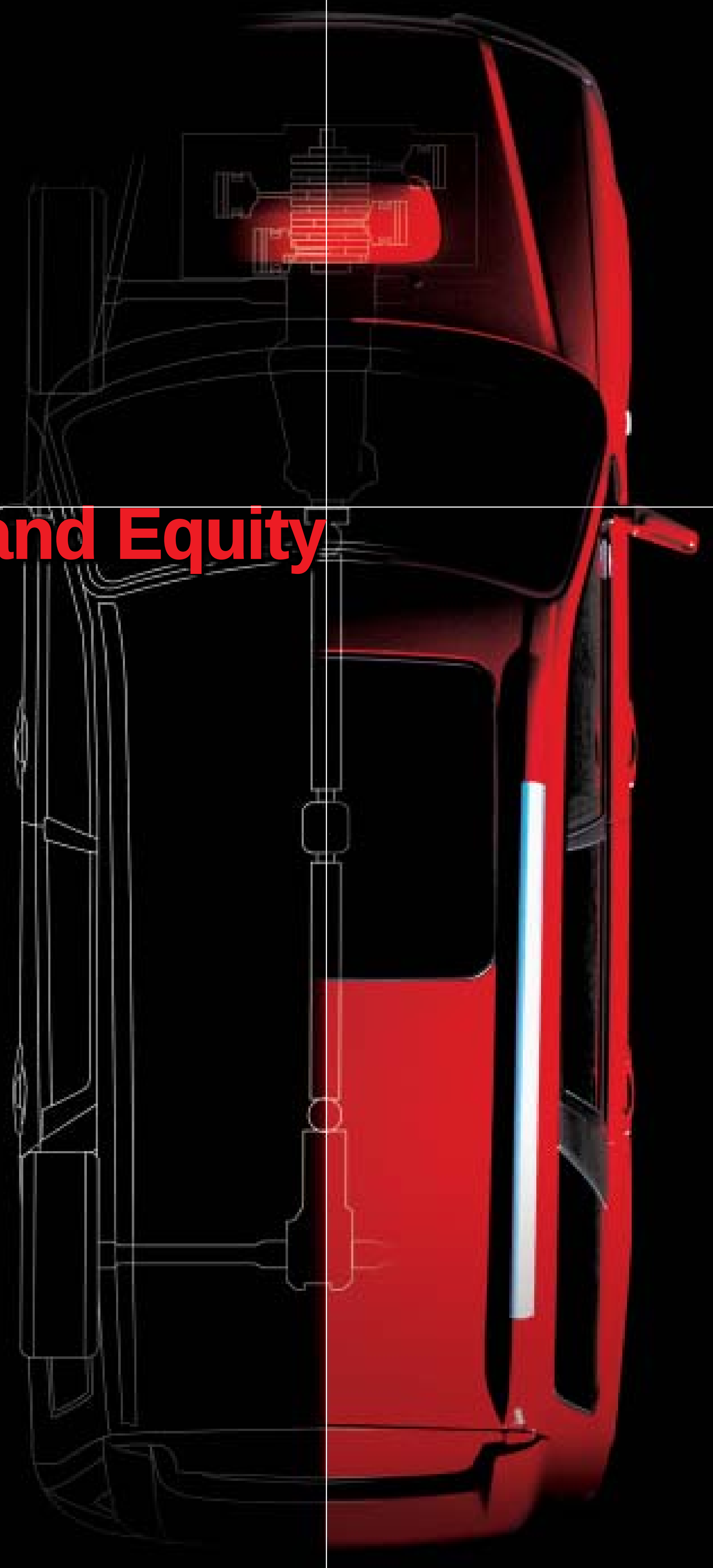
FUJI HEAVY INDUSTRIES LTD.

Annual Report 2002

For the year ended March 31, 2002

FUJI HEAVY INDUSTRIES LTD. Annual Report 2002

Focusing on
Our New Brand Equity



FHI's Brand Names

Subaru: Adopted in March 1958, Subaru refers to a group of stars also known by its original Japanese name *mutsura-boshi,* or series of six stars. This group of stars—known in Western countries as the Pleiades—belongs to the Taurus constellation and is the basis of the Subaru trademark. Subaru automobiles were the first to bear a name derived from the Japanese language.

Robin: Adopted in May 1956 and registered as an official trademark in July 1960, Robin is used for FHI general-purpose engines. The Robin trademark, with its lovely design of the diligent *komadori,* or Japanese robin, is known the world over.

Profile

Since its establishment in 1953, Fuji Heavy Industries Ltd. (FHI) has steadily grown as a comprehensive transportation machinery company, manufacturing and marketing the Subaru brand of automobiles, aircraft, and other vehicles, as well as the Robin brand of industrial machinery. Constantly in pursuit of superior mobility, the Subaru brand—with such distinct features as horizontally opposed engines and symmetrical all-wheel-drive systems—has attracted a multitude of supporters worldwide with its unique appeal. Always striving to be "a global player with premium brands," in June 2002, FHI converted to a new holding-company-style structure based primarily on its automotive business. Under this new framework, the aerospace, industrial products, and eco-technologies businesses are established as individual internal companies. FHI will continue to supply the products that satisfy its customers, while at the same time enhancing its efforts to meet today's demand for environmental protection, and will positively contribute to society through all of its future business endeavors.

