MANAGEMENT'S DISCUSSION AND ANALYSIS OF OPERATION AND FINANCIAL POSITION

SUMMARY

- Consolidated sales reached an all-time high, reflecting sustained growth in gas sales.
- This sales growth has been paralleled by a steady reduction in operating expenses, resulting in a 23.5% increase in operating income.
- Net income was lower because of decisions to take a lump-sum write-off of actuarial differences in retirement benefits, and to bring forward the application of impairment accounting to fixed assets. These measures will help to reduce the future cost burden.
- Without these extraordinary items, free cash flow* would have been substantially above the initial target. For this reason, the annual dividend has been increased by one yen per share.

* Tokyo Gas uses free cash flow as a key management indicator: Free cash flow = net income + depreciation* - capital expenditures**
*including amortization of long-term prepayments **purchases of tangible fixed assets + purchases of intangible fixed assets + long-term prepayments (accounting basis)

Trends in Core Profit Source of Gas Sales Volume

Note: All graph data for year ended March 31

Steady Increase in the Volume of Sales, Conspicuous Growth in Industrial Gas Sales

■ Residential Sector

Temperatures at the start of the fiscal year and during the summer were lower than in the previous year. This was reflected in increased demand for hot water in the first half of the year. Temperatures in the winter were higher than in the year before, with the result that demand for hot water and heating remained static. Overall, sales declined 10 million m^3, or 0.3%, at 3,292 million m^3. There was growth of 55 million m^3 brought on by an increase in the number of customers, and a decline of 52 million m^3 resulting from temperature-related factors. Declines due to other factors, such as reduced sales per household, amounted to 13 million m^3.

■ Commercial Sector

Demand for air conditioning stagnated because of low summer temperatures and mild winter temperatures. However, total sales in this sector increased 4.0%, or 103 million m^3, to 2,695 million m^3. Contributing factors included steady flow of newly commissioned facilities in new properties, including urban redevelopment schemes.

■ Industrial Sector

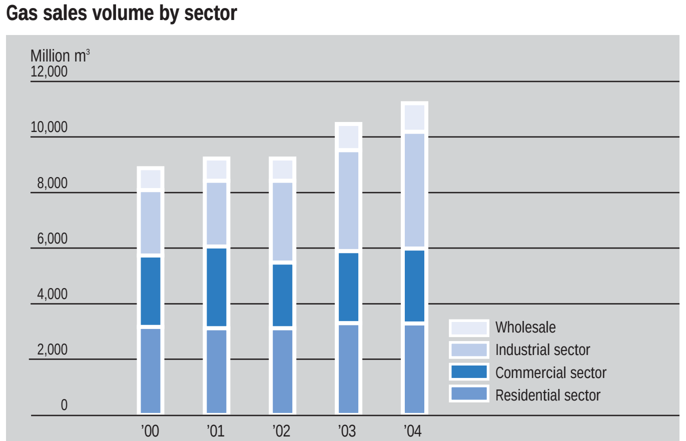
In addition to an increase in demand for use in existing facilities, especially cogeneration systems, there was also a rise in demand for gas used specifically for power generation. These factors brought substantial sales growth of 569 million m^3, or 15.7%, over the previous year's level to 4,201 million m^3. There was a particularly steep increase in demand from electric power companies and independent power producers (IPPs) for gas used solely for power generation. Sales in this area rose 35.3%, or 434 million m^3. This growth resulted in part from increased utilization of natural gas in thermal generation facilities when nuclear power plant operations were suspended. For other uses in the industrial sector (mainly for cogeneration systems), there was a 133 million m^3, or 5.6%, increase, amounting to 2,503 million m^3.

