accumulated depreciation	(1,768)
Net book value	¥ 174

	Millions of yen			Thousands of U.S. dollars (Note 1)		
Year ended March 31, 2001	Machinery & vehicles	Other	Total	Machinery & vehicles	Other	Total
Acquisition cost	¥27	¥762	¥789	$218	$6,145	$6,363
Accumulated depreciation	(26)	(718)	(744)	(210)	(5,790)	(6,000)
Net book value	¥ 1	¥ 44	¥ 45	$ 8	$ 355	$ 363

8 CONTINGENCIES

(a) Contingent liabilities for notes receivable discounted at banks with recourse and endorsed to others at March 31, 2001 were ¥889 million ($7,169 thousand).

(b) Contingencies at March 31, 2001 for loans guaranteed, in the ordinary course of business, by the Company and its consolidated subsidiaries, mainly for unconsolidated subsidiaries, affiliates and employees of the Company and its consolidated subsidiaries were ¥25,340 million ($204,354 thousand).

9 SECURITIES

The following tables summarize acquisition costs, book values and fair values of securities as of March 31, 2001:

(a) Held-to-maturity bonds

Bonds with fair value exceeding book value

	Millions of yen			Thousands of U.S. dollars (Note 1)		
	2001			2001		
	Book value	Fair value	Difference	Book value	Fair value	Difference
Bonds with fair value exceeding book value	¥3,296	¥3,456	¥160	$26,581	$27,871	$1,290
Other	9	8	(1)	72	64	(8)
Total	¥3,305	¥3,464	¥159	$26,653	$27,935	$1,282

(b) Available-for-sale securities sold in the year ended March 31, 2001

Millions of yen			Thousands of U.S. dollars (Note 1)		
2001			2001		
Amount of sales	Gain	Loss	Amount of sales	Gain	Loss
¥6,093	¥244	¥5,579	$49,137	$1,968	$44,992

The following tables summarize book values of securities with no available fair value as of March 31, 2001:

	Millions of yen	Thousands of U.S. dollars (Note 1)
	2001	2001
	Book value	Book value
(a) Held-to-maturity bonds		
Non-listed bonds	¥ 3,101	$ 25,008
(b) Shares issued by subsidiaries and affiliates		
Non-listed securities	23,275	187,702
(c) Available-for-sale securities		
Money market fund	31,206	251,661
Mutual fund	3,000	24,194
Non-listed securities	14,865	119,879
Total	¥49,071	$395,734

Available-for-sale securities with maturities and held-to-maturity debt securities as of March 31, 2001 are as follows:

	Millions of yen			
	Within one year	Over one year but within five years	Over five years but within ten years	Over ten years
Government bond and municipal bond	¥1,441	¥1,302	¥13	¥ 4
Corporate bond	117	497	—	3,020
Total	¥1,558	¥1,799	¥13	¥3,024

	Thousands of U.S. dollars (Note 1)			
	Within one year	Over one year but within five years	Over five years but within ten years	Over ten years
Government bond and municipal bond	$11,621	$10,500	$105	$ 32
Corporate bond	944	4,008	—`	24,355
Total	$12,565	$14,508	$105	$24,387

10 DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING TRANSACTIONS

(1) Nature and Objective of Derivative Transactions

The Company uses foreign currency forward contracts and currency option contracts to hedge risks due to the effect of currency exchange rate fluctuations on U.S.-dollar-denominated imports of crude oil and petroleum products. The Company uses interest rate swap contracts to exchange floating-rate payment obligations for fixed-rate payment obligations. The Company also uses crude oil and petroleum product swap contracts and commodity forward contracts to hedge risks stemming from commodity price fluctuations. The Company undertakes hedge accounting for these derivative transactions, where required.

A. Hedging Instruments and Hedged Items

Hedging instruments	Hedged items
Interest rate swaps	Borrowings
Crude oil and petroleum transactions	Purchases and sales of crude oil and petroleum products

B. Hedge Policy

In accordance with internal rules that determine derivative transaction-related authority levels and transaction value limits, hedging activities are undertaken within specified limits to hedge price fluctuation risks and interest rate fluctuation risks.

C. Method of Evaluating Hedge Effectiveness

The Company evaluates hedge effectiveness semi-annually by comparing cumulative changes in cash flows from or changes in fair value of hedged items and the corresponding changes in the hedging derivative instruments. The effectiveness evaluation is omitted, however, with regard to certain specially handled interest rate swaps.