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, 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.

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Consolidated Financial Highlights

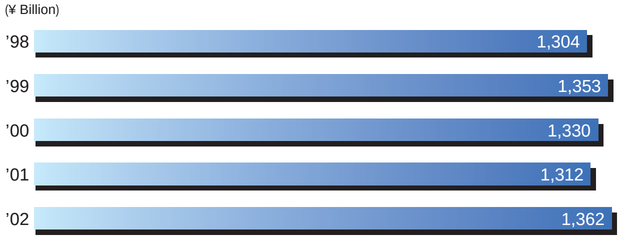
FUJI HEAVY INDUSTRIES LTD. AND CONSOLIDATED SUBSIDIARIES
Years ended March 31, 2002, 2001 and 2000

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars (Note)*
	2002	*2001*	*2000*	***2002***
For the year:				
Net sales	**¥1,362,493**	¥1,311,887	¥1,330,125	**$10,225,088**
Operating income	**88,480**	81,673	91,401	**664,015**
Net income	**30,283**	22,628	31,348	**227,265**
At year-end:				
Shareholders' equity	**¥ 396,112**	¥ 357,455	¥ 206,404	**$ 2,972,698**
Total assets	**1,269,558**	1,168,501	1,038,558	**9,527,640**
Per Share (in yen and U.S. dollars):				
Net income	**¥40.74**	¥30.44	¥51.90	**$0.31**
Return on equity	**8.0%**	8.0%	15.4%	

Note: U.S. dollar figures have been translated from yen, for convenience only, at the rate of ¥133.25 to US$1.00, the approximate rate of exchange at March 31, 2002.

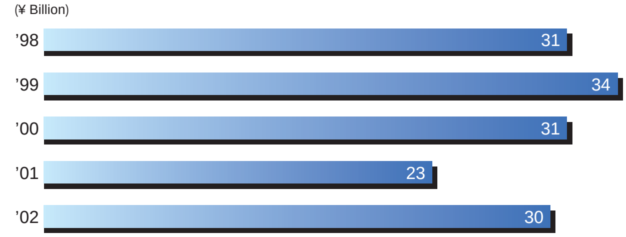
Net Sales (Years ended March 31)

(¥ Billion)



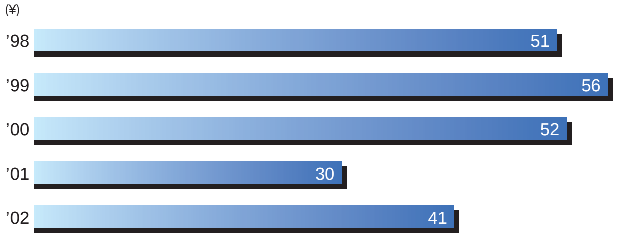
Net Income (Years ended March 31)

(¥ Billion)



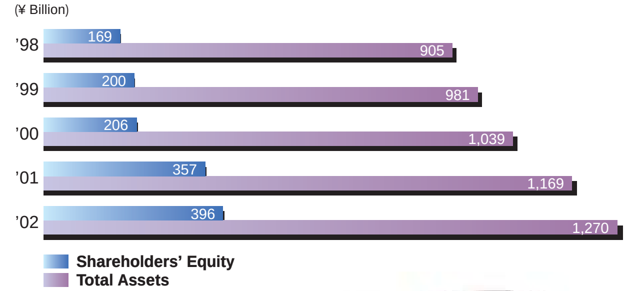
Net Income per Share (Years ended March 31)

(¥)



Shareholders' Equity and Total Assets

(¥ Billion)



To the Stakeholders of Fuji Heavy Industries Ltd.

Takeshi Tanaka
Chairman and CEO

Kyoji Takenaka
President and COO

Earnings for fiscal 2002

During fiscal 2002, ended March 31, 2002, the environment surrounding Fuji Heavy Industries Ltd. (FHI) grew even more severe. Japan's economic malaise persisted as consumer spending and employment conditions remained weak, and further decline was witnessed in stock prices and private sector capital investment. The September 11 terrorist attacks in the United States further exacerbated the situation, giving rise to concern over deepening economic recession.

Against this backdrop, despite a decline in Subaru unit sales volumes in both the domestic and European markets, consolidated net sales for the fiscal year increased 3.9%, to ¥1,362.4 billion, due to the strength of North American sales and favorable currency exchange rates during the term. Increases in selling costs and declines in domestic and European sales were compensated for by cost-cutting measures and favorable exchange rates, and operating income increased 8.3%, to ¥88.4 billion. Net income for the year climbed 33.8%, to ¥30.2 billion. This was due in large part to two factors that negatively influenced net income in the previous fiscal year: deferred taxes and the full amortization of net pension and severance obligations. The absence of these factors more than offset the recognition of losses on the valuation of investment securities and costs relating to affiliated companies' withdrawal from certain businesses.

