

Financial Section Management's Discussion and Analysis

Operating Environment and Results of Operations

Operating Environment

The fiscal year that ended in March 2004 began amid concerns about the global economy due to the outbreak of SARS and war in Iraq. However, the global economy was supported by a strong recovery in the United States and robust economic expansion in China and other Asian nations. The result was strong demand in containers, automobiles, natural resources, energy and almost all other categories of ocean shipping. On the other hand, crude oil prices remained high even after the May 2003 end of the war in Iraq because of historically low U.S. inventories, OPEC production cuts, speculation and other forces. The result was a 9% increase in the price of bunker compared with the prior fiscal year. In addition, the yen appreciated 7% versus the U.S. dollar compared with the prior fiscal year.

MOL was able to overcome the negative effects of the yen's strength and higher bunker prices through a variety of management initiatives, including the suitable structuring of the fleet, and continuous cost reduction measures. As a result, MOL succeeded in maximizing the benefits of favorable market conditions due to higher freight rates and growth in cargo volumes.

Results of Operations

Revenues

There was an increase of ¥87.0 billion, or 9.6%, in revenue to ¥997.3 billion. Growth in container volume due to the completion of larger capacity vessels, the restoration of freight rates on individual routes, an upturn in the dry bulk market and other factors raised revenue by ¥137.5 billion. However, the yen's appreciation reduced revenue by ¥50.7 billion.

Operating Income

Operating income rose 103.1% to ¥92.1 billion, climbing to 9.2% of revenue, 4.2 points higher than one year earlier.

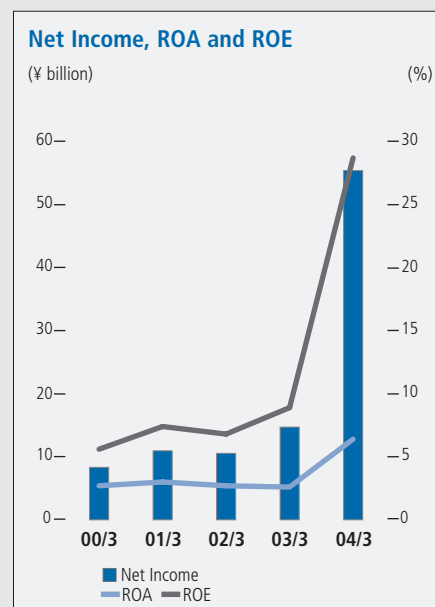
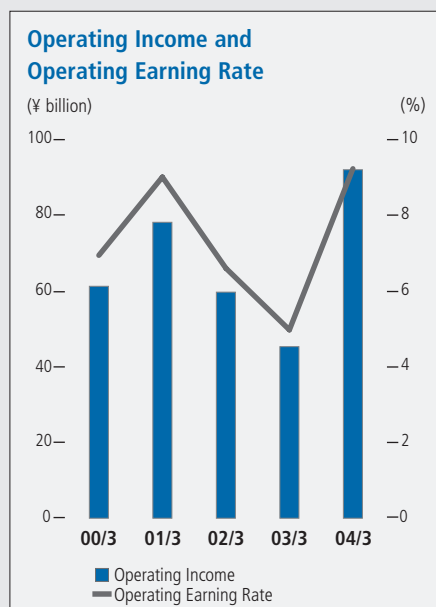
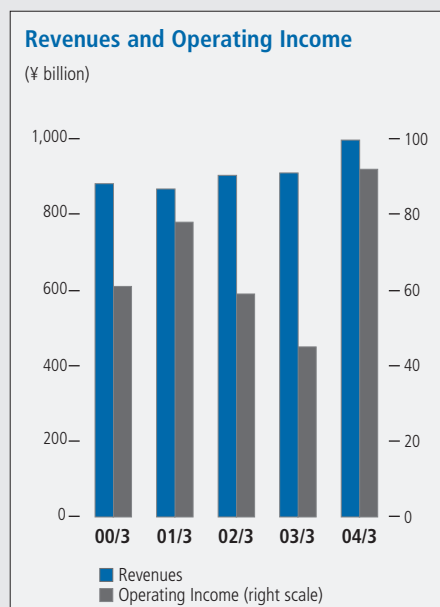
Operating income in the core overseas shipping segment was ¥83.1 billion, 90.2% of total operating income. This increase was mainly attributable to a substantial restoration in freight rates and cost reductions in the containership sector, and to an improvement in market conditions and addition of competitive vessels in the dry bulk and tanker sectors. The contributions of these items more than offset the negative impact of the yen's appreciation and high bunker prices. Due to the large volume of cargo during the fiscal year, there was also an improvement in earnings of consolidated subsidiaries engaged in "overseas shipping" and "shipping agents and harbor/terminal operation."