■ Wholesaling to Other Gas Companies

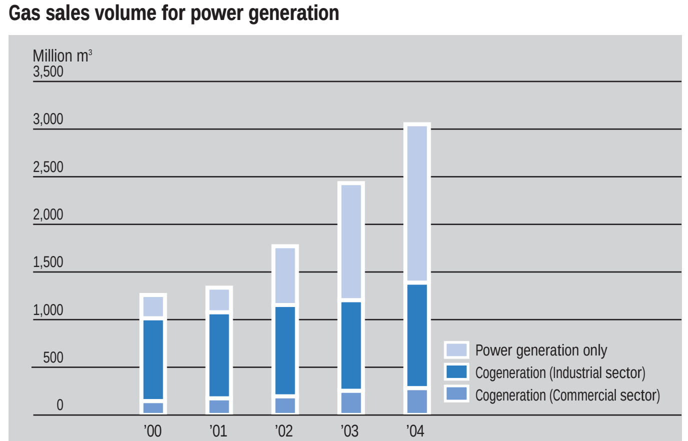
Sales expanded 9.1%, or 86 million m^3, to 1,030 million m^3 with increases in the volume taken by the gas companies to which gas is supplied.

Total sales amounted to 11,218 million m^3, an increase of 747 million m^3, or 7.1%, over the previous year's level.

Gas sales volume by sector



Gas sales volume for power generation



Analysis of Income

Robust Growth in Gas Sales Reflected in Sustained Expansion of Both Net Sales and Operating Income

Despite reduced sales in some segments, such as gas appliance sales and related construction, total sales rose ¥24.1 billion, or 2.1%, to a new record of ¥1,151.8 billion. The rise was attributable to healthy 4.9% growth in gas sales.

Although feedstock costs increased in step with growth in the volume of gas sales, operating expenses were minimized through further measures to improve operating efficiency. This was reflected in operating income, which rose ¥29.0 billion, or 23.5%, to ¥152.3 billion. Operating income increased in all segments.

Business results by segment (¥ Million)

Sales to outside customers

Years ended March 31	2002	2003	2004
Gas Sales	750,439	789,688	826,567
Gas Appliance Sales	148,271	141,225	132,254
Related Construction	67,633	67,045	64,944
Real Estate Rental Business	15,685	14,944	14,151
Other	115,561	114,732	113,909

Operating income

Years ended March 31	2002	2003	2004
Gas Sales	149,210	160,224	189,366
Gas Appliance Sales	7,243	7,842	7,904
Related Construction	3,650	4,175	4,456
Real Estate Rental Business	6,091	7,623	7,883
Other	10,799	9,626	11,270

Note: Segment sales are sales to outside customers, while operating income is the sum of sales to outside customers and intra-group transactions minus the operating expenses of outside and inside transactions.

■ Gas Sales

Higher Volumes Bring Sustained Growth in Both Sales and Income

There was a 7.1% increase in gas sales volumes, led by strong demand from power generation, in which unit prices are lower. The unit price also rose under the "sliding rate" system, which adjusts for fluctuations in gas resource costs. These factors helped to boost sales in this segment by ¥36.9 billion, or 4.7%, to ¥826.6 billion. Nonconsolidated sales increased 4.9%, or ¥38.4 billion. Rising sales volumes contributed ¥21.8 billion and price adjustments under the "sliding rate" system added ¥18.0 billion, while other factors had an adverse effect amounting to ¥1.3 billion. This segment's contribution to total sales rose from 70.0% to 71.8%.

Operating expenses were affected by a rise in gas resource costs in step with volume growth in gas sales. However, measures to reduce selling, general and administrative expenses allowed Tokyo Gas to hold its operating expenses to ¥641.7 billion, an increase of just 1.5% over the previous year's level.

The result was operating income of ¥189.4 billion representing an 18.2% year-on-year increase.

■ Gas Appliance Sales

Strong Sales of Products Designed to Compete with Electrical Appliances

Tokyo Gas recorded buoyant sales of products developed to compete with electrical appliances. However, sales of this segment declined due to static total sales volumes and reduced selling prices, amid strong competition. Despite the resulting decline in segment sales, lower procurement prices and successful efforts to reduce fixed costs and other operating expenses brought higher operating income.

