Annual Report 2005
For the year ended March 31, 2005

A Revolution in Motion

SUBARU

Harmony in Motion

SUBARU

Fuji Heavy Industries Ltd. (FHI) is a global manufacturer of transportation- and aerospace-related products and the maker of Subaru automobiles. FHI's roots go back to 1917, when Japan's first Aircraft Research Laboratory (later Nakajima Aircraft Co., Ltd.) was established, 14 years after the Wright Brothers' first successful flight of the Kitty Hawk flyer in 1903. While some of the world's automakers have their roots in the aircraft industry, FHI is the only automaker who continues to build aircraft today.

On July 15, 2003, the 50th anniversary of the Company's founding in 1953, FHI introduced the six-star ("mutsuraboshi") Subaru automobile emblem design as its new corporate symbol. The Company has been using this symbol to further fortify its brand image and awareness on a global basis.

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Disclaimer Regarding Forward-Looking Statements

Statements herein concerning plans and strategies, expectations or projections about the future, FHI's efforts with regard to various management issues, and other statements, except for historical facts, are forward-looking statements. These forward-looking statements are subject to uncertainties that could cause actual results to differ materially from those anticipated. These uncertainties include, but are not limited to, general economic conditions, demand for and prices of FHI's products, FHI's ability to continue to develop and market advanced products, raw material prices, and currency exchange rates. FHI disclaims any obligation to update any forward-looking statements, whether as a result of new information, future events, or otherwise.

Spirit in Motion

Performance Overview

(Billions of yen)

	Actual Results			Forecast for	
	FY2003	FY2004	FY2005	FY2006	FY2007
Automotive Sales Volume (thousand units, non-consolidated)	555	553	601	597	654
Net Sales	1,372.3	1,439.5	1,446.5	1,470.0	1,580.0
Operating Income	67.5	50.3	42.0	31.0	50.0
Ordinary Income	58.5	56.6	43.6	27.0	48.0
Net Income	33.4	38.6	18.2	15.0	27.0
Capital Investment	64.6	74.6	85.3	67.0	61.0
Depreciation	48.8	53.2	51.1	58.0	65.0
R&D Expenses	60.1	57.5	53.0	55.5	60.0
Interest-Bearing Debt	389.1	378.9	412.2	410.0	400.0
Exchange Rate (¥/$, non-consolidated)	124	116	108	105	105

2004

April	Subaru sales network in China is established
July	New SUV development alliance with Saab is agreed
September	Peter Solberg wins the first WRC Rally Japan
September	Cumulative passenger car sales in Japan surpass three million units
November	Subaru R2 is awarded 2005 RJC* Car of the Year " Special Award for Best Mini Passenger Car "
December	New Subaru R1 is launched

*RJC: The Automotive Researchers '& Journalists ' Conference of Japan

2005

January	"Subaru Academy" opens
January	Forester undergoes a major face-lift
March	Cumulative sales of Subaru vehicles in Japan surpass 10 million units
April	New directors'/executive officers' assignments are announced
May	Revised FDR-1 is announced
May	New Subaru B9 Tribeca is released in North American market
June	Finely tuned new Impreza is released

Moving Resolutely Ahead

Fundamental Reforms

Kyoji Takenaka
President and CEO

Fiscal 2005, ended March 31, 2005, was the third year of the Fuji Dynamic Revolution–1 (FDR-1) medium-term business plan, which covers the five fiscal years through fiscal 2007. Having revised the plan's targets in light of actual performance during the first three years, we are now placing top priority on stopping the downtrend in profit and making a turnaround through reforms that bolster the Company's profit base.

In fiscal 2005, consolidated net sales edged up 0.5% from the level in the previous year, to ¥1,446.5 billion. However, operating income decreased 16.5%, or ¥8.3 billion, to ¥42.0 billion, and net income amounted to ¥18.2 billion, down 52.8%.

Factors with a positive influence on profitability included a ¥16.4 billion reduction in the cost of materials along with decreases in R&D expenses and selling, general and administrative (SG&A) expenses, which had the combined effect of boosting operating profit ¥24.0 billion. However, this amount was more than offset by ¥32.3 billion in negative factors, including a loss on currency exchange, which decreased operating income by ¥15.1 billion, and a deterioration in sales volume and model mix, which reduced operating income by ¥17.2 billion. This resulted in an ¥8.3 billion drop in operating income.

Although both sales volume and sales revenue in Subaru automobile operations increased, domestic sales of relatively profitable Legacy and Subaru R2 models were sluggish. Overseas, such factors as an increase in marketing costs due to competition in the United States, additional costs to respond to safety and environmental regulations, and the rising prices of steel and other raw materials negatively impacted profitability. Rising sales in other markets and cost reduction efforts were not sufficient to cover such negative effects.

Because these circumstances have caused FHI's performance to diverge considerably from the FDR-1 targets, the Company has decided to increase its emphasis on business rebuilding measures during the remaining two years of the business plan. Accordingly, while FHI will retain its vision of being an attractive company with a strong market presence, it will be reexamining the nature of its strengths and weaknesses and is determined to implement fundamental reforms.

Looking at long-term performance indicators, we have revised our operating income ratio target from 10% to 8%, a level that we believe is compatible with sustained corporate growth. In view of our strong emphasis on high asset turnover, we are firmly maintaining our ROA target of 10%. At this point, I will explain the nature of the revised FDR-1 plan that will be guiding our efforts during the upcoming two years to attain these targets.

Reasons for the FDR-1 Target Attainment Shortfall and Principal Features of the Revised Plan

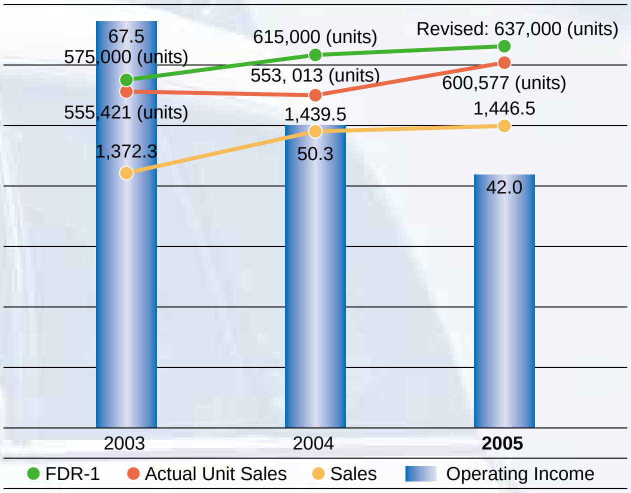
In brief, the revised FDR-1 plan is designed to accurately assess FHI's current situation and effectively adjust it so that the Company can reverse its recent profitability downtrend.

Unfortunately, the new targets for consolidated operating income—¥31.0 billion in fiscal 2006 and ¥50.0 billion in fiscal 2007—are considerably lower than the previous targets of ¥68.0 billion in fiscal 2006 and ¥91.0 billion in fiscal 2007. The main reasons for the revision are a sales volume level that was considerably lower than the original planned level and a rise in the cost of materials that was considerably greater than anticipated.

In contrast to FHI's situation, Japan's major automakers have recorded strong performance and record profits, but this reflects those companies' large-scale sales in markets other than Japan and the United States, high shares of overseas manufacturing operations, and other structural factors that make the effect of currency exchange rate fluctuations on their performance relatively small. FHI's business structure is the opposite—its profitability is highly dependent on the Japanese market and, particularly, the U.S. market. This kind of structural difference is presenting us with extremely severe challenges regarding our performance.

Overview of the First Three Years of FDR-1

(Billions of yen)



The original form of FDR-1 anticipated that the risk of such structural challenges would be offset by sales volume growth in Japan and the United States, but the intensification of market competition in both those countries restrained our fiscal 2005 automobile sales volume to 595,000 units, or more than 9% less than our consolidated target of 639,000 units. This reflects a domestic sales volume for the Subaru R2 that was much lower than planned and a rise in the U.S. sales volume following the launch of the Baja and the new Legacy that was smaller than expected.

Also, as previously mentioned, raw material prices were much higher than expected. Our profitability was heavily impacted by severe market conditions that did not allow us to raise selling prices to reflect such increases in raw material prices.

In view of all this, we must do our utmost to quickly restore balance among our sales volume, costs, and selling prices.

Management Vision

- **Small in size, but strong in market presence**
- **Establish a sustainable business model of high profitability with automobiles as the core business**

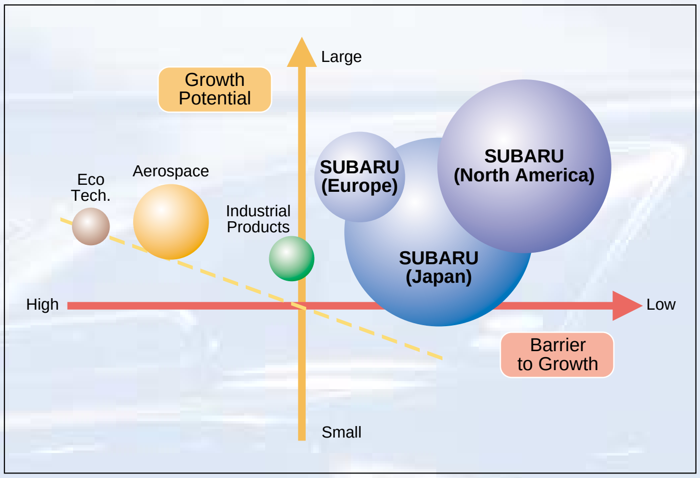
Operating income ratio of more than 8% and ROA of more than 10% by 2010

To survive and develop in line with our vision of being an attractive company with a strong market presence, I believe it is crucial that we maintain our traditional emphasis on marketing distinctive products that clearly differentiate us from the major automakers. We must move still further ahead with the unique core technologies that are characteristic of Subaru automobiles and provide products that accurately meet the needs of customers who have a taste and high expectations for Subaru. Subaru strengths include such technologies as horizontally opposed engines and symmetrical AWD systems to provide superb driving performance, which are combined with excellent powertrains, suspensions, chassis, and bodywork while drawing on sophisticated ergonomics expertise. These are Subaru's core strengths, which we must effectively leverage and extend while also working to offer superior environment-friendliness and safety so that we can provide customers with pleasure and a sense of security.

FHI will continue working to further increase the concentration of its resources in business segments and markets that enable the Company to proactively leverage its special technologies to generate competitive advantages.

With regard to sales opportunities, we are seeking to build a business portfolio concentrated in areas that offer considerable room for business growth where we can develop a strong sales network. In this perspective, the U.S. market appears to be the market in which we have the most potential for full-fledged growth, while Japan and Europe are more suitable for tightly focused operations on special markets and segments in which we can make the most out of our unique technologies.

Business Portfolio Overview



Based on these ideas, the revised form of FDR-1 emphasizes the following five strategic goals:

1. Implementing urgent total cost reductions

2. Restructuring product planning

3. Restructuring sales processes and networks

4. Increasing asset turnover

5. Streamlining the corporate structure

1. Implementing Urgent Total Cost Reductions

Expediting a total cost structure revolution will involve internal structural reforms and other measures designed to reduce FHI's overall costs.

The Company has been working to lower its costs. Nonetheless, when allocating resources, we have tended to give priority to new vehicle development. At this point, however, we will allocate resources with a strong emphasis on lowering the cost of materials based on due efforts to achieve an appropriate balance between levels of sales volume, manufacturing costs, and selling prices. We are taking thorough measures to reduce the cost of newly developed vehicles as well as models currently being mass-produced.

Regarding new models, we have set the clear-cut goal of achieving ¥100,000 in unit cost reductions, and we are also seeking a 30% cut in the cost of new model development, including the costs of engineering, molds, and dies. As for models already in mass production, we intend to intensify our current cost-reduction strategies. In particular, cost-cutting programs initiated in Japan are to be simultaneously implemented at our U.S.-based manufacturing subsidiary, Subaru of Indiana Automotive, Inc. (SIA), and these programs are to be very ambitious. We expect that cost-cutting programs will make considerable use of our alliance with General Motors Corporation (GM).

2. Restructuring Product Planning

With respect to product planning operations, FHI is strengthening its capabilities for marketing operations that place even more emphasis than previously on customer satisfaction.

The most important project in the Company's current product portfolio is the B9 Tribeca, which was launched in the U.S. market in May 2005 as the most premium model in the entire Subaru lineup. We are very pleased to note that the B9 Tribeca's marketing has got off to a smooth start. Situated in the hottest segment of the U.S. automobile market, it has attracted considerable attention as a new type of midsized SUV. By methodically implementing our marketing plan for the B9 Tribeca, we intend to develop it into a new pillar of profitability in our U.S. operations. Regarding existing models, we implemented major model changes for the Forester and the Impreza during 2005. As the remodeled versions of these products offer considerably improved fuel consumption performance, the current surge in fuel prices should further increase the appeal of our strengthened lineup in the United States.

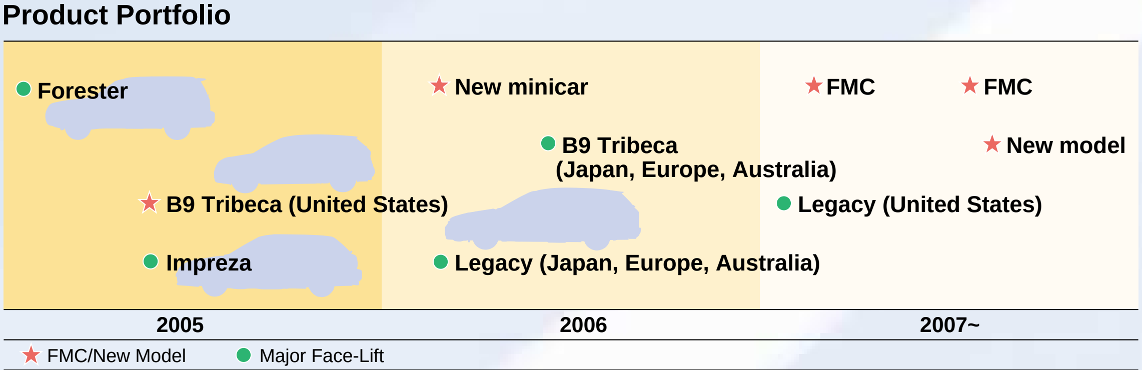
Beginning from a target date sometime in fiscal 2007, we plan to export B9 Tribecas manufactured by SIA to markets throughout the world, including the Japanese market. In this way, we will be able to respond to vigorous growth in the midsized SUV segment in the European and Australian markets and cater to a portion of the Japanese market for multi-passenger vehicles. At the same time, we will be able to boost the capacity utilization rate of SIA and hedge the foreign exchange risks we face.

In Japan, we plan to accelerate our launch of a third new passenger minicar model to next year, and we are expecting that this model will help motivate our dealers and sub-dealers to increase sales volumes and profitability more effectively than the Subaru R2, which was intended to play that role. Through this strategy and the addition of highly competitive special-version vehicles, we will do our best to improve domestic profitability.

Moreover, our joint development with GM of an SUV for Saab Automobile AB is scheduled to bear fruit in the upcoming fiscal year.

Regarding future product development themes, FHI will move forward with the development of the Legacy platform, further strengthen its special core technologies, and create new products that eloquently manifest the distinctive Subaru style. At the same time, the Company will work to increase the efficiency and speed of product development programs and steadily proceed with medium- to long-term projects to develop a wide range of environment-friendly technologies, including joint development projects involving such leading-edge GM technologies as those for hybrid cars and new-generation diesel engines.

Product Portfolio



3. Restructuring Sales Processes and Networks

In the United States, FHI has leveraged the launch of appealing new products to expand its relatively low market share in the sunbelt market and augment marketing capabilities nationwide. Our previous sales network strategy was not to increase the number of dealers, but rather to improve the quality of dealers by increasing the number of exclusive dealers and dealers with separate showrooms. Yet, with our expanded product lineup, we are now determined to increase the number of dealers. We currently have 581 dealers in the United States and plan to proactively work to increase that number to 630 by about 2010 through the establishment of new dealerships in promising locations. Moreover, we are expanding our network while retaining “Site Control” by having our U.S. marketing subsidiary, Subaru of America, Inc. (SOA), invest a portion of the funds initially needed to create a dealership and team up with dealer candidates who have excellent dealership operating experience. To implement this strategy methodically and with attention to detail, SOA is adjusting its regional administration systems and augmenting the specialized capabilities of its Dealer Development Department. We expect that improvement of the sales network will help us boost our annual U.S. sales volume to 250,000 units by 2009 or 2010.

We are also striving to enhance the profitability of our sales network in Japan. Our measures to augment domestic sales power have been somewhat delayed—as reflected in the time required to establish the “Partner 21” dealer sales support network system, which was begun at the start of FDR-1 and completed in spring 2005—and it is extremely important to accelerate these measures. One means of augmenting domestic marketing power we are considering is the integration of marketing-related operations in regional blocks, including the consolidation of administrative functions for dealers in each block and perhaps the establishment of regional holding companies.

About 40% of our sales come from our contract basis sub-dealers, including Subaru Shops. The launch of new minicar models is expected to increase the marketing power of more than 10,000 of these sub-dealers and to expand the sales volume of both minicars and passenger cars.

Regarding Europe, where our automobile business performance has greatly improved, we are strengthening the capabilities of our wholly owned subsidiary Subaru Europe N.V./S.A., while also reevaluating our distribution system, expanding our dealer network, and taking steps to pioneer new markets in Eastern Europe and the CIS region. We expect these measures to further expand the scale of our operations in Europe. FHI is also doing well in the Australian market, where the well established premium positioning of Subaru has contributed to its solid profitability.

4. & 5. Increasing Asset Turnover and Streamlining the Corporate Structure

In light of FHI's limited resources, it is increasingly evident that the Company must select strategic fields and concentrate its resources in those fields. In line with our goal of reducing consolidated total assets 10% and interest-bearing debt 20% by the end of fiscal 2008, we are considering a number of measures. In particular, we are strictly managing our asset levels in function-specific subsidiaries and the three main nonautomobile internal companies and determining our future strategies for those units based on repeated examination of their potential for future business growth. We are also taking measures to increase the efficiency and effectiveness of personnel deployment in the FHI Group, particularly in the parent company.

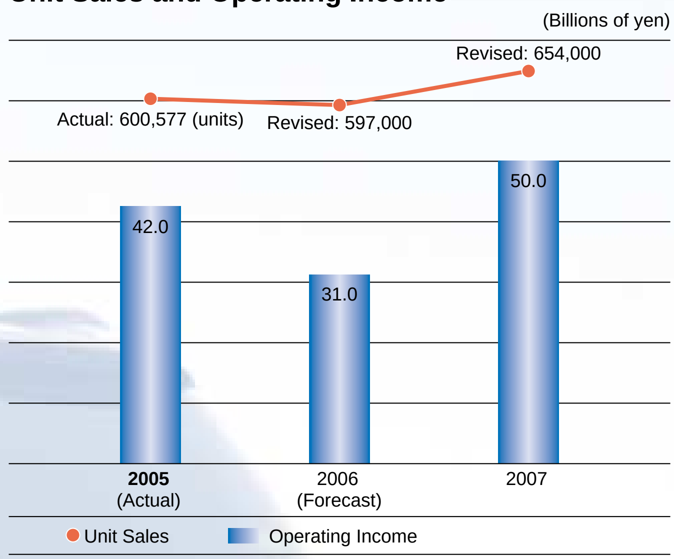
Looking a bit more closely at the three nonautomobile companies, the Aerospace company had suffered from the protracted slump in aircraft-related business following the September 11, 2001, terrorist attacks in the United States, but its operations are finally showing signs of improvement. The Aerospace company has been investing in several large-scale projects for the Japan Defense Agency and private-sector customers. These projects have advanced smoothly and will be making contributions to our net sales from the current fiscal year.

The Industrial Products company had also faced severe conditions for an extended period but has regained its profitability and begun making steadily growing contributions to consolidated profitability. This reflects the division's moves to tighten its focus on high-value-added engine models and proactively develop the OEM market.

Outlook

In conclusion, I will explain our profitability forecast for the next two fiscal years. In fiscal 2006, the launch of the B9 Tribeca in North America is projected to boost revenue. However, the positive effects on operating income of the B9 Tribeca launch and material cost reductions are expected to be offset by various factors, including a forecast loss on currency exchange as well as increases in domestic and overseas fixed costs, market conditions that preclude price rises, the expense of environmental protection and safety measures, higher raw material prices, and deterioration in the sales volume and mix. As a result, operating income is expected to decrease ¥11.0 billion from the previous fiscal year, to ¥31.0 billion.

Unit Sales and Operating Income



In fiscal 2007, we anticipate that our sales volume will rise, as our new passenger minicar model is expected to contribute to domestic sales and the B9 Tribeca to U.S. sales for a full year. This and efforts to lower the manufacturing costs are expected to halt the profitability downtrend, boosting operating income to ¥50.0 billion, a level exceeding the fiscal 2005 level.

We will subsequently implement various reforms aimed at ensuring that FHI is securely on track for sustained corporate growth.

At the time that the Company revised the FDR-1 plan, it undertook an additional analysis of FHI's strengths and weaknesses. Having done this, we concluded that we must maintain our Subaru-unique strategies—which emphasize superior functionality with respect to driving performance, safety, and environment friendliness—and move still further ahead with those strategies. I ask for the continued understanding and support of shareholders and investors as we strive during the next two years to effectively implement the strategies I have described and ensure that those strategies generate results.

