



Having largely achieved the targets for our five-year plan (fiscal 2003–fiscal 2007) in the first three years, we have now formulated a new medium-term management plan that allows Tokyo Gas to maintain its impetus and capitalize on business opportunities in a rapidly changing business environment. Our aim is to pursue further growth by creating and cultivating new markets for natural gas.

Mitsunori Torihara President

**Q:** Your appointment as President of Tokyo Gas coincided with the announcement of a new medium-term management plan at the start of the current year, 2006. You must be very determined to ensure that the plan's targets are achieved.

**Torihara** Competition is intensifying in the Japanese energy market. There is competition between different forms of energy, and between different companies within energy segments. I am confident that Tokyo Gas can continue to achieve growth and success in this business environment by further enhancing its strengths, including its outstanding technological and solid marketing capabilities.

As President, I intend to heed the wishes of all stakeholders, including shareholders and investors. My aim is to build a dynamic management approach based on trust. I am confident that we will be able to maximize our corporate value and enhance the attractiveness of the Tokyo Gas Group.

In April 2006, we took our first step on the path to this future by launching a new medium-term management plan for the period from fiscal 2006 to fiscal 2010. As Executive Vice President, I was deeply involved in the formulation of this plan, the content of which has been refined through repeated cycles of debate and discussion. My involvement in IR activities also dates from my time as Executive Vice President. I have attended numerous meetings with institutional investors in Japan and overseas, and I have had many opportunities to hear the views of investors about our management policies. I believe that those views are properly reflected in our new medium-term management plan. Our new plan is the product of long debate and thought. That process is now over, and the time has come to turn the plan into action.

Tokyo Gas must never betray the expectations and trust of its shareholders and investors. My task is to provide the leadership to ensure that the plan is implemented steadily.

This plan is an important step in our long-term strategy and I will use it to lead the Tokyo Gas Group to sustainable growth in the second decade of the 21st century.

**Q:** The previous medium-term management plan ended in fiscal 2005. How would you characterize that year?

**Torihara** We continued to make steady progress with policies contained in our “Frontier 2007”, the Tokyo Gas Group’s medium-term management plan for the period from fiscal 2003 to fiscal 2007. Fiscal 2005 was the third year of that plan, but our primary management targets were already within reach, and we also needed to adapt to market changes and utilize the business opportunities. We therefore decided to bring forward the transition to our newly formulated medium-term management plan. Fiscal 2005 in effect became the final year of “Frontier 2007”. It was an extremely challenging year, mainly because of continuing deterioration in the external environment.

Net income decreased by ¥21.9 billion from the previous year to ¥62.1 billion. The main factor for this decline was a significant rise in the cost of gas resources compared with levels in fiscal 2004, resulting from an upward trend in LNG prices in step with dramatic increases in crude oil prices.

However, we achieved significant successes in our sales operations. Growth in all sectors boosted gas sales volumes by 7.1% year on year to 13.1 billion m<sup>3</sup>. This expansion was led by the growth of the industrial and commercial cogeneration stock, which increased by 12% year on year to 1,340 MW.

Another impression from the previous year is that customers now have dramatically higher expectations for natural gas as a fuel providing greater economic and environmental benefits than crude oil, which has remained very expensive for the past year. We also made significant progress with our preparations for this expansion of demand, including the announcement of new pipeline expansion plans. One of these projects is the Chiba-Kashima Line, which is scheduled to start operation in fiscal 2010.

**Q:** Your previous five-year plan was scheduled to end in fiscal 2007 but was completed in just three years. Please tell us about your achievements under the plan.

**Torihara** Under the previous medium-term plan, we set quantitative targets for Tokyo Gas Economic Profit, or TEP, which is our version of EVA®, and for ROA, free cash flows and interest-bearing debt. Despite the serious erosion of profit levels by sharply higher gas resource costs led by appreciated crude oil costs, we had largely reached our final targets by fiscal 2005, the third year of the plan. In fact, we exceeded our target for the reduction of interest-bearing debt, and our D/E ratio in fiscal 2005 was significantly improved at 0.77.

We also achieved our target of reducing fixed costs per m<sup>3</sup> of gas sold by around 20%, through corporate restructuring measures designed to improve our cost structure.