Segment sales fell 6.4%, or ¥9.0 billion, to ¥132.3 billion, while operating expenses were reduced 6.5%, or ¥8.8 billion, to ¥126.0 billion. Operating income was ¥0.06 billion, or 0.8%, higher at ¥7.9 billion. This segment's contribution to total sales declined marginally from 12.5% to 11.5%.

■ Related Construction

Cost Savings Allow Income Growth Despite Slow Sales

There were declines in the number of new installations and safety upgrades. Despite the slowdown, operating income was higher thanks to reductions in fixed costs and other expenses.

At ¥64.9 billion, sales were ¥2.1 billion, or 3.1%, lower than in the previous year. Operating expenses were reduced 4.2%, or ¥2.8 billion, to ¥63.6 billion, with the result that operating income rose 6.7%, or ¥0.3 billion, to ¥4.5 billion. This segment's contribution to total sales was slightly lower at 5.6%, compared with 5.9% in the previous year.

■ Real Estate Rental Business

Cost Cutting Offsets Reduced Rent Revenue

Segment sales declined, in part because of rent reductions to reflect the state of the real estate market, falling 5.3%, or ¥0.8 billion, to ¥14.1 billion. Despite this, operating income improved because of lower depreciation and the reduction of selling, general and administrative expenses.

Operating expenses were reduced 4.0%, or ¥0.2 billion, to ¥27.6 billion, and operating income rose 3.4%, or ¥0.3 billion, to ¥7.9 billion. This segment's contribution to total sales declined from 1.3% in the previous year to 1.2%.

■ Other

Steady Expansion of Energy Service Business

Business areas in this segment include district heating and cooling systems, energy services and LPG sales. Despite positive factors, including sustained growth in energy service operations, segment sales declined 0.7%, or ¥0.8 billion, to ¥113.9 billion. Reasons for the lower result include a drop in orders for large-scale general engineering projects, and withdrawal from the coke business. This segment accounted for 9.9% of net sales, down from 10.2% in the previous year.

Segment operating expenses were ¥12.2 billion, or 8.2%, higher than in the previous year at ¥160.9 billion. Segment operating income increased 17.1%, or ¥1.6 billion, to ¥11.3 billion.

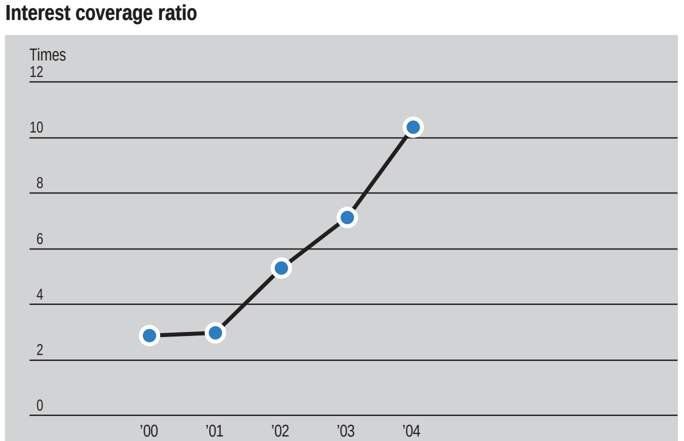
Temporary Decline in Net Income from Lump-sum Write-off of Actuarial Differences in Retirement Benefits

Other income totaled ¥17.5 billion, a year-on-year increase of ¥1.4 billion. This is mainly attributable to a ¥5.7 billion gain from the liquidation of excess allowances for retirement benefits resulting from reform of the corporate pension plan, and the receipt of ¥2.2 billion in proceeds from the sale of fixed assets.