(2) Operating Policy of Derivative Transactions

In accordance with internal rules that determine derivative transaction-related authority levels and transaction value limits, hedge target-related currency exchange rate fluctuation risks, interest rate fluctuation risks, and price fluctuation risks are hedged within a specified range. Each derivative transaction is based on actual business transactions, and the Company has a policy of not executing speculative derivative transactions.

(3) Risks Related to Derivative Transactions

The Company faces currency market fluctuation risks related to foreign currency forward contracts and currency option contracts, and also faces market interest rate fluctuation risks related to interest rate swaps associated with interest rate-related transactions. In addition, the Company faces market price fluctuation risks and currency market fluctuation risks related to commodity associated crude oil and petroleum product swap transactions. In all these types of transactions, the Company deals with large banks, trading companies, oil companies, and similar enterprises, therefore considers that there is almost no credit risk associated with these derivative transactions.

(4) Management of Risks Related to Derivative Transactions

Currency- and interest-related derivative transactions are implemented and controlled by the Finance Department in accordance with internally authorized rules. The General Manager of the Finance Department reports the results of transactions to, and obtains authorization of basic transaction policy from, the meeting of the Executive Committee on a quarterly basis for foreign currency forward contracts and semi-annually for other contracts.

Regarding commodity-related derivative transactions, the Demand & Supply Coordination Department, International Petroleum Department, Industrial Fuel Marketing Department, and the second Corporate Planning Department consult with each other, obtain approval of the annual basic transaction policy from the meeting of the Executive Committee, and implement and control transactions in accordance with internally authorized rules. Regarding control, the Demand & Supply Coordination Department, International Petroleum Department, and Industrial Fuel Marketing Department control derivative transactions on a single-department basis and the second Corporate Planning Department controls derivative transactions on a Companywide basis. General managers of the Demand & Supply Coordination Department, International Petroleum Department, and Industrial Fuel Marketing Department report to the meeting of the Executive Committee semi-annually.

(5) Other

The contract amount figures, notional amounts, and other figures shown in the items related to derivative transaction market prices do not necessarily indicate the magnitude of market risk associated with derivative transactions.

The following tables summarize market value information as of March 31, 2000 and 2001 of derivative transactions for which hedge accounting has not been applied:

(1) Currency related

Year ended March 31, 2000	Millions of yen: Contract amounts: Due within one year	Due after one year	Total	Market value	Unrealized loss
Currency option contracts purchased call U.S. dollars	¥5,850	—	¥5,850	¥51	¥(24)

Year ended March 31, 2001	Millions of yen: Contract amounts: Due within one year	Due after one year	Total	Market value	Unrealized gain
Forward exchange contracts purchased U.S. dollars	¥61,827	—	¥61,827	¥64,676	¥2,849
Currency option contracts purchased call U.S. dollars	¥ 2,478	—	¥ 2,478	¥ 89	¥ 61

	Thousands of U.S. dollars (Note 1): Contract amounts: Due within one year	Due after one year	Total	Market value	Unrealized gain
Forward exchange contracts purchased U.S. dollars	$498,605	—	$498,605	$521,581	$22,976
Currency option contracts purchased call U.S. dollars	$ 19,984	—	$19,984	$ 718	$ 492

(2) Interest related

Year ended March 31, 2000	Millions of yen: Notional amount: Due within one year	Due after one year	Total	Market value	Unrealized gain (loss)
Interest rate swap contracts					
Pay fixed rate, receive floating rate	¥3,000	¥49,900	¥52,900	¥(2,521)	¥(2,521)
Pay floating rate, receive fixed rate	—	¥ 5,000	¥ 5,000	¥ 2	¥ 2

(3) Commodity related

Year ended March 31, 2000	Thousands of barrels			Millions of yen	
	Notional amount			Market value	Unrealized gain (loss)
	Due within one year	Due after one year	Total		
Swap contracts of crude oil					
Pay fixed rate, receive floating rate	1,115	—	1,115	¥(41)	¥(41)
Pay floating rate, receive fixed rate	100	—	100	¥ 3	¥ 3

	Millions of yen				
	Notional amount				
	Due within one year	Due after one year	Total		
Forward contracts of crude oil					
Sell	¥1,803	—	¥1,803	¥1,714	¥ 88
Buy	¥1,804	—	¥1,804	¥1,714	¥(90)