“Frontier 2007” also stipulated the purposes for which free cash flows were to be allocated for use. Statistics for the three-year period show that approximately 17% of free cash flows were used for dividends, approximately 20% for stock repurchases designed to prevent dilution resulting from CB conversions, approximately 13% for new investments to expand our business in energy-related areas, and approximately 50% for the reduction of interest-bearing debt.

Compared to when we formulated the five-year plan, we allocated a smaller percentage to new business investment and larger percentages to shareholder returns in the form of dividends and stock repurchases, and the reduction of interest-bearing debt. Reasons for these changes include the fact that we were able to increase the dividend after it became apparent at the end of fiscal 2003 that free cash

flows would exceed the level targeted in the plan, and the fact that investment in the electric power business, which accounts for a relatively large share of our business expansion in energy-related areas, was scheduled for the second half of the plan period. There has been no change in policy on the allocation of



free cash flows.

The greatest achievement of "Frontier 2007" was the realization of our vision of Tokyo Gas as an energy frontier business group capable of generating added value not only from natural gas, but also from other energy forms and energy-related activities. I believe that we have built a solid foundation for our future growth. Of particular significance in the energy service business was our decision to

integrate the operations of ENERGY ADVANCE Co., Ltd., with those of Tokyo Gas Co., Ltd. By the end of fiscal 2005 we had signed 125 contracts for capacity amounting to 226 MW, which is the highest performance in Japan.

In addition to this expansion of our energy-related business operations, we have also enhanced our presence throughout the natural gas value chain through our involvement in upstream projects, transportation and other areas. Tokyo Gas has made significant progress toward its next stage of development.

**Q: What factors led to the formulation of the Tokyo Gas Group's new medium-term management plan, and what are the aims of the plan?**

**Torihara** We have already made significant progress toward the realization of our vision for the future of Tokyo Gas under "Frontier 2007." However, the environment in which Tokyo Gas operates has changed dramatically over the past few years.

Natural gas is seen increasingly as an environmentally friendly form of energy to combat global warming, and the relative advantage of the price of natural gas have increased because of rising crude oil prices. The geographical extent of energy market is expanding, and new areas of demand are apparent. At the same time, deregulation has caused further intensification of competition between energy forms and companies in the market for large-volume energy supplies. We also face greater challenges in the market for regulated supplies for residential and commercial sectors. In addition to the decreasing trend of gas sales of each household due to decline of the number of people per household as well as more energy efficient appliances, aggressive all-electric promotion has intensified sharply.

Our medium-term management plan for the period from fiscal 2006 to fiscal 2010 is an action plan designed to enhance our competitiveness by anticipating changes in our business environment so that we can capitalize on business opportunities. The aim of the plan is to create and cultivate new markets for natural gas. We will go beyond "Frontier 2007" to create a broad-based profit structure in the energy sector.

I see this plan as an important step in a long-term strategy focusing on the future of the Tokyo Gas Group in the second decade of the 21st century. We need to concentrate our management resources and focus our efforts on aggressive investment. I am convinced that by achieving the goals of this plan we can ensure a future of sustainable growth for the Tokyo Gas Group. To do this, we must build up the abilities of the entire Tokyo Gas Group in a determined drive to strengthen our competitiveness at the organizational, marketing, technological and service levels.

**Q: What are the key strategic points of your new medium-term management plan?**

**Torihara** Our vision of the Tokyo Gas Group as the leading company in a total energy business beyond 2010 will require sustainable growth driven by solid competitiveness. To achieve this, we will use the strength of our global LNG value chain, which encompasses all stages from upstream to downstream, to provide our customers with wide-ranging value and services. We also intend to expand our services across an area within a 200 km radius around Tokyo in the Kanto region.

Specifically, we will work to meet the diverse needs of our customers through a multi-energy supply including city gas and electricity. We also aim to establish a one-stop energy service structure capable of providing the optimal mix of appliances and systems. By further expanding and enhancing our presence in the LNG value chain, we will transform the Tokyo Gas Group into a business structure with a broad earning base and the ability to translate a competitive advantage in the energy sector into profitability and high growth.

