

# Containerships



**Hiroyuki Sato**  
Deputy President

## Years of hard work produce a strong recovery

After many difficult years during the 1980s and 1990s, containership performance finally began to rebound as the current decade began. The turnaround was mainly the result of MOL's aggressive steps to cut costs and enhance services along with better market dynamics.

A central goal of MOL *next* was to build a framework for sustainable profitability and growth. Due to challenging market conditions early in MOL *next*, notably in the wake of the 9-11 terrorist attacks, containership earnings fell well short of goals during the plan's first two years. However, performance in the plan's final year was solid, backed chiefly by strong growth in cargo volume, relentless cost-cutting measures and the success of rate restorations in the key east-west trades. North-south trades also returned to profitability. The overall result was a ¥29.7 billion improvement compared with the ¥9.7 billion loss in the prior fiscal year.

## The containership business transformation gains momentum

Containership operations are undergoing the greatest transformation in well over a decade. Most obvious is the change in the fleet, with the delivery of 16 containerships having been completed late in 2003. Ranging from 4,500TEU to 6,400TEU, these highly efficient vessels are now plying routes linking Asia with North America or Europe. With annual growth in container cargo volume projected at 8% to 10% over the next few years, the additional capacity is timely. As the new vessels joined the fleet, many mid-size capacity vessels were cascaded to north-south trades, making MOL more cost competitive.

The ongoing transformation is making MOL more resilient to volatility in freight rates, an inherent facet of containership operations due to the absence of long-term contracts. Most significant are the great strides in recent years in making operations more cost competitive. In fact, ¥24.0 billion was removed from the containership cost structure during MOL *next* alone. With a lean operating structure, MOL will be able to preserve a better financial position than competitors

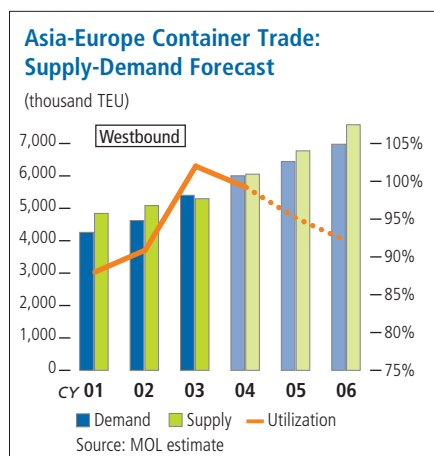
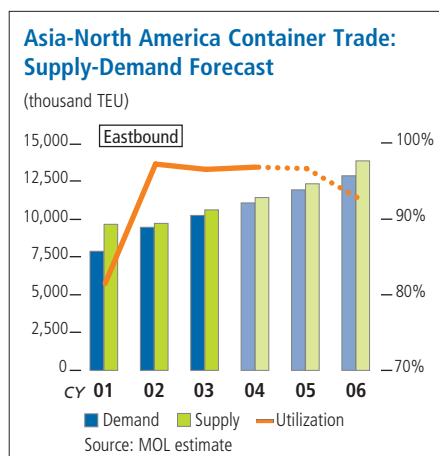
even during market downturns. And MOL is now confident that markets will rebound from downturns more quickly than before because container operators have learned that, with today's narrower differences of operating costs, self-destructive rate-cutting competition will produce no winners. Stronger demands for profits by their shareholders are also helping to prevent excessive rate cutting.

## Investments continue to upgrade and enlarge the fleet

Due to the strong final year of MOL *next*, MOL has raised its containership earnings target for the three years of MOL STEP, foreseeing strong and generally stable earnings during the entire period.