K. Takenaka.

Kyoji Takenaka
President and CEO

Internal Reforms Aimed at Profitability Resurgence by Fiscal 2007

Expediting a Total Cost Structure Revolution (TSR) is a central goal of the revised FDR-1 medium-term business plan. FHI is taking thorough measures to reduce its manufacturing costs, aiming to halt the trend of profitability decline and support a resurgence of profitability during the current fiscal year. To enforce the current companywide reform program, Hiroshi Komatsu, who turned around the Industrial Products internal company by restructuring its business in his position as the company president, has been designated Executive Vice President with responsibility for cost planning and management, manufacturing, procurement, and quality assurance.

Thorough Cost Reductions to Enable a Profitability Upsurge during Fiscal 2006

FHI's strong commitment to providing excellent products has enabled the Company to carry through amid tough competition to the present day. It has been accepted that companies may produce excellent products if willing to spend sufficient money. Nowadays, however, it is increasingly accepted that companies must seek to produce excellent products as a matter of course, and they must also devise systems for producing excellent products economically or be forced out of business. The global economy currently does not allow companies to spend whatever sum of money is necessary to create excellent products, and FHI has missed out on adjusting to the new conditions.

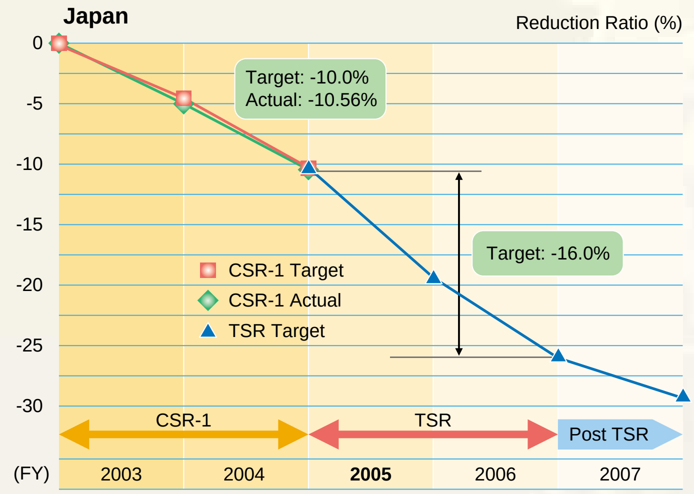
The most important element of successful reforms is always a clear understanding of the current situation. When there is a problem causing a negative trend in corporate performance, it is crucial to identify the cause. If the cause is understood and proper countermeasures are taken, it may be possible to quickly reverse the negative trend. The attainment of FHI's profit targets for the next two years will depend greatly on the progress made in internal reforms, but the reforms will not be fruitful if the Company does not ensure that reform consciousness becomes an integral part of its employees' day-to-day operations.

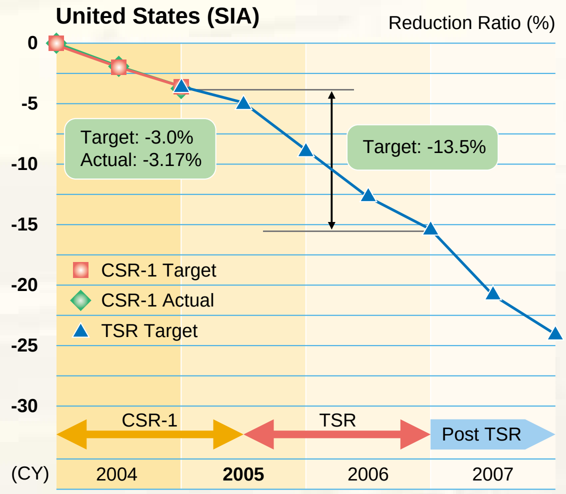
It is obvious that we must design future products based on strong cost-consciousness or we cannot survive. To gain momentum, FHI believes it crucial to implement cost-cutting measures to contribute to Company profits during the next two years.

Greatly Reducing Automobile Manufacturing Materials Costs in Japan and Overseas

With regard to cost-cutting, we will start a new measure, called the “Total Cost Structural Revolution” (TSR) strategy, which sets automobile manufacturing direct materials cost cuts of 16% in Japan and 13.5% in the United States (over a 20-month

TSR





period) during the next two years. This program calls for further accelerating the rate of cost cuts. In the past two years, the Company had set a target of reducing direct materials costs 10.0% in Japan and was able to reduce those costs 10.56%. In the United States, although our cost reduction target of 3.0% was not substantial, we were able to reduce those costs 3.17% in the past two years. The current target of 13.5% in cost cuts over two years is considerably more ambitious. Attaining these targets will entail proactive efforts to augment procurement from new suppliers in Asia and other regions.

FHI's commitment to excellence in Subaru automobile manufacturing led to certain unnecessary costs, and eliminating such excess costs is a top priority. Moreover, while the Company previously adopted an approach of eliminating various types of costs over specified periods of time, its new approach is to implement prospective cost cuts immediately whenever possible.

Current goals regarding newly developed automobile models are to reduce unit costs ¥100,000 per vehicle and lower tooling and dies costs and development costs 30%.

Hiroshi Komatsu
Director of the Board, Executive Vice President

The automobile industry has established benchmarks regarding new model development, and FHI should not be sharply deviating from those benchmarks. However, the Company has faced problems due to allowances made for exceptional deviations with respect to its flagship Legacy models. We are returning to our natural posture of setting investment targets for each automobile model and insisting that investment be kept within the target range. Of course, as the Legacy models take the role of the Company's flagship product, they are equipped with brand-new technologies intended for incorporation in other automobile models at later dates. A separate budget is provided for such new technology to ensure that cost-cutting programs do not undermine efforts to develop new technologies and nip promising new initiatives in the bud.

Speed of Reforms Dependent on Reform-Consciousness of Each Individual Employee

After becoming responsible for automobile manufacturing, my first feelings were that our operations were not speedy enough and that many employees were still a bit complacent and lacked sufficient crisis consciousness. People unable to solve problems now are also likely to be unable to solve the problems next year or the year after that. Increasing individual employees' consciousness of problems is a crucial prerequisite to speedy reforms. To maintain our current employment levels, we must take the marketing measures needed to support our sales and manufacturing volumes. In brief, we absolutely must take more decisive problem-solving steps than many FHI employees have been able to take so far.

If we have the resolve to take the natural and proper steps, then we will overcome the problems. We simply have to make decisions decisively and have the courage to act on those decisions.

We are working to ensure that all managers are highly conscious of the need for decisive reforms and that they transmit that consciousness to their subordinates. To effectively strengthen the FHI Group, we have to create a culture and an organization that encourages employees to take the initiative. We will attain our strategic reform objectives by ensuring that each employee has the resolve to take the natural and proper steps.

Restructuring Sales Processes and Networks

In the revised FDR-1 plan, we regard the North American market as a focal market with possibilities for further growth. In addition to the North American market, we will strengthen our sales networks in Japan, Europe, and other areas.

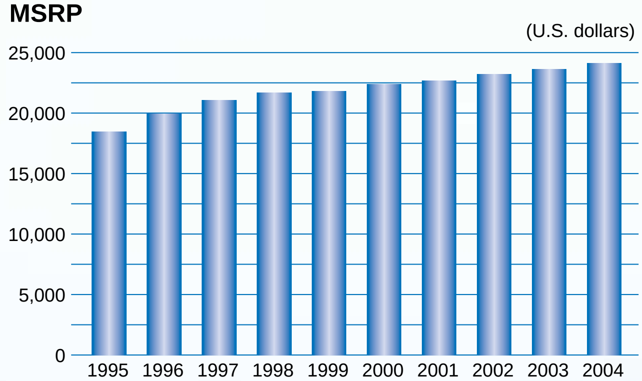
North America

Measures during the First Three Years of FDR-1

In the U.S. market, FHI was able to smoothly increase the sales volume of vehicles while annually increasing the weighted average of the manufacturer's suggested retail prices (MSRPs) of those vehicles. The approach of adding high-performance features that started with the Impreza WRX STI was extended to the Legacy GT, and the strategy of developing a two-pillared marketing strategy—with high-performance models forming one pillar and Outback and Forester crossover models forming the other—proved to be effective.

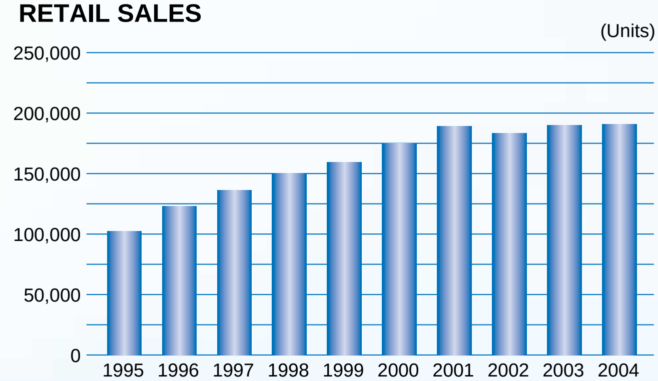
The target of increasing sales volume to above the 200,000-unit level was not attained, however, and intensifying competition led to challenges such as rising incentive payments. These factors and the difficulty of passing on the cost of environmental and safety countermeasures in the form of higher selling prices prevented the attainment of the Company's profit target.

MSRP



(Model year wtd.)

RETAIL SALES



Measures during the Next Two Years

North America is the most important market for FHI's future growth, and efforts during the next two years will determine the direction of the Company's future business development. Growth strategy measures aimed at boosting sales volume to 250,000 units in 2009 or 2010 are to be implemented during the next two years, but top priority will be given to augmenting profitability. Regarding products, the Company will work to secure sales volume and profit by promoting sales of price-competitive models. Meanwhile, the Company will also elevate brand value and increase per-unit profit by promoting sales of high-added-value models, such as the newly introduced B9 Tribeca. The Company also intends to restrict its incentive payments to a low level compared with competitors.

Specific Measures

Along with vigorous efforts to strengthen its sales network in the sunbelt region, FHI is now striving to strengthen the dealer network in metropolitan areas throughout the United States to expand its customer base and is making investments in sales network upgrades. The "Site Control" operation planned in such a market as Dallas, Texas, is one example of augmenting the network in urban areas, while steps to increase exclusive dealerships and separate showroom dealerships is another. By the end of 2006, the Company aims to create a network of 608 dealerships, with 415 (68%) exclusive and separate showroom dealerships and 385 (63%) "Signature Facility" dealerships. These activities are currently supervised by SOA's sales division, but SOA is creating a new department to more dynamically upgrade the dealer network. During 2005, SOA will reorganize its regional responsibilities to further strengthen the sunbelt region, increasing the number of sales districts from 37 to 47 to tighten the focus of market development and sales promotion activities in each district.

Subaru of Jacksonville

Japan

Principal strategic tasks regarding the sales network in Japan include the following:

Reforming Sales Systems and Operations by Utilizing the "Partner 21" Dealer Support Network System

Dealer operations within individual regions will be consolidated and measures to improve efficiency through the integration of administrative functions and other support operations will be implemented from fiscal 2006.

Creating Regional Block Management

Management integration of FHI-owned dealers is to be achieved through the establishment of regional holding companies to strengthen the relationship with FHI and to enhance operational speed.

Enhancing the Quality of Customer Service

FHI is giving additional emphasis to the quality of customer service offered by dealer frontline staff, and measures are to be taken to dramatically improve the quality of customer interface in showrooms and service facilities. A specialized team has been established to promote the improvements among frontline staff and additional programs are to be organized for augmenting the importance of customer service quality among store managers with the goal of becoming the top automobile manufacturer in service quality as evaluated by outside agencies.

Yokohama

Osaka

Kobe

Europe and Other Regions

Operations in European markets are considered the third major pillar of FHI's marketing operations, and the Company is seeking to boost its regional sales volume to 100,000 units by implementing the following strategies:

Strengthening the Capabilities of Subaru Europe

Subaru Europe N.V./S.A., established in March 2002, is augmenting its public relations and marketing capabilities, resulting in increased sales of the G3X Justy and other FHI models. It is proactively endeavoring to promote greater sales by increasing its involvement in the management of principal distributors and striving to achieve distribution cost reductions to enable competitive selling prices.

Reinforcing the Sales Network

FHI is aiming to increase the number of its dealerships to expand its geographic market coverage in urban and other regions while concurrently working to increase dealership quality. The number of dealerships was 974 in 2004, and plans call for increasing this number to 1,140 in 2006 by establishing additional dealerships in such countries as Germany, the United Kingdom, Italy, France, Norway, and Russia.

Developing Additional New Markets

FHI is also taking steps to create and strengthen its presence in promising markets in the Eastern Europe, Central Europe, and CIS regions.

Subaru Australia posted record sales for the ninth consecutive year in 2004, selling over 33,000 units, and it has been making steady progress in elevating the position of the Subaru brand. Another promising market is China, where Subaru established a dealer network in 2004. We place the Chinese market as key to expanding Subaru sales in Asia.

Subaru Europe N.V./S.A.

Boosting the Efficiency of Asset Utilization and Streamlining the Corporate Structure

The revised FDR-1 medium-term business plan calls for FHI to implement measures related to two additional strategic goals not included in the original version of FDR-1: boosting the efficiency of asset utilization and streamlining the corporate structure.

Boosting the Efficiency of Asset Utilization

FHI is aiming to reduce consolidated total assets 10% (from ¥1,357.5 billion, as of March 31, 2005) and interest-bearing debt 20% (from ¥412.2 billion, as of March 31, 2005) by March 31, 2008.

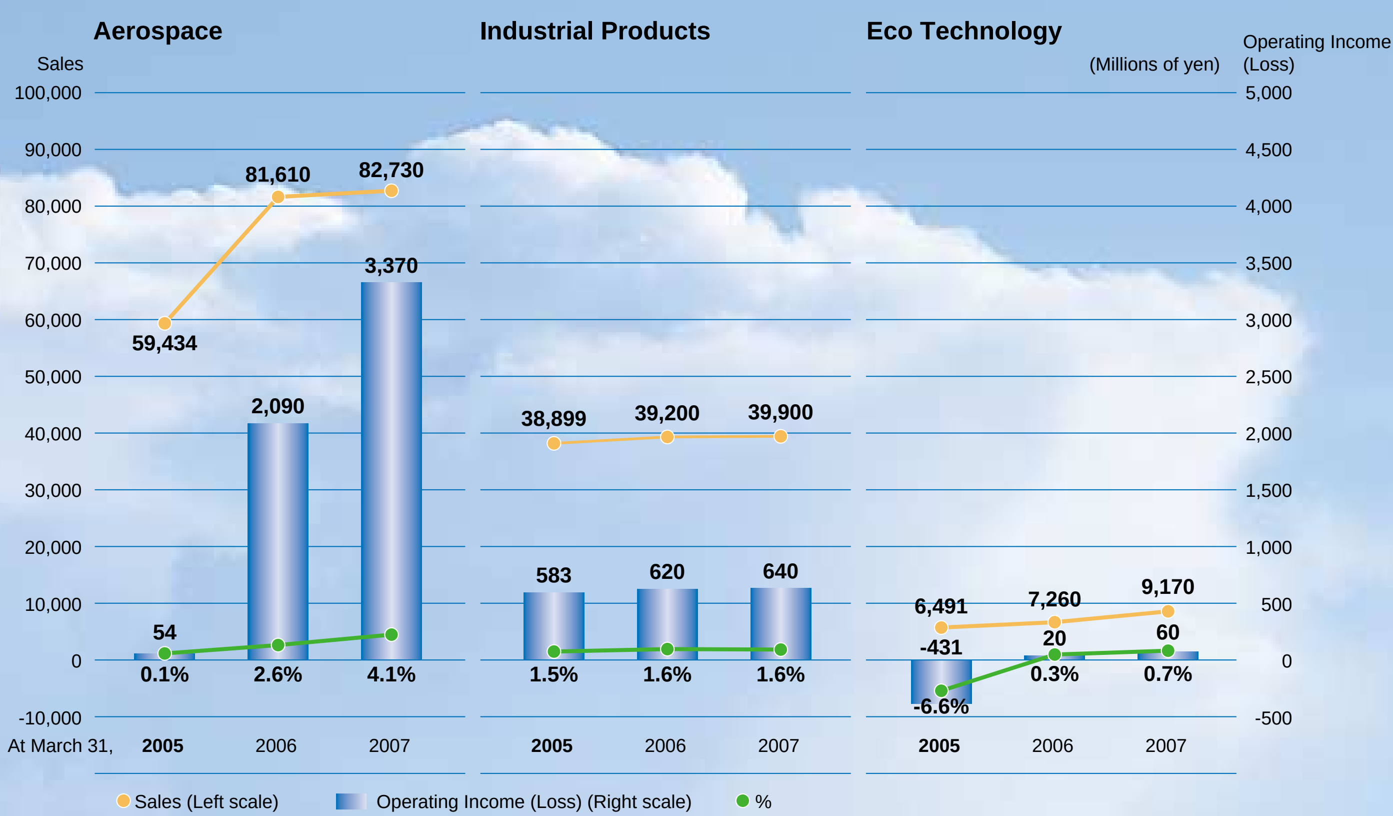
Measures to boost the efficiency of asset utilization are to be applied resolutely and empirically in all areas of operations, without exception. The diverse measures to be taken in this regard are to include those aimed at (1) strictly managing asset levels in function-specific subsidiaries and the main three nonautomobile business divisions, (2) reducing inventory assets through process management, and (3) liquefying assets and selling businesses. In particular, the Company will naturally be striving to realize substantial recoveries in the profitability of the main three nonautomobile business divisions, and it will strictly manage the asset efficiency of the divisions while annually reevaluating its business portfolio and considering whether those divisions should be maintained.

Streamlining the Corporate Structure

FHI will take measures to optimize the workforces of the parent company and manufacturing plants and rationalize affiliates while making organizational and systemic reforms designed to facilitate the rapid attainment of targets. To promote organizational streamlining, personnel revitalization, and expedited decision making, reforms are to be made to retirement and pension systems.

To promote the effective implementation of these measures, FHI has established the Operational Reform Committee, which is working to (1) focus attention on strategic tasks by improving time management and (2) take steps aimed at boosting productivity in administrative support units.

