

Management's Discussion and Analysis

Sales and Income

Sales and Cost of Sales

For the year ended March 31, 1998, consolidated net sales increased 5.3 percent from the prior fiscal year to ¥455,585 million (US\$3,449 million), supported by higher sales in the United States and Taiwan. Geographically, domestic sales decreased 10.2 percent to ¥230,550 million, while overseas sales increased 27.9 percent to ¥225,035 million. By group, Semiconductor Production Equipment (SPE) sales, which include sales of LCD production equipment, increased 6.8 percent to ¥380,184 million. Computer Systems (CS) sales were 5.9 percent higher at ¥15,262 million, while Electronic Components (EC) sales decreased 3.8 percent to ¥60,139 million.

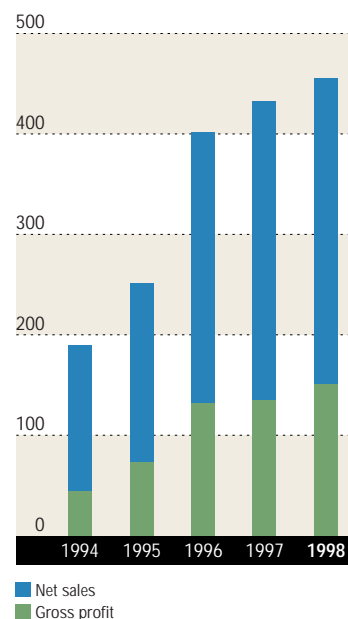
Tokyo Electron only reports orders received and order backlog on a non-consolidated basis. Orders received increased 7.9 percent to ¥376,519 million because of a rebound in capital spending among memory manufacturers in the first half of the fiscal year and solid order growth in the United States and Taiwan. In the second half, however, the economic downturn in Asia and lower DRAM prices caused manufacturers to revise their spending plans downward, which negatively affected orders. Tokyo Electron considers orders to be cancelled upon receipt of written notice of cancellation from customers or upon receiving notice that a delivery schedule has been delayed for more than six months. As a result, order backlog decreased 26.4 percent to ¥131,572 million.

Cost of sales increased 2.4 percent, well below the rate of increase in net sales because relatively higher-margin products made up a greater proportion of sales and larger production volume of original products lowered unit costs. The cost of sales ratio therefore decreased to 66.9 percent from 68.8 percent in the prior fiscal year. Gross profit increased 11.5 percent to ¥150,760 million; the gross profit margin increased to 33.1 percent from 31.2 percent for the prior fiscal year.

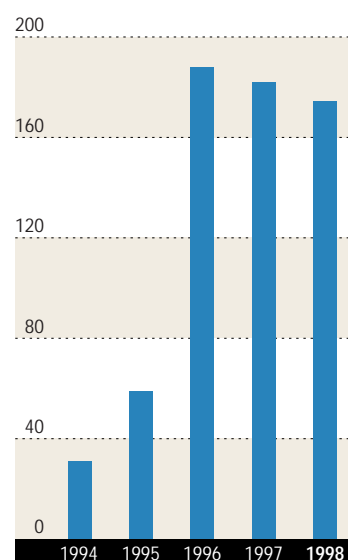
Expenses and Net Income

Selling, general and administrative (SG&A) expenses rose 16.9 percent due to additions to personnel and increased depreciation expenses that resulted from capacity expansions in recent years. In addition, research and development expenses, which are included in SG&A expenses, rose 27.7 percent to ¥26,813 million as Tokyo Electron continued working aggressively to commercialize next-generation equipment. In particular, the Company invested heavily in developing 0.18 micron processes and 300mm equipment. Management believes that continuous and considerable R&D investment, even during market slowdowns, is indispensable for the Company to remain competitive in the semiconductor equipment industry, which is characterized by rapid technological change. Despite higher expenses, operating income

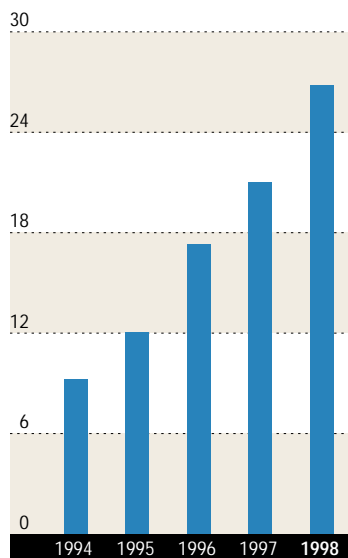
Net Sales & Gross Profit
(¥ Billions)



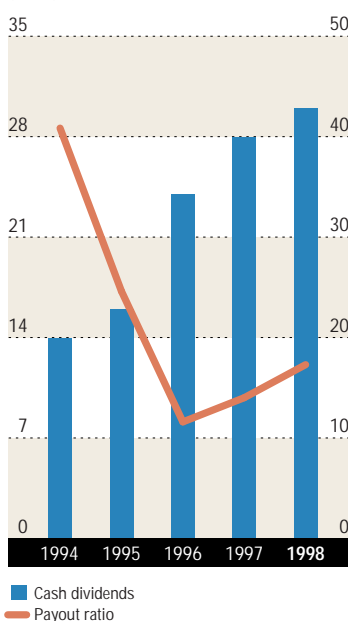
Net Income per Share
(¥)



R&D Expenses (¥ Billions)



Cash Dividends per Share & Payout Ratio (¥ / %)



increased 4.8 percent to ¥63,296 million because of the increase in gross profit. The operating income margin was 13.9 percent, compared to 14.0 percent for the prior fiscal year.