Exports from China continue to be the primary source of growth in demand for containership services, as global out-sourcing of production progresses. In 2003, container volume rose 7.4% on the trans-pacific trade and 16.9% on Asia-Europe trade. During MOL STEP, six 6,350TEU containerships will join MOL's fleet, followed by two more soon afterward along with four 8,100TEU vessels. On the other hand, our initiatives to reduce our expenses continue. Plans to eliminate approximately ¥3 billion each year during MOL STEP will target terminals, trucks and other cargo-related expenses; measures to use equipment more effectively; and the cutting of administrative and ship expenses. Participation in TNWA, which covers about 100 containerships, will remain a central element in holding down expenses while maximizing the quality of services on trunk routes. Making MOL even more competitive is one of the industry's strongest customer-driven teams of professionals in container logistics.

Overall, the outlook for containerships is good. Favorable supply-demand dynamics indicate that rates will be stable at the least and may even rise, although visibility for rates drops over a longer time frame. As MOL introduces new vessels while making further gains in cost cutting, containership operations will be even better structured to generate consistently solid returns on capital over the long term.



# Bulkships



**Dry bulkers**  
**Masao Sagara**  
 Senior Managing Director

## Dry bulkers

### Solidifying MOL's global leadership

In this category, which mainly represents the transportation of iron ore, coal, wood chips, grain and steel, operating results were generally in line with the goals of MOL *next*, despite a brief downturn in 2002 as dry bulker rates fell to an unusually low level. Most significantly, MOL was well over its targets with regard to the restructuring of the fleet, the placement of timely orders for new launchings, and the acquisition of new contracts. Overall, this business is now well positioned to achieve the targets set forth in MOL STEP.

During 2003, MOL placed a large number of orders for bulkers, mainly in the Capesize class. The timing was perfect: Today, the cost of building bulkers is much higher. Furthermore, these new vessels are being delivered precisely as demand for large-scale bulkers is expected to be strongest. A total of 35 Capesize bulkers began joining the MOL fleet in January 2004; long-term contracts have already been signed for more than two-thirds of these vessels.

For smaller sizes of bulkers, the fleet has been restructured. Charter contracts with relatively high charterages were terminated, and most of the small handy-size bulkers in the 18,000 to 26,000 ton range were replaced by larger vessels that match current demand patterns. When MOL merged with Navis in April 1999, there were about 100 Panamax and handy-size vessels. By the end of MOL *next*, the small bulker fleet had been reborn as a highly cost-competitive fleet of about 60 time-chartered and 15-20 spot-chartered vessels.

Dry bulker operators witnessed the most buoyant market conditions in almost a decade during the past fiscal year. But the speed of the recovery increased idle time for bulkers due to port congestion, preventing companies from fully reaping

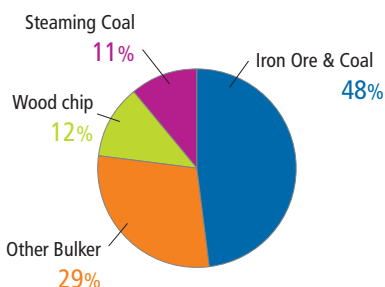
the benefits of the upturn. A full-scale rebound in operating results will thus not begin until the 2004 fiscal year. The long-term outlook is solid. In the iron ore category, for example, current market conditions are likely to last at least until 2008. A large increase in demand for iron ore is foreseen, especially in China. But since the world's shipbuilders are operating at full capacity, new orders for bulkers cannot be accepted until at least 2007.

As in recent years, MOL's basic policy will be to take advantage of strong market conditions and the competitive fleet to enter into medium- and long-term contracts on the current favorable terms, thus locking in long-term revenue streams. About half of the Capesize bulker fleet of 65 to 70 vessels operates on long-term contracts. The goal is to operate the remainder on COA (Contract of Affreightment) contracts with a length of about three years. In line with this policy, the lock-in rate is 95% in fiscal 2004, 70% to 80% in fiscal 2005 and 60% to 70% in fiscal 2006. Furthermore, due to consistently strong demand, considerable earnings are foreseen from smaller sizes of bulkers as well. Most of specialized carriers for wood chips and steaming coals operate on long-term contracts.