Other income (expenses)

Net other income (expenses) improved by ¥17.9 billion to a net expense of ¥2.3 billion. There was a ¥4.2 billion decrease in interest expense because of a reduction in debt and lower yen and U.S. dollar interest rates, and a ¥3.2 billion increase in equity in earnings of unconsolidated subsidiaries and affiliated companies. Also contributing to the improvement was the completion of aggressive measures that ended in the prior fiscal year aimed at giving MOL a sounder base of operations. Actions included the sale of uneconomic vessels and the liquidation and streamlining of unprofitable subsidiaries and assets. A large improvement in valuation gains on securities due to higher stock prices was another reason for the decline in net other expenses.

Net Income

Income before income taxes and minority interests rose from ¥25.1 billion to ¥89.8 billion, an increase of 257.5%. After deducting current and deferred income taxes, there was a 276.6% increase in net income from ¥14.7 billion to ¥55.4 billion. This was 5.6% of revenue, 3.9 points higher than one year earlier.



Operating Results by Segments

The upper row for each segment is revenues and the bottom row is operating income.

(unit: ¥ billion)

	2004.3	2003.3	% increase/ decrease
Overseas shipping	830.2	743.0	87.2 / 11.7%
	83.1	37.5	45.6 / 121.8%
Ferry and domestic shipping	35.4	33.5	2.0 / 5.9%
	1.3	0.6	0.6 / 93.8%
Shipping agents and harbor/ terminal operation	84.7	78.9	5.8 / 7.4%
	5.4	2.3	3.0 / 132.2%
Cargo forwarding & warehousing	47.0	48.4	-1.4 / -2.9%
	0.2	-0.1	0.3 / -%
Others	72.1	74.8	-2.7 / -3.6%
	2.9	4.0	-1.1 / -27.4%

Overseas shipping: In this segment, revenues were higher and there was a large increase in earnings due to the reasons described earlier in this section.

Ferry and domestic shipping business: There was a significant improvement in profitability in ferry operations because of streamlining and cost cutting programs conducted by all ferry companies. Results at Shosen Mitsui Ferry Co., Ltd. benefited from the start of joint operations between Tokyo and Hakata and Oarai and Tomakomai, as well as from other actions. In domestic shipping, integrations of activities within the group produced an improvement in profitability.

Shipping agency and harbor/terminal operation: This segment generated higher revenues and a strong increase in earnings, a performance that reflected growth in shipping agency and container terminal activities due to higher cargo volume and favorable freight rates in overseas shipping operations.

Cargo forwarding and warehousing: Revenues were lower because of the effects of SARS, war in Iraq and the discontinuation of unprofitable businesses. However, profitability improved as the newly established head office Logistics Business Division established and executed a unified group strategy while the group companies' strengthening sales activities and cutting costs.

Other businesses: This segment includes trading, real estate, construction, financial services and other activities. Revenues and earnings were lower because of the completion of large construction projects.

Revisions to Business Segments

Beginning in the fiscal year ending on March 31, 2005, MOL will report operating results based on the following six segments instead of the five segments used until the past fiscal year as shown in the above table.

Overseas shipping, which accounted for 83% of consolidated revenue in the past fiscal year, will be divided into two segments: "containerships," and "bulkships." Along with this change, business units and group companies involved in ship chartering, shipping agents and harbor/terminal operation will be integrated with one of these two segments to further clarify responsibility for the oversight of these activities.

Group companies involved in customs clearance, cargo forwarding and warehousing that are overseen by the Logistics Business Division will be combined with the "logistics" segment to provide a framework for conducting the logistics business in a more unified manner that draws on all MOL Group resources.