Asset Turnover



Recovering demand in commercial business (Boeing, etc.) Increasing sales of defense business	Expanding major OEM contracts mainly in the United States	Securing the top market share of Fuji Mighty

Management (As of July 1, 2005)

Troy A. Clarke
Director of the Board

- To create more value in the partnership between Fuji Heavy Industries Ltd. and General Motors Corporation

Takao Tsuchiya
Representative Director
of the Board
Executive Vice President

- Be persistent in demanding perfection for the benefit of all customers

Kyoji Takenaka
Representative Director
of the Board
President and CEO

- Derive energy from challenges
- Start by accurately assessing our own abilities, the nature of competition and the levels of customer satisfaction
- Be meticulous about systems for generating sales revenue and profit

Representative Director of the Board
President and CEO
Kyoji Takenaka

Representative Director of the Board
Senior Executive Vice President
Hiroshi Suzuki

Representative Directors of the Board
Executive Vice Presidents
Takao Tsuchiya
Shunsuke Takagi

Directors of the Board
Executive Vice Presidents
Kiyoshi Inoh
Hiroshi Komatsu

Director of the Board
Troy A. Clarke

Senior Vice Presidents
Hiroyuki Oikawa
Yoji Ishimaru
Kazushige Okuhara
Norihisa Matsuo
Shoichi Washizu
Kunio Ishigami
Jun Kondo
Ikuo Mori
Takashi Ishihara

Vice Presidents
Ichiro Kudo
Tsunenori Hoshi
Shizuhiro Okazaki
Masaharu Yuasa
Satoshi Sakurai
Hideki Ishido
Takashi Mochizuki
Derek C. Leck
Yoichi Serizawa
Kazuyoshi Shimizu
Yoshio Hasunuma
Naoto Muto
Yasuyuki Yoshinaga
Tamaki Kamogawa
Masakazu Kimura
Akira Mabuchi
Thomas C. Englin

Standing Corporate Auditors
Takeo Tsumuji
Masayoshi Nagano
Masatake Yashiro

Corporate Auditor
Morihiko Tashiro

Hiroshi Suzuki
Representative Director
of the Board
Senior Executive Vice President

- Prefer to regret overdoing things rather than leaving things undone
- Reform entails change, and clinging to the past will prevent progress

Shunsuke Takagi
Representative Director
of the Board
Executive Vice President

- Play the role of the villain for the sake of attaining the target level of consolidated operating income

Kiyoshi Inoh
Director of the Board
Executive Vice President

- Maintain a strong emphasis on results

Hiroshi Komatsu
Director of the Board
Executive Vice President

- Rather than thinking about whether something is possible, just think of a way to do it
- Give preference to action over proposals and results over action
- Those unable to succeed will fade from sight

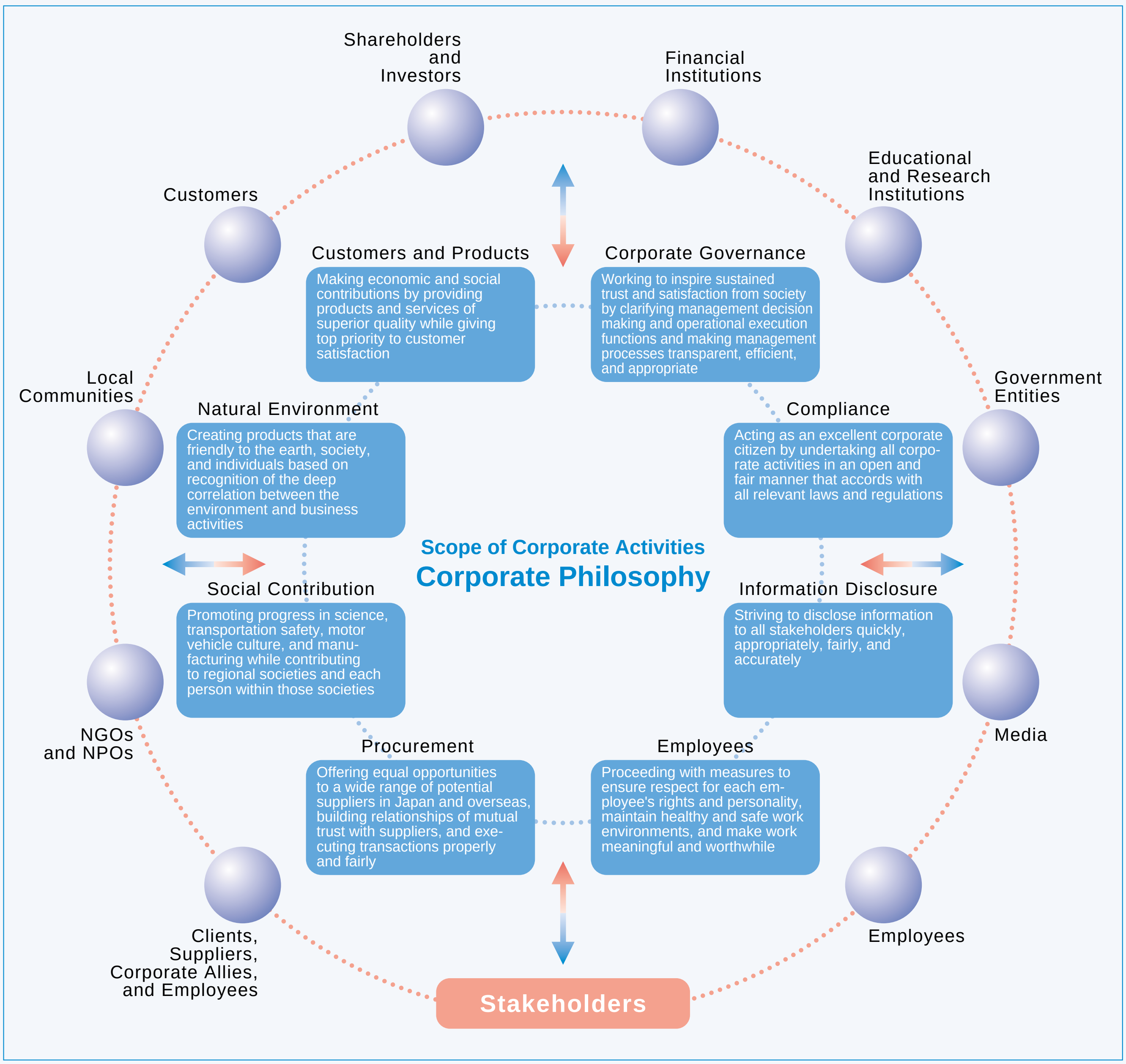
Corporate Social Responsibility (CSR)

The FHI CSR Policy

To be good corporate citizens, companies have the responsibility to society to undertake various types of CSR activities. FHI's CSR activities and other activities all reflect the Corporate Philosophy, which is also the CSR policy.

Corporate Philosophy and CSR Policy

1. We will strive to create advanced technology on an ongoing basis and provide consumers with distinctive products with the highest level of quality and customer satisfaction.
2. We will aim to continuously promote harmony among people, society, and the environment while contributing to the prosperity of society.
3. We will look to the future with a global perspective and aim to foster a vibrant, progressive company.



1. Environmental Management

Establishment of Our Environmental Logo

In June 2005, FHI established the Subaru Group's environmental logo. Centered on a plant leaf design, the logo is designed to represent a world with green land and blue skies. The display of the logo is meant to promote greater awareness of FHI's proactive efforts in line with the policy of “creating products and an environment that are good for the world and society.”

The Subaru Group recognizes that its operations are deeply connected with the natural environment. By striving to create products and an environment that are good for the world and society, the Group is seeking to help create an abundant future for mankind.

Based on its voluntary environmental plan, the “FHI Environmental Conservation Program,” FHI is undertaking activities aimed at reducing the burden on the environment at every stage of business—from product development to procurement, production, use, and disposal.

In fiscal 2005, FHI attained its green procurement objective of increasing the share of its automobile operations related suppliers that have environmental management systems (EMSs) to more than 95%.

Environmental auditing systems have already been introduced at all the parent company's principal facilities, and measures were taken during fiscal 2005 to progressively expand the scope of EMSs to other Group units. For example, two of our overseas sales subsidiaries, U.S.-based Subaru of America, Inc. (SOA), and Canada-based Subaru Canada, Inc. (SCI), obtained ISO 14001 certification during the year.

Regarding environmental accounting, FHI has calculated that its environmental costs were ¥21,045 million in fiscal 2005, compared with ¥25,043 million in fiscal 2004 and ¥26,017 million in fiscal 2003. Economic effects were ¥2,298 million in fiscal 2005, compared with ¥1,980 million in fiscal 2004 and ¥1,226 million in fiscal 2003. These figures reflect the steady annual improvement being achieved in the Company's environmental performance. One particularly noteworthy environmental protection initiative was the February 2005 use of the Energy Performance Contract (ESCO) method to introduce a 6,030kW gas-engine-type, natural-gas-powered cogeneration system at the Utsunomiya plant. The use of the ESCO method enables such benefits as reduction of energy consumption and CO_2 emissions without entailing any initial investment or risk.

Having responded to European laws regarding the recycling of end-of-life vehicles (ELVs) since July 2003, FHI is moving ahead in collaboration with other automobile manufacturers with efforts to respond to a Japanese ELV recycling law and has established the Automobile Recycle System of Subaru in Japan.

2. Corporate Governance

Basic Corporate Governance Policy

FHI is working to strengthen its corporate governance policies to ensure that it can measure up to the trust and confidence placed in the Company by all its shareholders, customers, and other stakeholders.

- Since June 1999, the Company has employed an executive officer system that helps clarify responsibilities for operational execution in each division.
- Since June 2003, the Company has reduced the terms of directors and executive officers from two years to one.
- Since June 2004, the Company has given responsibility for the nomination of corporate officers to its Executive Nomination Meeting and given responsibility for evaluating performance and determining the remuneration of corporate officers to its Executive Compensation Meeting.
- Since June 2005, the Company has reduced the number of directors of the board from eight to seven.

All these measures are designed to clarify management decision making and operational execution functions, increase management transparency, and accelerate management functions.

The Board of Corporate Auditors Meeting consists of four corporate auditors, including two outside corporate auditors, and is responsible for receiving reports on important auditing issues and deliberates accordingly.

The Executive Management Board performs preliminary reviews of issues before their presentation to the Board of Directors Meeting and deliberates on companywide management strategies and the execution of important business operations.

As FHI proceeds with the implementation of the revised FDR-1 plan, it will be taking various measures to further strengthen its internal control systems and auditing systems while also considering whether to recruit outside directors.

3. Compliance

Aiming to maintain the trust and support of society, FHI is engaged in systematic compliance activities throughout all Group companies. In 2001, the Company announced its compliance policy, which is summarized as “FHI views compliance as a top-priority management issue, recognizes that rigorous companywide compliance systems are an important part of the foundation of its operations, and seeks to ensure strict compliance with all relevant public laws and internal regulations as a means of promoting maximum levels of fairness and openness in line with the highest societal standards.” The Company has also set up a companywide compliance promotion committee to deliberate, discuss, and decide on important compliance issues and promote exchanges of related information. From February 2003, we launched a “compliance hotline system” enabling employees to report directly to the Compliance Hotline Desk of the Legal Department when compliance problems arise. In addition to continually maintaining compliance-related educational and training programs, the Company began implementing groupwide measures to fully comply with Japan's new personal information protection law from April 2005.

4. Customer Satisfaction

In line with its distinctive Subaru strategies that emphasize superior functionality with respect to driving performance, safety, and environment friendliness, FHI is proactively developing new products while seeking to provide customers with products that both excite and satisfy. The Company has announced that its quality policy is to “consistently give top priority to customer satisfaction, work to increase the quality of operations, and provide products and services characterized by top-class quality.” In line with this policy, the Company has established a Subaru Customer Center to improve capabilities for handling customer consultations, promoting customer satisfaction, and providing diverse services. In January 2005, the Company established the Subaru Academy, which is working to help further increase groupwide capabilities for developing and applying technologies and for responding to customer needs and inquiries.

To maintain strong quality assurance performance, FHI compiles quality-related information from around the world, quickly assesses the importance of the information, and promptly takes resolute measures to rectify quality problems. The Company makes relentless quality assurance efforts at all operational stages—from product development through manufacturing.

5. Employee Satisfaction

Aiming to make its workforce an “autonomously motivated and proactively creative group,” FHI is taking various measures to reform and invigorate its corporate culture. To increase the distinctive dynamism of its organization, the Company is taking measures related to salary systems as well as career planning, education, and employee welfare systems that are designed to help build an organization able to boldly address new challenges. A Japanese law effective from April 2005, the Next Generation Development Support Countermeasure Promotion Law, calls for companies to take various measures, including those to offer improved work environments. In response, FHI has been progressively augmenting its related companywide “positive action” programs since April 2005.

6. Social Contribution

Aiming to be an excellent corporate citizen, FHI recognizes the importance of its responsibility to make special contributions to society in line with its distinctive Subaru strategies and capabilities. Accordingly, the Company is striving to make contributions in product-related fields, foster the development of personnel able to create next-generation products, promote the development of communities surrounding its facilities, and support the individual social contribution initiatives of its employees. In these ways, FHI is endeavoring to help contribute to sound and sustainable social development.

Financial Section

CONTENTS

Consolidated Five-Year Financial Summary

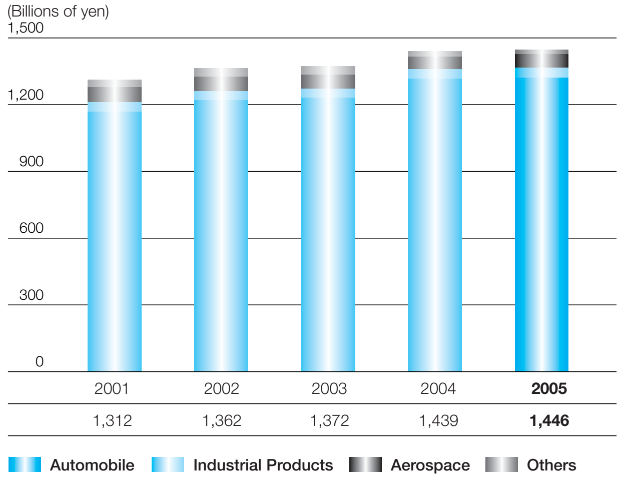
FUJI HEAVY INDUSTRIES LTD. AND CONSOLIDATED SUBSIDIARIES
Years ended March 31

	Millions of yen	*Millions of yen*	*Millions of yen*	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	*2003*	*2002*	*2001*	***2005***
For the Year:						
Net sales	**¥1,446,491**	¥1,439,451	¥1,372,337	¥1,362,493	¥1,311,887	**$13,469,513**
Cost of sales	**1,107,718**	1,085,716	1,011,582	992,950	978,841	**10,314,908**
Gross profit	**338,773**	353,735	360,755	369,543	333,046	**3,154,605**
Selling, general and administrative expenses	**296,756**	303,411	293,234	281,063	251,373	**2,763,349**
Operating income	**42,017**	50,324	67,521	88,480	81,673	**391,256**
Income before income taxes and minority interest	**21,066**	56,266	46,970	56,136	21,291	**196,164**
Net income	**18,238**	38,649	33,484	30,283	22,628	**169,830**
At Year-End:						
Shareholders' equity	**¥ 471,149**	¥ 453,708	¥ 411,252	¥ 396,112	¥ 357,455	**$ 4,387,271**
Total assets	**1,357,459**	1,349,727	1,344,072	1,269,558	1,168,501	**12,640,460**
Ratio of shareholders' equity to total assets (%)	**34.7%**	33.6%	30.6%	31.2%	30.6%	
Per Share (in yen and U.S. dollars):						
Net income:						
Basic	**¥ 23.27**	¥ 50.62	¥ 44.84	¥ 40.74	¥ 30.44	**$ 0.22**
Diluted	**23.27**	49.66	42.91	38.83	29.06	**0.22**
Shareholders' equity	**604.51**	582.60	553.90	532.88	480.86	**5.63**
Other Information:						
Depreciation/amortization expenses	**¥ 71,010**	¥ 71,112	¥ 67,896	¥ 63,964	¥ 64,070	**$ 661,235**
Capital expenditures (addition to fixed assets)	**147,759**	128,026	119,423	118,376	102,301	**1,375,910**
R&D expenses	**52,962**	57,541	60,110	54,903	46,622	**493,174**
Number of shares issued (thousands of shares)*	**782,866**	782,866	746,521	746,506	746,502	
Number of shareholders*	**34,558**	34,704	35,584	33,094	32,996	
Number of employees*:						
Parent only	**12,703**	12,928	13,064	13,374	13,603	
Consolidated	**26,989**	27,296	27,478	26,483	26,502	

Note: U.S. dollar figures have been translated from yen, for convenience only, at the rate of ¥107.39 to US$1.00, the approximate rate of exchange at March 31, 2005.
** As of March 31*

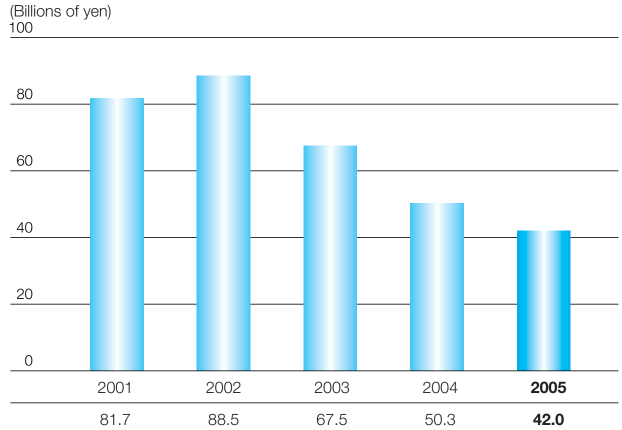
Net Sales

(Billions of yen)



Operating Income

(Billions of yen)



Management's Discussion and Analysis of Results of Operations and Financial Position

OVERVIEW

In the fiscal year 2005, ended March 31, 2005, conditions in the Japanese economy were firm, owing to such factors as recovering corporate earnings and rising private-sector capital investment, although the persistent appreciation of the yen against the U.S. dollar and rapid rises in the prices of crude oil and certain other raw materials continued to make anticipating future economic trends very difficult. In the United States, which is a key overseas market, the Federal Reserve Bank raised interest rates several times, causing concern over the possibility of additional interest rate hikes. This and a cooling of consumer sentiment due to such factors as surging gasoline prices sustained fears of a recession.

Amid these conditions, FHI's mainstay Subaru Automotive Business Unit recorded a lower domestic sales volume for passenger cars, as the new model effect of the Legacy had run its course, although the Subaru R2 and Subaru R1 minicar models supported a 3.5% rise in the overall sales volume in Japan, compared with the previous fiscal year, to 254.0 thousand units. Overseas sales volume grew 3.0%, compared with the previous fiscal year, to 340.7 thousand units, reflecting double-digit growth in Europe and Australia along with increased growth in the important U.S. market due to sales of the new Legacy. The growth in both domestic and overseas sales volumes more than offset the strong yen's negative impact on overseas sales, and consolidated sales for the year rose ¥7.0 billion, or 0.5%, compared to the previous fiscal year, to ¥1,446.5 billion.

Regarding profitability, despite efforts to reduce various costs, operating income declined ¥8.3 billion, or 16.5%, to ¥42.0 billion, compared with the previous fiscal year, due to the strong yen against the U.S. dollar and deterioration of the automotive sales volume and model mix. Income before income taxes and minority interest decreased ¥35.2 billion, or 62.6%, to ¥21.1 billion. Due to a loss on devaluation of inventories related to one of the Aerospace division's projects and other factors as well as an increase in the tax expenses of a U.S. subsidiary, net income decreased ¥20.4 billion, or 52.8%, compared with the previous fiscal year, to ¥18.2 billion. Earnings per share fell from ¥50.62 to ¥23.27, while return on equity dropped from 8.9% to 3.9%.

The Company generated 91.2% of its consolidated sales from the Automobile division, 4.1% from the Aerospace division, 3.2% from the Industrial Products division, and the rest from the Other division. The Automobile division accounted for 97.4% of operating income. While the other three business divisions all posted losses during the previous fiscal year, the Aerospace division and Industrial Products division were able to regain their profitability during the fiscal year 2005. The Aerospace division contributed 0.5% of operating income, and the Industrial Products division contributed 2.0%. Moreover, the operating loss of the Other division was cut by more than half, improving from a loss of ¥1.5 billion to a loss of ¥0.6 billion.

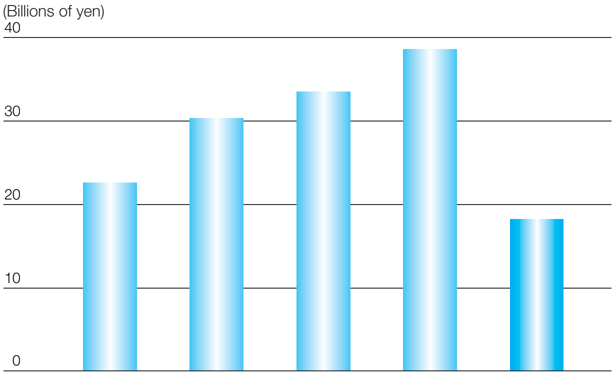
By region, the Japan division, including exports from Japan, accounted for 61.3% of consolidated sales, up 2.9 percentage points from the previous fiscal year, and operating income grew 7.6%, to ¥40.5 billion. The North America division considerably countervailed this improvement, as sales decreased 7.7% and operating income fell from ¥1.1 billion to an operating loss of ¥6.7 billion. Although sales of the new Legacy were strong in North America, profitability was affected by a temporary rise in costs associated with the launch of the new Legacy models. Other region sales grew 68.9% and operating income increased 41.7%, to ¥0.4 billion.

REVIEW OF OPERATIONS BY DIVISION

Consolidated net sales in the fiscal year 2005 rose 0.5% from the previous fiscal year, to ¥1,446.5 billion. Information for each division follows.

Net Income

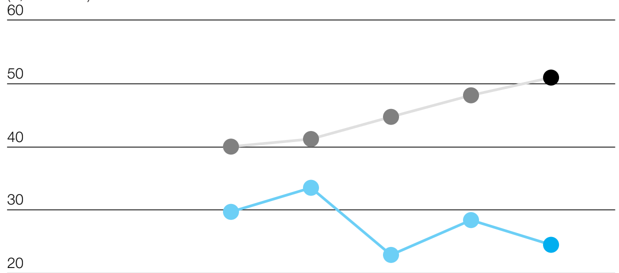
(Billions of yen)



2001	2002	2003	2004	**2005**
22.6	30.3	33.5	38.6	**18.2**

Automobile Inventory

(1,000 units)



	2001	2002	2003	2004	**2005**
Japan	29.7	33.5	22.9	28.4	**24.5**
United States	40.0	41.2	44.7	48.1	**50.9**

Automobile Division

Sales of the Automobile division were up ¥2.9 billion, or 0.2%, from the previous fiscal year, to ¥1,323.7 billion. The size of the increase was restrained by yen appreciation. In terms of global sales volume, FHI reported a year-on-year increase of 18.3 thousand units, or 3.2%, to 594.8 thousand units. In Japan, the total automobile sales volume grew 8.5 thousand units, or 3.5%, to 254.0 thousand units; of this, the number of passenger cars sold decreased 7.1 thousand units, or 6.4%, to 104.0 thousand units, and the number of minicars sold rose by 15.6 thousand units, or 11.6%, to

Consolidated Automobile Sales by Region (Number of units)

	2005	*2004*	*2003*	*2002*	*2001*
Japan	**254,039**	245,541	245,525	264,257	290,301
United States	**193,917**	189,633	192,389	191,381	172,686
Canada	**16,506**	16,154	17,699	15,632	15,005
Europe	**60,517**	53,578	41,325	32,373	39,951
Australia	**35,414**	30,685	29,455	26,923	27,976
Others	**21,241**	15,652	14,051	12,675	14,378
Subtotal	**581,634**	551,243	540,444	543,241	560,297
CKD* Overseas	**0**	2,800	1,500	3,288	3,941
Total	**581,634**	554,043	541,944	546,529	564,238
SIA Consignment Production	**13,150**	25,239	—	—	—

** CKD: Complete Knocked Down*

Non-Consolidated Automobile Sales by Model (Number of units)

	2005	*2004*	*2003*	*2002*	*2001*
Domestic Units:					
Legacy	**59,843**	73,676	49,179	59,209	67,424
Impreza	**27,437**	22,263	25,471	24,899	32,362
Forester	**19,457**	20,097	25,389	22,922	28,994
Others	**1,397**	2,479	4,174	4,244	297
Subtotal	**108,134**	118,515	104,213	111,274	129,077
Minicars	**164,624**	143,502	147,712	167,265	173,754
Total	**272,758**	262,017	251,925	278,539	302,831
Export Units:					
Legacy	**44,102**	33,865	21,421	24,727	26,254
Impreza	**69,945**	67,349	75,354	75,700	54,721
Forester	**90,131**	99,463	99,145	72,629	85,453
Others	**8,324**	161	—	—	—
Subtotal	**212,502**	200,838	195,920	173,056	166,428
Minicars	**—**	—	—	22	108
Total	**212,502**	200,838	195,920	173,078	166,536
CKD Overseas	**115,317**	90,158	107,576	104,234	111,783
(SIA Portion)	**115,317**	87,358	106,076	100,946	107,842
U.S. Retail Sales*:					
Legacy	**89,453**	79,839	85,359	95,291	96,391
Impreza	**32,209**	36,525	38,226	35,612	19,220
Forester	**58,424**	59,761	53,922	55,041	56,605
Baja	**7,316**	10,694	2,513	—	—
Total	**187,402**	186,819	180,020	185,944	172,216
U.S. Production Units*:					
Legacy	**105,550**	96,993	102,813	103,010	107,955

** U.S. Retail Sales and U.S. Production Units are the aggregate figures for the calendar year from January through December.*

150.0 thousand units, resulting in a decline in the average unit price of automobiles sold. Although sales of the Impreza were bolstered by a victory at the 2004 FIA World Rally Championship (WRC) Rally Japan held in September 2004, there was a decrease in the sales of the flagship Legacy as the new model effect faded out. However, minicar sales were boosted by the high evaluations of the Subaru R2, which, since its launch in December 2003, has received such awards as the “2005 RJC Car of the Year Special Award for the Best Minicar” and the “2004-2005 Car of the Year Japan Best 10 Cars,” along with an additional contribution from the Subaru R1, which was launched in January 2005.

