An Interview with the President

Q Looking back, what kind of year was fiscal 2007? In particular, what was the impact of rising crude oil prices on revenue and expenditure?

TORIHARA Fiscal 2007 was the second year of the medium-term management plan for fiscal 2006–2010. Crude oil prices reached all-time highs, so the business environment for Tokyo Gas continued to be severe, because natural gas is at the core of our business.

Reflecting this situation, net sales in fiscal 2007 reached an all-time high of ¥1,487.5 billion as a result of an increased gas sales volume and higher unit gas rates under the gas rate adjustment system. However, operating income declined by ¥92.3 billion from the previous fiscal year to ¥70.0 billion and net income declined by ¥58.2 billion to ¥42.5 billion. The major factors behind these declines were: rising gas resource costs resulting from the recent rise in crude oil prices; rising labor costs due to an actuarial differential on retirement benefits*; and an increase in depreciation due to a tax revision. Despite these large declines, we maintained a total payout ratio of 74% by allocating dividends of ¥8 per share to our shareholders and carrying out stock repurchases of ¥10.0 billion in fiscal 2008. We intend to continue the policy of returning the benefits to our shareholders through more efficient management, as promised in the medium-term management plan.

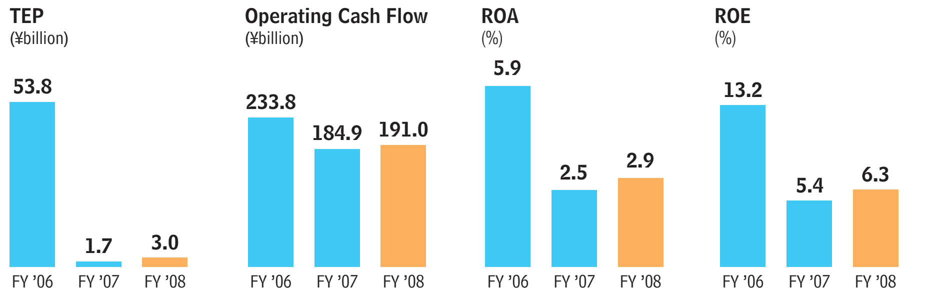
Tokyo Gas imports liquefied natural gas (LNG), a major source of city gas, from overseas. The prices of LNG imported by Japan are generally linked to crude oil prices, which have been continuously rising in recent times. Under the gas rate adjustment system, fluctuations in gas resource costs are reflected in the gas rates after six months at most. However, crude oil prices rose on and off throughout fiscal 2007, so we were not able to completely pass on the gas resource costs, which had already increased dramatically, via sales price throughout the year. As a result, we ended up with large excess expenditures for which we were unable to compensate through our management efforts to cut costs.

Trends in crude oil prices are still uncertain, but Tokyo Gas intends to continue its efforts to keep down the procurement cost of the gas resources. Furthermore, during the current fiscal year we expect to commence importing LNG from Sakhalin II project. Its transportation distance is shorter than that of any other project. We hope that this economic advantage will contribute to reductions in gas resource costs.

As for our business environment, demand for air conditioning in the commercial sector as well as for heating and hot water in the residential sector increased due to high temperatures in summer and cold weather in winter. Moreover, due to the price competitiveness and environmental advantages of natural gas relative to petroleum products, both industrial demand and wholesale supply saw an increase in sales volume, resulting in a healthy overall gas sales volume of 14.22 billion m^3—6.8% higher than the previous fiscal year. The number of our customers exceeded 10 million on September 13, 2007, 122 years after our founding, reflecting the influx of population into major urban areas. We will continue to endeavor to be a company that continuously achieves sustainable growth and development based on the long-term trust that we have built up with our customers.

* Tokyo Gas calculates its retirement benefit liabilities and expenditures using actuarial computations based on specific assumptions. Actuarial differentials are all shown and depreciated as cost items in the accounts for the following year.

Meeting Management Targets Ahead of Schedule



TEP (Tokyo Gas Economic Profit) = net operating profit after tax prior to interest payments – cost of capital (invested capital x WACC)

(WACC FY06 Results : 3.8%
WACC FY07 Results : 3.6%
WACC FY08 Outlook : 3.4%)

Operating cash flow =net income + depreciation

ROA = net income/total assets (average of positions at start and end of fiscal year)

ROE = net income/total equity (average of positions at start and end of fiscal year)

Q Please tell us your plans for restoring business performance in fiscal 2008. Will there be any changes to the promotion or execution of the medium-term management plan going forward?

TORIHARA We are assuming that in fiscal 2008 crude oil prices will remain high and the environment surrounding Tokyo Gas will continue to be severe. Furthermore, the aggressive sales efforts by electric power companies to promote the all-electric concept will continue to have an impact, so we must remain extremely vigilant regarding our competitors. Based on this situation, Tokyo Gas announced its fiscal 2008 earnings estimates on April 25. Net sales in the current fiscal year are expected to be ¥1,712.0 billion—a 15.1% year-on-year increase. Both operating income and ordinary income are expected to recover somewhat, relative to the previous fiscal year, and to reach ¥75.0 billion and ¥68.0 billion, respectively. To achieve these figures in the face of all obstacles, we set priorities for the current fiscal year as follows.