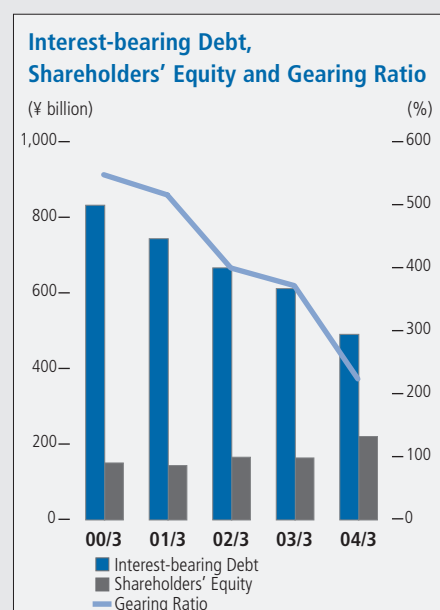
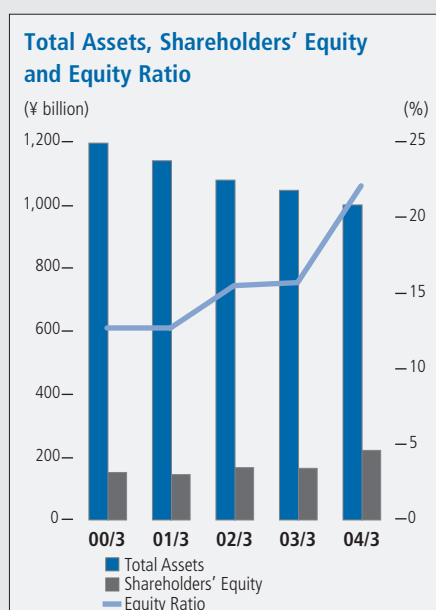
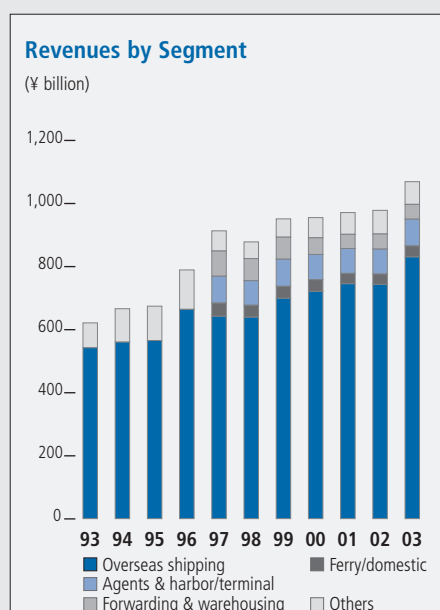
The ferry and domestic shipping segment, excluding tugboat operation, have been combined with group companies involved in domestic cargo forwarding to form the new "ferry and domestic transport" segment.

Tugboats, cruiseships and other associated businesses have been combined to create the "associated businesses" segment.

The "others" segment represents mainly MOL Group companies involved in administrative activities.

Liquidity and Capital Resources

The MOL Group places great priority on reducing working capital by receiving payments from shippers more promptly and utilizing the group's internal funds more efficiently. During the past fiscal year, as the group was able to use sales of ships and other assets to generate sufficient funds for capital expenditures, primarily the purchase of vessels, there was a large reduction in debt because



operating cash flows were used almost entirely for the repayment of debt. During MOL STEP, the group is planning to make substantial capital expenditures to achieve growth in line with its goal of becoming the world's largest ocean transportation group, backed by a unique identity. While making these expenditures, part of operating cash flows will continue to be used to reduce debt in order to create an even sounder financial position.

Comparison of Financial Position at March 31, 2004 and 2003

Assets

As of March 31, 2004, total assets were ¥1,000.2 billion, ¥46.4 billion less than one year earlier. The decrease was mainly the result of a ¥116.0 billion decline in vessels. The increase in current assets was mainly attributable to an ¥8.4 billion increase in deferred and prepaid expenses as the growth in cargo volumes and higher market rates raised charterages and other expenses for vessels that have not completed voyages. Vessels, property and equipment, at cost, decreased mainly because the vessels category declined ¥116.0 billion. The number of owned vessels fell while the number of chartered and leased vessels increased. Investments and other assets increased ¥35.3 billion mainly because higher stock prices caused revaluations of investment securities.

Liabilities and Shareholders' Equity

Liabilities decreased ¥102.6 billion to ¥771.5 billion. In line with MOL *next*, aggressive debt-reduction measures continued during the fiscal year, including the repayment of long-term and short-term loans. As a result, debt was ¥491.7 billion, ¥121.0 billion less than one year earlier. The ¥8.0 billion increase in advances received, which is closely related to the increase in deferred and prepaid expenses, reflects increases in payments for ocean freight and charterages for vessels that have not completed voyages, due to growth in cargo volumes and higher market rates. The ¥88.0 billion decrease in long-term bank loans due after one year is approximately the same as the decrease of asset in vessels after depreciation.