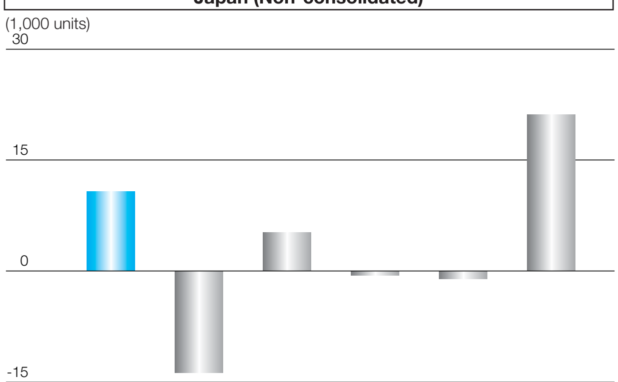
In overseas markets, total sales volume was increased 21.9 thousand units, or 7.2%, to 327.6 thousand units. When consignment production by Subaru of Indiana Automotive, Inc. (SIA), is included, the number increases 9.8 thousand units, or 3.0%, to 340.7 thousand units. In the North America region, although the Impreza and Forester showed declines, sales of the all-new Legacy, which began in June 2004, along with OEM production to Saab Automobile AB, contributed to an increase of 4.6 thousand units, or 2.3%, compared with the previous fiscal year, to 210.4 thousand units.

In Europe, sales of the all-new Legacy were solid, and sales of the new G3X Justy (an OEM vehicle from Suzuki Motor Corporation) also made a significant contribution to an increase in overall sales of 6.9 thousand units, or 13.0%, to 60.5 thousand units. Furthermore, growth in the sales of the all-new Legacy and the sound performance of the Impreza and the Forester led to sales of 35.4 thousand units in Australia, an increase of 4.7 thousand units, or 15.4%, from the previous fiscal year.

Operating income decreased ¥11.2 billion, or 21.4%, to ¥40.9 billion, due to the deterioration of sales volume and model mix as well as a loss on currency exchange.

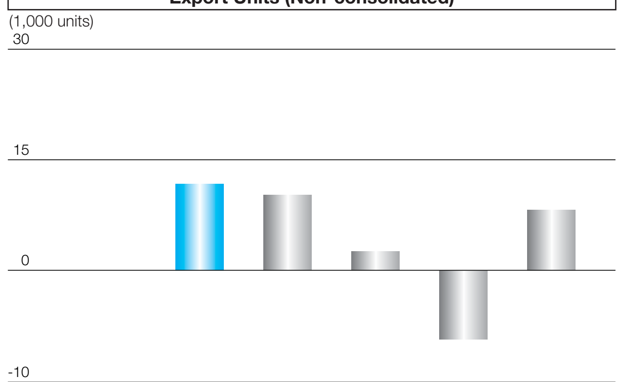
Change in Units Sold by Model (Comparison of units sold in fiscal 2005 and fiscal 2004)

Japan (Non-consolidated)



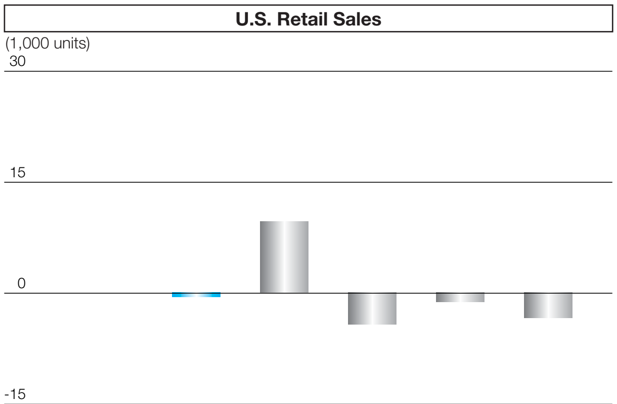
	Total	Legacy	Impreza	Forester	Traviq	Minicars
Change	+10.7	-13.8	+5.2	-0.6	-1.1	+21.1

Export Units (Non-consolidated)



	Total	Legacy	Impreza	Forester	Others
Change	+11.7	+10.2	+2.6	-9.3	+8.2

U.S. Retail Sales



	Total	Legacy	Impreza	Forester	Baja
Change	-0.6	+9.6	-4.3	-1.3	-3.4

Industrial Products Division

Total sales of the Industrial Products division, which handles such products as general-use engines and generators, increased ¥4.5 billion, or 10.6%, to ¥47.1 billion. In Japan, sales of pump engines decreased, but overall sales were up owing to strong sales of newly redesigned generators. Overseas sales were up considerably, as exports to the United States of engines for leisure vehicles were strong, and the development strategy for the U.S. market in regard to engines used in conjunction with industrial machinery proceeded smoothly. While an operating loss of ¥0.3 billion was recorded in the previous year, the rise in sales during the year under review supported a surge in operating income, to ¥0.8 billion.

Aerospace Division

The Aerospace division increased its total sales ¥2.6 billion, or 4.6%, to ¥59.5 billion. Sales to the Japan Defense Agency rose due to the start of full-scale deliveries for the next-generation Maritime Patrol Aircraft and Cargo Transport Aircraft (PX/CX), which more than offset declines in sales of UH-1J utility helicopters and unmanned target drones. Commercial sector operations faced challenges due to a decrease in deliveries of components to Boeing and the appreciation of the yen, but sales in the sector grew owing to the start of deliveries of vertical fins for the Airbus A380 and the delivery of an experimental Stratospheric Platform Airship System to the Japan Aerospace Exploration Agency. The rise in sales was instrumental in enabling a ¥0.5 billion improvement in operating income, from an operating loss of ¥0.3 billion in the previous fiscal year to ¥0.2 billion in operating income.

Other Businesses

Sales in this segment declined ¥3.3 billion, or 12.1%, to ¥23.6 billion. This primarily reflected a drop in the sales of Fuji Mighty sanitation trucks following a temporary surge in demand in the previous fiscal year stemming from the tightening of diesel vehicle emission restrictions in the Tokyo metropolitan area. Sales were also reduced by the transfer of House Division operations to an affiliated company in April 2004. Despite the drop in sales, operating loss for the segment shrank ¥0.9 billion, from ¥1.5 billion to ¥0.6 billion.

COST OF SALES, EXPENSES, AND OPERATING INCOME

The cost of sales rose ¥22.0 billion, or 2.0%, to ¥1,107.7 billion. This boosted the cost of sales ratio 1.2 percentage points, from 75.4% to 76.6%. Though net sales increased ¥7.0 billion, gross profit decreased ¥15.0 billion, or 4.2%, to ¥338.8 billion. This decrease reflected a rise in raw material prices as well as the effect of yen appreciation and a deterioration of the automobile model mix. Progressive measures taken to reduce research and development costs and other expenses lowered SG&A expenses ¥6.7 billion, or 2.2%, to ¥296.8 billion. However, operating income decreased ¥8.3 billion, or 16.5%, to ¥42.0 billion, and the operating income ratio declined 0.6 percentage point, from 3.5% to 2.9%.

Net Sales by Division (Excluding intersegment sales) (Billions of yen)

	2005	2004	2003	2002	2001
Automobile	**¥1,319.6**	¥1,316.9	¥1,229.8	¥1,219.7	¥1,167.2
Industrial Products	**46.8**	42.2	41.5	39.4	44.2
Aerospace	**59.4**	56.6	63.0	66.2	65.5
Other	**20.6**	23.6	37.9	37.0	34.9
Total	**¥1,446.5**	¥1,439.4	¥1,372.3	¥1,362.4	¥1,311.8

Operating Income (Loss) by Division (Billions of yen)

	2005	2004	2003	2002	2001
Automobile	**¥40.9**	¥52.1	¥67.3	¥85.6	¥82.2
Industrial Products	**0.8**	(0.2)	(0.8)	(0.2)	0.7
Aerospace	**0.2**	(0.3)	3.3	7.4	2.4
Other	**(0.6)**	(1.4)	(3.1)	(4.2)	(4.1)
Corporate and Elimination	**0.6**	0.3	0.8	(0.0)	0.3
Total	**¥42.0**	¥50.3	¥67.5	¥88.4	¥81.6

Factors positively affecting operating income included a ¥16.4 billion reduction in the cost of materials, comprising the net value including the price rise of raw materials, a ¥4.5 billion decrease in research and development expenses, and a ¥3.1 billion drop in SG&A and other expenses. The aggregate value of these cost reductions was ¥24.0 billion. Factors negatively affecting operating income included a loss on currency exchange, mainly from yen/U.S. dollar fluctuations, which decreased operating income by ¥15.1 billion, and a deterioration of the sales volume and model mix, taking into account the additional costs for overseas environmental and safety regulations, which reduced operating income by ¥17.2 billion. The aggregate value of these operating income reductions was ¥32.3 billion.

Net other income (expenses) decreased ¥26.9 billion, from a ¥5.9 billion gain in the previous fiscal year to a ¥21.0 billion loss. Regarding other income, amortization of consolidation adjustments grew ¥2.0 billion, due to offsetting accounts related to SIA operations, from ¥4.9 billion to ¥6.9 billion. Other expenses consisted of such items as an ¥8.1 billion loss on devaluation of inventories related to a significant delay in an aircraft development project, a ¥4.2 billion loss on compensation to suppliers associated with the partial rescheduling of automobile business development plans, a ¥3.5 billion loss on discontinued operations due to the termination of trailer train parts operations and other operations of wholly owned subsidiary Yusoki Kogyo K.K., and a ¥3.1 billion loss on revaluation of derivatives. These losses are considered to be temporary. As a result of these factors, income before income taxes and minority interests decreased ¥35.2 billion, or 62.6%, to ¥21.1 billion.

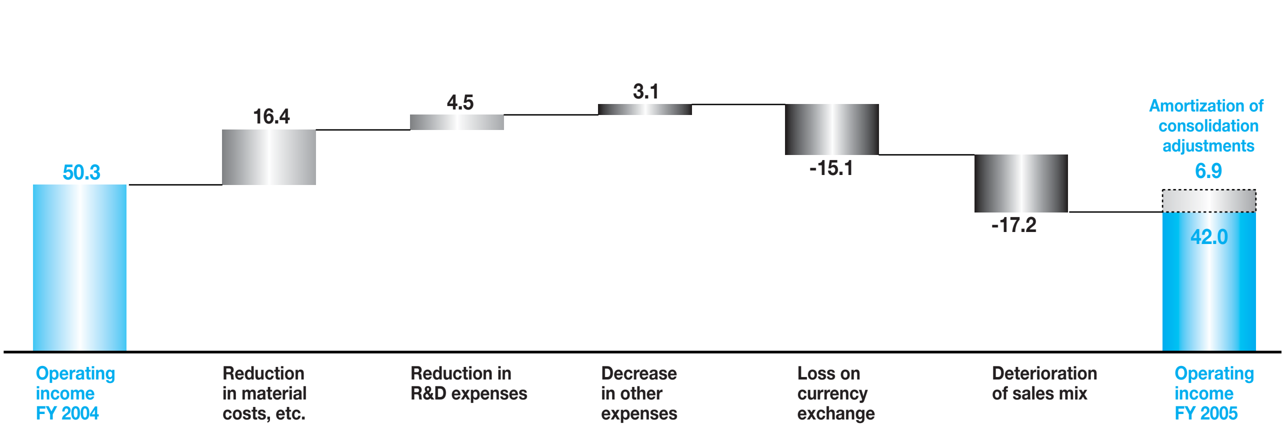
Income taxes for the year fell to ¥5.9 billion, from ¥12.0 billion in the previous fiscal year, and deferred tax credits totaled ¥3.3 billion, reducing the effective tax rate to 12.6%. Minority interest in consolidated subsidiaries amounted to a loss of ¥179 million. Consequently, net income decreased ¥20.4 billion, or 52.8%, to ¥18.2 billion.

FINANCIAL POSITION

Total assets increased ¥7.7 billion, or 0.6%, to ¥1,357.5 billion. Total current assets decreased ¥5.8 billion, to ¥649.1 billion, as a ¥26.3 billion rise in short-term loans, to ¥128.2 billion, was more than offset by decreases in cash and time deposits, notes and accounts receivable, trade, marketable securities, and inventories. Property, plant and equipment, net, rose by ¥34.0 billion to ¥543.7 billion, resulting from an increase in capital investment for new Legacy production and transactions related to SIA's leased facilities. Regarding investments and other assets, investment securities increased ¥14.1 billion, to ¥71.1 billion. However, reflecting the withdrawal of ¥29.1 billion of restricted collateral cash deposits made by SIA, the "other assets" item in investments and other assets fell ¥35.3 billion, to ¥21.5 billion, causing the total value of investments and other assets to decrease ¥20.4 billion, to ¥164.7 billion.

Total liabilities fell ¥9.9 billion, to ¥882.8 billion, largely due to drops in such items as notes and accounts payable, trade, consolidation adjustments, accrued expenses, and accrued

Analysis of Increases and Decreases in Operating Income (Consolidated)
(Billions of yen)



pension and severance liability. Consolidation adjustments in particular decreased, largely resulting from the July 2004 termination of Isuzu OEM production at SIA as well as from transactions related to SIA's leased facilities. Total interest-bearing debt rose ¥33.2 billion, to ¥412.2 billion, owing mainly to a ¥12.0 billion rise in commercial paper, to ¥22.0 billion, and an ¥18.8 billion increase in long-term debts, to ¥59.1 billion.

Total shareholders' equity grew ¥17.4 billion, to ¥471.1 billion, reflecting a rise in retained earnings. Accordingly, the shareholders' equity ratio increased 1.1 points, from 33.6% to 34.7%, and shareholders' equity per share increased from ¥582.60 to ¥604.51. Despite the growth in interest-bearing debt, the rise in shareholders' equity greatly restrained deterioration in the debt/equity ratio, which rose only to 0.87, from 0.84. The Company thus continued to maintain a solid financial position while keeping its debt/equity ratio well within the upper limits of 1.0.

CAPITAL EXPENDITURES

The FHI Group proactively implemented investments during the year, and its capital expenditures amounted to ¥85.3 billion. This figure, up ¥10.8 billion from the ¥74.5 billion level of the previous fiscal year, includes ¥14.9 billion in temporary costs associated with transactions related to SIA's leased facilities. These investments were based on the FDR-1 medium-term business plan and were mostly for the automobile operations, but a revision of that plan is projected to result in an ¥18.3 billion drop in investments for the current fiscal year, ending March 31, 2006, to ¥67.0 billion. Those investment reductions are aimed at enhancing efficiency and making other improvements rather than postponing automobile development projects. Reductions also targeted R&D expenses, which were reduced to ¥53.0 billion from ¥57.5 billion in the previous fiscal year, and this investment reduction policy is to be continued during the current fiscal year. However, while depreciation decreased to ¥51.1 billion, from ¥53.2 billion in the previous fiscal year, depreciation in the current fiscal year is expected to rise to ¥58.0 billion. In addition, recognizing that R&D programs play a crucial role in supporting its corporate development, FHI plans R&D expenses of ¥55.5 billion during the current fiscal year.

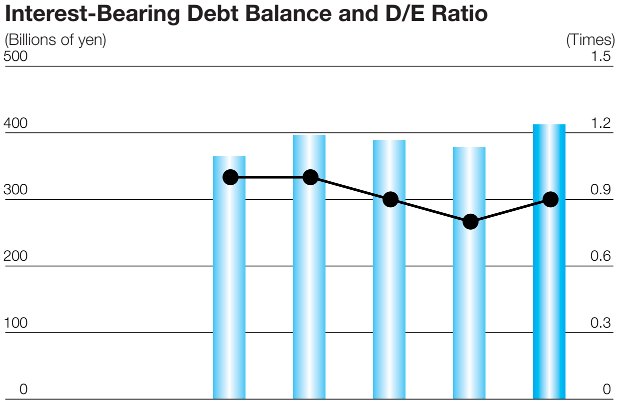
CASH FLOWS

Cash and cash equivalents at the end of the year under review totaled ¥131.7 billion, down ¥7.7 billion from the previous fiscal year-end. Net cash provided by operating activities fell ¥42.4 billion, to ¥57.3 billion. Net cash used in investing activities decreased ¥37.4 billion, to ¥89.8 billion. Net cash provided by financing activities grew ¥23.9 billion, to ¥26.2 billion.

Free cash flow, defined as net cash provided by operating activities plus net cash used in investing activities, decreased ¥5.1 billion from negative ¥27.4 billion in the previous fiscal year to negative ¥32.4 billion. This resulted from a significant decrease in net cash from operating activities.

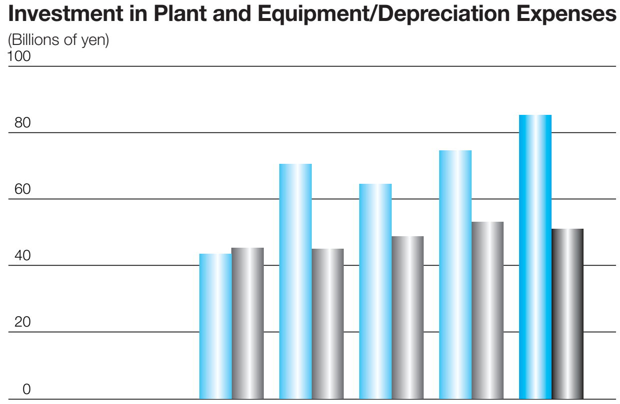
The principal reasons for the large drop in net cash provided by operating activities included a ¥35.2 billion decrease in income before income taxes and minority interest, a

Interest-Bearing Debt Balance and D/E Ratio



	2001	2002	2003	2004	**2005**
Interest-bearing debt	365.1	396.7	389.1	379.0	**412.2**
D/E ratio	1.0	1.0	0.9	0.8	**0.9**

Investment in Plant and Equipment/Depreciation Expenses



	2001	2002	2003	2004	**2005**
Investment in plant and equipment	43.6	70.6	64.6	74.6	**85.3**
Depreciation expenses	45.3	45.0	48.8	53.2	**51.1**

¥17.2 billion increase in inventories, and a ¥26.8 billion reduction of amortization of consolidation adjustments, due to offsetting accounts related to SIA operations, including transactions associated with leased facilities.

The decrease in net cash used in investing activities reflected a ¥17.1 billion drop in the purchase of marketable securities along with the recording of ¥29.4 billion in proceeds from the withdrawal of restricted collateral cash, which was used as seed money for consolidation adjustments.

The rise in net cash provided by financing activities reflected a shift from short-term to long-term fund procurement that entailed increases of ¥44.6 billion in long-term debts and ¥11.0 billion in commercial paper, which was partially offset by an ¥8.5 billion increase in repayment on long-term debts and a ¥22.8 billion drop in short-term borrowings. In the previous fiscal year, repayment on long-term debts amounted to ¥28.6 billion and commercial paper ¥1.0 billion, while proceeds from long-term debts and net increase in short-term borrowings amounted to ¥5.3 billion and ¥21.7 billion, respectively. In the fiscal year under review, repayments on long-term debts and net decrease in short-term borrowings amounted to ¥37.2 billion and ¥1.1 billion, respectively, while net increase in commercial paper and proceeds from long-term debts amounted to ¥12.0 billion and ¥49.9 billion, respectively.

