# Interim Financial Report
# Speech by President Takenaka

I'm Kyoji Takenaka.
Thank you very much for taking time out of your busy schedule to attend this meeting today.
First I'm going to give you a brief overview of our activities for the first half of this fiscal year. Mr. Takagi will then talk about our interim results in more detail.

**<Dissolution of Alliance with GM and a New Business Collaboration with Toyota>**

As you are already aware, last month Fuji Heavy Industries (FHI) dissolved its strategic alliance and capital relationship with General Motors Corporation (GM) that had lasted for 6 years and reached an agreement with Toyota Motor Corporation (Toyota) to form a new business collaboration. GM sold 68 million shares to Toyota out of its 157 million shares which comprised a 20.1% stake in FHI, making Toyota the top shareholder in FHI. GM sold the remaining 89 million shares through open market sales. FHI bought back 62 million of its own shares and is holding them as treasury stocks. We have not decided what to do with these treasury stocks yet.

While our business collaboration with Toyota has been widely reported in the media, FHI and Toyota have so far only set up a joint steering committee to study possible joint projects that will produce synergistic effects for meeting the R&D and production challenges facing our automobile divisions, and are now just finalizing the details of the alliance. We can not announce anything specific at this moment, but once we are finished hammering out all the details, I will set up a meeting to share some of information with you.
As I have said before, we can definitely learn a lot from Toyota's superior management strategies and techniques. These will be helpful to highlight the unique characteristics of Subaru products and actively adopt any aspects we can learn from their management, development and sales techniques in order to get the most mileage out of our alliance.

**<Overview of Interim Financial Results>**

Now I will give you a brief overview of our interim financial results. Mr. Takagi will give you a more detailed explanation later.
We saw a slight increase in our financial performance for the first half of this fiscal year to which we recently announced some revisions. Although our fist-half results

significantly exceeded our forecast made at the beginning of the year, in terms of year-on-year basis, we saw a decrease in sales, ordinary income, and net income while operating income increased.

First-half sales dropped by 3.4% on a year-on-year basis. Although the lackluster performance in domestic sales of minicars was offset by robust sales in Europe and Australia, the net sales decline was caused mainly by no sales to Saab/GM in addition to the end of consignment production for Isuzu at our production facility in the U.S.

The depreciation of yen, which fell in value from 105 to 109 yen against the US dollar on the foreign exchange market, is not only the factor to increase operating profit from our forecast in May, but also progress in our Total-Cost Structure Revolution (TSR), reducing overall costs at both FHI and SIA more than our projection, is another factor. More specifically, we cut material costs by approximately 3 billion yen. Our streamlining efforts in the area of R&D as well as efforts to reduce SG&A expenses resulted in successfully reducing overall costs. This shows that TSR, which is the primary focus of our revised FDR-1, has already been proven effective. We have worked on TSR with clear goals in mind, to reduce material costs for our new models and the next-generation models, FMC, which are currently under development as well as for cars currently being manufactured. I am confident that we are making giant strides forward through the collaborative efforts of the product planning, development and manufacturing divisions.

Our cost reduction efforts made up for lost sales and deterioration of the product mixture in the domestic market. Consequently we reaped an operating income of 17.4 billion yen, which significantly exceeded our initial projection of 4 billion yen.

Ordinary income fell by 1.6 billion yen due to foreign exchange losses. As we announced earlier, net income for this period was down by 0.3 billion yen to 8 billion yen due to a 5.6 billion yen extraordinary loss derived from the discontinuation of the joint development project with GM.

Despite the current trend in foreign exchange rates, with the Japanese yen being weaker than our projection at the beginning of the year, domestic sales still remain lackluster due to a decreased number of minicar sales and deteriorated product mixture for passenger cars. We are also facing flagging sales in the U.S. market due to rising oil prices and the downward trend in overall demand as well as increases in material costs both in Japan and overseas. We created some leeway for these unpredictable factors in our forecast for fiscal year ending March 31, 2006 and revised only the operating income upward 3 billion yen to 39 billion yen.

**<Progress of Revised FDR-1>**

As I briefed you back in May, we revised our FDR-1 medium-term business plan in order to spur a turnaround toward increased profitability. We are working on five strategic goals for improving our financial health over the next two years.

We are already seeing some results of our efforts to achieve the first of these five goals, “Urgent Total Cost Reduction.” We are enthusiastically moving forward with other goals to “Restructure Product Planning” and to “Restructure the Sales Process and Network,” making this year a period for preparation in order to achieve specific goals next year.

**<Streamlining Corporate Structure>**

Today I would like to explain our initiatives for meeting the challenge of streamlining our corporate structure.

Since we started our FDR-1 three years ago, we have been working on operational restructuring that led to withdraw from the railway vehicle and bus businesses and terminate other underperforming businesses including those of our subsidiaries. We believe that continuing to place more emphasis on profitable businesses is one of our top priorities.

After going the extra mile to save jobs through group-wide cooperation, we still found ourselves drowning in a pool of surplus labor. We have been working to find the best solution to this issue through group-wide efforts involving our subsidiaries since the beginning of this year.

Our revised FDR-1 plan is designed to cut out the fat, build up the muscle and transform the entire FHI group into a lean, mean, smooth-running organization.

Our subsidiaries announced at the shareholders’ meeting in June that they reduced the number of board members by 13% from 125 to 109 and are working to enhance productivity even more.

At the same time, we are aware that the personnel composition of our company is unbalanced. The high percentage of employees who are 50 years of age or older results in higher labor costs and poses a problem to corporate vitality.

In light of this situation, we have decided to cut back the number of employees by 1,000 through 1) voluntary early retirement coupled with a reemployment and career change assistance program and 2) promoting the permanent transfer of employees who are on loan. The purpose of these measures is to optimize the personnel composition and labor costs, to foster a corporate climate that elicits a sense of urgency, and to create vitality among our employees.

We will solicit voluntary retirement mainly among employees over 45 years old toward the end of January next year, thereby reducing the workforce by 5% or 700 people.
Among the approximately 1,100 employees currently loaned to our affiliated companies we will permanently transfer 300 employees who are either 50 years of age or older or on loan for a long-term period to the companies they are assigned to. This will be completed by the end of March next year.

In implementing these measures we will offer an extra retirement payment and career change assistance through outplacement service providers to those who accept voluntary retirement in order to facilitate the launch of their new careers. In promoting transfers of loaned employees to our affiliate companies, we will offer them a certain incentive to make up for any pay gap in an effort to help make their second career more fulfilling. Costs to be incurred from these measures have already been included in our second-half forecast.

We will continue to strive to clear the hurdles we face one by one in order to ensure the successful implementation of our revised FDR-1 plan. I would like to ask for your continued support in the years to come.

Now, Senior Vice President Takagi will talk in greater detail about the financial results. Thank you.