Firstly, we must steadily promote the various measures laid out in the current medium-term management plan. Tokyo Gas is currently operating an "integrated energy business" in an area extending for a radius of 200 km from Tokyo. While developing the strong latent demand for natural gas in the Kanto region, we are providing utility services, including electric power, to customers in an optimal format as energy services. In April 2008, Kawasaki Natural Gas Power Generation Co., Ltd., which is 49% owned by Tokyo Gas, began operation of an 800-MW facility. This enables us to further deepen our integrated energy business, using the weapon of the greenness of natural gas and high efficiency of the combined-cycle generator.

Secondly, we must strengthen our strategy against the all-electric systems for homes and develop further demand. For this reason, in April 2008 Tokyo Gas launched Tokyo Gas LIFEVAL, a new regional energy company. The purpose is to let the new company lead our future efforts to compete with electricity. By integrating Tokyo Gas Customer Service Co., Ltd., which previously provided customer services such as meter reading and safety inspections, etc., and Enesta, which carried out maintenance and sales of gas appliances, we are aiming for more meticulous one-stop services to increase contact points with customers and identify customer needs more appropriately.

Thirdly, we must respond to the recent privatization of a variety of government-owned gas businesses. To strengthen our response to this trend, Tokyo Gas launched the Gas Business Privatization Department in April 2008. Of course, when participating in such businesses, we carry out sufficient business value evaluations and carefully verify the maintenance conditions of facilities and a given project's potential to enhance our corporate value. Through these initiatives, we are aiming to expand the scale of our business and intend to build a solid business foundation in an area extending for a radius of 200 km from Tokyo.

Finally, as the business environment surrounding Tokyo Gas undergoes rapid changes, we will formulate a new medium-term management plan during fiscal 2008. We are aware that the current business environment is extremely severe due to higher LNG prices resulting from the global rise in crude oil prices. In order to achieve sustainable growth, Tokyo Gas will aim for the deepening and development of our integrated energy business and further reinforce our business platform.

In April 2008, we established a new IR Department. We have continued to monitor the expectations of the capital market through dialogues with investors. These expectations will be more clearly reflected in the various measures of the management.

Q In April 2008, you revised the gas rates downward by an average of 1.5%. Why did you carry out the revision at that time?

TORIHARA I believe that our customers are important stakeholders, just like our shareholders. In our current medium-term management plan, we promised a total payout ratio of 60% to our shareholders. At the same time, we promised our customers that we would carry out rate reductions during the period of the plan in order to return some of the benefits of reducing our fixed costs through more efficient management. The rate revision is a part of that policy.

Currently, Tokyo Gas is operating in a severe business environment marked by rising gas resource costs and intensifying competition among different forms of energy. However, due to the sharp increase in global energy prices in recent times, gas rates continue to move upward, based on the gas rate adjustment system. Therefore, we carried out this gas rate revision by returning some of the benefits of the reduced fixed costs, in order to alleviate the burden on our customers as quickly as possible.

The change resulting from this revision is a reduction averaging 1.51% in our tariffs for the entire small-volume segment encompassing both service and optional agreement tariffs in Tokyo and in other districts that have the greatest numbers of customers. The financial impact on Tokyo Gas caused by this rate reduction is expected to be approximately ¥10.0 billion per annum.

Q Is a restructuring of the gas industry possible in Japan? Also, please tell us your views on M&A involving Tokyo Gas.

TORIHARA In Japan, there are currently over 200 city gas suppliers, with nearly 60 of those suppliers concentrated in the Kanto region alone. Furthermore, in addition to these city gas suppliers, there are approximately 1,600 community gas suppliers and approximately 24,600 LPG gas businesses nationwide, all of which provide energy supplies for their respective customers. In Europe and North America, the realignment of the energy industry is occurring rapidly, and investors often ask me if industry realignment is likely to happen in Japan, which has so many energy companies. Although I cannot rule out that possibility, I think that the development of infrastructure is a precondition for such realignment in Japan, where the electricity and gas infrastructure connecting different regions is not as developed as it is in Europe and North America.

Tokyo Gas is already supplying wholesale gas to 26 gas suppliers in its service area. The sales volume to these companies accounts for approximately 13% of our total sales volume. Unlike M&A transactions, the wholesale supply business earns income with high capital efficiency. That is why we are aggressively developing this business. We do not intend to propose any purchases of stakes in other companies. However, if a company approaches us with such a proposal, we may consider entering into a capital partnership after evaluating the corporate value of the company. In April 2008, we launched the new Gas Business Privatization Project Department to respond to government-owned gas suppliers' privatization projects. Tokyo Gas will participate in this kind of project utilizing our previous experience of purchasing government-owned gas suppliers, including the Konosu City and Nagano City gas businesses, if we are convinced that this business will enhance our corporate value and increase benefits to our customers through the promotion of sound due diligence.

Mitsunori Torihara, president