On the earning side, we estimate a 15.3% growth in total sales by fiscal 2010, as compared with fiscal 2005, and we also aim to achieve further cost savings. Our target is a 20% reduction in fixed costs per m<sup>3</sup> of gas sold by fiscal 2010, as compared with fiscal 2005\*. We estimate that by achieving these goals we can lift our EPS to ¥38.2 by fiscal 2010, the final year of the current medium-term management plan. Of course, there can be no final goal for cost reductions. We will strengthen our corporate structure, build a more robust earning base and maximize our profits will continue after 2010.

\*Compared with projections of fiscal 2005 made in the medium-term management plan.

**Q: What are your views on cash flow allocation strategy and financial strategy?**

**Torihara** Financial strategy is as important to our future as business strategy. We will allocate cash flows of ¥1,190 billion to the implementation of our business strategy, including total operating cash flows of ¥1,120 billion over a five-year period, as well as ¥70 billion in other cash flows.

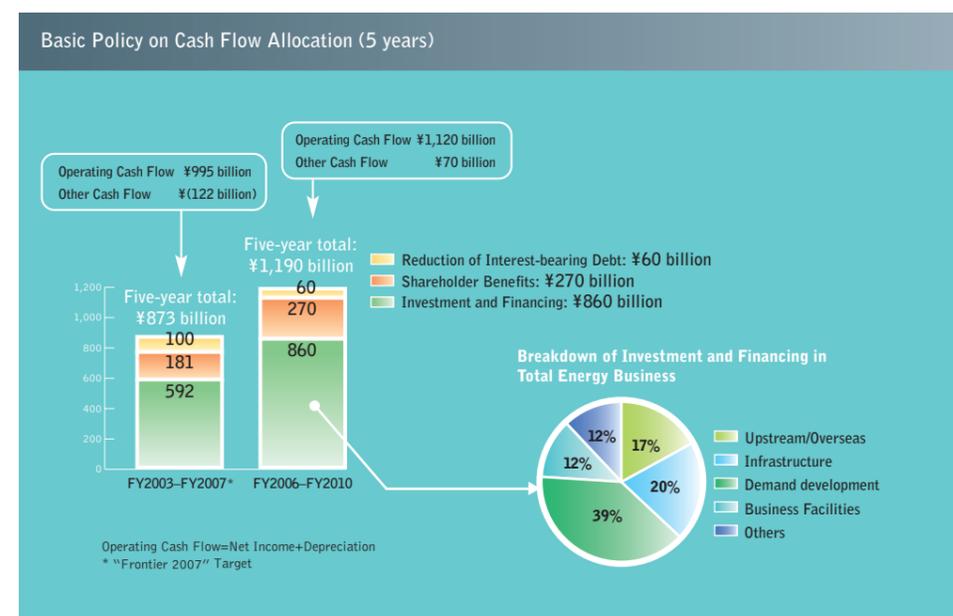
We will invest ¥860 billion in the whole of our core total energy business. Approximately 39% of this amount will be allocated to demand development, including investment in pipelines to increase



the gas sales volumes and the expansion of electric power business and energy services business. We will also invest in infrastructure development in readiness for future demand growth. Investment allocations will include 20% for infrastructure for pipelines and safety and approximately 17% for participation in upstream interests, LNG tanker construction and other priorities. We plan to allocate a total of ¥270 billion to shareholder returns over the next five years in order to regulate the total payout ratio to our shareholders (dividends plus stock repurchases divided by current net income). The reduction of interest-bearing debt was a key management issue under our previous medium-term management plan. As a result, our D/E ratio had reached 0.77 by the end of fiscal 2005. From a financial leverage perspective, I believe we have emerged from the rigorous reduction stage, and we are aiming for a reduction of ¥60 billion under the new medium-term management plan.

We have set four management targets: (1) ROA of 5.5% by 2010, (2) ROE of 10.9% by 2010, (3) Tokyo Gas Economic Profit (TEP, the Tokyo Gas version of EVA®) of ¥51 billion by 2010, and (4) total operating cash flows of ¥1,120 billion for the five-year period. During periods of active investment, maintaining a good ROA is an indicator of our ability to raise assets efficiency through investment while also placing appropriate weight on profitability. We aim to raise this indicator by 1.8 points from the fiscal 2005 result of 3.7%. Our ROE target represents an increase of 1.9 points from the fiscal 2005 result of 9.0%. Our aim is to build an appropriate capital structure, despite the conversion of convertible bonds during the period covered by the plan. Our TEP target will require an increase of ¥28.1 billion compared with the figure for fiscal 2005. Capital costs will remain a key focus as we work to achieve this. To generate operating cash flows of ¥1,120 billion during the five-year period, we will work tirelessly to increase our income.