Year ended March 31, 2001	Millions of yen				
	Notional amount			Market value	Unrealized gain
	Due within one year	Due after one year	Total		
Forward contracts of crude oil					
Sell	¥17	—	¥17	¥16	¥1

	Thousands of U.S. dollars (Note 1)				
	Notional amount			Market value	Unrealized gain
	Due within one year	Due after one year	Total		
Forward contracts of crude oil					
Sell	$137	—	$137	$129	$8

11
RETIREMENT AND SEVERANCE BENEFITS

The Company and its consolidated subsidiaries provide two types of post-employment benefit plans, unfunded lump-sum payment plans and funded non-contributory pension plans, under which all eligible employees are entitled to benefits based on the level of wages and salaries at the time of retirement or termination, length of service and certain other factors.

The liabilities for severance and retirement benefits included in the liability section of the consolidated balance sheet as of March 31, 2001 consists of the following:

	Millions of yen	Thousands of U.S. dollars (Note 1)
Projected benefit obligation	¥(90,116)	$(726,742)
Pension assets	57,572	464,290
Unrecognized net transition obligation	18,957	152,879
Unrecognized actuarial differences	11,947	96,347
Less prepaid pension costs	(1,972)	(15,903)
Liability for severance and retirement benefits	¥ (3,612)	$ (29,129)

Included in the consolidated statement of income for the year ended March 31, 2001 are severance and retirement benefit expenses comprised of the following:

	Millions of yen	Thousands of U.S. dollars (Note 1)
Service costs	¥3,105	$25,040
Interest cost on projected benefit obligation	2,614	21,080
Expected return on plan assets	(1,802)	(14,532)
Amortization of net transition obligation	4,739	38,218
Severance and retirement benefit expenses	¥8,656	$69,806

The discount rate and the rate of expected return on plan assets used by the Company are 2.5% (at April 1, 2000 the Company used 3.5%) and 3.5%, respectively. The estimated amount of all retirement benefits to be paid at the future retirement date is allocated equally to each service year using the estimated number of total service years. Actuarial gains or losses are recognized as an expense in equal amounts over 10 years, the average of the estimated remaining service lives of the employees, commencing with the following period. The net transition obligation will be recognized in expenses in equal amounts primarily over 5 years commencing with the year ended March 31, 2001.

12 INCOME TAXES

The Company and its consolidated domestic subsidiaries are subject to a number of taxes based on income, which, in the aggregate, indicate statutory rates in Japan of approximately 40.87% for the years ended March 31, 2000 and 2001.

The following table summarizes the significant differences between the statutory tax rate and the Company's effective tax rate for financial statement purposes for the year ended March 31, 2000 and 2001:

Year ended March 31, 2000	
Statutory tax rate	40.87%
Non-Japanese taxes	13.94
Foreign tax credits taken	(3.61)
Non-taxable dividend income	(5.43)
Non-deductible expenses	13.47
Per capital inhabitants taxes	1.02
Other	0.76
Effective tax rate	61.02%

Year ended March 31, 2001	
Statutory tax rate	40.87%
Non-Japanese taxes	15.20
Non-taxable dividend income	(2.65)
Non-deductible expenses	8.10
Equity in earning of affiliates	(2.47)
Other	(2.62)
Effective tax rate	56.43%

Significant components of the Company's and its consolidated subsidiaries' deferred tax assets and liabilities as of March 31, 2000 and 2001 are as follows:

Year ended March 31, 2000	Millions of yen
Current deferred tax assets:	
Accounts receivable	¥ 2,638
Unrealized gains	582
Excess bonuses accrued	540
Other	546
Total current deferred tax assets	4,306
Valuation allowance	(126)
Net current deferred tax assets	¥ 4,180
Current deferred tax liabilities:	
Allowance for doubtful accounts	¥ (111)
Exchange losses	(106)
Other	(21)
Total current deferred tax liabilities	(238)
Net current deferred tax assets	¥ 3,942
Non-current deferred tax assets:	
Unrealized gains	¥10,765
Net operating loss carry forward	4,916
Depreciation	3,414
Other	2,296
Total non-current deferred tax assets	21,391
Valuation allowance	(3,247)
Total non-current deferred tax assets	18,144
Account offset against deferred tax liabilities	(15,151)
Net non-current deferred tax assets	¥ 2,993
Non-current deferred tax liabilities:	
Reserve for deferred gains on sales of fixed assets for tax purposes	¥(17,587)
Reserve for losses on overseas investments	(672)
Special depreciation	(351)
Other	(32)
Total non-current deferred tax liabilities	(18,642)
Account offset against deferred tax assets	15,151
Net non-current deferred tax liabilities	¥ (3,491)