Analyzed by individual segment, in the core Automobile Division, sales grew 4.5%, to ¥1,222.7 billion, and operating income increased 4.2%, to ¥85.6 billion. Strong sales in the North American market, which increased to 207 thousand units, contributed significantly to these results. In the Japanese market, we launched the Traviq seven-seater passenger wagon and added the GT30 (six-cylinder engine touring wagon) and the RS30 (six-cylinder engine B4 sedan) to our flagship Legacy lineup. These efforts to expand sales were further augmented by the introduction of the All-New Forester in February 2002. However, as new introductions to our core product lines fell near the end of the term, overall registrations unfortunately slid 12.3%, to 108 thousand units. Total unit sales for the term, both domestic and overseas, declined 3.0%, to 543 thousand units.

Reconfiguring operations toward a company with even greater appeal and stronger market presence

FHI has worked tirelessly toward the attainment of its vision of being "an appealing company with strong market presence." It also pursues the redistribution of managerial resources through selectivity and concentration, the strengthening of consolidated global operations, and efficient and agile management toward the attainment of the medium-term business plan goal of being a "global player with premium brands." In May 2002, to implement more effective application of resources and proactive management, the Company drew up and unveiled its new medium-term plan. The details of this plan will be described later in this report, but in essence we have adopted a holding-company-style management strategy centered around the automotive business and established the Aerospace, Industrial Products, and Eco Technologies divisions as largely self-sustaining in-house companies. Under this strategy, we will significantly reduce costs by merging overlapping segments and integrating related operations and strive to provide unique Fuji Heavy products by concentrating resources on our areas of expertise and growing segments.

Furthermore, with regard to the environment—an extremely crucial issue for the automotive industry—we will make comprehensive efforts to reduce waste emission volumes. In addition, we will strive to decrease the emissions and increase the fuel efficiency and recyclability of our vehicles, along with engaging in the full-fledged development of hybrid cars.

The Company's efforts are dedicated to its foremost task of satisfying customers by providing advanced and unique products that are available only from Subaru and FHI in a variety of fields, including automobiles, aerospace, and industrial products. We will also work proactively to strengthen corporate governance, fulfill the expectations of our shareholders, customers, and all stakeholders, and focus the total strength of the Group toward increasing corporate value.

T. Tanaka

Takeshi Tanaka
Chairman and CEO

K. Takenaka.

Kyoji Takenaka
President and COO

By executing its new FDR-1 medium-term business plan, Fuji Heavy Industries Ltd. will strive to create superior premium brands and become a company with even greater individual identity.

President's Interview

Kyoji Takenaka

Q: The new Fuji Dynamic Revolution-1 (FDR-1) medium-term business plan, aimed at achieving FHI's 10-year vision, has now commenced. Please describe the philosophy behind it.

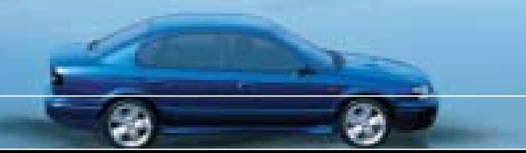
Takenaka: In 2003, FHI will celebrate the 50th anniversary of its establishment. After holding office as president for one year, I have taken part in numerous efforts that FHI has implemented to be a global player with premium brands. In the past decade, I witnessed numerous changes in social values and fully expect notions of value to change even further over the next decade. Although FHI has pursued product manufacturing based on its technological strength, I believe a slight change of focus to total human-oriented corporate activities is now required. We at FHI are now positioning ourselves to achieve our desired form. We will attain this form by converting from technologies that focus on material goods to technologies that resonate in peoples' hearts and minds, as well as by raising the premium on not only the added value of manufactured goods, but also the entire value chain that our automobile business and other divisions create. We have also added to these goals the attainment of top-ranking status in the categories in which we specialize, which we have compiled into our FDR-1 plan.

Under FDR-1, in pursuing the form that we seek to have attained in 10 years' time, we have set net sales targets for Japan and the United States of ¥1 trillion each. We will conduct planning, development, production, and sales for each market and assemble a customer-focused business framework. We have also set a 10-year ROA target of 10%, a recurring profit margin target of 10%, and an R&D investment target of ¥100 billion. I consider these figures to be the goals that will enable us to follow through with the next stage of growth by generating a continuous cycle in which revenue is secured and then invested in the next stage of new product creation.