Due to this environment, MOL is virtually certain to meet the dry bulker goals set forth in MOL STEP.

MOL is the world's largest operator of dry bulkers. This position gives the company unsurpassed access to market and customer information, along with greater flexibility in supplying vessels when and where customers require them. Thanks to these strengths, MOL was recently able to capture in long-term contracts to supply five 230,000/320,000-ton-class large Capesize bulkers to three steel mills in Japan and one in China. During MOL STEP, still more progress will be made in building on this strength to establish an operating framework for bulkers that is highly profitable and resilient to market downturns.

### Dry Bulkers Revenue Breakdown



**Car carriers**  
**Setsuyasu Hagiwara**  
 Managing Executive  
 Officer



**Tankers  
 LNG carriers**  
**Tokinao Hojo**  
 Deputy Chairman



## Car carriers

### Targeting overseas opportunities for growth

Continued growth in Japanese car exports during 2003 helped MOL to significantly increase its car carrier operations. The addition of larger, more efficient vessels to the MOL car carrier fleet, and an increase in the volume of vehicles carried in cross trades, also contributed to this expansion.

Due to strong demand in 2002, the car carrier industry was at times unable to supply sufficient capacity to meet customer needs. In 2003, with six new car carriers joining the fleet, MOL was comfortably positioned to accommodate the increase in car exports from Japan, and finished the year with a strong performance. The arrival of these six new vessels in 2003 had a significant impact on operations. In addition, four vessels are scheduled for delivery in 2004, six in fiscal 2005 and two in fiscal 2006. By 2007, all 18 car carriers ordered in the early 2000s will be in service, giving MOL a highly competitive, modern car carrier fleet.

Over the long term, the greatest growth in auto exports is expected in South-east Asia, China, and emerging producing regions such as Mexico and South America. MOL will use its competitive strength and emphasis on customer care and satisfaction to retain and build upon its existing business. MOL will also seek new opportunities to generate the consistent growth called for by MOL STEP, the new three year management plan.

MOL is proud to offer its customers a car carrier service that places a premium on safe and efficient operation, backed by many vessels that incorporate sophisticated environmental protection measures. MOL's workforce is trained to closely monitor all aspects of operations to identify ways to improve services and to ensure damage-free loading and unloading. The car carrier sector has good prospects for continuous growth, and MOL is well placed to be a primary beneficiary.

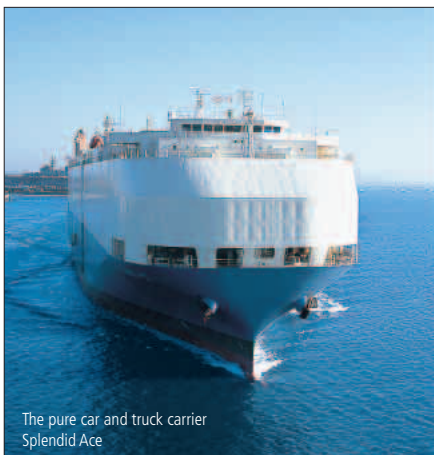
## Tankers

### Prioritizing profitability and safe navigation

During MOL *next*, energy-related shipping was positioned as one of MOL's primary sources of growth. Fleet expansion coupled with generally strong market conditions enabled MOL to meet or exceed performance targets in this category. Improvements in tanker operations highlighted these improvements. Only a break-even business as recently as 1999, tankers now generate solid returns thanks to a relentless drive to sell or refinance high-cost vessels and take other steps to restructure the fleet. Today, MOL has one of the most competitive and credible tankers fleets in the world.

During the three years of MOL *next*, MOL ordered nine VLCCs, an investment that will make its entire VLCC fleet double-hulled by March 2007. An IMO Marine Environment Protection Committee decision in principle bans the use of single-hull VLCCs from 2010. By completing this process early, MOL has held down the cost of its VLCC fleet by avoiding an expected increase in the cost of building these vessels as the deadline approaches. While MOL's basic policy is to operate VLCCs on long-term contracts, between 10% and 15% of the fleet is typically operated on spot rates. Rising demand for crude oil in China and the United States is holding spot rates high, a trend that MOL expects will continue.