Total other expenses increased ¥53.1 billion to ¥96.7 billion. The increase is attributable to the write off in this fiscal year of the entire amount of actuarial differences in retirement benefits, totaling ¥59.0 billion, taken on the occasion of the reform of the corporate pension plan. Another factor that increased expenses was the decision to bring forward the application of impairment accounting to fixed assets in order to strengthen the financial structure. There were impairment losses of ¥3.3 billion on certain assets, including a once planned site for branch offices.

On the other hand, there were no environmental conditioning costs, which were recorded as an extraordinary expenditure item amounting to ¥5.7 billion in the previous year. Interest expenses were reduced ¥2.6 billion through aggressive repayment of interest-bearing debt.

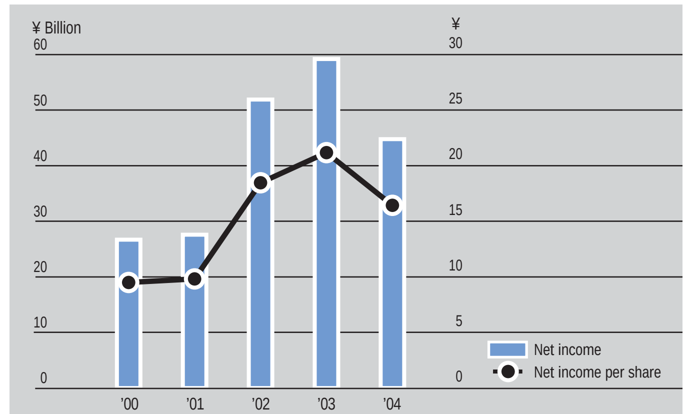
Interest coverage ratio



Interest coverage ratio = (operating income + interest and dividend income) / interest expense

As a consequence, other expenses, net amounted to ¥79.2 billion, compared with ¥27.4 billion in the previous year. Net income declined ¥14.4 billion, or 24.3%, below the previous year's level to ¥44.8 billion.

Net income and net income per share



REFORMS OF THE PENSION PLAN

Following the enforcement of the Defined Benefit Corporate Pension Law, Tokyo Gas undertook major reforms of its pension plan by switching from a tax-qualified pension plan to a contract-type corporate pension plan and by introducing a cash balance plan in fiscal 2003. This resulted in a reduction in the benefit rate, and ¥5.7 billion in profit as a gain from reducing the retirement benefit reserve was recorded in the accounts as a result.

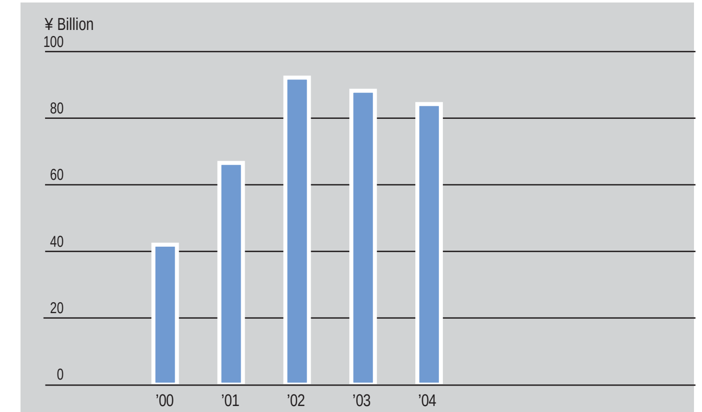
Further to the reform of the pension plan, the Company decided to change the number of years over which the unrecognized actuarial differences are written off from ten years to one year. The full amount of unrecognized actuarial differences from past years was recorded as a loss totaling ¥59.0 billion in this fiscal year. This change allows the status of the retirement benefit obligations to be reflected in the Company's financial statements in a timely manner. It also reduces the future burden and strengthens the Company's financial structure.