Year ended March 31, 2001	Millions of yen	Thousands of U.S. dollars (Note 1)
Current deferred tax assets:		
Accounts receivable	¥ 1,541	$ 12,427
Unrealized gains	453	3,653
Excess bonuses accrued	1,124	9,065
Other	510	4,113
Total current deferred tax assets	3,628	29,258
Valuation allowance	(72)	(581)
Total current deferred tax assets	3,556	28,677
Account offset against deferred tax liabilities	(78)	(629)
Net current deferred tax assets	¥ 3,478	$ 28,048
Current deferred tax liabilities:		
Allowance for doubtful accounts	¥ (76)	$ (613)
Other	(12)	(97)
Total current deferred tax liabilities	(88)	(710)
Account offset against deferred tax assets	78	629
Net current deferred tax assets	¥ (10)	$ (81)
Non-current deferred tax assets:		
Unrealized gains	¥ 10,048	$ 81,032
Net operating loss carry forward	5,916	47,710
Depreciation	2,271	18,314
Costs for retirement and severance benefits	797	6,427
Other	955	7,702
Total non-current deferred tax assets	19,987	161,185
Valuation allowance	(846)	(6,822)
Total non-current deferred tax assets	19,141	154,363
Account offset against deferred tax liabilities	(16,035)	(129,315)
Net non-current deferred tax assets	¥ 3,106	$ 25,048
Non-current deferred tax liabilities:		
Reserve for deferred gains on sales of fixed assets for tax purposes	¥(19,860)	$(160,161)
Retirement and severance benefits	(1,249)	(10,073)
Non-Japanese taxes	(4,984)	(40,194)
Reserve for losses on overseas investments	(674)	(5,435)
Special depreciation	(310)	(2,500)
Other	(62)	(500)
Total non-current deferred tax liabilities	(27,139)	(218,863)
Account offset against deferred tax assets	16,035	129,315
Net non-current deferred tax liabilities	¥(11,104)	$ (89,548)

13
SEGMENT INFORMATION

The Company and its consolidated subsidiaries primarily operate in the oil business, importing and refining crude oil to produce and distribute a variety of petroleum products.

For the year ended March 31, 1999 business segment information was not required to be disclosed as all of sales, operating income and assets of the oil business segment exceeded 90% of total segment sales (including inter-segment sales or transfers), operating income of all segments which did not record any operating loss, and total segment assets, respectively.

For the year ended March 31, 2000 and 2001, business operations of the Company and its consolidated subsidiaries are summarized by product groups as follows:

	Millions of yen					
Year ended March 31, 2000	Petroleum	Real estate	Others	Total	Elimination or corporate	Consolidated
Sales:						
Outside customers	¥1,523,699	¥6,373	¥54,606	¥1,584,678	¥ —	¥1,584,678
Inter-segment	3,329	—	15,127	18,456	(18,456)	—
Total	1,527,028	6,373	69,733	1,603,134	(18,456)	1,584,678
Operating expenses	1,516,189	1,830	68,779	1,586,798	(18,785)	1,568,013
Operating income	¥ 10,839	¥4,543	¥ 954	¥ 16,336	¥ 329	¥ 16,665
Identifiable assets, depreciation and amortization and capital expenditures:						
Assets	¥1,173,266	¥6,227	¥36,510	¥1,216,003	¥79,690	¥1,295,693
Depreciation and amortization	24,179	151	178	24,508	(1,072)	23,436
Capital expenditures	¥ 24,710	¥ —	¥ 170	¥ 24,880	¥ (107)	¥ 24,773