OUTLOOK

FHI disclosed its revised FDR-1 in May 2005, and the first target of the remaining two years of the medium-term business plan is to establish a profitable base for the future. Our goals of an operating income ratio of more than 8% and ROA of more than 10% by 2010 still stand. However, considering the past three years, our urgent task is to overcome such difficulties as high costs and a weak sales network. FHI forecasts consolidated net sales of ¥1,470.0 billion (up 1.6%), operating income of ¥31.0 billion (down 26.2%), and net income of ¥15.0 billion (down 17.8%).

Regarding mainstay automobile operations, in Japan, the beneficial effects of minor face-lift changes to the Forester and Impreza are expected to boost passenger car sales volume 3.3%, to 107.5 thousand units, and the fading of new model benefits from the launch of the Subaru R2 and Subaru R1 is expected to depress minicar sales volume 4.5%, to 143.3 thousand units. Thus, it is anticipated that total automobile sales volume in Japan will decline 1.3%, to 250.7 thousand units.

While the new Legacy models helped boost overseas sales volume 7.2% during the fiscal year under review, overseas sales volume in the current fiscal year is projected to rise to 331.0 thousand units, a sharp deceleration to a growth rate of only 1.0%, excluding SIA consignment production terminated in July 2004. In the North American market, the beneficial effects of the new Legacy helped boost sales volume 2.3% during the fiscal year under review, and robust growth of 4.3% is expected during the current fiscal year, to 219.4 thousand units, as the new B9 Tribeca will be launched in early summer 2005. However, it is anticipated that gains in other markets will be rolled back slightly because of inventory adjustments.

Operating income is projected to decline ¥11.0 billion, from ¥42.0 billion to ¥31.0 billion. The projected decline reflects a ¥22.0 billion reduction comprising a ¥2.5 billion rise in R&D expenses, a ¥1.7 billion increase in SG&A expenses and other expenses, an ¥8.6 billion loss on currency exchange fluctuations, and a ¥9.2 billion decrease resulting from deterioration of sales volume and model mix. On the positive side, an ¥11.0 billion reduction in the cost of materials, which is the net value including the forecasted rise of price of raw materials, is expected to contribute to operating income.

FHI expects the current fiscal year to be one characterized by the bottoming out of performance and return to recovery.

Consolidated Balance Sheets

FUJI HEAVY INDUSTRIES LTD. AND CONSOLIDATED SUBSIDIARIES
As of March 31, 2005 and 2004

	Millions of yen	Millions of yen	Thousands of U.S. dollars (Note 1)
ASSETS	***2005***	*2004*	***2005***
Current assets:			
Cash and time deposits (Note 4)	**¥ 40,742**	¥ 46,684	**$ 379,384**
Marketable securities (Notes 4 and 5)	**87,003**	113,490	**810,159**
Notes and accounts receivable, trade (Note 9)	**116,278**	122,724	**1,082,764**
Allowance for doubtful accounts	**(1,259)**	(661)	**(11,724)**
Inventories (Note 6)	**175,087**	179,338	**1,630,385**
Short-term loans (Note 4)	**128,202**	101,871	**1,193,798**
Deferred tax assets (Note 12)	**34,859**	34,149	**324,602**
Other current assets (Note 9)	**68,158**	57,284	**634,677**
Total current assets	**649,070**	654,879	**6,044,045**
Property, plant and equipment (Notes 7, 8 and 9)	**1,174,358**	1,125,117	**10,935,450**
Less—accumulated depreciation	**(630,632)**	(615,374)	**(5,872,353)**
Net property, plant and equipment	**543,726**	509,743	**5,063,097**
Investments and other assets:			
Investment securities (Note 5)	**65,323**	52,926	**608,278**
Investments in non-consolidated subsidiaries and affiliated companies	**6,970**	5,298	**64,904**
Long-term loans	**5,976**	4,918	**55,648**
Goodwill	**16,961**	17,753	**157,938**
Intangibles, net	**26,250**	22,700	**244,436**
Deferred tax assets (Note 12)	**24,481**	29,707	**227,964**
Other assets (Note 9)	**21,453**	56,759	**199,767**
Allowance for devaluation of investments	**(41)**	(280)	**(382)**
Allowance for doubtful accounts	**(2,710)**	(4,676)	**(25,235)**
Total investments and other assets	**164,663**	185,105	**1,533,318**
Total assets	**¥1,357,459**	¥1,349,727	**$12,640,460**

LIABILITIES AND SHAREHOLDERS' EQUITY	*Millions of yen* **2005**	*Millions of yen* 2004	*Thousands of U.S. dollars (Note 1)* **2005**
Current liabilities:			
Short-term borrowings (Note 9)	**¥ 217,928**	¥ 207,029	**$ 2,029,314**
Current portion of long-term debts (Note 9)	**34,667**	40,888	**322,814**
Notes and accounts payable, trade	**190,790**	193,186	**1,776,608**
Accrued expenses (Note 2)	**110,093**	113,908	**1,025,170**
Accrued income taxes (Note 12)	**8,872**	5,092	**82,615**
Other current liabilities (Note 12)	**47,961**	43,128	**446,606**
Total current liabilities	**610,311**	603,231	**5,683,127**
Long-term liabilities:			
Long-term debts (Note 9)	**159,595**	131,079	**1,486,125**
Accrued pension and severance liability (Note 11)	**59,002**	61,654	**549,418**
Consolidation adjustments (Note 3)	**12,352**	44,027	**115,020**
Other long-term liabilities (Notes 8 and 12)	**41,583**	52,709	**387,215**
Total long-term liabilities	**272,532**	289,469	**2,537,778**
Minority interest in consolidated subsidiaries	**3,467**	3,319	**32,284**
Contingent liabilities (Note 19)			
Shareholders' equity (Note 13):			
Common stock			
Authorized—1,500,000,000 shares			
Issued—782,865,873 shares	**153,795**	153,795	**1,432,117**
Capital surplus	**160,071**	160,107	**1,490,558**
Revaluation reserve for land (Notes 8 and 12)	**421**	421	**3,920**
Retained earnings	**178,022**	165,192	**1,657,715**
Net unrealized holding gains on securities	**16,945**	10,291	**157,789**
Translation adjustments	**(35,874)**	(33,300)	**(334,053)**
Less—treasury stock, at cost, 2005—3,761,911 shares	**(2,231)**	—	**(20,775)**
2004—4,480,160 shares	**—**	(2,798)	**—**
Total shareholders' equity	**471,149**	453,708	**4,387,271**
Total liabilities and shareholders' equity	**¥1,357,459**	¥1,349,727	**$12,640,460**

The accompanying notes are an integral part of these balance sheets.

Consolidated Statements of Income

FUJI HEAVY INDUSTRIES LTD. AND CONSOLIDATED SUBSIDIARIES
Years ended March 31, 2005, 2004 and 2003

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars (Note 1)*
	2005	*2004*	*2003*	***2005***
Net sales	**¥1,446,491**	¥1,439,451	¥1,372,337	**$13,469,513**
Cost of sales	**1,107,718**	1,085,716	1,011,582	**10,314,908**
Gross profit	**338,773**	353,735	360,755	**3,154,605**
Selling, general and administrative expenses (Note 14)	**296,756**	303,411	293,234	**2,763,349**
Operating income	**42,017**	50,324	67,521	**391,256**
Other income (expenses):				
Interest and dividend income	**2,393**	2,081	1,855	**22,283**
Interest expenses	**(2,437)**	(2,416)	(2,941)	**(22,693)**
Gain (loss) on sale of securities	**541**	4,153	(994)	**5,038**
Foreign exchange gains (losses)	**915**	7,348	(1,538)	**8,520**
Loss on devaluation of securities	**(23)**	(221)	(3,884)	**(213)**
Loss on sale and disposal of property, plant and equipment, net	**(4,752)**	(3,089)	(4,822)	**(44,250)**
Loss on revaluation of derivatives	**(3,132)**	—	—	**(29,165)**
Loss on devaluation of inventories at Aerospace division (Note 16)	**(8,122)**	—	—	**(75,631)**
Loss on discontinued operations (Note 15)	**(3,467)**	—	(1,882)	**(32,284)**
Amortization of consolidation adjustments (Note 3)	**6,868**	4,912	—	**63,954**
Loss on compensation to suppliers (Note 17)	**(4,174)**	—	—	**(38,868)**
Gain on prior period adjustment	**—**	1,049	—	**—**
Pension and severance cost (Note 11)	**—**	(1,268)	—	**—**
Other, net	**(5,561)**	(6,607)	(6,345)	**(51,783)**
	(20,951)	5,942	(20,551)	**(195,092)**
Income before income taxes and minority interest	**21,066**	56,266	46,970	**196,164**
Income taxes (Note 12):				
Current	**5,913**	12,030	20,359	**55,061**
Reversal of prior year's accrued income taxes	**—**	—	(2,973)	**—**
Deferred	**(3,264)**	5,603	(3,810)	**(30,394)**
	2,649	17,633	13,576	**24,667**
Income before minority interest	**18,417**	38,633	33,394	**171,497**
Minority interest in consolidated subsidiaries	**(179)**	16	90	**(1,667)**
Net income	**¥ 18,238**	¥ 38,649	¥ 33,484	**$ 169,830**

	Yen	*Yen*	*Yen*	*U.S. dollars (Note 1)*
Per share data (Note 2):				
Net income—Basic	**¥23.27**	¥50.62	¥44.84	**$0.22**
—Diluted	**23.27**	49.66	42.91	**0.22**
Cash dividends (Note 13)	**9.00**	9.00	9.00	**0.08**

The accompanying notes are an integral part of these statements.

Consolidated Statements of Shareholders' Equity

FUJI HEAVY INDUSTRIES LTD. AND CONSOLIDATED SUBSIDIARIES
Years ended March 31, 2005, 2004 and 2003

	Thousands								*Millions of yen*
	Number of shares issued	*Common stock*	*Capital surplus*	*Revaluation reserve for land*	*Retained earnings*	*Net unrealized holding gains on securities*	*Translation adjustment*	*Less—treasury stock, at cost*	*Total shareholders' equity*
Balance, March 31, 2002	746,506	¥144,450	¥150,762	¥381	¥107,328	¥ 4,997	¥ (9,579)	¥(2,227)	¥396,112
Foreign currency translation adjustment							(8,658)		(8,658)
Cash dividends					(6,689)				(6,689)
Payment of bonuses to directors and statutory auditors					(161)				(161)
Shares issued upon conversion of convertible bonds	15	5	4						9
Increase in treasury stock								(526)	(526)
Revaluation reserve for land				8					8
Increase in unrealized holding gains on securities						(1,551)			(1,551)
Comprehensive loss					(776)				(776)
Net income					33,484				33,484
Balance, March 31, 2003	746,521	144,455	150,766	389	133,186	3,446	(18,237)	(2,753)	411,252
Foreign currency translation adjustment							(15,063)		(15,063)
Cash dividends					(6,846)				(6,846)
Payment of bonuses to directors and statutory auditors					(171)				(171)
Shares issued upon conversion of convertible bonds	36,345	9,340	9,305						18,645
Increase in treasury stock								(45)	(45)
Gain on disposal of treasury stock			36						36
Reversal of revaluation reserve for land					(31)				(31)
Revaluation reserve for land				32					32
Increase in unrealized holding gains on securities						6,845			6,845
Comprehensive income					405				405
Net income					38,649				38,649
Balance, March 31, 2004	782,866	153,795	160,107	421	165,192	10,291	(33,300)	(2,798)	453,708
Foreign currency translation adjustment							**(2,574)**		**(2,574)**
Cash dividends					**(7,013)**				**(7,013)**
Payment of bonuses to directors and statutory auditors					**(157)**				**(157)**
Increase in the number of companies accounted for by the equity method					**1,496**				**1,496**
Decrease in treasury stock								**567**	**567**
Loss on disposal of treasury stock			**(36)**		**(77)**				**(113)**
Increase in unrealized holding gains on securities						**6,654**			**6,654**
Comprehensive income					**343**				**343**
Net income					**18,238**				**18,238**
Balance, March 31, 2005	**782,866**	**¥153,795**	**¥160,071**	**¥421**	**¥178,022**	**¥16,945**	**¥(35,874)**	**¥(2,231)**	**¥471,149**
									Thousands of U.S. dollars (Note 1)
Balance, March 31, 2004		$1,432,117	$1,490,893	$3,920	$1,538,244	$ 95,828	$(310,084)	$(26,055)	$4,224,863
Foreign currency translation adjustment							**(23,969)**		**(23,969)**
Cash dividends					**(65,304)**				**(65,304)**
Payment of bonuses to directors and statutory auditors					**(1,462)**				**(1,462)**
Increase in the number of companies accounted for by the equity method					**13,930**				**13,930**
Decrease in treasury stock								**5,280**	**5,280**
Loss on disposal of treasury stock			**(335)**		**(717)**				**(1,052)**
Increase in unrealized holding gains on securities						**61,961**			**61,961**
Comprehensive income					**3,194**				**3,194**
Net income					**169,830**				**169,830**
Balance, March 31, 2005		**$1,432,117**	**$1,490,558**	**$3,920**	**$1,657,715**	**$157,789**	**$(334,053)**	**$(20,775)**	**$4,387,271**

The accompanying notes are an integral part of these statements.

Consolidated Statements of Cash Flows

FUJI HEAVY INDUSTRIES LTD. AND CONSOLIDATED SUBSIDIARIES
Years ended March 31, 2005, 2004 and 2003

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars (Note 1)*
	2005	*2004*	*2003*	***2005***
Cash flows from operating activities:				
Income before income taxes and minority interest	**¥ 21,066**	¥ 56,266	¥ 46,970	**$ 196,164**
Adjustments to reconcile income before income taxes and minority interest to net cash provided by operating activities:				
Depreciation/amortization expenses	**71,010**	71,112	67,896	**661,235**
Loss on sale and disposal of property, plant and equipment, net	**4,752**	3,089	4,822	**44,250**
Increase (decrease) in accrued pension and severance liability	**(2,730)**	73	(106)	**(25,421)**
(Gain) loss on sale of securities	**(541)**	(4,153)	994	**(5,038)**
Loss on devaluation of securities	**23**	221	3,884	**214**
Decrease in notes and accounts receivable, trade	**5,353**	1,191	2,613	**49,846**
(Increase) decrease in inventories	**(11,272)**	5,889	(12,017)	**(104,963)**
Increase (decrease) in notes and accounts payable, trade	**33**	(13,979)	16,534	**307**
Income taxes paid	**(6,197)**	(18,374)	(31,099)	**(57,706)**
Loss on compensation to suppliers	**4,174**	—	—	**38,868**
Loss on discontinued operations	**3,467**	—	1,882	**32,284**
Amortization of consolidation adjustments	**(31,675)**	(4,912)	—	**(294,953)**
Gain on prior period adjustments	**—**	(1,049)	—	**—**
Other, net	**(136)**	4,400	5,690	**(1,266)**
Net cash provided by operating activities	**57,327**	99,774	108,063	**533,821**
Cash flows from investing activities:				
Purchase of property, plant and equipment	**(137,998)**	(125,351)	(115,553)	**(1,285,017)**
Proceeds from sale of property, plant and equipment	**36,411**	38,634	32,213	**339,054**
Purchase of investment securities	**(7,690)**	(11,718)	(10,167)	**(71,608)**
Purchase of marketable securities	**(37,119)**	(54,192)	(38,596)	**(345,647)**
Proceeds from sale of investment securities	**5,395**	11,178	9,114	**50,237**
Proceeds from sale of marketable securities	**50,474**	43,239	72,588	**470,007**
Increase due to acquisition of Isuzu's share of Subaru of Indiana Automotive, Inc. (Note 3)	**—**	—	12,989	**—**
Purchase of intangible assets	**(8,009)**	(8,070)	(6,240)	**(74,579)**
Disbursement of loans receivable	**(122,633)**	(90,041)	(75,898)	**(1,141,940)**
Collection of loans receivable	**101,195**	70,101	62,889	**942,313**
Other, net	**30,213**	(920)	573	**281,339**
Net cash used in investing activities	**(89,761)**	(127,140)	(56,088)	**(835,841)**
Cash flows from financing activities:				
Proceeds from long-term debts	**49,867**	5,269	55,150	**464,354**
Repayment on long-term debts	**(37,166)**	(28,635)	(58,324)	**(346,084)**
Issuance of bonds	**20,000**	20,000	10,000	**186,237**
Redemption of bonds	**(10,000)**	(10,129)	(22,027)	**(93,119)**
Net increase in short-term borrowings	**10,898**	22,662	10,732	**101,481**
Purchase of treasury stock	**(399)**	(49)	(531)	**(3,715)**
Proceeds from disposal of treasury stock	**24**	70	—	**223**
Dividends paid	**(7,013)**	(6,846)	(6,689)	**(65,304)**
Other, net	**(12)**	(7)	—	**(112)**
Net cash provided by (used in) financing activities	**26,199**	2,335	(11,689)	**243,961**
Effect of exchange rate changes on cash and cash equivalents	**(1,481)**	(5,512)	(4,050)	**(13,791)**
Net increase (decrease) in cash and cash equivalents	**(7,716)**	(30,543)	36,236	**(71,850)**
Cash and cash equivalents:				
Balance at beginning of year	**139,401**	169,944	133,708	**1,298,081**
Balance at end of year (Note 4)	**¥131,685**	¥139,401	¥169,944	**$1,226,231**
Supplementary information on cash flows:				
Cash paid during the period for interest	**¥ 2,432**	¥ 2,361	¥ 3,327	**$ 22,646**
Conversion of convertible bonds	**—**	18,645	9	**—**

The accompanying notes are an integral part of these statements.

1. Basis of Presentation of the Financial Statements

The accompanying consolidated financial statements have been prepared in accordance with the provisions set forth in the Japanese Securities and Exchange Law and its related accounting regulations and in conformity with accounting principles generally accepted in Japan, which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards.

The accounts of overseas subsidiaries are based on their accounting records maintained in conformity with generally accepted accounting principles prevailing in the respective countries of domicile. The accompanying consolidated financial statements have been restructured and translated into English (with some expanded descriptions and the inclusion of consolidated statements of shareholders' equity) from the consolidated financial statements of the Company prepared in accordance with Japanese GAAP and filed with the appropriate Local Finance Bureau of the Ministry of Finance as required by the Securities and Exchange Law. Some supplementary information included in the statutory Japanese language consolidated financial statements, but not required for fair presentation, is not presented in the accompanying consolidated financial statements.

The translation of the Japanese yen amounts into U.S. dollars are included solely for the convenience of readers outside Japan, using the prevailing exchange rate at March 31, 2005, which was ¥107.39 to U.S.$1. The convenience translations should not be construed as representations that the Japanese yen amounts have been, could have been, or could in the future be, converted into U.S. dollars at this or any other rate of exchange.

2. Summary of Significant Accounting Policies

Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its significant subsidiaries. All significant intercompany transactions and balances have been eliminated in consolidation. The fiscal year-end of the consolidated domestic subsidiaries is the same as that of the parent company, while the fiscal year-end of the consolidated foreign subsidiaries is December 31. Although these consolidated foreign subsidiaries are included based on their fiscal year ended December 31, significant transactions that occurred in the period between December 31 and March 31 are reflected in the consolidated financial statements.

The consolidated financial statements include the accounts of the Company and 68 subsidiaries in the fiscal year 2005 and 66 subsidiaries in the fiscal years 2004 and 2003.

In addition, 4 non-consolidated subsidiaries and an affiliated company are accounted for by the equity method in the fiscal year 2005, while there was no affiliated company accounted for by the equity method in the fiscal year 2004 and an affiliated company was accounted for by the equity method in the fiscal year 2003.

Investments in insignificant non-consolidated subsidiaries and affiliated companies not accounted for by the equity method are carried at cost. The difference between the cost and underlying net equity of investments in subsidiaries and affiliated companies is allocated to identifiable assets based on fair value at the date of acquisition. The unallocated residual value of the excess of the cost over the underlying net equity is recognized as consolidation adjustments and goodwill and is amortized over a period of 5 years on the straight-line basis. However, consolidation adjustments that arose from making Subaru of Indiana Automotive, Inc. (SIA), a wholly owned subsidiary of the Company, are amortized differently. The portion that clearly corresponds to the forecasted future losses is amortized according to the generation of those losses, and the remaining portion of the consolidation adjustments is amortized by the straight-line method over 5 years.

All assets and liabilities of subsidiaries, which include not only the Company's interest in the subsidiary but also the minority interest portion, are valued based on fair value at the time the Company consolidated the subsidiary.

Translation of foreign currency accounts

Under the Japanese accounting standard for foreign currency translation, monetary assets and liabilities denominated in foreign currencies are translated into Japanese yen at the exchange rates prevailing at each balance sheet date with the resulting gain or loss included in the current statements of income.

Assets and liabilities of foreign subsidiaries and affiliated companies are translated into Japanese yen at the exchange rates in effect at the balance sheet date of the foreign subsidiaries and affiliated companies, except for common stock and capital surplus, which are translated at historical rates. Revenue and expense accounts are translated at the average exchange rates during the current year. The resulting foreign currency translation adjustments are included in "Translation adjustments" in shareholders' equity and minority interest in the accompanying consolidated balance sheets.

Cash equivalents

Cash and cash equivalents include all highly liquid investments, generally with original maturities of three months or less that are readily convertible to known amounts of cash and have negligible risk of changes in value due to their short maturities.