Free Cash Flow of ¥84.2 Billion

Tokyo Gas has made free cash flow a key management indicator, which is calculated by adding depreciation* to net income and subtracting capital expenditures**. One of the goals set down in Frontier 2007 is the achievement of free cash flow averaging ¥97 billion per annum and totaling ¥480 billion over a five-year period. The result for this term fell short of this target at ¥84.2 billion, a year-on-year decline of ¥4 billion, or 4.5%. Depreciation increased 4.2% to ¥146.8 billion, while capital expenditures were reduced 4.1% to ¥107.4 billion. Though both of these factors had the effect of increasing free cash flow, net income declined 24.3% to ¥44.8 billion because of measures to improve the Company's financial structure, as described above. The decline in free cash flow resulted from this lower net income figure.

*including amortization of long-term prepayments
**purchases of tangible fixed assets + purchases of intangible fixed assets + long-term prepayments (accounting basis)

Free cash flow



Decision to Increase Annual Dividend

Frontier 2007 established a basic policy of distributing ¥81 billion to shareholders as dividends, nearly 17% of the total free cash flow of about ¥480 billion generated over the five-year period from fiscal 2003 to fiscal 2007. Transient factors caused a year-on-year decline in free cash flow in this term, and if this factor is discounted, free cash flow would be substantially higher than the target. On the completion of the first year of Frontier 2007, business projections now strongly indicate that the targets for the final year of the plan will be exceeded. For this reason, it was decided to allocate part of the free cash flow in excess of the targets to dividends, in order to pass on the rewards to shareholders. The annual dividend per share has been increased from ¥6 to ¥7 per share.

Increased Sales, Lower Operating Income, and Higher Net Income Projected for the New Fiscal Year

Gas sales volumes in the year ending March 31, 2005 are expected to increase 2.6% to 11.5 billion m^3. Sales to the residential sector are expected to increase 0.9%, from aggressive marketing of floor-heating systems and products developed to compete with electrical appliances. Sales to the commercial sector are to grow 6.9%, driven by stepped-up demand for gas air conditioning. Sales to the industrial sector are estimated to decline 0.4% due to the leveling of special demand for use in power generation, which increased dramatically in fiscal 2003. However, wholesale gas sales are projected to rise 8.3%, reflecting an increase in the volume taken by gas companies to which gas was supplied.

Although gas sales will increase in volume terms, unit prices are expected to fall under the "sliding rate" system, which adjusts for fluctuations in gas resource costs. Tokyo Gas is therefore projecting a decline of 0.6% in revenues from its gas sales business. An increase in the scope of consolidation from 18 companies to about 50 in the new fiscal year is expected to lift total net sales to ¥1,197 billion, a year-on-year increase of 3.9%. Expenses will also increase, however, and operating income is projected to decline 4.8% to ¥145 billion. In the absence of the extraordinary losses that affected earnings in fiscal 2003, net income is expected to rise 92.0% to ¥86 billion.

Cash Flows and Financial Position

Operating Cash Flows Increased, but Year-end Net Cash Declined because of Bond Redemptions and the Acquisition of Treasury Stock

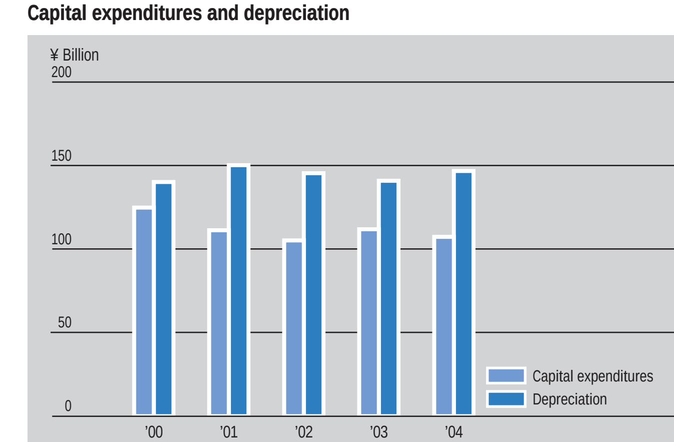
■ Cash Flows from Operating Activities

Income before income taxes and minority interests declined because of the write-off of reserve obligations for retirement benefits and the early application of impairment accounting. However, there was a large inflow of ¥143.1 billion for depreciation of fixed assets, including special depreciation of the newly completed LNG tank facilities at the Ohgishima LNG Terminal, as well as the aforementioned write-off of retirement benefit reserve obligations. Subsequently, net cash provided by operating activities increased ¥4.1 billion year on year to ¥217.6 billion.