	Millions of yen					
Year ended March 31, 2001	Petroleum	Real estate	Others	Total	Elimination or corporate	Consolidated
Sales:						
Outside customers	¥1,766,456	¥5,412	¥73,974	¥1,845,842	¥ —	¥1,845,842
Inter-segment	3,931	—	6,087	10,018	(10,018)	—
Total	1,770,387	5,412	80,061	1,855,860	(10,018)	1,845,842
Operating expenses	1,734,873	3,150	80,421	1,818,444	(9,184)	1,809,260
Operating income	¥ 35,514	¥2,262	¥ (360)	¥ 37,416	¥ (834)	¥ 36,582
Identifiable assets, depreciation and amortization and capital expenditures:						
Assets	¥1,204,473	¥3,712	¥37,495	¥1,245,680	¥74,280	¥1,319,960
Depreciation and amortization	25,247	157	153	25,557	(885)	24,672
Capital expenditures	¥ 19,394	¥ 1	¥ 177	¥ 19,572	¥ (220)	¥ 19,352

Year ended March 31, 2001	Thousands of U.S. dollars (Note 1) Petroleum	Real estate	Others	Total	Elimination or corporate	Consolidated
Sales:						
Outside customers	$14,245,613	$43,645	$596,565	$14,885,823	$ —	$14,885,823
Inter-segment	31,701	—	49,089	80,790	(80,790)	—
Total	14,277,314	43,645	645,654	14,966,613	(80,790)	14,885,823
Operating expenses	13,990,911	25,403	648,557	14,664,871	(74,064)	14,590,807
Operating income	$ 286,403	$18,242	$ (2,903)	$ 301,742	$ (6,726)	$ 295,016
Identifiable assets, depreciation and amortization and capital expenditures:						
Assets	$ 9,713,492	$29,935	$302,379	$10,045,806	$599,033	$10,644,839
Depreciation and amortization	203,605	1,266	1,234	206,105	(7,137)	198,968
Capital expenditures	$ 156,403	$ 8	$ 1,427	$ 157,838	$ (1,774)	$ 156,064

Geographic segment information is not disclosed as the Company and its consolidated subsidiaries operate mainly in one geographic segment, being Japan.

Overseas sales information is not disclosed as the amount of overseas sales is less than 10% of the consolidated net sales.

As described in Note 2, the Company changed in the inventory costing method. As a result, operating income for petroleum was increased by ¥13,566 million ($109,403 thousand).

As described in Note 1, the Company and its consolidated domestic subsidiaries adopted the new accounting standard for severance and pension benefits. As a result, operating income for petroleum and real estate and others and elimination or corporate were increased by ¥2,203 million ($17,766 thousand) and ¥22 million ($177 thousand) and ¥114 million ($919 thousand) and ¥24 million ($194 thousand), respectively.

14
SUBSEQUENT EVENTS

On June 28, 2001, the Company's annual shareholders' meeting approved the payment of a year-end cash dividends of ¥3.00 (US$0.02) per share, or a total of ¥1,895 million (US$15,282 thousand) to shareholders of record, at March 31, 2001.

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

COSMO OIL COMPANY, LIMITED and Its Consolidated Subsidiaries

ASAHI & CO
ARTHUR ANDERSEN

ASAHI & CO
ARTHUR ANDERSEN

CERTIFIED PUBLIC ACCOUNTANTS
(ASAHI KANSA-HOJIN)

To the Shareholders and the Board of Directors of
COSMO OIL COMPANY, LIMITED:

We have audited the accompanying consolidated balance sheets of COSMO OIL COMPANY, LIMITED (a Japanese corporation) and its consolidated subsidiaries as of March 31, 2000 and 2001, and the related consolidated statements of income, shareholders' equity and cash flows for each of the three years in the period ended March 31, 2001, expressed in Japanese yen. Our audits were made in accordance with generally accepted auditing standards in Japan and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the consolidated financial position of COSMO OIL COMPANY, LIMITED and its consolidated subsidiaries as of March 31, 2000 and 2001, and the consolidated results of their operations and their cash flows for each of the three years in the period ended March 31, 2001 in conformity with accounting principles generally accepted in Japan applied on a consistent basis during the periods, except as noted in the following paragraph.

As explained in Note 1, COSMO OIL COMPANY, LIMITED and its consolidated subsidiaries prospectively adopted new Japanese accounting standards for consolidation and equity method accounting, and income taxes in the year ended March 31, 2000, and for foreign currency translation,financial instruments and employees' severance and retirement benefits in the year ended March 31, 2001. Also, COSMO OIL COMPANY, LIMITED changed the method of inventory costing, effective April 1, 2000, as referred to in Note 2.