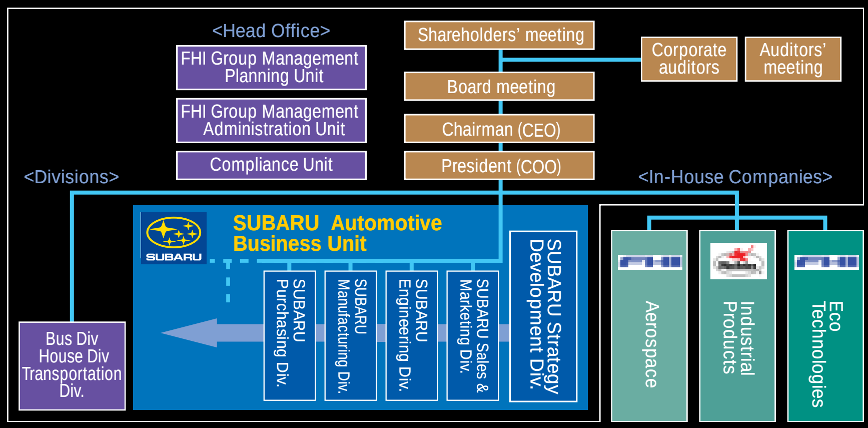
As one step toward our 10-year goal, our medium-term plan calls for a 35% increase in net sales, to ¥1,840 billion, and a 25% increase in operating income, to ¥110 billion, it also sets a unit sales volume of 760 thousand units for fiscal 2007, ending March 31, 2007. The plan is built upon the pillars of structural reform, brand strategy, manufacturing cost reform, creation of new core technologies, and the reform of corporate culture.

Q: What does the new holding company style organizational strategy entail?

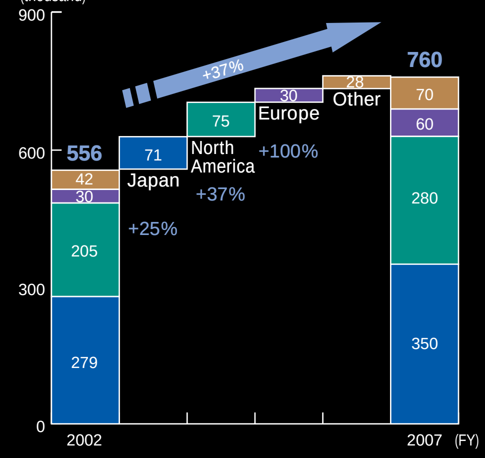
Takenaka: In today's world of dramatic fluctuations in business environments, speed in managerial decision making has become a critical issue. FHI had already adopted an executive officer system, but now, to further separate managerial and executive functions and accelerate decision making in a more organized manner, we have converted to a holding-company-style management strategy centered around the automotive business. We will place the Subaru Automotive Business Unit—which accounts for approximately 90% of our net sales—under the direct control of the head office. In addition, we will establish a Subaru Strategy Development Division and give that division cross-functional features so that we can take action along specific vectors in planning, development, production, and sales. In other business divisions, we have concentrated authority and appropriately distributed resources among those with independent growth potential and established the three in-house companies of Aerospace, Industrial Products, and Eco Technologies in preparation for the creation of new value chains. Regarding bus and railroad car operations, we have decided to withdraw from new vehicle production and retain these operations within the head office for conversion and reorganization into new businesses.



New Management Structure (The Holding-Company-Style Management Structure)



Targeted Sales by Region



Q: What are the premium brands being pursued by FHI?

Takenaka: In its product strategy, FHI is aiming to assemble world-class premium brands. The objective of our corporate activities is not simply greater quantity, but higher quality, strength, and growth in our operational foundation. In a group of 100 customers, premium brands would not necessarily be the products that satisfy the majority, but would be those that delight and leave a lasting impression on as few as 10. FHI aims to develop such products and to constantly propose solutions that will triumph in the competition for individuality. Brands are not composed of products alone. We must increase customer satisfaction from a variety of perspectives, including global services, supply of service parts, and the visual appeal of sales outlets. FHI will cast off the traditional perception that sees it as a purely technology-driven company, fuse design and technology together, leverage Subaru's unique qualities—both interior and exterior—and pursue individuality from a worldwide perspective as a global supplier.

Q: Please describe FHI's brand strategy.

Takenaka: In 2003, we will introduce the next-generation Legacy in Japan, and then roll it out all over the world, which we believe will be perfectly suited to the new value standard of the global market.

Next, we will introduce our new concept minicars. Subaru will not simply produce a model following the current market trends, but will bring out new minicars with premium value and individualism specific to the compact car category. We are targeting 2004 for the launch of these new cars. In the next stage, we will expand our introduction of new concept automobiles to the North American market. Given the volatility of currency exchange rates, we will strive to achieve business operations that are not affected by exchange rates and establish the foundation for United States–Japan bipolar operations. Through this framework, we will strive to develop locally designed, produced, and marketed products such as a crossover concept car that is one step above the Legacy that we will position as a flagship car for North America.