Revenue recognition

Revenue from sales of finished products is generally recognized when such products are shipped to dealers or customers. Revenue from operating leases is recognized on a straight-line basis over the lease term.

Change of accounting policy:
The Company changed the revenue recognition policy for the Aerospace division's production contracts with the production term exceeding one year and the amount of each contract exceeding ¥5,000 million, from the delivery basis to the percentage-of-completion method from the fiscal year ended March 31, 2004. The Company changed the accounting policy for the purpose of more accurately matching revenues against costs in the period in which they were incurred in light of the recent trend that terms of production contracts of the Aerospace division tend to extend over periods and the amounts of such contracts tend to become larger, and such a trend is expected to continue.

As a result of the change, net sales increased by ¥4,013 million and gross profit, operating income and income before income taxes and minority interest increased by ¥231 million in the fiscal year ended March 31, 2004 as compared with amounts resulting from the application of the previous policy.

Allowance for doubtful accounts

Allowance for doubtful accounts is provided based on the amount calculated as the actual ratio of bad debt for ordinary receivables and the amount required for uncollectible accounts for specific doubtful receivables.

Allowance for devaluation of investments

Allowance for devaluation of investments is provided for losses from decrease in the value of investment securities for which fair value is not available and investments in non-consolidated subsidiaries and affiliated companies based on the evaluation of the investees' financial conditions, such as net assets and the probability of recovering the value.

Marketable securities and investment securities

Under the Japanese accounting standard for financial instruments, securities for which fair value is available are stated at the fair value as of the balance sheet date with unrealized holding gains and losses included as a component of shareholders' equity until realized, while securities for which fair value is not available are stated at cost as determined by the moving-average method, after devaluation for any permanent impairment. Held-to-maturity debt securities are stated using the amortized interest cost method.

Derivative financial instruments and hedge accounting

The Japanese accounting standard for financial instruments requires the Company and consolidated domestic subsidiaries to state derivative financial instruments at fair value and to recognize changes in the fair value as gains or losses unless derivative financial instruments are used for hedging purposes.

For interest rate swap contracts used as hedges and which meet certain hedging criteria, the net amount to be paid or received under the interest rate swap contract is added to or deducted from the interest on the assets or liabilities for which the swap contract is executed.

Derivative financial instruments qualifying as a hedge, along with the related transactions, assets and liabilities are as follows:

Financial Instrument	Transaction, Assets and Liabilities
Interest swaps	Borrowings

The risk exposures to movements in interest rates are hedged according to the Company's and consolidated subsidiaries' risk management policy. Evaluation of hedge effectiveness is not considered necessary as the terms and notional amounts of these hedge instruments are the same as those of the related transactions, assets and liabilities, and therefore they are assumed to be highly effective in offsetting movements in interest rates at their inception as well as during their term.

Change of accounting policy:
Previously, for foreign exchange contracts used as hedges and which met certain hedging criteria, the Company translated hedged foreign currency receivables using the contracted forward rates, for forward exchange contracts hedging future transactions, the Company deferred recognition of gains or losses resulting from changes in fair value of the foreign exchange contracts until related gains or losses on the hedged items were recognized. However, the Company stopped applying the hedge accounting from the fiscal year 2005.

The reason for the change is that the Company reconsidered the appropriateness of application of hedge accounting in connection with reviewing the hedge policy and the management activities for foreign exchange contracts.

As a result of this change, operating income increased by ¥141 million and income before income taxes and minority interest decreased by ¥1,623 million as compared with amounts resulting from the application of the previous hedge accounting policy.

The impact of such change on segment information is stated in Segment Information (Note 21).

Inventories

Finished products are stated principally at cost determined by the moving-average method. Raw materials, work in process and supplies are stated principally at cost determined by the first-in, first-out method.

Property, plant and equipment

Property, plant and equipment are stated at cost. Significant renewals and additions are capitalized; ordinary maintenance, ordinary repairs, minor renewals and minor improvements are charged to consolidated statement of income as incurred.

Depreciation of property, plant and equipment of the Company and consolidated domestic subsidiaries is principally computed by the declining-balance method, except for the buildings (excluding building improvements) acquired on or after April 1, 1998, for which the straight-line method is applied. Depreciation of property, plant and equipment of consolidated foreign subsidiaries is computed by the straight-line method at rates based on the estimated useful lives of the assets according to general class, type of construction and use.

Estimated useful lives for depreciable assets are as follows:

Building and structures: 7–50 years

Machinery, equipment and vehicles: 2–11 years

In the fiscal year ended March 31, 2005, the Company and the consolidated subsidiaries did not adopt early the new accounting standard for impairment of fixed assets ("Opinion Concerning Establishment of Accounting Standard for Impairment of Fixed Assets" issued by the Business Accounting Deliberation Council on August 9, 2002) and the implementation guidance for the accounting standard for impairment of fixed assets (the Financial Accounting Standard Implementation Guidance No. 6 issued by the Accounting Standards Board of Japan on October 31, 2003). The new accounting standard is required to be adopted effective April 1, 2005. The Company estimates that the effect of adopting the new accounting standard will have a material effect on the Company's consolidated financial statements.

Accounting for leases

In principle, finance leases are accounted for on a similar basis to sales by lessors or purchases by lessees. However, finance leases which do not transfer ownership of the leased assets to lessees as stipulated in lease contracts can be accounted for as operating leases. Therefore, as a lessee, the Company and consolidated subsidiaries have accounted for those leases as operating leases and have charged periodic lease payments to expenses as incurred. Certain “as if capitalized” information is disclosed in Note 18 to the financial statements.

Intangible assets

Goodwill is principally amortized by the straight-line method based on the accounting principles generally accepted in the respective countries of domicile. However, goodwill of the consolidated subsidiary in the United States is not amortized in accordance with SFAS 142, while other identifiable assets are amortized by the straight-line method.

Computer software used internally by the Company and consolidated subsidiaries is amortized by the straight-line method over the relevant economic useful lives (3 or 5 years).

Accrued pension and severance liability

On terminating employment, employees of the Company and consolidated subsidiaries in Japan are entitled, under most circumstances, to lump-sum indemnities or pensions as described below, based on current rates of pay, length of service, and conditions under which the termination occurs. The minimum payment is an amount based on voluntary retirement. In addition to the minimum payment based on voluntary retirement, employees receive additional benefits for retirement due to age limit, death or other defined reasons.

Certain consolidated subsidiaries in Japan have contributory funded defined benefit pension plans, which are pursuant to the Japanese Welfare Pension Insurance Law. The contributory pension plans cover a portion of the governmental welfare pension program, under which the contributions are made by the companies and their employees, and an additional portion representing the substituted noncontributory pension plan.

Under the Japanese accounting standard for pension and severance benefits, accrued pension and severance liability for employees has been provided based on the estimated amounts of projected pension and severance obligation and fair value of plan assets at the end of the fiscal year. Prior service cost is being amortized as incurred by the straight-line method over the period (14–18 years), which is shorter than the average remaining service periods of the eligible employees. Actuarial gains and losses have been amortized from the following fiscal year by the straight-line method over the periods (primarily 18 years), which are shorter than the average remaining service periods of the eligible employees.

Accrued pension contribution for defined benefit pension plans is included in accrued pension and severance liability.

Directors and statutory auditors of the Company and consolidated domestic subsidiaries are entitled to receive lump-sum payments at the time of severance or retirement, subject to the approval of the shareholders. The liabilities for such benefits are determined based on the Company’s and consolidated subsidiaries’ internal rules and are included in “Other long-tem liabilities” in the accompanying consolidated balance sheets.

Accrued warranty claims

The Company and consolidated subsidiaries provide for accrued warranty claims on products sold based on their past experience of warranty services and estimated future warranty costs, which are included in “Accrued expenses” in the accompanying consolidated balance sheets.

Research and development costs

Research and development costs are expensed as incurred and amounting to ¥52,962 million (US$493,174 thousand), ¥57,541 million and ¥60,110 million for the fiscal years ended March 31, 2005, 2004 and 2003, respectively.

Income taxes

The provision for income taxes is computed based on the pretax income for the financial reporting purposes. Deferred tax assets and liabilities are recognized for expected future tax consequences of temporary differences between the financial statement carrying amounts and the tax bases of assets and liabilities. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

Effective April 1, 2004, the “Corporation Size-Based Enterprise Tax System” for enterprises has been introduced. Due to the introduction, the Accounting Standards Board of Japan issued Practical Solutions Report No. 12, “Practical Solutions on Presentation for Size-Based Components of Corporate Enterprise Tax on Income Statements” on February 13, 2004, which prescribes the new accounting standard for enterprise taxes. In compliance with the report, the value-added and the capital components of the enterprise taxes, which are not related to income, are included in selling, general and administrative expenses from the fiscal year 2005.

As a result, selling, general and administrative expenses increased by ¥1,009 million (US$9,396 thousand), and operating income, ordinary income and income before income taxes and minority interest decreased by the same amount as compared with the previous fiscal year.

The impact of such change on segment information is stated in Segment Information (Note 21).

Net income per share

Basic net income per share (EPS) is computed based on the average number of shares of common stock outstanding during each year. Diluted EPS assumes the potential dilution that could occur if all convertible securities were converted or other contracts to issue common stock were exercised to the extent that it is not antidilutive.

Reclassifications

Certain reclassifications within the financial statements for the fiscal years ended March 31, 2004 and 2003 have been made to conform to the presentation for the fiscal year ended March 31, 2005.

3. Acquisition of Isuzu’s Share of Subaru of Indiana Automotive, Inc.

Subaru of Indiana Automotive, Inc. (SIA, formerly Subaru-Isuzu Automotive, Inc.), a consolidated subsidiary in the United States, was a joint venture company of Isuzu Motors Ltd. and the Company (the Company held a 51% share of SIA). On January 1, 2003, as a result of the dissolution of the joint venture relationship with Isuzu Motors Ltd. and execution of an agreement for the consignment of production, the Company acquired Isuzu’s share of SIA to make SIA a wholly owned subsidiary of the Company, and SIA was assigned to produce certain Isuzu vehicles as well as Subaru vehicles.

Due to the use of a class stock system at SIA, the Company had previously consolidated only the Subaru Division of SIA which had been governed by the Company through ownership of class F common stock, while the Isuzu Division of SIA, which had been governed by Isuzu Motors Ltd. through ownership of class I common stock, was excluded from the consolidated financial statements of the Company. However, as a result of the acquisition of Isuzu’s share of SIA, the Company consolidated SIA as a whole, including the Consignment division (formerly the Isuzu division).

Prior to the Company’s acquisition of Isuzu’s share of SIA, Isuzu Motors Ltd. had made a capital injection into SIA in connection with the forecasted future losses related to the former Isuzu division. In relation to the consignment of the production agreement with Isuzu, the Company has operated the former Isuzu division as the Consignment division. As the consigned production activities have been completed, SIA has been expected to incur certain losses on the disposal of fixed assets, losses on cancellation of operating leases, and losses related to personnel reduction. Consequently, the consolidation adjustments (credit side) arose.

The portion of the consolidation adjustments that clearly corresponds to the forecasted future losses has been amortized according to the generation of those losses, and the remaining portion has been amortized by the straight-line method over 5 years.

The amortization of the consolidation adjustments for the year ended March 31, 2005 was ¥31,654 million (US$294,757 thousand), out of which, ¥6,847 million (US$63,954 thousand) was reflected as amortization of the consolidation, and ¥24,807 million (US$230,999 thousand), which corresponded to the loss on the cancellation of the operating lease at SIA as a result of the termination of the consignment production of Isuzu vehicles, was offset against ¥27,603 million (US$257,035 thousand) expenses on the cancellation of the operating lease at SIA and was included in "other, net" under other income (expenses) in the accompanying consolidated statement of income.

The amortization of the consolidation adjustments for the year ended March 31, 2004 was ¥4,892 million and reflected as "amortization of consolidation adjustments" in the accompanying statement of income. The annual amortization based on currently forecasted losses was as follows:

	Millions of yen	*Thousands of U.S. dollars*
March 31, 2006	¥ 6,600	$ 61,458
March 31, 2007	3,800	35,385
March 31, 2008	(300)	(2,793)
March 31, 2009 and thereafter	2,212	20,598
	¥12,312	$114,648

4. Additional Cash Flow Information

(a) Cash and cash equivalents as of March 31, 2005 and 2004 consisted of the following:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	***2005***
Cash and time deposits	**¥ 40,742**	¥ 46,684	**$ 379,384**
Marketable securities	**87,003**	113,490	**810,159**
Short-term loans	**128,202**	101,871	**1,193,798**
	255,947	262,045	**2,383,341**
Less maturity over three months	**(124,262)**	(122,644)	**(1,157,110)**
Cash and cash equivalents	**¥131,685**	¥139,401	**$1,226,231**

(b) Assets and liabilities of newly consolidated subsidiary through acquisition of shares:
Assets and liabilities of NIIGATA SUBARU Inc. and relationship with the acquisition cost and net cash outflow of such acquisition, which are included in "Other, net" under "Cash flows from investing activities" for the year ended March 31, 2004, were as follows:

	Millions of yen
Current assets	¥2,268
Long-term assets	4,065
Goodwill	212
Current liabilities	(3,145)
Long-term liabilities	(1,217)
Acquisition cost of NIIGATA SUBARU Inc.	2,183
Cash and cash equivalents of NIIGATA SUBARU Inc.	(324)
Net cash used for acquisition of NIIGATA SUBARU Inc.	¥1,859

(c) Significant non-cash transaction:
On August 2004, the Company executed a share exchange agreement and made Yusoki Kogyo K.K. a wholly owned subsidiary of the Company. As a result of the share exchange, consolidation adjustments rose by ¥833 million and treasury stock decreased by ¥942 million.

5. Marketable Securities and Investment Securities

Information as to the value of marketable securities and investment securities as of March 31, 2005 and 2004 was as follows:

(1) Held-to-maturity debt securities for which fair market value was available:

As of March 31, 2004:

			Millions of yen
	Book value	*Fair market value*	*Difference*
Fair market value not exceeding book value:			
Government bonds	¥5	¥5	¥—
Total	¥5	¥5	¥—

(2) Other investment securities (available-for-sale securities) for which fair market value was available:

(a) As of March 31, 2005:

			Millions of yen
	Acquisition cost	*Book value*	*Difference*
Book value exceeding acquisition cost:			
Equity securities	**¥20,761**	**¥49,214**	**¥28,453**
Debt securities			
Government and municipal bonds	**100**	**100**	**0**
Corporate bonds	**2,500**	**2,501**	**1**
Other	**36**	**181**	**145**
Other	**4,281**	**4,282**	**1**
Subtotal	**27,678**	**56,278**	**28,600**
Book value not exceeding acquisition cost:			
Equity securities	**256**	**205**	**(51)**
Debt securities			
Government and municipal bonds	**6,656**	**6,627**	**(29)**
Corporate bonds	**4,740**	**4,724**	**(16)**
Other	**501**	**500**	**(1)**
Other	**2,344**	**2,338**	**(6)**
Subtotal	**14,497**	**14,394**	**(103)**
Total	**¥42,175**	**¥70,672**	**¥28,497**

			Thousands of U.S. dollars
	Acquisition cost	*Book value*	*Difference*
Book value exceeding acquisition cost:			
Equity securities	**$193,323**	**$458,274**	**$264,951**
Debt securities			
Government and municipal bonds	**931**	**931**	**0**
Corporate bonds	**23,280**	**23,289**	**9**
Other	**335**	**1,685**	**1,350**
Other	**39,864**	**39,874**	**10**
Subtotal	**257,733**	**524,053**	**266,320**
Book value not exceeding acquisition cost:			
Equity securities	**2,384**	**1,909**	**(475)**
Debt securities			
Government and municipal bonds	**61,980**	**61,710**	**(270)**
Corporate bonds	**44,138**	**43,989**	**(149)**
Other	**4,665**	**4,656**	**(9)**
Other	**21,827**	**21,770**	**(57)**
Subtotal	**134,994**	**134,034**	**(960)**
Total	**$392,727**	**$658,087**	**$265,360**

(b) As of March 31, 2004:

			Millions of yen
	Acquisition cost	*Book value*	*Difference*
Book value exceeding acquisition cost:			
Equity securities	¥18,869	¥36,167	¥17,298
Debt securities			
Government and municipal bonds	6,818	6,821	3
Corporate bonds	5,299	5,331	32
Other	36	161	125
Other	5,570	5,573	3
Subtotal	36,592	54,053	17,461
Book value not exceeding acquisition cost:			
Equity securities	2,011	1,889	(122)
Debt securities			
Corporate bonds	4,801	4,799	(2)
Other	1,546	1,546	0
Other	848	845	(3)
Subtotal	9,206	9,079	(127)
Total	¥45,798	¥63,132	¥17,334

(3) Other investment securities (available-for-sale securities) sold during the years ended March 31, 2005 and 2004:

(a) For the year ended March 31, 2005:

Sales amount	*Total gain*	*Total loss*
¥640,095 million	¥633 million	¥56 million
US$5,960,471 thousand	US$5,894 thousand	US$521 thousand

The above sales amount included sales of short-term investments in commercial paper and other amounting to ¥584,226 million (US$5,440,227 thousand).

(b) For the year ended March 31, 2004:

Sales amount	*Total gain*	*Total loss*
¥426,839 million	¥4,760 million	¥420 million

The above sales amount included sales of short-term investments in commercial paper and other amounting to ¥372,422 million.

(4) Book values of major securities without available fair market value (except for held-to-maturity debt securities stated in (1) above) as of March 31, 2005 and 2004:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	***2005***
Money management fund	**¥47,688**	¥52,202	**$444,064**
Commercial paper	**19,838**	31,062	**184,729**
Unlisted stocks (excluding over-the-counter stocks)	**6,544**	6,640	**60,937**
Negotiable certificated deposit	**5,000**	—	**46,559**
Beneficiary rights to the trust	**2,579**	8,367	**24,015**
Held-to-maturity debt securities	**6**	6	**56**
Medium-term government bond fund	**—**	4,500	**—**
Free financial fund	**—**	501	**—**

Note: The Company and consolidated subsidiaries recognized ¥23 million (US$214 thousand) and ¥198 million in loss on devaluation of securities for the years ended March 31, 2005 and 2004, respectively, out of which, the devaluation of investment securities with fair market value was ¥10 million for the year ended March 31, 2004.

For purpose of recording the loss on devaluation of securities, the Company and consolidated subsidiaries consider all securities whose fair market value has fallen below 50% of the book value to be permanently impaired, and records the relevant loss on devaluation. For securities whose fair market value has declined between 30% to 50% in relation to book value, the Company and consolidated subsidiaries specifically consider the probability of recovery of the fair value, and records a loss on devaluation in an amount deemed sufficient.

(5) Schedule of redemption for other securities with maturity and held-to-maturity debt securities as of March 31, 2005 and 2004:

(a) As of March 31, 2005:

	Millions of yen				*Thousands of U.S. dollars*			
	Within 1 year	*1 to 5 years*	*5 to 10 years*	*Over 10 years*	*Within 1 year*	*1 to 5 years*	*5 to 10 years*	*Over 10 years*
Debt securities								
Government and municipal bonds	**¥ 1,412**	**¥3,393**	**¥1,420**	**¥501**	**$ 13,149**	**$31,593**	**$13,223**	**$4,665**
Corporate bonds	**4,195**	**2,747**	**262**	**22**	**39,063**	**25,580**	**2,439**	**205**
Other	**21,805**	**—**	**—**	**—**	**203,045**	**—**	**—**	**—**
Other	**5,763**	**425**	**54**	**359**	**53,664**	**3,957**	**503**	**3,343**
Total	**¥33,175**	**¥6,565**	**¥1,736**	**¥882**	**$308,921**	**$61,132**	**$16,165**	**$8,213**

(b) As of March 31, 2004:

	Millions of yen			
	Within 1 year	*1 to 5 years*	*5 to 10 years*	*Over 10 years*
Debt securities				
Government and municipal bonds	¥ 960	¥4,760	¥ 875	¥232
Corporate bonds	8,440	1,125	403	—
Other	32,604	161	—	—
Other	10,124	174	103	228
Total	¥52,128	¥6,220	¥1,381	¥460

6. Inventories

Inventories as of March 31, 2005 and 2004 consisted of the following:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	***2005***
Finished products	**¥103,285**	¥107,679	**$ 961,775**
Work in process	**54,110**	55,491	**503,864**
Raw materials	**15,882**	13,588	**147,891**
Supplies	**1,810**	2,580	**16,855**
	¥175,087	¥179,338	**$1,630,385**

7. Property, Plant and Equipment

Property, plant and equipment as of March 31, 2005 and 2004 were as follows:

	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2005	2004	**2005**
Buildings and structures	**¥280,438**	¥263,128	**$2,611,398**
Machinery and vehicles	**494,199**	468,636	**4,601,909**
Other	**216,021**	205,900	**2,011,556**
	990,658	937,664	**9,224,863**
Less accumulated depreciation	**(630,632)**	(615,374)	**(5,872,353)**
Land	**170,809**	166,518	**1,590,548**
Construction in progress	**12,891**	20,935	**120,039**
Total	**¥543,726**	¥509,743	**$5,063,097**

8. Revaluation Reserve for Land

In accordance with the Land Revaluation Law (Law No. 34, enacted on March 31, 1998), land owned by a consolidated subsidiary for business use was revalued on March 31, 2002. The unrealized gains from the revaluation were included in shareholders' equity as "Revaluation reserve for land," net of deferred taxes. The deferred taxes of the unrealized gains were included in other long-term liabilities. Unrecorded loss on revaluation as of March 31, 2005 was ¥393 million (US$3,660 thousand). According to the Law, the Company and consolidated subsidiaries are not permitted to revalue the land after April 1, 2002.