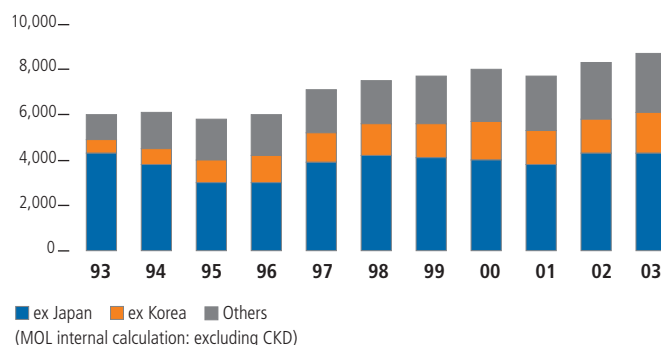
Significant growth is occurring in the product tanker fleet. MOL is targeting many opportunities in the transport of refined petroleum products. In December 2002, an order was placed that will raise MOL's fleet of MR (25,000 to 55,000 tons) tankers from 10 to 25. In February 2004, MOL ordered seven LR1 (55,000 to 85,000 tons) tankers, which will increase this fleet to 10 vessels. Oil-producing nations are increasing exports of refined products at the same time industrialized nations are finding it difficult to expand refining capacity due to environmental and other considerations. Demand for imports of these products is thus certain to grow, especially in China and the United States.



The pure car and truck carrier  
 Splendid Ace

### World Car Carrier Trade

(thousand vehicles)



Also MOL is solidifying its world-leading position in the ocean transport of methanol, a steadily growing market that requires considerable expertise.

Overall, MOL *next* was generally a period for acquiring and ordering the tools for growth. Having largely completed this process, the company is positioning MOL STEP as a time to reap the benefits of its larger, more powerful energy fleet while making more investments for growth.

## LNG carriers

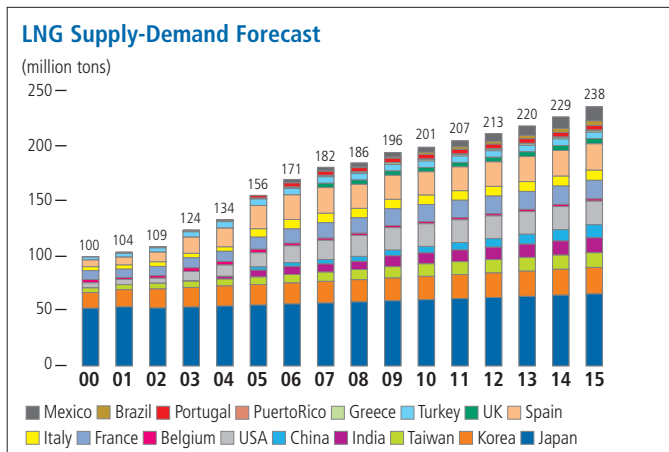
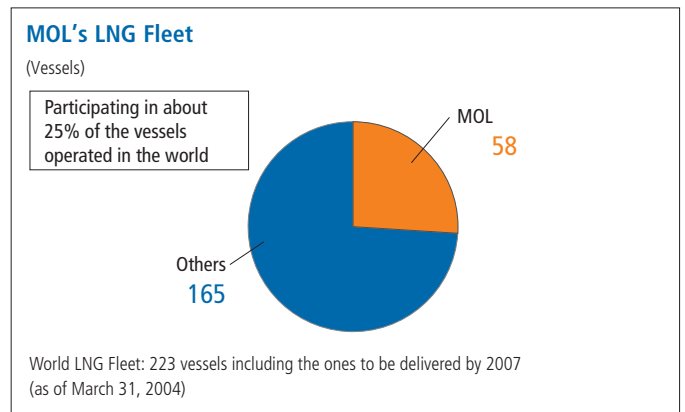
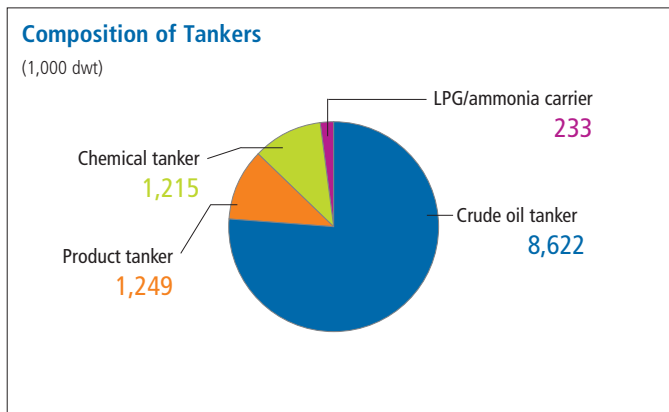
### A market with excellent long-term growth prospects