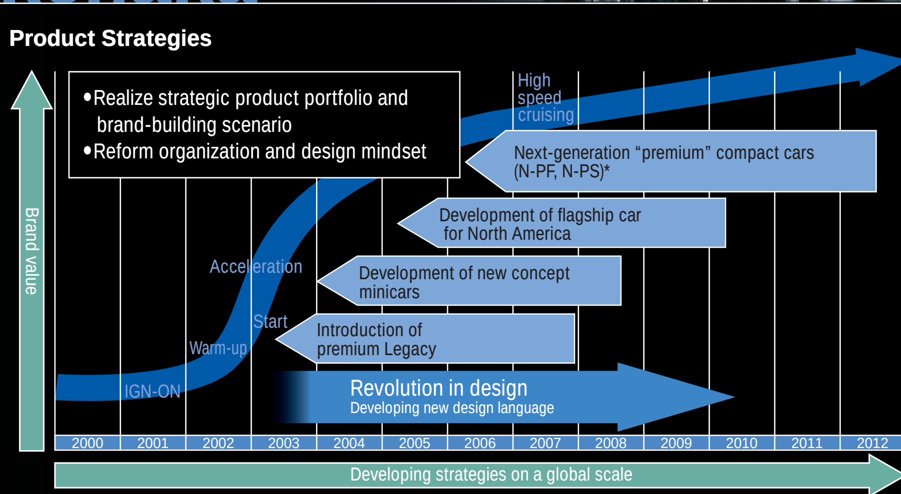
Previously, we have considered such strategic new cars as candidates for joint development with General Motors Corporation. However, with emphasis on respect for the individual identities of both the GM and Subaru brands, it was decided that joint development would best be leveraged in other concepts. Our aim is to further elevate the identity and added value of the Subaru brand and firmly establish its position in the market.

Not limited merely to joint development, the alliance with GM is a comprehensive and deeply rooted partnership. We expect to attain excellent results on the sales side in the North American market, particularly in the development of marketing and dealership operations in the Sunbelt region of the United States. We are also implementing a variety of other joint businesses, encompassing close cooperation not only in technology and development, but manufacturing and information as well.

FHI holds a 1% share of the world's 60 million unit automobile market. It is because our share is 1% that we are able to concentrate marketing efforts on our specialty segments and adopt coherent strategies. We face the tasks of emphasizing the merits of our small market share—promoting our quality over quantity—and implementing innovation in the three main pillars of our Subaru's individuality: the uniqueness of the Subaru driving experience, its safety, and its environmental soundness.

President's Interview

Kyoji Takenaka



*N-PF: Next-generation new platform
N-PS: Next-generation hybrid power source

Q: Please describe your marketing strategies to raise brand awareness.

Takenaka: On the sales side, we will strive to attain uniformity in the establishment of the Subaru brand in each region. There is a great difference in brand image in the northern and mid-southern regions of the United States, and we will work to upgrade the quality of our sales operations in those areas, thereby raising brand recognition in regions where it is currently low. To achieve this goal, we will add high performance lines to our existing crossover lines and fuse the two together. In Japan as well, as in the case of the Legacy, there is a significant difference in brand recognition between the Tokyo area and other regions. The key to the Japanese market is the reform of sales systems through incorporating IT tools. We are currently developing our Partner 21 System, which uses such IT tools to directly tie into customer needs and predict future requirements. With this system, we will provide equal quality service nationwide, from sales systems through to the supply of service parts. We will also establish customer centers as the focal point for data such as service information and concentrate customer interaction at these centers.