■ Cash Flows from Investing Activities

Net cash used in investing activities amounted to ¥126.0 billion, an outflow increase of ¥15.9 billion from the previous year's level of ¥110.1 billion. Capital expenditures, which are the sum of acquisitions of tangible fixed assets and intangible fixed assets, increased ¥6.0 billion to ¥113.2 billion. Major investments included gas pipelines.

Capital expenditures and depreciation



Capital expenditures represent the amount of payments for fixed assets in the relevant fiscal year.

Cash Flows from Financing Activities

Net cash used in financing activities rose ¥21.2 billion, from ¥78.5 billion in the previous year to ¥99.7 billion. Though bond issues raised ¥50.0 billion, there was an overall reduction in cash and cash equivalents because of outflows of ¥78.8 billion for bond redemptions and ¥28.0 billion for the repurchase of common stock.

(¥ Million)

Years ended March	2002	2003	2004
Net cash provided by operating activities	191,676	213,533	217,608
Net cash used in investing activities	(111,821)	(110,144)	(126,038)
Net cash used in financing activities	(117,176)	(78,517)	(99,744)

The changes noted above had the effect of reducing cash and cash equivalents at the year-end by ¥8.2 billion to ¥44.0 billion.

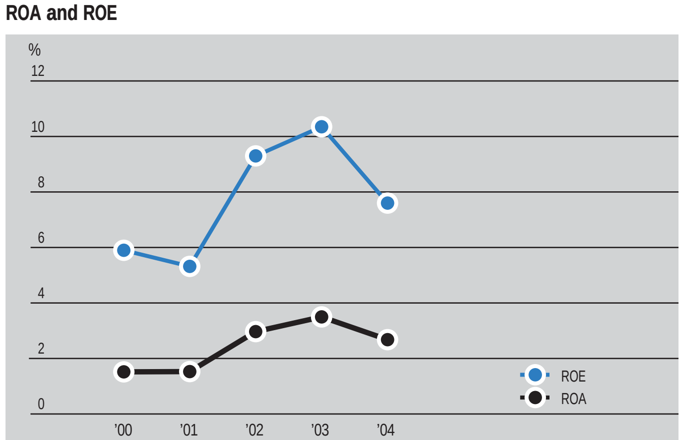
Despite Business Expansion, Fixed Assets to be Reduced through Capital Expenditure Focusing on Asset Efficiency

Total assets at the end of the year under review amounted to ¥1,666.8 billion, a reduction of ¥9.2 billion from the previous year's level. Property, plant and equipment was reduced ¥47.0 billion to a year-end total of ¥1,170.4 billion through ongoing depreciation. Investments and other non-current assets grew ¥45.0 billion to ¥218.4 billion. This resulted from an increase in unrealized gains on investment securities because of rising share prices. Current assets declined ¥5.4 billion to ¥259.1 billion, in part because of a reduction in cash and cash equivalents and receivables.

One of the management policies defined in Frontier 2007 calls for an increase in return on assets (ROA*). This will be achieved through stringent screening of investment in tangible fixed assets. In fiscal 2003, ROA declined from 3.5% in the previous year to 2.7% due to a decrease in net income as a result of transient factors. However, an improvement to 5.1% is projected for fiscal 2004.