The LNG carriers business is becoming one of the most competitive categories of energy-related shipping. The undisputed leader in this market, MOL can combine reliable vessel operations with low-cost financing schemes. This is critical now as financing costs are typically the most decisive factor in the selection of LNG carrier owners and operators. Growth has been consistent. The number of LNG carriers that MOL operates or participates in has grown from 37 in April 2001, when MOL *next* began, to 42 in March 2004. During the same period, MOL captured

contracts for 16 vessels, well over the MOL *next* target of 10 vessels. By March 2007, this fleet is expected to grow to 58, about one-fourth of all LNG carriers projected to be in operation at that time.

The United States is expected to be a primary source of growth in demand because of limitations on the production of domestic gas and on imports from Canada. Using LNG to meet only 10% of total U.S. demand would translate into annual imports of 50 million tons, about the same as Japan imports now. Based on current growth forecasts, which include Europe, India and other emerging LNG markets, between 50 and 60 LNG carriers will be needed to handle the exports of Qatar alone. Many players are drawn to this growing market, including LNG producers and buyers themselves, leading to increasingly fierce competition. MOL is using its unmatched expertise to form more mutually beneficial relationships with producing countries. Most significant was a May 2003 agreement with the Sultanate of Oman to help develop that country's ocean transport industry, particularly for LNG shipping.

Since new LNG carriers are ordered only after the signing of long-term contracts, contributions to earnings are highly visible and reliable.