To enhance our financial soundness, we intend to maintain and improve our fund procurement ability. At the same time, we will seek to reduce our D/E ratio to 0.51 by fiscal 2010. However, we have already made considerable progress with the reduction of our interest-bearing debt, so I am prepared to be flexible with this numerical target.



**Q: What are your thoughts on shareholder dividend allocations?**

**Torihara** We intend to allocate a total of ¥270 billion to shareholder returns over the five years covered by our current medium-term management plan. For the first time we have announced the concept of a "total payout ratio" as an indicator of our position on profit distribution. Our target for this ratio, which is calculated by dividing the sum of dividends and stock repurchases by net income\*, is 60%. We aim to meet shareholder expectations by raising both our profit level and per-share value. We have reached this position after talking to numerous shareholders and investors and considering how to meet their expectations as a company involved in a regulated utility business. I believe that, at present, this is the best way to meet the expectations of all stakeholders, including our customers and shareholders.



Stock repurchases have traditionally been used as a way of counteracting the dilution effect that occurs when convertible bonds are converted into shares. In the future, we intend to use this method primarily as a way of achieving a genuine improvement in corporate value, including the redemption of stock.

\*Total payout ratio of year n = [(dividends from unappropriated profit in year n) + (amount of treasury stocks acquired in year n + 1)] / (consolidated net income in year n)

**Q: Tell us about your vision for Tokyo Gas in the approach to the second decade of the 21st century?**

**Torihara** As President of Tokyo Gas, my task is not only to implement our new medium-term management plan effectively and reliably, but also to maintain the status of Tokyo Gas as a company that is trusted and preferred by shareholders and investors, as well as customers, society and communities. My vision is based not just on short-term economic value, but on sustained long-term growth achieved through the continuing enhancement of our brand value, which is built on our long-accumulated expertise in security, safety and reliability. In addition to accelerated growth driven by the steady implementation of the business and financial strategies that I have outlined, I believe our reliability as a company is also extremely important to our future success.

I aspire to make Tokyo Gas corporate culture even more transparent and open. The changes made last year to our officer remuneration systems were part of this process. Meetings of our Board of Directors, which includes outside corporate directors, have become forums for lively debate. To ensure prompt, appropriate management decision-making, we have established an investment assessment committee to screen each investment proposal thoroughly.



Our new medium-term management plan includes strategies designed to create a foundation for strong growth performance in the period to 2010 and beyond. We began to put these strategies into effect on April 1, 2006, and must now maintain this momentum.

I intend to focus my greatest efforts on the following areas: First, we will target overall Group optimization.

All of our business segments are linked to the LNG value chain, and I intend to ensure that Group optimization remains a continual focus in relation to the allocation of management resources, including personnel and money, so that we can achieve our full potential as a company.

Second, the Tokyo Gas Group will restructure its marketing scheme by strengthening the local roots. Our greatest asset is a customer base consisting of over 9.8 million customers. We aim to improve our services and reliability by building an integrated operational structure encompassing the various tasks handled by Tokyo Gas itself, its local agents, such as Enesta and Enefit, and Group companies involved in customer service and other areas.

Third, as President of Tokyo Gas, I am determined to ensure our success in this rapidly changing environment by making sustained progress toward the creation of a broad-based profit structure for the decade after 2010. We will also work to maximize our business opportunities by evolving from a conventional gas business into a total energy company, and seek to create and cultivate new markets for natural gas.

The path ahead will not be smooth. However, I am convinced that we can achieve sustainable growth by living up to the expectations and trust of all stakeholders. I approach my management role with a strong determination and commitment to the future success of Tokyo Gas.

A handwritten signature in black ink, reading "M. Torihara". The signature is written in a cursive, flowing style.

Mitsunori Torihara, President