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

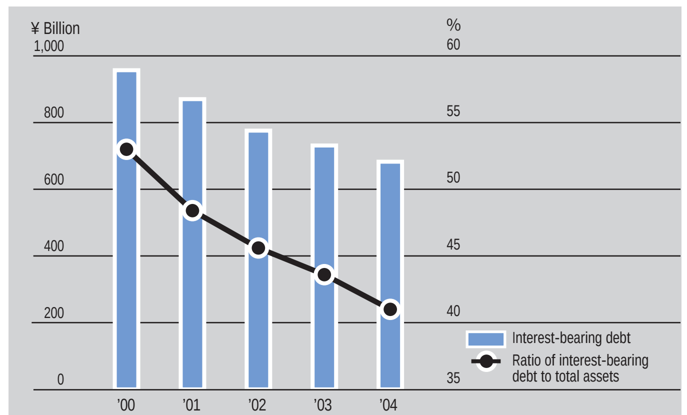
ROA and ROE



Steady Reduction of Interest-bearing Debt

Efforts to strengthen the Company's financial structure brought a significant reduction in interest-bearing debt. The total at the end of the year was ¥682.7 billion, a year-on-year decline of ¥48.6 billion. This resulted mainly from the redemption of straight bonds through debt assumption contracts, retirement by purchase of straight bonds, and the redemption of convertible bonds. The ratio of interest-bearing debt to total assets improved from 43.6% to 41.0%.

Interest-bearing debt and ratio of interest-bearing debt to total assets

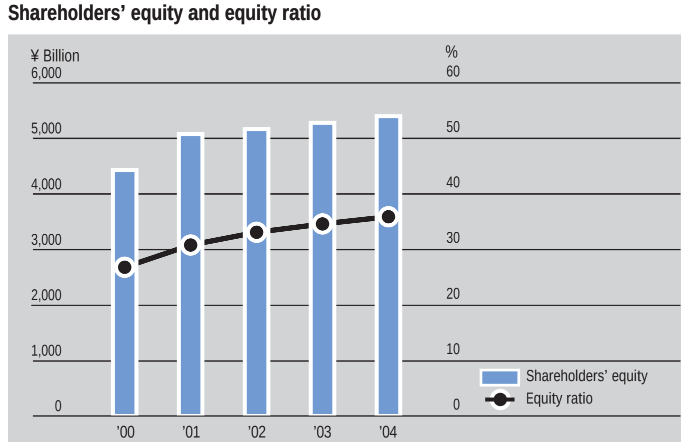


Interest-bearing debt = long-term debt due after one year + long-term debt due within one year + bank loans

Repurchase of Common Stock

Shareholders' equity at the year-end totaled ¥598.5 billion, an increase of ¥18.7 billion over the year. While there was a decrease of ¥27.9 billion, due mainly to repurchase of our own stock, retained earnings was ¥28.3 billion higher, and there was a rise of ¥18.7 billion in net unrealized holding gains on securities. The repurchase of 2.9 million shares of common stock for ¥9.9 billion in the previous year was followed in fiscal 2003 by the acquisition of 76.6 million shares for ¥27.8 billion. To prevent dilution caused by the conversion of convertible bonds into shares, Frontier 2007 calls for the allocation of about 20% of free cash flow (¥100 billion) to the continuing repurchase of stock. Tokyo Gas will continue to implement this policy.

Shareholders' equity and equity ratio



The shareholders' equity ratio improved from 34.6% to 35.9%. However, the return on equity (ROE*) declined from 10.4% to 7.6% because of the lower net income result. An improvement to 13.8% is predicted for fiscal 2004.

* ROE=Net income/shareholders' equity (average of position at start and end of fiscal year)

External Risks Affecting Business Activities

Gas Rate Decline Risk

Progress in deregulation has caused competition to intensify among energy suppliers. There is a risk that the price of gas will need to be reduced to attract and retain customers in the face of price reductions by the Tokyo Electric Power Company, which is the greatest competitor of Tokyo Gas.