# Logistics



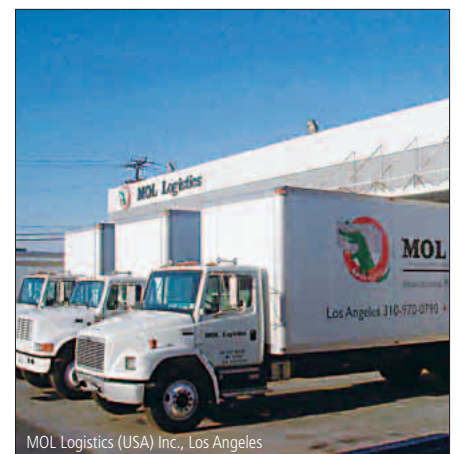
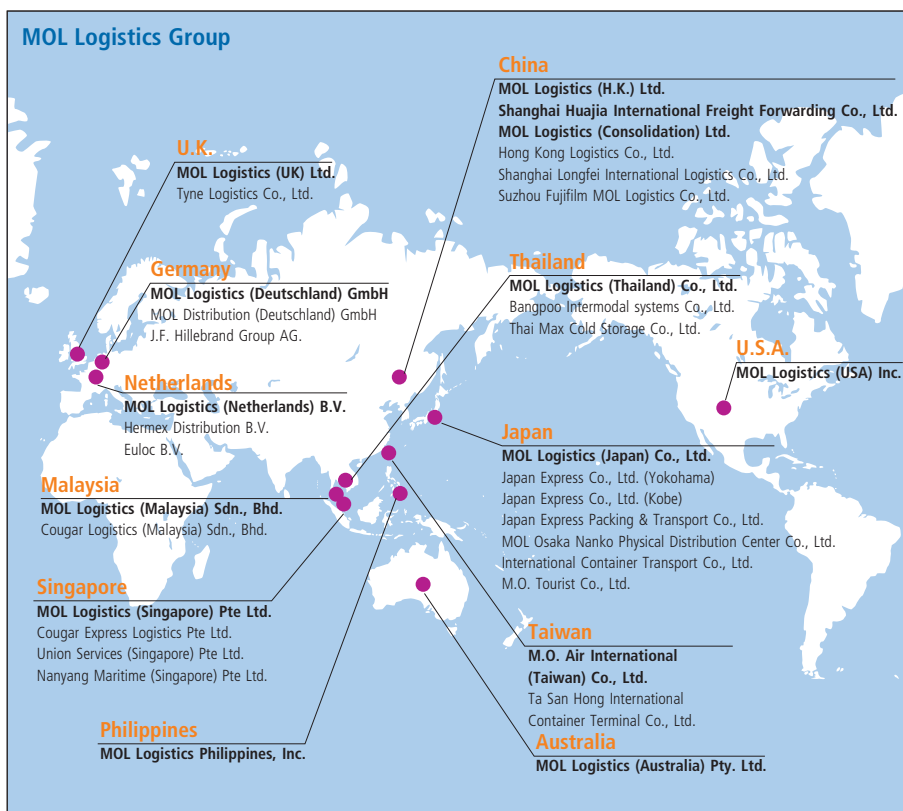
**Masakazu Yakushiji**  
Managing Executive Officer

## Leveraging the MOL brand to reinforce the logistics business

In the years leading up to *MOL next*, logistics operations were realigned and consolidated to serve primarily as an integral element of MOL's containership operations. Since much progress had been made by 2002, the strategic realignment advanced to the next stage in 2003, which involved adopting an even more aggressive stance. To centralize oversight of logistics, the Logistics Office was upgraded to the Logistics Business Division in 2003. Overseeing 36 companies, this division is concentrating on providing logistics services that originate from customers' needs and are located wherever customers are. Examples include an ocean consolidation business and the management of the European inventory of a Japanese manufacturer. This approach is sharply different from the conventional approach of simply seeking to fill space in MOL's own warehouses and trucks. At the nucleus of this drive is the powerful MOL brand. To take full advantage of this brand, and create a more unified image, the names of almost all logistics operating companies worldwide now incorporate the MOL Logistics name.

While the numerous actions taken during *MOL next* have given MOL a logistics organization that is much more efficient, it is not yet able to generate a

meaningful profit. During *MOL STEP*, the goal is therefore to use the customer-centric business models to raise sales by more than 50% from the current level of about ¥50 billion while improving profitability. By 2008, logistics operations aim to generate annual revenues of at least ¥100 billion. Achieving this scale will require more changes at the MOL Logistics group of companies. The aim is to position MOL Logistics as a source of comprehensive logistics solutions, based on expertise in containers and air cargo forwarding. As one way to accomplish this, a number of logistics specialists were recruited during 2003, adding considerable depth to MOL's global logistics capabilities. And network expansion is drawing on the MOL Logistics brand to go beyond air and sea forwarding, serving as a one-stop source of consolidation and other value-added services. Measures will target the establishment of a framework able to meet specific logistics needs of customers without the need for large investments. Emphasis is being placed on serving major users of MOL shipping services, especially for containerships and car carriers, in order to capture the greatest possible synergies. By offering a diverse lineup of support in this manner, MOL is determined to make logistics an even more important element of its operations.