Other expenses totaled ¥462 million, compared to other income of ¥98 million in the prior fiscal year. This change resulted because one-time losses from write-down of securities and the sale or disposal of fixed assets and inventories offset higher dividend income from subsidiaries and lower interest expenses. Income before income taxes increased 3.9 percent to ¥62,834 million. Provision for income taxes increased 7.6 percent. Net income was marginally higher at ¥30,009 million. The net income margin was 6.6 percent, compared to 6.9 percent for the prior fiscal year. Fully diluted net income per share was ¥168.43, compared to ¥172.74 when adjusted for a 1.1-for-1 stock split in the prior fiscal year. Tokyo Electron increased cash dividends per share ¥2.00 to ¥30.00; the payout ratio was 17.3 percent, up from 14.0 percent in the prior fiscal year.

Our dividend policy is to link dividends with the Company's profitability by consistently maintaining the payout ratio at approximately 20 percent of non-consolidated earnings.

The Company retains earnings for reinvestment in research and development, production assets and overseas expansion in order to build our business base. Doing so raises Tokyo Electron's ability to generate growth in shareholder returns through increased earnings.

	Millions of yen (percentage of net sales)		Thousands of U.S. dollars
	1998	1997	1998
Net sales.....	¥455,585 (100.0)	¥432,785 (100.0)	\$3,448,789
Cost of sales.....	304,825 (66.9)	297,546 (68.8)	2,307,532
Gross profit	150,760 (33.1)	135,239 (31.2)	1,141,257
SG&A expenses.....	87,464 (19.2)	74,850 (17.3)	662,105
Operating income	63,296 (13.9)	60,389 (14.0)	479,152
Other income (expenses).....	(462) -	98 (0.0)	(3,497)
Income before income taxes.....	62,834 (13.8)	60,487 (14.0)	475,655
Provision for income taxes.....	32,825 (7.2)	30,512 (7.1)	248,486
Net income.....	¥ 30,009 (6.6)	¥ 29,975 (6.9)	\$ 227,169

Effect of Exchange Rates

In general, exports from Japan are denominated in yen. Changes in exchange rates therefore have no material effect on Tokyo Electron's results. However, the depreciation of the yen relative to the U.S. dollar in the past fiscal year had a positive effect on competitiveness. The ratio of U.S. dollar-denominated transactions involving equipment imported to Japan is comparatively low and did not have a material effect on results in the past fiscal year.

Financial Position and Cash Flows

Financial Position

Current assets at March 31, 1998 increased 27.7 percent from a year earlier to ¥373,083 million. A primary factor in the increase was higher cash and time deposits at the balance sheet date due to issues of commercial paper and bonds to fund capital expenditures and working capital needs. Moreover, inventories rose as demand slowed in the second half and at the balance sheet date Tokyo Electron was carrying a comparatively large volume of equipment slated for delivery. However, this situation is not expected to result in a significant amount of dead stock. Current liabilities increased 43.2 percent to ¥144,715 million, mainly because of an increase in short-term borrowings. The current portion of long-term debt, however, dropped to zero as an issue of bonds with warrants was successfully redeemed with stock during the fiscal year. Working capital increased to ¥228,369 million, and the current ratio was to 2.6 to 1, compared to 2.9 to 1 for the prior fiscal year. Total assets increased 27.5 percent to ¥493,600 million, due to factors including the increase in current assets and a rise in fixed assets resulting from the completion of projects such as a new Process Technology Center and new factories at manufacturing subsidiaries in Japan and the United States. Investments in and advances to subsidiaries and affiliates during the past fiscal year included increases in the capital of Tokyo Electron Miyagi Ltd. and Tokyo Electron Taiwan Ltd., and the capitalization of new subsidiary Tokyo Electron Arizona, Inc.

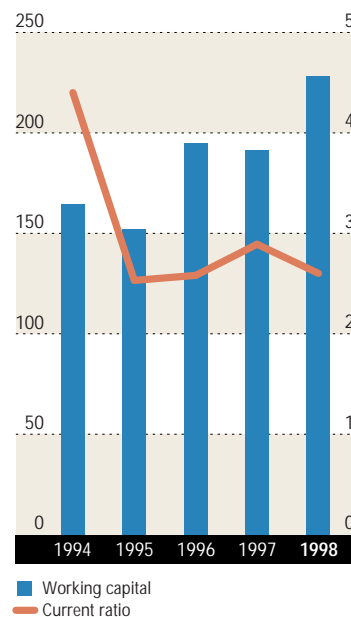
Long-term debt increased 10.0 percent year-on-year to ¥77,657 million as Tokyo Electron issued straight bonds to fund global expansion. Shareholders' equity increased 25.8 percent to ¥261,009 million because of higher retained earnings and the increase in common stock resulting from the conversion of convertible bonds and exercise of warrants. Shareholders' equity as a percentage of total assets was 52.9 percent, compared to 53.6 percent at the prior fiscal year-end. Despite higher net income, return on average shareholders' equity declined to 12.8 percent, compared to 15.4 percent in the prior fiscal year, due to the increase in shareholders' equity.