Also, in our opinion, the U.S. dollar amounts in the accompanying consolidated financial statements have been translated from Japanese yen on the basis set forth in Note 1.

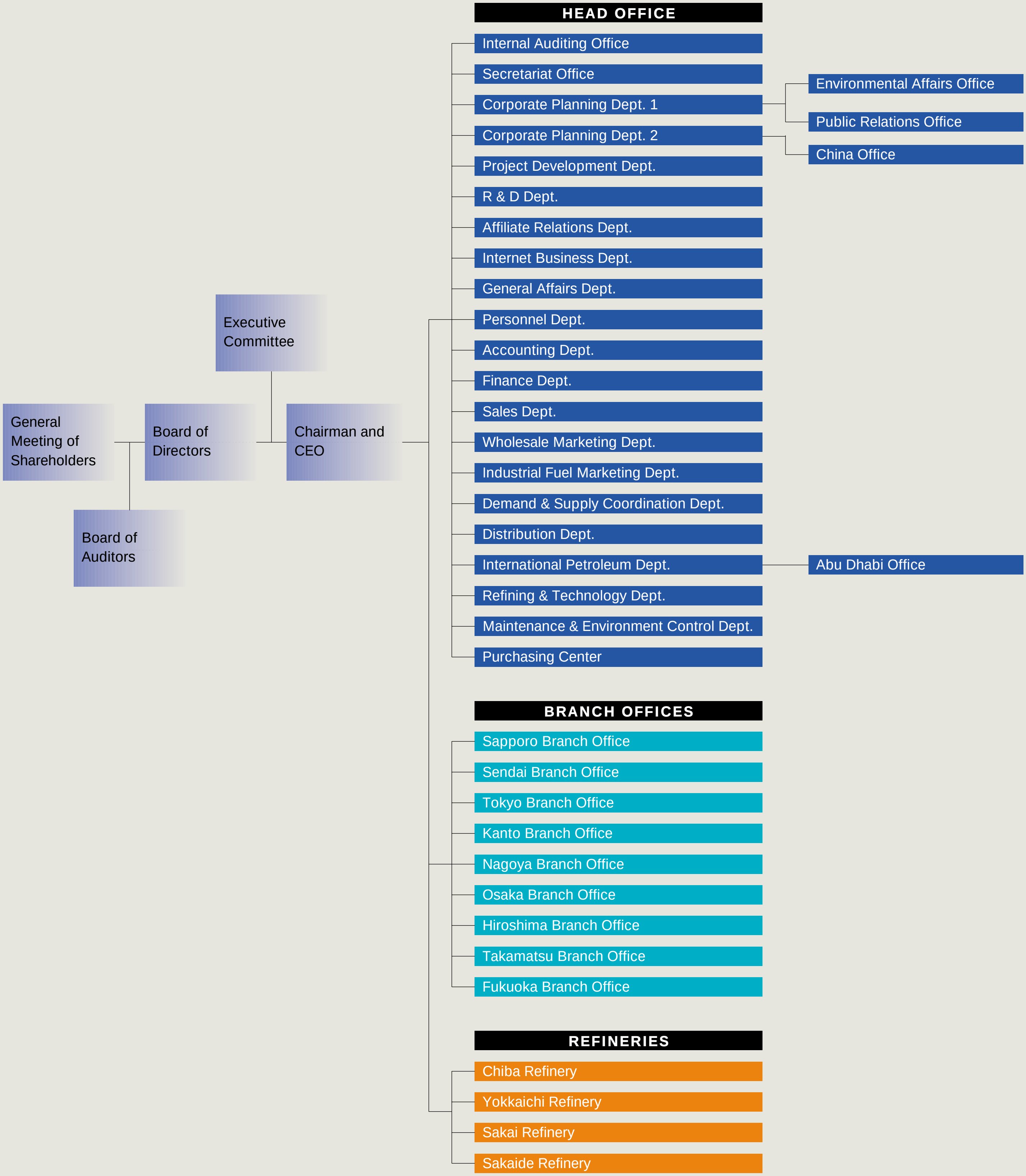
Asahi & Co.

Tokyo, Japan
June 28, 2001

Statement on Accounting Principles and Auditing Standards
This statement is to remind users that accounting principles and auditing standards and their application in practice may vary among nations and therefore could affect, possibly materially, the reported financial position and results of operations. The accompanying consolidated financial statements are prepared based on accounting principles generally accepted in Japan, and the auditing standards and their application in practice are those generally accepted in Japan. Accordingly, the accompanying consolidated financial statements and the auditors' report presented above are for users familiar with Japanese accounting principles, auditing standards and their application in practice.