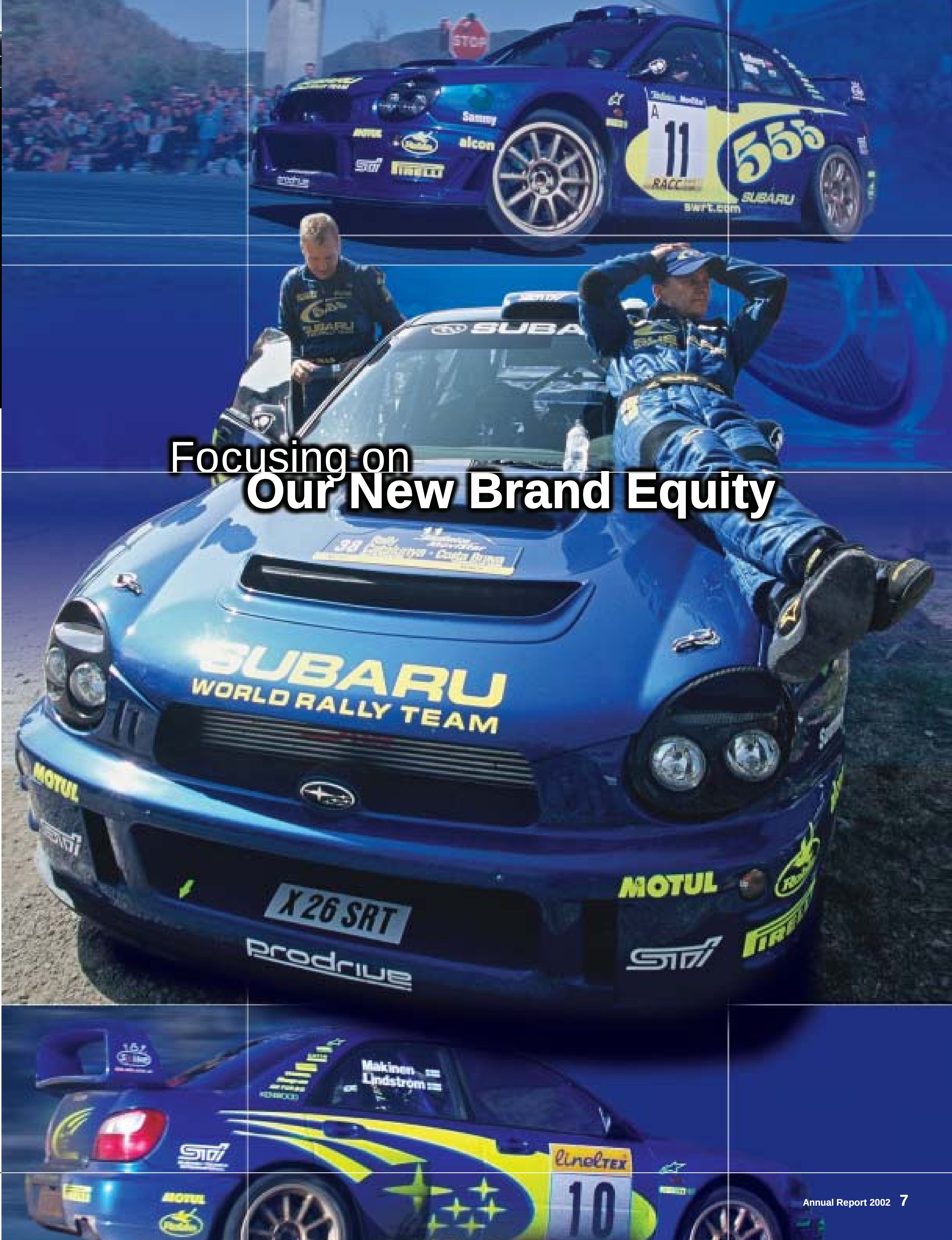
Sales volume for the North American market is currently just under 200 thousand units, but in pursuit of our 10-year goal, we aim to increase this to the 300 thousand unit level. As a comprehensive result of all of these efforts, we will strive to attain a 35% increase in sales volume, to 760 thousand units, by fiscal 2007.

Q: What is FHI's policy concerning hybrid cars, which are considered the key to the future of the automobile industry?

Takenaka: With the turning of the century, corporate efforts to protect the global environment are now a standard criterion for evaluation. In particular, demand is growing for new environmentally compliant power sources, and FHI has spent many years studying the feasibility of producing a hybrid car that retains the successful Subaru characteristics. The question has been whether we could deliver these essential characteristics along with the three fundamentals of driving performance, safety, and environmental friendliness. In other words, we have worked to achieve a hybrid car that not only contributes to environmental protection, but also retains the unique Subaru driving experience. The biggest challenge was the question of the battery. After a long period of joint development together with NEC Corp., we settled on the development of a manganese-lithium battery and have decided to establish a joint venture to make mass production feasible. FHI is aiming to develop a battery with 2.5 times the capacity of the nickel-hydride batteries used in most hybrid cars on the market today in terms of both energy density (cruising distance) and power density (torque). We also believe that these second-generation manganese-lithium batteries will aid the development of fuel cell units. We are aiming to make the new battery the de facto standard and have attracted the keen interest of the world's premier automakers.

In closing, I would like to add that the reforms that FHI is currently implementing will not be able to succeed without corresponding reforms to its corporate culture. These reforms are not merely additions to previous improvement efforts. We will thoroughly indoctrinate the three keywords of Innovative, Individual, and Courageous; implement selection, concentration, creation, and innovation; and strive to become an innovative and proactive Company.

Focusing on
Our New Brand Equity



The New Forester: The Embodiment of the Subaru Philosophy.

Hideki Ishido
Project General Manager
SUBARU Product & Portfolio Planning Division

Sales objectives and developmental philosophy of the new Forester

In February 2002, the Forester received its first full model change. The sales objectives and developmental philosophy of the new Forester can be summed up in our desire to bring the true value of the Forester and the essence of the Subaru brand to the world. We have always deeply infused every product we have developed with the Subaru philosophy, and our purpose in changing the Forester was to communicate this philosophy. Subaru's approach to automobiles and technology is that all technologies are meant to benefit humanity and must be rational and place top priority on functionality. Therefore, Subaru has its own philosophy on automobile production, the actualization of which requires core competence, design identity, and—above all—individuality. This mindset also sums up Subaru's brand philosophy. For example, the reason Subaru insists upon all-wheel drive is that years of research have shown that it is essential for safe, fast, and comfortable driving under any conditions, no matter the driver. It has therefore been adopted as Subaru's core competence.