# Ferry and Domestic Transport

**Kazuichi Okai**  
Managing Executive Officer



# Associated Businesses

## Return to profitability bodes well for ferry operations during MOL STEP

For many years, MOL has been integrating subsidiaries, forming alliances, withdrawing from selected routes and taking other decisive actions to turn around its ferry operations. One key action was the formation in 2001 of Shosen Mitsui Ferry Co., Ltd., which downsized previous ferry operations, withdrew from an unprofitable route and entered into an alliance with another ferry operator that had been a competitor. In parallel with these activities, investments were made in several vessels that made ferry transportation more appealing to truckers, cargo shippers and individual travelers. Japan's policy of encouraging a "modal shift" is one positive trend, prompting truck operators to rely on ferries for long-distance segments of their routes. Due to these initiatives, the final year of MOL *next* saw MOL's ferry operations return to profitability.

One means of expanding business is a tie-up with Nippon Express Co., Ltd., one of Japan's largest logistics firms. MOL and this partner now jointly operate four high-speed roll-on, roll-off (RORO) ferries between Tokyo and Kyushu. Operations began in October 2003 with daily service from January 2004. One more venture is a "Shanghai Super Express" ferry between Fukuoka, Japan, and Shanghai targeting cargo that can be transported at a speed between conventional ships and air freight.

During MOL STEP, ferry operations will continue to pursue the same strategies that have proven successful in the past. On underperforming routes, cost-cutting, alliances and other actions will be taken to establish a profitable operating framework. And further investments will be made to capitalize on opportunities in the cargo as well as passenger markets. At the same time, operations will be streamlined wherever possible.

MOL's domestic shipping operations are conducted primarily by MOL Naikou, Ltd., mainly for the transport of cement, steel, LPG and salt. This company became profitable from the first year of its formation in 2003 thanks to initiatives to restructure operations it succeeded. Domestic shipping recently began to transport imported coal from coal centers in Japan to power stations. To spur more growth, this activity is being linked with MOL's fleet of bulkers and backed by alliances with other operators of cargo ships within Japan.

Overall, improvements made during the past few years provide a sound base for further progress in strengthening MOL's ferry and domestic shipping operations during MOL STEP.

## Focusing on ocean transport related fields

Most activities in associated businesses are linked in some way to MOL's core shipping operations. Representative activities include trading to procure fuel and supplies required by ships, manning services, tugboat services, civil engineering and construction services, and building management. This segment also includes two cruise ships, one owned by MOL and the other held by a company owned by MOL and a partner.

During MOL *next*, companies in this segment streamlined and bolstered their operations, significantly boosting productivity and profitability. Looking ahead, the central objective is to contribute to fulfilling the strategic goals of MOL STEP by seeking more opportunities for growth in businesses peripheral to ocean shipping. This process will be conducted so as to take full advantage of the collective resources of the MOL Group. Due to the breadth of its activities in associated businesses, MOL has numerous opportunities to establish new sources of earnings through the provision of services that can make ocean shipping operations more efficient. In the past, for example, both manning and data processing services were begun as an extension of shipping operations. Plans call for capitalizing on similar opportunities in the coming years.



The roll-on, roll-off ferry Sunflower Hakata



The tug boat Kamiya Maru

## CO<sub>2</sub> Unit-Emissions by Mode of Transportation

(Unit: g-C/ton-km)

Large tankers	1
Large containerships	3
Trains	6
Domestic cargo ships	11
Trucks	49
Small trucks	226
Airplanes	398

Note: CO<sub>2</sub> unit-emissions represent the volume of CO<sub>2</sub> (g-C/ton-km, coal equivalent) emitted when transporting one ton of cargo over one kilometer.

(Sources: "Transportation Energy Handbook, Fiscal 2001, 2002," Ministry of Land, Infrastructure and Transport, and MOL data)