ORGANIZATION CHART

(As of June 28, 2001)



(As of March 31, 2001)

JAPAN

Crude Oil Development

*Abu Dhabi Oil Co., Ltd. (Japan)
- Tokyo
- ¥10,090 million
- 51.14%
- Petroleum exploration and production

*Cosmo Oil Ashmore Ltd.
- Tokyo
- ¥638 million
- 51.0%
- Petroleum exploration

#United Petroleum Development Co., Ltd.
- Tokyo
- ¥34,073 million
- 13.27%
- Petroleum exploration and production

#Mubarraz Oil Co., Ltd.
- Tokyo
- ¥32,877 million
- 20.30%
- Petroleum exploration and production

Transportation

*Cosmo Tanker Co., Ltd.
- Tokyo
- ¥490 million
- 100.00%
- Marine transportation

Cosmo Kaiun Co., Ltd.
- Tokyo
- ¥330 million
- 50.00%
- Marine transportation and shipping agency

Tokyo Cosmo Logistics Co., Ltd.
- Chiba Pref.
- ¥50 million
- 52.00%
- Trucking and transportation services

Petrochemical Production

*Cosmo Matsuyama Oil Co., Ltd.
- Ehime Pref.
- ¥500 million
- 100.00%
- Manufacture and sales of petrochemical products

#Maruzen Petrochemical Co., Ltd.
- Tokyo
- ¥10,000 million
- 30.00%
- Petrochemical development

Distribution & Storage

*Yokkaichi LPG Terminal Co., Ltd.
- Mie Pref.
- ¥1,600 million
- 55.00%
- LPG import, storage, and shipment

Tozai Oil Terminal Co., Ltd.
- Tokyo
- ¥480 million
- 50.00%
- Contracts for oil receiving and shipping works

Okinawa CTS Corp.
- Okinawa Pref.
- ¥4,000 million
- 35.00%
- Oil storage, receiving, and shipping works

Ogishima Oil Terminal Co., Ltd.
- Kanagawa Pref.
- ¥1,000 million
- 50.00%
- Oil storage

*Hokuto Kogyo Co., Ltd.
- Hokkaido
- ¥20 million
- 100.00%
- Oil receiving and shipping works

Sakaide Cosmo Kosan Co., Ltd.
- Kagawa Pref.
- ¥30 million
- 50.00%
- Marine transportation agency and port services

Sales

*Cosmo Oil Lubricants Co., Ltd.
- Tokyo
- ¥1,620 million
- 100.00%
- Information and technical services related to lubricating oil

*Cosmo Petroleum Gas Co., Ltd.
- Tokyo
- ¥300 million
- 100.00%
- Import and sales of LPG

*Cosmo Asphalt Co., Ltd.
- Tokyo
- ¥300 million
- 98.09%
- Sales of asphalt

*Cosmo Oil Service Co., Ltd.
- Tokyo
- ¥584 million
- 100%
- Marketing and sales of oil products

*Toyo Kokusai Oil Co., Ltd.
- Tokyo
- ¥232 million
- 94.09%
- Marketing and sales of oil products

Research & Development

*Cosmo Research Institute
- Tokyo
- ¥200 million
- 100.00%
- Research and development

*Cosmo Technology Research Institute
- Tokyo
- ¥10 million
- 100%
- Research and development of petroleum refining technology, etc.

Engineering

*Cosmo Engineering Co., Ltd.
- Tokyo
- ¥385 million
- 50.00%
- General plant and equipment engineering

Others

Cosmo Ventures Inc.
- Tokyo
- ¥300 million
- 100.00%
- Integrated human resources services and management of leased real estate

*Cosmo Trade & Service Co., Ltd.
- Tokyo
- ¥200 million
- 100.00%
- Service-station-related business and other services

Cosmo Computer Center Co., Ltd.
- Tokyo
- ¥50 million
- 100.00%
- Computer business consignee

*Cosmo Carelife Co., Ltd.
- Mie Pref.
- ¥100 million
- 100%
- Home care services

OVERSEAS

*Cosmo Oil International Pte., Ltd.
- Singapore
- S$19,500,000
- 100.00%
- Purchase and sale of crude oil and finished products

Cosmo Oil of U.S.A., Inc.
- New York
- US$250,000
- 100.00%
- Business services for Cosmo Oil Co., Ltd.