The original Forester and Subaru's SUVs

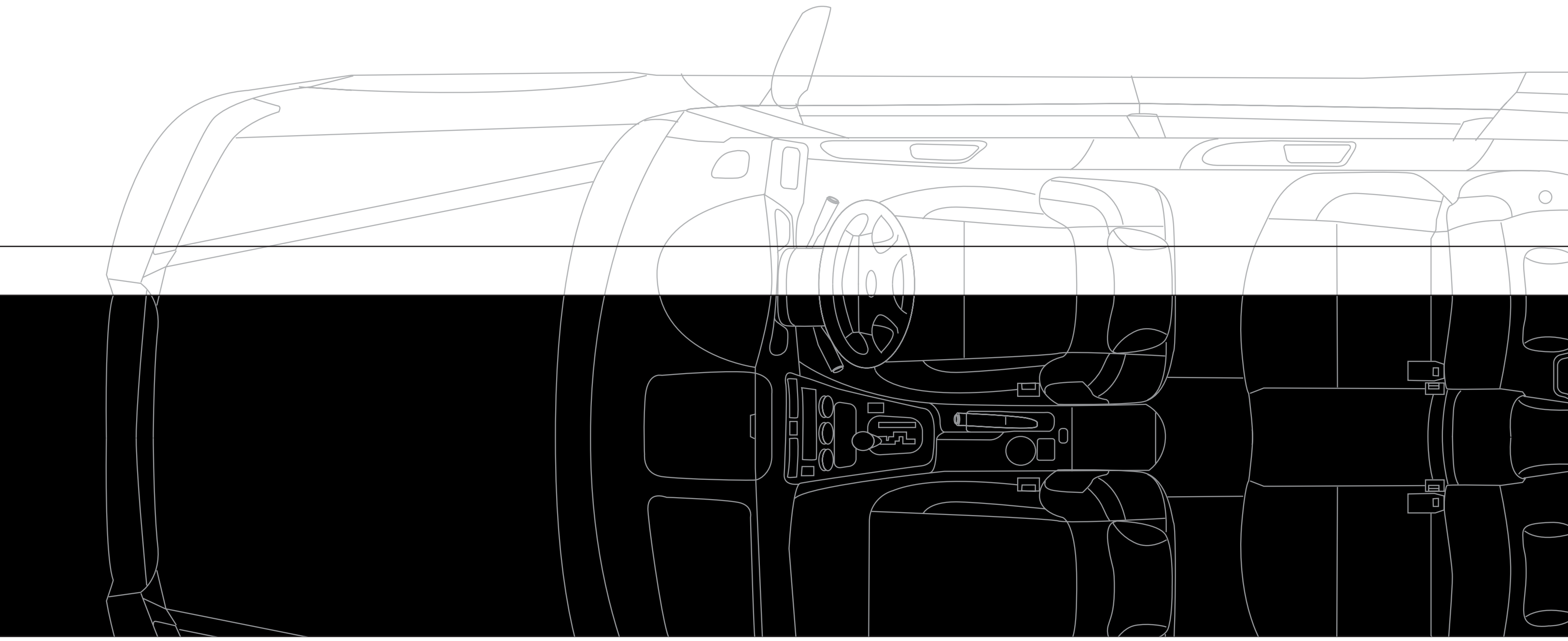
The original Forester was Subaru's first "trendy" product. However, that is not to say that we simply copied whatever happened to be popular at the time. Rather than mimic the SUVs on the U.S. market, we wanted to make an SUV with Subaru DNA, and sought to discover what that would be like. Further weighing of SUV merits under the scrutiny of the Subaru development ideals resulted in the first Forester. The advantages of SUVs lie in their superior drivabililty through high ground clearance and the sense of security from an elevated vantage point. By pursuing the "Best of Both" concept—incorporating the benefits of both SUVs and general passenger cars—Subaru has become acknowledged as the forerunner of the crossover segment of the U.S. automobile market.

The Forester is rooted in the original Subaru core technologies of low center of gravity, lateral symmetry, a horizontally opposed engine, and all-wheel drive, and it embodies all Subaru development criteria for the essential automobile functions of stable operation, collision safety, fuel efficiency, driving comfort, and handling. Hence, the Forester—a fully functional car with hitherto unknown vehicle height and original packaging—was born.

Striving for the ideal car for the 21st century: The new Forester

The new Forester retains all of the fundamental concepts of the original. From the outset, the Forester embodied an outstanding spirit of innovation and delivered all the fundamental functions of the ideal automobile—safety, speed, and comfort under any conditions—and was ultimately the most ideal vehicle to drive anywhere around the world. By enhancing these features in the second-generation