Shareholders' equity increased ¥56.7 billion to ¥221.5 billion, mainly the result of growth in retained earnings due to the higher net income and an increase in unrealized holding gains on available-for-sale securities, net of tax.

Cash Flows

Net cash provided by operating activities was ¥114.6 billion, ¥31.7 billion more than one year earlier. The ¥64.7 billion increase in income before income taxes and minority interests was the largest factor. Also contributing to cash flows was a smaller change in trade receivables.

Net cash provided by investing activities was ¥0.4 billion, a difference of ¥51.1 billion compared with cash used one year earlier. The main sources of cash were proceeds from sale of vessels and a net decrease in short-term loans receivable.

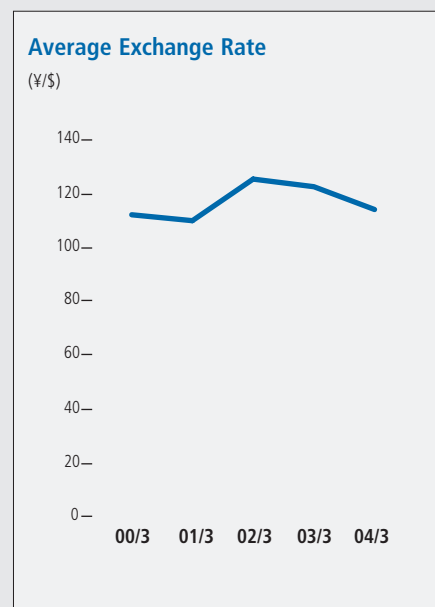
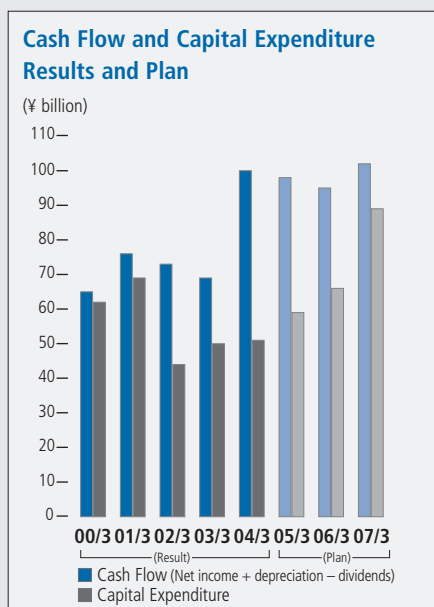
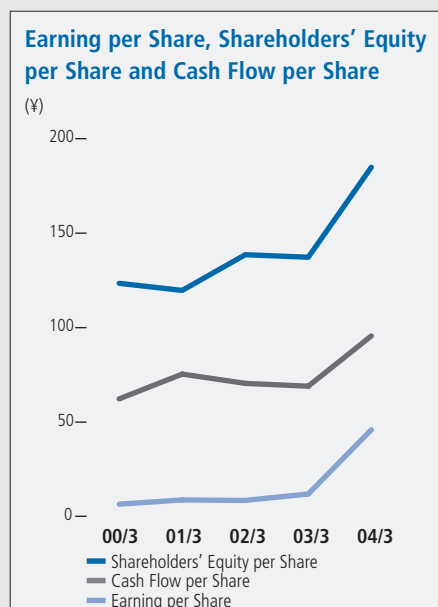
Net cash used in financing activities was ¥110.9 billion, ¥83.6 billion higher than in the previous fiscal year, mainly because of the repayment of long-term and short-term loans and a decrease in commercial paper.

Due to the above items, there was a net increase of ¥2.2 billion in cash and cash equivalents to ¥45.3 billion at the end of the fiscal year.

Capital Expenditures

Capital expenditures amounted to ¥50.5 billion, mainly for the acquisition of vessels. During MOL *next*, the three-year period that ended in March 2004, a total of about ¥300.0 billion was used to construct 71 vessels. During MOL STEP, the three-year period ending in March 2007, MOL plans to increase this by over 60%, constructing 117 vessels at a total cost of approximately ¥490.0 billion. Slightly less than half of the total cost of these new vessels (¥214.0 billion) will appear on the balance sheet as vessels, long-term loans receivable and investments in and advances to unconsolidated subsidiaries and affiliated companies. The remainder is to be procured through long-term charter contracts, leases and other arrangements that do not appear on the balance sheet. Please refer to Note 9 of the notes to the consolidated financial statements for more information on leases.