9. Short-Term Borrowings and Long-Term Debts

Short-term borrowings as of March 31, 2005 and 2004 consisted of the following:

	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2005	2004	**2005**
Bank loans with average interest rate of 0.52% and 0.69% per annum as of March 31, 2005 and 2004, respectively	**¥195,928**	¥197,029	**$1,824,453**
Commercial paper with average interest rate of 0.04% per annum as of March 31, 2005 and 2004	**22,000**	10,000	**204,861**
	¥217,928	¥207,029	**$2,029,314**

Long-term debts as of March 31, 2005 and 2004 consisted of the following:

	Millions of yen 2005	Millions of yen 2004	Thousands of U.S. dollars 2005
Loans principally from banks and insurance companies due through 2025 with average interest rate of 1.96% and 2.50% per annum as of March 31, 2005 and 2004, respectively	**¥ 83,462**	¥ 71,167	**$ 777,186**
Unsecured 2.30% bonds due September 30, 2005	**10,000**	10,000	**93,118**
Unsecured 1.76% bonds due April 30, 2004	**—**	10,000	**—**
Unsecured 0.97% bonds due May 15, 2006	**20,000**	20,000	**186,237**
Unsecured 1.22% bonds due September 30, 2008	**30,000**	30,000	**279,356**
Unsecured 0.89% bonds due September 28, 2007	**10,000**	10,000	**93,118**
Unsecured 0.68% bonds due June 18, 2010	**20,000**	20,000	**186,237**
Unsecured 1.31% bonds due April 28, 2011	**20,000**	—	**186,237**
Secured 1.80% bonds of a consolidated subsidiary due July 7, 2005	**300**	300	**2,794**
Unsecured 0.93% bonds of a consolidated subsidiary due February 15, 2007	**500**	500	**4,656**
	194,262	171,967	**1,808,939**
Less—Portion due within one year	**(34,667)**	(40,888)	**(322,814)**
	¥159,595	¥131,079	**$1,486,125**

Annual maturities of long-term debts as of March 31, 2005 were as follows:

	Millions of yen	Thousands of U.S. dollars
2006	¥ 34,667	$ 322,814
2007	27,377	254,930
2008	17,390	161,933
2009	44,578	415,104
2010	10,239	95,344
2011 and thereafter	60,011	558,814
	¥194,262	$1,808,939

The following assets as of March 31, 2005 and 2004 were pledged as collateral for certain loans:

	Millions of yen 2005	Millions of yen 2004	Thousands of U.S. dollars 2005
Notes and accounts receivable, trade	**¥ 11,665**	¥ 30,924	**$ 108,623**
Other current assets	**—**	415	**—**
Property, plant and equipment	**108,664**	95,904	**1,011,863**
Other assets	**271**	248	**2,524**
	¥120,600	¥127,491	**$1,123,010**

The unexecuted balance of commitments for borrowings by the Company and consolidated subsidiaries (Subaru of America, Inc. and Subaru Europe N.V./S.A.) as of March 31, 2005 and 2004 was as follows:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	***2005***
Total commitments	**¥86,434**	¥103,500	**$804,861**
Less amounts currently executed	**10,000**	19,318	**93,119**
Unexecuted balance	**¥76,434**	¥ 84,182	**$711,742**

10. Unexecuted Balance of Overdraft Facilities and Lending Commitments

The unexecuted balance of overdraft facilities and lending commitments at a consolidated subsidiary (Subaru Finance Co., Ltd.) as of March 31, 2005 and 2004 was as follows:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	***2005***
Total overdraft facilities and lending commitments	**¥12,350**	¥8,170	**$115,001**
Less amounts currently executed	**7,510**	4,244	**69,932**
Unexecuted balance	**¥ 4,840**	¥3,926	**$ 45,069**

A portion of the overdraft facilities and lending commitments above is subject to credit considerations as documented in the customer contracts. Therefore, the total balance above is not always executable.

11. Pension and Severance Plans

The Company and consolidated domestic subsidiaries have non-contributory funded defined benefit pension plans. The plan of the Company covers 80% of retirement and severance benefits for employees who terminate employment at age 50 or over. Consolidated foreign subsidiaries primarily have defined contribution plans.

"Pension and severance cost" under "Other income (expenses)" in the accompanying consolidated statement of income for the year ended March 31, 2004 represents costs resulting from changes made by certain consolidated subsidiaries in the method of calculating projected pension and severance obligation from the simplified method to the principal method. Under the simplified method, accrued pension and severance liability is provided at the amount that would be payable if all employees voluntarily retired at the end of the fiscal year, less the amount covered by the plan assets, while accrued pension and severance liability is provided based on the estimated amount of pension and severance obligation (projected benefit obligations), less the fair value of plan assets at the end of the fiscal year under the principal method.

One of the consolidated subsidiaries changed the calculation method to the principal method because the number of employees exceeded 300 due to a merger, and other subsidiaries changed the calculation method as a result of an increase in reliability in actuarial calculation based on certain assumptions.

As a result, other income decreased by ¥1,268 million and income before income taxes and minority interest decreased by the same amount.

Reconciliation between the projected pension and severance obligation and accrued pension and severance liability as of March 31, 2005 and 2004 was as follows:

	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2005	2004	**2005**
a. Projected pension and severance obligation	**¥138,357**	¥139,686	**$1,288,360**
b. Plan assets	**(59,548)**	(54,946)	**(554,502)**
c. Unfunded pension and severance obligations	**78,809**	84,740	**733,858**
d. Unamortized actuarial gain/loss	**(17,472)**	(19,613)	**(162,697)**
e. Unamortized prior service cost	**(2,423)**	(3,546)	**(22,562)**
f. Net amount recorded in balance sheet	**58,914**	61,581	**548,599**
g. Prepaid pension cost	**(88)**	(73)	**(819)**
h. Accrued pension and severance liability	**¥ 59,002**	¥ 61,654	**$ 549,418**

Notes: 1. The above amounts included the government pension plan funded by social security taxes paid by employees and employer.
2. Certain insignificant consolidated subsidiaries calculated the liability using the simplified method.
3. In addition to the above plan assets, there were plan assets for the multi-employer pension plan amounting to ¥15,081 million (US$140,432 thousand) and ¥16,824 million for the years ended March 31, 2005 and 2004, respectively. The plan assets for the multi-employer pension plan could not be allocated to each specific participating employer and were allocated based on the number of participants.

Periodic pension and severance costs for the years ended March 31, 2005, 2004 and 2003 consisted of the following:

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2005	2004	2003	**2005**
a. Service cost	**¥ 9,647**	¥10,695	¥10,004	**$ 89,831**
b. Interest cost	**2,636**	3,075	3,047	**24,546**
c. Expected return on plan assets	**(1,175)**	(1,155)	(1,262)	**(10,941)**
d. Amortization of actuarial gain/loss	**1,853**	1,269	770	**17,255**
e. Amortization of prior service cost	**257**	295	296	**2,393**
f. Pension and severance cost	**¥13,218**	¥14,719	¥12,855	**$123,084**

Notes: 1. The above amounts did not include the social security taxes paid by employees.
2. Service costs of consolidated subsidiaries using the simplified method were included in service cost above.
3. Service costs above included service cost for the multi-employer pension plan amounting to ¥877 million (US$ 8,166 thousand), ¥1,096 million and ¥907 million for the years ended March 31, 2005, 2004 and 2003, respectively, for which plan assets could not be allocated to each specific participating employer.
4. Service costs above included contributions for the defined contribution plans of consolidated foreign subsidiaries amounting to ¥1,476 million (US$13,744 thousand), ¥1,549 million and ¥1,579 million for the years ended March 31, 2005, 2004 and 2003, respectively.
5. In addition to the pension and severance cost above, additional retirement payments amounting to ¥371 million (US$ 3,455 thousand), ¥120 million and ¥137 million were made for the years ended March 31, 2005, 2004 and 2003, respectively. For the year ended March 31, 2005, ¥92 million (US$857 thousand) out of the entire additional retirement payment was included in "selling, general and administrative expenses," and the remaining ¥279 million (US$2,598 thousand) was reflected as "loss on discontinued operations" in the accompanying consolidated statement of income, whereas the entire additional retirement payment was included in "selling, general and administrative expenses" in the accompanying consolidated statements of income for the years ended March 31, 2004 and 2003.

Actuarial assumptions used in computation of pension and severance liability were as follows:

a. Attribution of expected benefit obligation	The straight-line method
b. Discount rate	2.0%–2.5%
c. Expected rate of return on plan assets	1.4%–4.0%
d. Amortization of actuarial gain/loss	Primarily 18 years (Amortized by the straight-line method starting from the following fiscal year based on the periods shorter than the average remaining service periods of the eligible employees)
e. Amortization of prior service cost	14 to 18 years (The fiscal year 2004: 14 years)

12. Income Taxes

The Company and consolidated subsidiaries were subject to a number of taxes based on income, which in aggregate, resulted in normal statutory income tax rates of approximately 40.5% for the year ended March 31, 2005 and 41.8% for the fiscal years ended March 31, 2004 and 2003.

A reconciliation of the statutory income tax rate in Japan to the Company's effective income tax rate for the fiscal years ended March 31, 2005, 2004 and 2003 was as follows:

	2005	*2004*	*2003*
Statutory income tax rate in Japan	**40.5%**	41.8%	41.8%
Increase (reduction) in taxes resulting from:			
Changes in valuation allowance and tax benefit realized from the losses carried forward	**19.8**	1.6	(8.1)
Adjustment of past corporate income taxes and corporate income taxes refundable	**(1.6)**	(5.3)	(6.3)
Adjustment of past corporate income taxes of a consolidated subsidiary in the United States	**15.8**	—	—
Special deduction on corporate income taxes	**(5.4)**	(4.9)	(3.1)
Entertainment and other non-deductible expenses	**1.6**	0.9	2.5
Effect of change in the statutory income tax rate in Japan	**—**	1.3	1.5
Amortization of consolidation adjustments	**(59.0)**	(3.4)	—
Other	**0.9**	(0.7)	0.6
Effective income tax rate	**12.6%**	31.3%	28.9%

Significant components of the deferred tax assets and liabilities as of March 31, 2005 and 2004 were as follows:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	***2005***
Deferred tax assets:			
Deficit carryforwards	**¥ 7,628**	¥ 4,696	**$ 71,031**
Unrealized gain on sales of inventories	**4,444**	7,660	**41,382**
Accrued pension and severance liabilities	**22,473**	22,294	**209,265**
Accrued expenses	**11,075**	10,631	**103,129**
Accrued bonus	**6,177**	6,924	**57,519**
Accrued warranty claims	**7,637**	8,049	**71,115**
Unrealized gain on sales of property, plant and equipment	**6,552**	6,477	**61,011**
Loss on devaluation of inventories	**6,016**	—	**56,020**
Impairment loss on fixed assets of consolidated foreign subsidiary	**7,760**	—	**72,260**
Other	**15,204**	18,979	**141,578**
Total deferred tax assets	**94,966**	85,710	**884,310**
Valuation allowance	**(11,890)**	(9,202)	**(110,718)**
Total deferred tax assets, net of valuation allowance	**83,076**	76,508	**773,592**
Deferred tax liabilities:			
Depreciation/amortization expenses	**(15,261)**	(11,946)	**(142,108)**
Net unrealized holding gains on investment securities	**(11,496)**	(6,999)	**(107,049)**
Revaluation reserve for land	**(478)**	(478)	**(4,451)**
Advanced depreciation reserve	**(468)**	(468)	**(4,358)**
Other	**(2,455)**	(1,745)	**(22,861)**
Total deferred tax liabilities	**(30,158)**	(21,636)	**(280,827)**
Net deferred tax assets	**¥52,918**	¥54,872	**$492,765**

Net deferred tax assets were included in the following accounts in the accompanying consolidated balance sheets.

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	***2005***
Current assets—Deferred tax assets	**¥34,859**	¥34,149	**$324,602**
Investments and other assets—Deferred tax assets	**24,481**	29,707	**227,964**
Current liabilities—Other current liabilities	**—**	0	**—**
Long-term liabilities—Other long-term liabilities	**(6,422)**	(8,984)	**(59,801)**
Total net deferred tax assets	**¥52,918**	¥54,872	**$492,765**

Effective for years commencing on April 1, 2004 or later, according to the revised local tax law, income tax rates for enterprise taxes have been reduced as a result of introducing the “Corporation Size-based Enterprise Tax System” for enterprises. Based on the change of income tax rates, for calculation of deferred tax assets and liabilities, the Company and consolidated domestic subsidiaries used the aggregate statutory income tax rates of 41.8% for current items and 40.5% for non-current items as of March 31, 2003 and 40.5% for both current and non-current item as of March 31, 2004 and 2005.

As a result of the change in the aggregate statutory income tax rates, net deferred tax assets decreased by ¥640 million and income taxes—deferred on the consolidated statement of income, net unrealized holding gains on securities, revaluation reserve for land and minority interest increased by ¥728 million, ¥73 million, ¥8 million and ¥7 million, respectively, in the fiscal year 2003.

13. Shareholders’ Equity

Under the Commercial Code of Japan, the entire amount of the issue price of shares is required to be accounted for as capital, although a company may, by resolution of its Board of Directors, account for an amount not exceeding one-half of the issue price of the new shares as additional paid-in capital, which is included in capital surplus.

The Commercial Code provides that an amount equal to at least 10% of cash dividends and other cash appropriations shall be appropriated and set aside as a legal earnings reserve until the total amount of legal earnings reserve and additional paid-in capital equals 25% of common stock. (The total amount of legal earnings reserve and additional paid-in capital of the Company has reached 25% of common stock, and therefore the Company is no longer required to provide legal earnings reserve.) The legal earnings reserve and additional paid-in capital may be used to eliminate or reduce a deficit by resolution of the shareholders’ meeting or may be capitalized by resolution of the Board of Directors. On condition that the total amount of legal earnings reserve and additional paid-in capital remains equal to or exceeds 25% of common stock, they are available for distribution by the resolution of the shareholders’ meeting. Legal earnings reserve is included in retained earnings in the accompanying financial statements.

The maximum amount that the Company can distribute as dividends is calculated based on the non-consolidated financial statements of the Company in accordance with the Commercial Code.

In accordance with customary practice in Japan, the appropriations are not accrued in the financial statements for the period to which they relate, but are recorded in the subsequent accounting period after shareholders’ approval has been obtained. Retained earnings at March 31, 2005 include amounts representing final cash dividends of ¥3,507 million (US$32,657 thousand), ¥9 (US$0.08) per share, and directors’ bonuses of ¥55 million (US$512 thousand), which were approved at the shareholders’ meeting held on June 24, 2005.

14. Selling, General and Administrative Expenses

Selling, general and administrative expenses for the fiscal years ended March 31, 2005, 2004 and 2003 consisted of the following:

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	*2003*	***2005***
Transportation and packing expenses	**¥ 15,316**	¥ 14,004	¥ 14,089	**$ 142,620**
Advertisement cost	**47,884**	53,257	51,279	**445,889**
Sales incentives	**33,670**	33,150	25,640	**313,530**
Salary and bonus	**50,047**	52,211	55,446	**466,030**
Research and development expenses	**52,042**	56,405	58,788	**484,608**
Others	**97,797**	94,384	87,992	**910,672**
	¥296,756	¥303,411	¥293,234	**$2,763,349**

15. Loss on Discontinued Operations

The Company terminated the operation of Bus and Train Production in the fiscal year ended March 31, 2003. Loss on discontinued operations due to the termination of bus production was ¥893 million and train production was ¥989 million.

The Company terminated the operation of Trailer, Train parts and other operations of Yusoki Kogyo K.K. in the fiscal year ended March 31, 2005. Loss on discontinued operations due to the termination of such operations was ¥3,467 million (US$32,284 thousand).

16. Loss on Devaluation of Inventories at the Aerospace Division

In the fiscal year ended March 31, 2005, the Company recorded ¥8,122 million (US$75,631 thousand) loss on the devaluation of inventories because the prospective realization of the "Work in process" of Aerospace division's certain project had become uncertain due to a substantial delay in the schedule of the project.

17. Loss on Compensation to Suppliers

In the fiscal year ended March 31, 2005, the Company recorded a ¥4,174 million (US$38,868 thousand) loss on compensation to suppliers based on the anticipated compensation loss for suppliers' development costs which arose from the Company's partial rescheduling of a certain development plan in the Automotive division.

18. Leases

(1) Information as lessee

As allowed under Japanese accounting standards, the Company and consolidated subsidiaries in Japan account for finance lease which do not transfer ownership of leased assets to lessees as stipulated in lease contracts as operating leases. The "as if capitalized" information of such leases was as follows:

Details of the leased assets:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	***2005***
Machinery, equipment and vehicles	**¥1,325**	¥1,465	**$12,338**
Other tangible assets	**2,137**	2,634	**19,900**
Intangibles assets	**33**	435	**307**
	3,495	4,534	**32,545**
Accumulated depreciation/amortization	**(1,506)**	(2,268)	**(14,024)**
Net	**¥1,989**	¥2,266	**$18,521**

Information related to finance leases for the years ended March 31, 2005, 2004 and 2003 was as follows:

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	*2003*	***2005***
Rent paid	**¥665**	¥757	¥990	**$6,192**
Depreciation/amortization expenses	**599**	739	895	**5,578**
Interest expense portion	**57**	51	54	**531**

The future minimum lease/rent payments, excluding the portion of interest thereon, as of March 31, 2005 and 2004 were as follows:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	***2005***
Finance leases:			
Due within one year	**¥ 526**	¥ 581	**$ 4,898**
Due after one year	**1,574**	1,773	**14,657**
	¥2,100	¥ 2,354	**$19,555**
Operating leases:			
Due within one year	**¥ 694**	¥ 8,538	**$ 6,462**
Due after one year	**3,287**	50,700	**30,608**
	¥3,981	¥59,238	**$37,070**

(2) Information as lessor

Capitalized lease assets for finance leases as of March 31, 2005 and 2004 were as follows:

	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2005	2004	**2005**
Machinery, equipment and vehicles	**¥22,595**	¥22,505	**$210,401**
Other tangible assets	**9,666**	9,353	**90,008**
Intangible assets	**1,535**	1,261	**14,294**
	33,796	33,119	**314,703**
Accumulated depreciation/amortization	**(16,458)**	(14,814)	**(153,254)**
	¥17,338	¥18,305	**$161,449**

Information related to finance leases for the years ended March 31, 2005, 2004 and 2003 was as follows:

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2005	2004	2003	**2005**
Rent received	**¥9,417**	¥8,882	¥9,273	**$87,690**
Depreciation/amortization expenses	**7,187**	6,438	6,236	**66,924**
Interest income portion	**1,313**	1,579	1,688	**12,226**

The future minimum lease/rent payments receivable, excluding the portion of interest thereon, as of March 31, 2005 and 2004 was as follows:

	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2005	2004	**2005**
Finance leases:			
Due within one year	**¥ 6,989**	¥ 7,663	**$ 65,081**
Due after one year	**13,189**	13,947	**122,814**
	¥20,178	¥21,610	**$187,895**
Operating leases:			
Due within one year	**¥ 4,097**	¥ 4,161	**$ 38,151**
Due after one year	**5,163**	4,502	**48,077**
	¥ 9,260	¥ 8,663	**$ 86,228**

19. Contingent Liabilities

Contingent liabilities as of March 31, 2005 and 2004 were as follows:

	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2005	2004	**2005**
Trade notes receivable discounted with banks	**¥ —**	¥ 23	**$ —**
As guarantor of the indebtedness from financial institutes	**40,408**	38,031	**376,273**

20. Derivative Financial Instruments

In the normal course of business, the Company and consolidated subsidiaries employ derivative financial instruments, including foreign exchange forward contracts, foreign currency options and interest rate swaps, to manage their exposure to fluctuations in foreign currency exchange rates and interest rates. The Company and consolidated subsidiaries do not use derivatives for speculative or trading purposes.