Cosmo Oil (U.K.) Plc.
- London
- US$4,982,342
- 100.00%
- Purchase and sale of crude oil and finished products

Cosmo Lubricants (Taiwan) Co., Ltd.
- Taipei
- NT$15,000,000
- 100.00%
- Lubricating oil sales

■ Location
■ Paid-in Capital
■ Direct Equity Participation
■ Principal Business
*Consolidated
#Consolidated by the equity method

(As of March 31, 2000)

COSMO OIL CO., LTD.

Head Office
1-1-1, Shibaura, Minato-ku,
Tokyo 105-8528, Japan
Phone: (03) 3798-3211
Fax: (03) 3798-3237
URL: http://www.cosmo-oil.co.jp

Established
April 1, 1986

Common Shares
Authorized: 1,700,000,000
Issued: 631,705,087

Paid-in Capital
¥51,887 million

Stock Listings
Tokyo, Osaka, Nagoya

Number of Employees
1,970

Number of Dealers
416

Number of Service Stations Owned
5,600

Number of Branches
9

Number of Shareholders
42,266

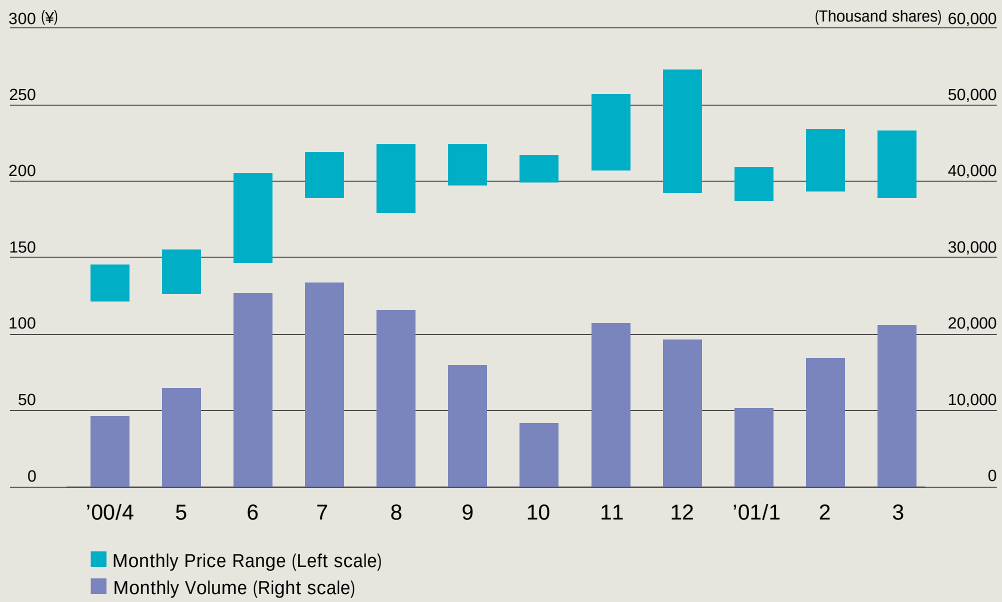
Transfer Agent
The Chuo Mitsui Trust & Banking Co., Ltd.
33-1, Shiba 3-chome, Minato-ku,
Tokyo 105-8574, Japan

Independent Certified Public Accountants
Asahi & Co.

Principal Shareholders

	Number of shares owned (Thousands)	Percentage of total shares issued
The Industrial Bank of Japan, Limited	31,531	4.99%
The Sanwa Bank, Limited	25,259	3.99
Cosmo Oil Employees' Shareholding Association	20,955	3.31
The Kansai Electric Power Company, Incorporated	18,600	2.94
The Tokio Marine and Fire Insurance Company, Limited	16,337	2.58
The Sumitomo Marine and Fire Insurance Company, Limited	15,930	2.52
The Yasuda Fire and Marine Insurance Company, Limited	14,473	2.29
The Bank of Tokyo-Mitsubishi, Limited	13,415	2.12
The Toyo Trust and Banking Company, Limited	12,792	2.02
The Nippon Life Insurance Company, Limited	11,985	1.89

Price Range of Stock and Trading Volume



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