The balance of convertible bonds outstanding at March 31, 1998 was ¥19,038 million. The potential number of shares issuable if all convertible bonds had been converted at the balance sheet date represented 3.46 percent of total common stock issued and outstanding.

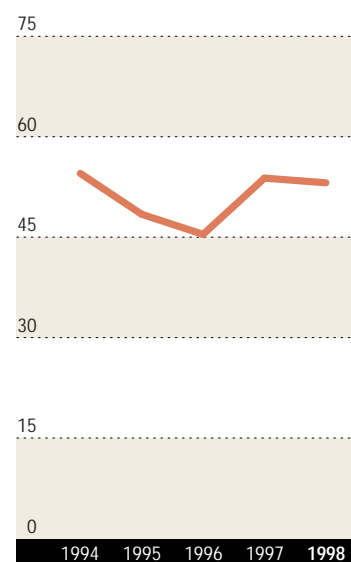
Cash Flows

Operating activities generated net cash of ¥18,346 million, compared to ¥24,642 million in the prior fiscal year. This decrease was primarily the result of the increase in inventories. Net cash flow, the sum of net income and depreciation, increased 6.3 percent to ¥42,661 million.

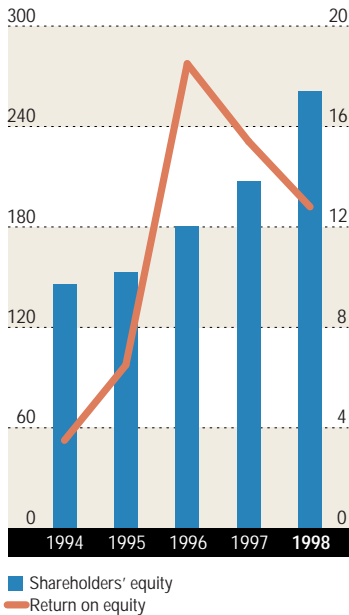
Working Capital & Current Ratio
(¥ Billions / Times)



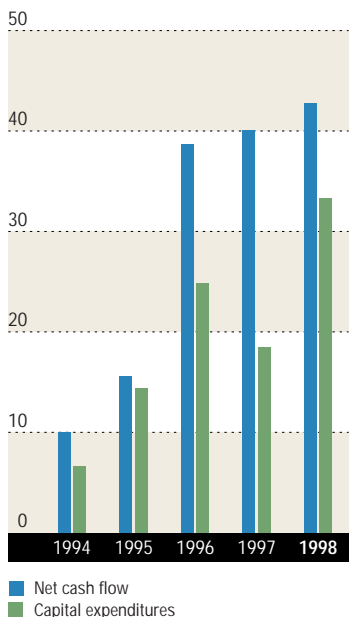
Shareholders' Equity Ratio
(%)



Shareholders' Equity and ROE
(¥ Billions / %)



Net Cash Flow & Capital Expenditures
(¥ Billions)



Investing activities used net cash of ¥45,326 million, compared to ¥23,977 million in the prior fiscal year. Capital expenditures increased 80.4 percent to ¥33,302 million, and were 78.1 percent of net cash flow, compared to 46.0 percent of net cash flow for the prior fiscal year. Representative projects included the completion of a new Process Technology Center in Yamanashi and facility expansions at Tokyo Electron Kyushu Ltd. With the completion of these projects in the past fiscal year, management expects capital expenditures to decrease in the year to March 1999.

Financing activities provided net cash of ¥66,878 million, while they used net cash of ¥18,992 million in the prior fiscal year. In the past fiscal year, Tokyo Electron issued commercial paper and straight bonds, resulting in increases in both short-term borrowings and long-term debt. Cash dividends paid increased 11.9 percent to ¥4,689 million. Cash and cash equivalents at the end of the year more than doubled to ¥71,892 million.

Management believes that Tokyo Electron's stable cash flow, manageable debt and strong working capital give the Company the liquidity and financial base necessary to invest in profitable growth and steadily expand global operations.

Acquisition

To strengthen its position in the metallization business, Tokyo Electron purchased the semiconductor production equipment operations of U.S. company Materials Research Corporation in February 1998. The assets acquired were transferred to the balance sheets of Tokyo Electron Arizona, Inc. and other subsidiaries. The Company did not record an increase in goodwill in connection with this acquisition. Tokyo Electron Arizona was an unconsolidated subsidiary for the past fiscal year.

Forward-Looking Statements

This publication contains forward-looking statements based on projections and estimates that involve many variables. Tokyo Electron operates in an extremely competitive business environment. Moreover, the semiconductor industry that Tokyo Electron participates in is characterized by rapid changes in technology and supply-demand balance. Consequently, certain risks and uncertainties could cause the Company's results to differ materially from any projections and estimates presented in this publication.