Fair value information of the derivative financial instruments as of March 31, 2005 and 2004 was as follows:

(1) Foreign currency contracts:

(a) As of March 31, 2005:

	Millions of yen			*Thousands of U.S. dollars*		
	Contract amount	*Fair value*	*Valuation gains (losses)*	*Contract amount*	*Fair value*	*Valuation gains (losses)*
Foreign exchange forward contracts:						
Sell—						
U.S. dollar	**¥100,153**	**¥102,393**	**¥(2,240)**	**$932,610**	**$953,469**	**$(20,859)**
Euro	**8,906**	**8,979**	**(73)**	**82,931**	**83,611**	**(680)**
CAN dollar	**6,183**	**6,438**	**(255)**	**57,575**	**59,950**	**(2,375)**
Buy—						
U.S. dollar	**20,021**	**20,274**	**253**	**186,433**	**188,789**	**2,356**
Foreign currency options contracts:						
Sell—						
Call U.S. dollar	**26,843**			**249,958**		
	[419]	**841**	**(422)**	**[3,902]**	**7,831**	**(3,929)**
Call Euro	**690**			**6,425**		
	[13]	**7**	**6**	**[121]**	**65**	**56**
Call CAN dollar	**855**			**7,962**		
	[7]	**28**	**(21)**	**[65]**	**261**	**(196)**
Buy—						
Put U.S. dollar	**21,626**			**201,378**		
	[336]	**133**	**(203)**	**[3,129]**	**1,238**	**(1,891)**
Put Euro	**675**			**6,286**		
	[13]	**1**	**(12)**	**[121]**	**9**	**(112)**
Put CAN dollar	**855**			**7,962**		
	[6]	**2**	**(4)**	**[56]**	**19**	**(37)**

(b) As of March 31, 2004:

			Millions of yen
	Contract amount	*Fair value*	*Valuation gains (losses)*
Foreign currency options contracts:			
Sell—			
Call U.S. dollar	¥29,726		
	[398]	¥ 93	¥305
Buy—			
Put U.S. dollar	29,571		
	[398]	255	(143)

Note: The amounts in [brackets] are the carrying amounts of the premium on the option recorded as other current assets or liabilities.

(2) Interest rate contracts:

(a) As of March 31, 2005:
None.

(b) As of March 31, 2004:

			Millions of yen
	Contract amount	*Fair value*	*Valuation gains (losses)*
Interest swap contracts:			
Receive floating rate			
pay fixed rate	¥5,300	¥(74)	¥(74)

The method to determine fair value is based on quotations obtained from financial institutions.

Derivative financial instruments that qualify as a hedge and are accounted for using the deferred hedge accounting method are excluded from the above table according to the disclosure requirements.

21. Segment Information

Information by industry segment

The Company and consolidated subsidiaries operate principally in four industry segments: automobiles, industrial products, aerospace and other business fields (including eco-related equipment).

A summary of net sales, operating income, assets, depreciation/amortization expenses and capital expenditures by industry segments for the years ended March 31, 2005, 2004 and 2003 was shown below:

Net sales:

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	*2003*	***2005***
Net sales:				
Automobiles—				
Outside customers	**¥1,319,603**	¥1,316,951	¥1,229,807	**$12,287,950**
Intersegment	**4,069**	3,847	3,231	**37,890**
Subtotal	**1,323,672**	1,320,798	1,233,038	**12,325,840**
Industrial products—				
Outside customers	**46,814**	42,257	41,586	**435,925**
Intersegment	**307**	333	75	**2,859**
Subtotal	**47,121**	42,590	41,661	**438,784**
Aerospace—				
Outside customers	**59,434**	56,632	63,009	**553,441**
Intersegment	**40**	218	76	**372**
Subtotal	**59,474**	56,850	63,085	**553,813**
Other—				
Outside customers	**20,640**	23,611	37,935	**192,196**
Intersegment	**2,994**	3,284	3,526	**27,880**
Subtotal	**23,634**	26,895	41,461	**220,076**
Total	**1,453,901**	1,447,133	1,379,245	**13,538,513**
Corporate and elimination	**(7,410)**	(7,682)	(6,908)	**(69,000)**
Consolidated total	**¥1,446,491**	¥1,439,451	¥1,372,337	**$13,469,513**

Segment profit or loss:

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	*2003*	***2005***
Operating income (loss):				
Automobiles	**¥40,942**	¥52,114	¥67,307	**$381,246**
Industrial products	**849**	(299)	(866)	**7,906**
Aerospace	**195**	(327)	3,359	**1,816**
Other	**(590)**	(1,482)	(3,114)	**(5,494)**
Total	**41,396**	50,006	66,686	**385,474**
Corporate and elimination	**621**	318	835	**5,782**
Consolidated total	**¥42,017**	¥50,324	¥67,521	**$391,256**

Assets:

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2005	*2004*	*2003*	***2005***
Total assets:				
Automobiles	**¥1,136,372**	¥1,139,138	¥1,140,525	**$10,581,730**
Industrial products	**57,611**	57,432	55,793	**536,465**
Aerospace	**127,548**	109,684	101,130	**1,187,709**
Other	**74,449**	76,695	75,360	**693,258**
Total	**1,395,980**	1,382,949	1,372,808	**12,999,162**
Corporate and elimination	**(38,521)**	(33,222)	(28,736)	**(358,702)**
Consolidated total	**¥1,357,459**	¥1,349,727	¥1,344,072	**$12,640,460**

Other significant items:

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2005	*2004*	*2003*	***2005***
Depreciation/amortization expenses:				
Automobiles	**¥ 64,630**	¥ 65,486	¥ 61,743	**$ 601,825**
Industrial products	**1,999**	2,115	2,133	**18,615**
Aerospace	**1,912**	1,712	1,772	**17,804**
Other	**2,469**	1,799	2,248	**22,991**
Total	**71,010**	71,112	67,896	**661,235**
Corporate and elimination	**—**	—	—	**—**
Consolidated total	**¥ 71,010**	¥ 71,112	¥ 67,896	**$ 661,235**
Capital expenditures for segment assets:				
Automobiles	**¥135,972**	¥118,591	¥111,584	**$1,266,151**
Industrial products	**1,013**	852	3,551	**9,433**
Aerospace	**2,614**	2,893	1,284	**24,341**
Other	**8,160**	5,690	3,004	**75,985**
Total	**147,759**	128,026	119,423	**1,375,910**
Corporate and elimination	**—**	—	—	**—**
Consolidated total	**¥147,759**	¥128,026	¥119,423	**$1,375,910**

Notes: 1. Definition of business segments:
Business segments are defined based on product line and market.

2. Main products by each business segment:

Business Segment	*Main Products*
Automobiles	*Legacy, Impressa, Forester, R1, R2, Pleo, Samber*
Industrial products	*Robin engine, power generators, pumps*
Aerospace	*Aircraft, parts of space-related devices*
Other	*Garbage collection vehicles, specialized vehicles, real estate leasing*

3. All operating costs and expenses are allocated to each business segment.

4. All figures in corporate and elimination represent elimination.

5. "Rail cars" and "buses" are excluded from the main products of the Other segment as a result of the termination of the operation of Bus and Train Production by March 31, 2003.

6. "Houses" are excluded from the main products of the Other segment as a result of the transfer of the business to a non-consolidated subsidiary, which is accounted for by the equity method, on April 1, 2004.

7. Changes of accounting policies:

(Fiscal 2005)

Method of hedge accounting

As stated in the "Summary of Significant Accounting Policies," the Company stopped applying hedge accounting from the fiscal year 2005. As a result of this change, net sales and operating income increased by ¥133 million (US$1,238 thousand) in the Automobile segment and ¥8 million (US$74 thousand) in the Industrial Products segment as compared with the amounts resulting from the application of the previous hedge accounting policy.

(Fiscal 2004)

Revenue recognition

The Company changed the revenue recognition policy for the Aerospace division's production contracts with the production term exceeding one year and the amount of each contract exceeding ¥5,000 million, from the delivery basis to the percentage-of-completion method from the fiscal year ended March 31, 2004. As a result of the change, in the Aerospace segment, net sales increased by ¥4,013 million and operating income increased by ¥231 million as compared with amounts resulting from the application of the previous policy.

(Fiscal 2003)

None.

8. The introduction of the "Corporation Size-Based Enterprise Tax System":

As stated in the "Summary of Significant Accounting Policies," the "Corporation Size-Based Enterprise Tax System" for enterprise taxes was introduced from the fiscal year ended March 31, 2005. As a result, operating expenses increased by ¥881 million (US$8,204 thousand) in the Automobile segment, ¥46 million (US$428 thousand) in the Industrial Products segment , ¥61 million (US$568 thousand) in the Aerospace segment and ¥21 million (US$196 thousand) in the Other segment, and operating income decreased by the same amount as compared with the previous fiscal year.

Information by geographic area

A summary of net sales, operating income and assets by geographic area for the years ended March 31, 2005, 2004 and 2003 was shown below:

Net sales:

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	*2003*	***2005***
Net sales:				
Japan—				
Outside customers	**¥ 886,793**	¥ 840,330	¥ 786,257	**$ 8,257,687**
Intersegment	**241,860**	263,260	295,900	**2,252,165**
Subtotal	**1,128,653**	1,103,590	1,082,157	**10,509,852**
North America—				
Outside customers	**544,753**	590,271	582,326	**5,072,661**
Intersegment	**2,027**	1,692	1,971	**18,875**
Subtotal	**546,780**	591,963	584,297	**5,091,536**
Other—				
Outside customers	**14,945**	8,850	3,754	**139,166**
Intersegment	**391**	344	231	**3,641**
Subtotal	**15,336**	9,194	3,985	**142,807**
Total	**1,690,769**	1,704,747	1,670,439	**15,744,195**
Corporate and elimination	**(244,278)**	(265,296)	(298,102)	**(2,274,682)**
Consolidated total	**¥1,446,491**	¥1,439,451	¥1,372,337	**$13,469,513**

Segment profit or loss:

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars*
	2005	*2004*	*2003*	***2005***
Operating income:				
Japan	**¥40,517**	¥37,670	¥57,136	**$377,288**
North America	**(6,678)**	1,071	15,824	**(62,185)**
Other	**367**	259	127	**3,418**
Total	**34,206**	39,000	73,087	**318,521**
Corporate and elimination	**7,811**	11,324	(5,566)	**72,735**
Consolidated total	**¥42,017**	¥50,324	¥67,521	**$391,256**

Assets:

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2005	2004	2003	**2005**
Assets:				
Japan	**¥1,080,303**	¥1,077,341	¥1,020,224	**$10,059,624**
North America	**307,858**	309,842	373,125	**2,866,729**
Other	**2,439**	2,102	1,141	**22,711**
Total	**1,390,600**	1,389,285	1,394,490	**12,949,064**
Corporate and elimination	**(33,141)**	(39,558)	(50,418)	**(308,604)**
Consolidated total	**¥1,357,459**	¥1,349,727	¥1,344,072	**$12,640,460**

Notes: 1. Geographic areas are based on geographical proximity.
2. Principal countries or districts in each geographic area:
North America: United States and Canada
Other: Europe
3. All operating costs and expenses are allocated to each segment.
4. All figures in corporate and elimination represent elimination.
5. Changes of accounting policies:
(Fiscal 2005)
Method of hedge accounting
As stated in the "Summary of Significant Accounting Policies," the Company stopped applying hedge accounting from the fiscal year 2005. As a result of this change, net sales and operating income increased by ¥141 million (US$1,313 thousand) in the Japan segment as compared with amounts resulting from the application of the previous hedge accounting policy.
(Fiscal 2004)
Revenue recognition
The Company changed the revenue recognition policy for the Aerospace division's production contracts with the production term exceeding one year and the amount of each contract exceeding ¥5,000 million, from the delivery basis to the percentage-of-completion method from the fiscal year ended March 31, 2004. As a result of the change, in the Japan segment, net sales increased by ¥4,013 million and operating income increased by ¥231 million as compared with amounts resulting from the application of the previous policy.
(Fiscal 2003)
None.
6. The introduction of the "Corporation Size-Based Enterprise Tax System":
As stated in the "Summary of Significant Accounting Policies," the "Corporation Size-Based Enterprise Tax System" for enterprise taxes was introduced from the fiscal year ended March 31, 2005. As a result, operating expense increased by ¥1,009 million (US$9,396 thousand) in the Japan segment and operating income decreased by the same amount as compared with the previous fiscal year.

Overseas sales

Overseas sales for the years ended March 31, 2005, 2004 and 2003 were summarized as follows:

	Millions of yen		Millions of yen		Millions of yen		Thousands of U.S. dollars
	2005		2004		2003		**2005**
Overseas sales:							
North America	**¥ 593,249**	**41.0%**	¥ 624,372	43.4%	¥ 622,783	45.4%	**$ 5,524,248**
Europe	**117,826**	**8.2**	101,049	7.0	72,841	5.3	**1,097,178**
Other	**108,357**	**7.5**	86,113	6.0	77,453	5.6	**1,009,005**
Total	**¥ 819,432**	**56.7%**	¥ 811,534	56.4%	¥ 773,077	56.3%	**$ 7,630,431**
Consolidated net sales	**¥1,446,491**	**100.0%**	¥1,439,451	100.0%	¥1,372,337	100.0%	**$13,469,513**

Notes: 1. Geographic areas are based on geographical proximity.
2. Principal countries or districts in each geographic area:
North America: United States and Canada
Europe: Germany, Switzerland and England
Other: Australia
3. Overseas sales are sales outside of Japan by the Company and consolidated subsidiaries.
4. Changes of accounting policies:
(Fiscal 2005)
Method of hedge accounting
As stated in the "Summary of Significant Accounting Policies," the Company stopped applying hedge accounting from the fiscal year 2005. As a result of this change, net sales increased by ¥56 million (US$521 thousand) in the North America segment and ¥85 million (US$792 thousand) in the Europe segment as compared with amounts resulting from the application of the previous hedge accounting policy.
(Fiscal 2004)
None.
(Fiscal 2003)
None.

Independent Auditors' Report

To the Board of Directors of
FUJI HEAVY INDUSTRIES LTD.

We have audited the accompanying consolidated balance sheets of FUJI HEAVY INDUSTRIES LTD. ("the Company") and consolidated subsidiaries as of March 31, 2005 and 2004, and the related consolidated statements of income, shareholders' equity and cash flows for each of the three years in the period ended March 31, 2005, expressed in Japanese yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to independently express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and subsidiaries as of March 31, 2005 and 2004, and the consolidated results of their operations and their cash flows for each of the three years in the period ended March 31, 2005, in conformity with accounting principles generally accepted in Japan.

Without qualifying our opinion, we draw attention to the following.

(1) As discussed in Note 2 to the consolidated financial statements, the Company stopped applying the hedge accounting for foreign exchange contracts in fiscal year 2005.

(2) As discussed in Note 2 to the consolidated financial statements, the Company changed the method of the revenue recognition policy for Aerospace Division's production contracts in fiscal year 2004.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2005 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 1 to the consolidated financial statements.

KPMG AZSA & Co.

Tokyo, Japan
June 24, 2005

Consolidated Subsidiaries and Affiliates (As of March 31, 2005)

JAPAN

Fuji Robin Industries Ltd. (58.1%)
Manufacture, service, and sales of agricultural/forestry equipment, engines, fire pumps, and related parts
http://www5.mediagalaxy.co.jp/fujirobin/

Fuji Machinery Co., Ltd. (69.5%)
Manufacture and sales of automobile parts and industrial product parts
http://www.fuji-machinery.co.jp/

Ichitan Co., Ltd. (51.0%)
Manufacture and sales of forged automobile/industrial product parts
http://www.ichitan.co.jp/

Kiryu Industrial Co., Ltd. (97.5%)
Manufacture of Subaru specially equipped automobiles and distribution of Subaru automobile parts
http://www.kiryu-kougyo.co.jp/

Subaru Kosan Co., Ltd. (100.0%)
Sales and leasing of real estate and travel agency operations

Subaru UI Co., Ltd. (100.0%)
Refurbishment, distribution, and sales of used Subaru automobiles
http://www.subaru-ui.jp/

FICS Corporation (100.0%)
Distribution and service of Volvo automobiles

Subaru Finance Co., Ltd. (100.0%)
Leasing and rental of Subaru automobiles and equipment and credit, financing, accounting service, and sales of insurance
http://www.subaru-finance.co.jp/

Yusoki Kogyo K.K. (100.0%)
Manufacture and sales of parts for crane trucks and aerospace
http://www.yusoki.co.jp/

TOKYO SUBARU INC. (100.0%)
and 39 other dealerships
Distribution, sales, and service of Subaru automobiles
http://www.tokyo-subaru.co.jp/

OVERSEAS

Subaru of America, Inc. (100.0%)
and 10 subsidiaries
Subaru Plaza, 2235 Route 70 West, Cherry Hill, NJ 08002, U.S.A.
Phone: +1-856-488-8500
Fax: +1-856-488-3137
Distribution and sales of Subaru automobiles and parts
http://www.subaru.com/

Fuji Heavy Industries U.S.A. Inc. (100.0%)
and one subsidiary
c/o Subaru of America, Inc.
Subaru Plaza, 2235 Route 70 West, Cherry Hill, NJ 08002, U.S.A.
Phone: +1-856-488-8532
Fax: +1-856-488-9279
Distribution and sales of Subaru automobiles and parts to foreign countries

Subaru Research & Development, Inc.
3995 Research Park Drive, Ann Arbor, MI 48108, U.S.A.
Phone: +1-734-623-0075
Fax: +1-734-623-0076
Research and development of automobiles

Subaru of Indiana Automotive, Inc. (100.0%)
and one subsidiary
5500 State Road 38 East, Lafayette, IN 47905, U.S.A.
Phone: +1-765-449-1111
Fax: +1-765-449-6952
Manufacture of Subaru automobiles
http://www.subaru-sia.com/

Subaru of Taiwan Co., Ltd. (80.0%)
8F-1, No. 100, Sec. 2, Chung Hsiao E. Rd.,
Taipei, Taiwan
Phone: +886-2-8866-6630
Fax: +886-2-2832-4021
http://www.subaru-sot.com.tw/

Subaru Canada, Inc. (100.0%)
and one subsidiary
560 Suffolk Court, Mississauga, Ontario, Canada L5R 4J7
Phone: +1-905-568-4959
Fax: +1-905-568-8087
Distribution and sales of Subaru automobiles and parts
http://www.subaru.ca/

Subaru Europe N.V./S.A. (100.0%)
Hermesstraat 6C, 1930 Nossegem-Zaventem, Belgium
Phone: +32-2-714-0400
Fax: +32-2-725-7792
Distribution, sales and marketing of automobiles, parts and accessories

Robin Manufacturing U.S.A., Inc. (60.0%)
1201 Industrial Road, Hudson, WI 54016, U.S.A.
Phone: +1-715-381-5902
Fax: +1-715-381-5901
Manufacture and sales of general-purpose, four-wheel buggy and golf cart engines

Investor Information (As of March 31, 2005)

Head Office
Subaru Building, 7-2, Nishi-Shinjuku 1-chome, Shinjuku-ku,
Tokyo 160-8316, Japan
Phone: +81-3-3347-2111
Fax +81-3-3347-2338

Investor Relations Office
Subaru Building, 7-2, Nishi-Shinjuku 1-chome, Shinjuku-ku,
Tokyo 160-8316, Japan
Phone: +81-3-3347-2655
Fax: +81-3-3347-2295

Established
July 15, 1953

Paid-in Capital
¥153,795 million

Number of Shareholders
46,007

Number of Common Stock Issued and Outstanding
782,865,873

Domestic Manufacturing Divisions
Gunma Manufacturing Division (Automobile Division)
Utsunomiya Manufacturing Division (Aerospace Division and Eco technologies Division)
Saitama Manufacturing Division (Industrial Products Division)

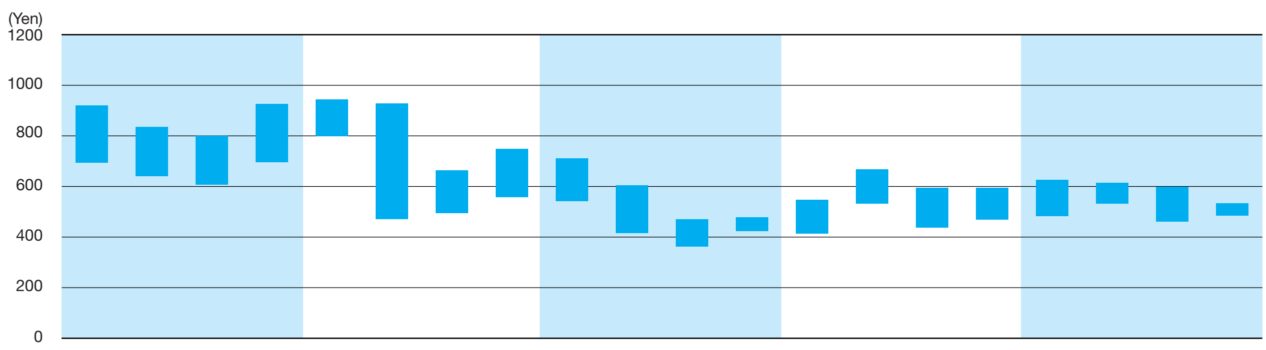
Major Shareholders
General Motors of Canada Limited
Japan Trustee Services Bank, Ltd.
The Chase Manhattan Bank, N.A. London
The Master Trust Bank of Japan, Ltd.
Mizuho Corporate Bank, Ltd.
Depositary Nominees Inc.
Nippon Life Insurance Company
Suzuki Motor Corporation
Sompo Japan Insurance Inc.
Northern Trust Company (AVFC) Sub-account American Client

Stock Listings
Tokyo Stock Exchange

Transfer Agent
Mizuho Trust & Banking Co., Ltd.
2-1, Yaesu 1-chome, Chuo-ku, Tokyo 103-8670, Japan

Web Site Address
http://www.fhi.co.jp/english/

Quarterly Common Stock Price Range (Tokyo Stock Exchange)



FY	2001	2002	2003	2004	**2005**
High	¥925	¥944	¥712	¥668	**¥627**
Low	608	471	362	414	**462**

FUJI HEAVY INDUSTRIES LTD.
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Shinjuku-ku, Tokyo 160-8316, Japan

http://www.fhi.co.jp/english/

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