MOL is planning capital expenditures of ¥214.0 billion during MOL STEP, well below projected cash flows of ¥291.0 billion during this three-year period. The difference of ¥77.0 billion is to be used to further reduce debt through the repayment of long-term and short-term loans and the redemption of bonds. The goal is to reduce debt to ¥420.0 billion by March 2007.



Off-Balance-Sheet Transactions, Contractual Liabilities and Contingent Liabilities

Guarantees extended to joint venture companies that own LNG carriers represent the majority of the group's contingent liabilities as guarantor or co-guarantor of indebtedness of related and other companies.

The group's contractual liabilities consist mainly of long-term and short-term loans, bonds, commercial paper, and leases for vessels and equipments. Please refer to Notes 5, 6 and 9 of the notes to the consolidated financial statements for more information on contractual and contingent liabilities.

Risk Management

In overseas shipping, the MOL Group's core business, the group is exposed to foreign exchange, bunker price, interest rate and a variety of other risks due to the nature of this business. The group manages these risks by using its own risk management framework and methodology.

Exchange Rate Fluctuations

U.S. dollar-based overseas shipping revenue accounts for a large share of consolidated revenue. A large share of expenses as well are denominated in U.S. dollars and other foreign currencies. Since foreign currency revenue is greater than foreign currency expenses, an appreciation of the yen, especially relative to the U.S. dollar, has a detrimental effect on consolidated earnings. Accordingly, the group is working on increasing the share of U.S. dollar-denominated expenses while establishing currency hedges and taking other actions to minimize the negative effect of fluctuations in the value of the U.S. dollar. The group estimates that a change of one yen in the U.S. dollar-yen exchange rate raises or lowers consolidated ordinary income by approximately ¥1.3 billion based on current operations.

Bunker Price Fluctuations

Procurement of fuel to operate vessels is vital to MOL's operations. Since the market price of bunker is generally linked to the price of crude oil, any increase in the price of crude oil can have a detrimental effect on earnings. All vessels

operated by the group consume almost 5 million tons of bunker each year. Approximately half of the risk involving price fluctuations is assumed by customers, charterers and other external parties. Therefore, an increase of US\$1 per metric ton in the average annual price of bunker would lower consolidated ordinary income by approximately ¥0.3 billion. Furthermore, the group uses fuel hedge transactions to even out and reduce the cost of procuring bunker.

Interest Rate Fluctuations

MOL depends mainly on funds procured from external sources to meet working capital and capital expenditure requirements. Funds procured at variable interest rates may be affected by interest rate fluctuations. Consequently, MOL is limiting exposure to interest rate risk by procuring funds through fixed-rate loans and using interest rate swaps. As of March 31, 2004, yen-denominated and U.S. dollar-denominated interest-bearing liabilities totaled ¥491.7 billion, and approximately 70% of this amount had fixed interest rates for the principal amount. As a result, the impact of an increase of one percentage point in interest rates would impact annual consolidated ordinary income by between ¥1 billion and ¥2 billion.

Vessel Operations

With a fleet of more than 500 vessels in constant operation around the world, there is a risk of a marine accident. To prevent accidents, MOL, based on its Corporate Principle of "protecting the marine and global environment through safe navigation," has established its own safety management system, operates a comprehensive crew education and training system, and takes other steps to ensure safety. Furthermore, the group has adequate insurance coverage to prevent a material impact on operating results in the unlikely event that a collision, sinking, fire or other marine accident involving an MOL-operated vessel causes damages at MOL and a third party.

Outlook for Fiscal 2004

In MOL STEP, the new medium-term management plan that was announced in March 2004, MOL has established the goal of ¥330.0 billion in operating income during the plan's three years. This is the total of ¥105.0 billion in fiscal 2004, ¥110.0 billion in fiscal 2005 and ¥115.0 billion in fiscal 2006. This goal is based on a U.S. dollar-yen exchange rate of ¥110 and a bunker price of US\$150/MT.

When fiscal 2003 results were released in May 2004, MOL announced consolidated forecasts of ¥115.0 billion for operating income and ¥62.0 billion for net income in fiscal 2004. This assumes a U.S. dollar-yen exchange rate of ¥110 and a bunker price of US\$180/MT. This forecast represents an increase of ¥22.9 billion over fiscal 2003 operating income, which was far above MOL's previous record for this earnings category. MOL aims to generate higher earnings in all new business segments in fiscal 2004, but higher earnings in dry bulk and containerships are expected to make the largest contributions to operating results.