Tokyo Gas recognizes this risk and has allocated capital resources totaling ¥180.0 billion over the five-year period of Frontier 2007 to cover price reductions.

Temperature Fluctuation Risk

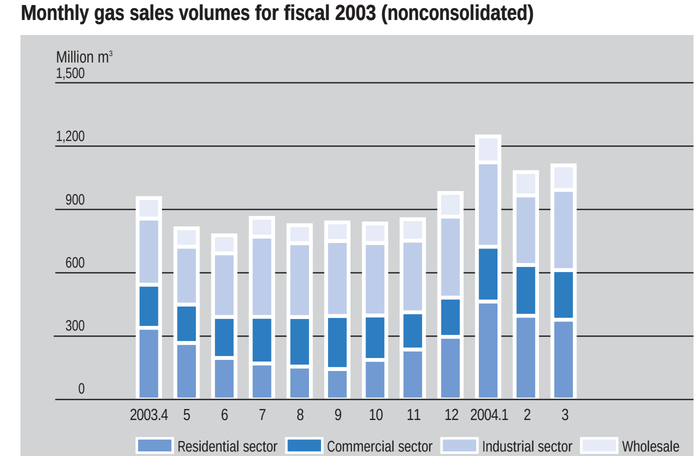
Temperatures affect the volume of city gas sales, which account for around 70% of consolidated sales and 80% of income. Gas is used mainly for water heating and space heating especialy in residential use. Mild winter weather can erode revenues and income by reducing the volume of gas sold.

The average temperatures in fiscal 2003 were 21.7ºC in the first half of the year, 11.0ºC in the second half, and 16.3ºC over the whole year. Forecasts for fiscal 2004 are based on averages of 22.7ºC in the first half, 10.9ºC in the second half, and 16.8ºC over the whole year.

Impact of 1˚C temperature rise on gas sales volume

	Rate of change
Summer (June–September)	0.2%
Winter (December–March)	-2.4%
Intervening months (April, May, October, November)	-1.9%
Annual	-1.5%

Monthly gas sales volumes for fiscal 2003 (nonconsolidated)



Gas Resource Cost Fluctuation Risk

City gas supplied by Tokyo Gas is produced mainly from imported LNG. Since contracts are denominated in U.S. dollars, earnings are at risk from fluctuations in the yen-dollar exchange rate. Also, the dollar-denominated LNG prices are linked to crude oil prices on a sliding scale, which exposes the Company to risk from changes in the international market price for crude oil.

The extent to which these fluctuations affect gas resource costs over a year is as follows.

Approximately ¥2.1 billion for each ¥1 movement in the yen-dollar exchange rate

Approximately ¥4.3 billion for each $1 movement in the per-barrel price of crude oil

Fluctuations in the cost of gas resources are reflected in gas rates after approximately six months under the "sliding rate" system*. Under this system, although earnings may be subject to temporary increases and decreases, crude oil prices and currency exchange rates have no net effect on results over the medium- to long-term perspective.

In fiscal 2003, the crude oil price averaged $29.42 per barrel, and the average exchange rate was ¥113.19 to one dollar. Forecasts for fiscal 2004 are based on an average crude oil price of $30 per barrel and an exchange rate of ¥110 to one dollar.

* Depending on the contract, changes may be reflected without a six-month time lag. Adjustment has an upper limit (please refer to the accompanying Investors' Guide 2004, P. 4).

Interest Rate Fluctuation Risk

Tokyo Gas negotiates fixed interest rates for both short-term and long-term interest-bearing debt, which precludes risk of interest rate fluctuation during the term of an obligation. However, there may be risk of fluctuation when loans are refinanced.

Share Price Fluctuation Risk

Tokyo Gas primarily holds equities to maintain corporate relationships essential to the conduct of its business operations. Equity of publicly listed companies is subject to market risk. Tokyo Gas has established management policies and rules for handling of such equities.