SUBARU
2XTN 880
California



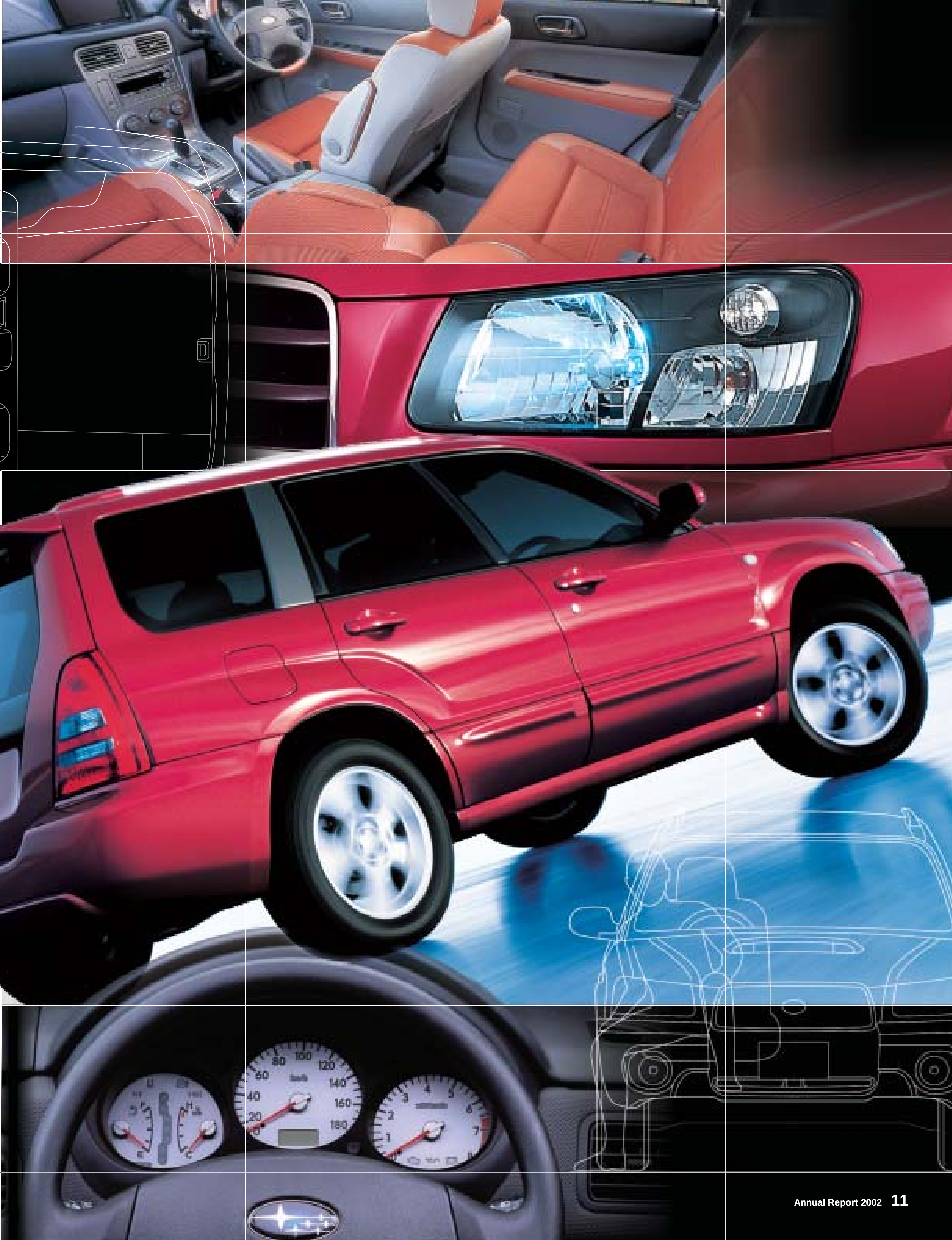
Forester, we drew forth its latent potential to be the ideal means of transportation for the 21st century and seized the opportunity to show the world the Forester's true value and the essence of the Subaru brand.

In designing the new model, we wanted to emphasize the Forester's superior features. We strove to evoke the idea that the Forester's superb performance is a form of beauty. Without pursuing the superiority of its design, neither development efforts nor the product's contributions to society will reach their fruition. It is well known that Subaru places priority on functionality, but with the new Forester, we heavily emphasized the improvement of the design quality of both its exterior and interior. We have also made improvements in the areas of safety and environment-friendliness, which are major demands of the current era and its markets. In basic features, we used a compact body that delivers light weight and efficient use of space and further enhanced comfort, primarily by improving handling and collision safety. For the Japanese market, we installed a faster and more responsive use turbo engine with outstanding fuel economy—the highest for a turbocharged model—while retaining top horsepower.

Aspiring to produce the world's No. 1 crossover sports vehicle

Although the Forester may appear to be a product that follows current trends, it is in fact quite different. It is the culmination of the essence of Subaru—the uncompromising pursuit of excellence in fundamental automobile functions—and its target market is formed of customers who want to share in this essence. Subaru's best customers are those who understand Subaru's individuality, philosophy, driving experience, and core technologies. Even if they account for only 20% of car buyers, our intention is to impart our philosophy to those customers who share Subaru's ideals, and we believe that the second-generation Forester is precisely the car to communicate Subaru's philosophy.

We are also planning to incorporate a turbo engine into the new Forester in all world markets and are determined to make it the world's top crossover sports vehicle. Our goal is to make the Forester not only the ideal means of transportation but also the world's top "triathlete."



Design Strategies for Establishing Premium Brands

Andreas Zapatinas

Chief Designer, Advanced Design

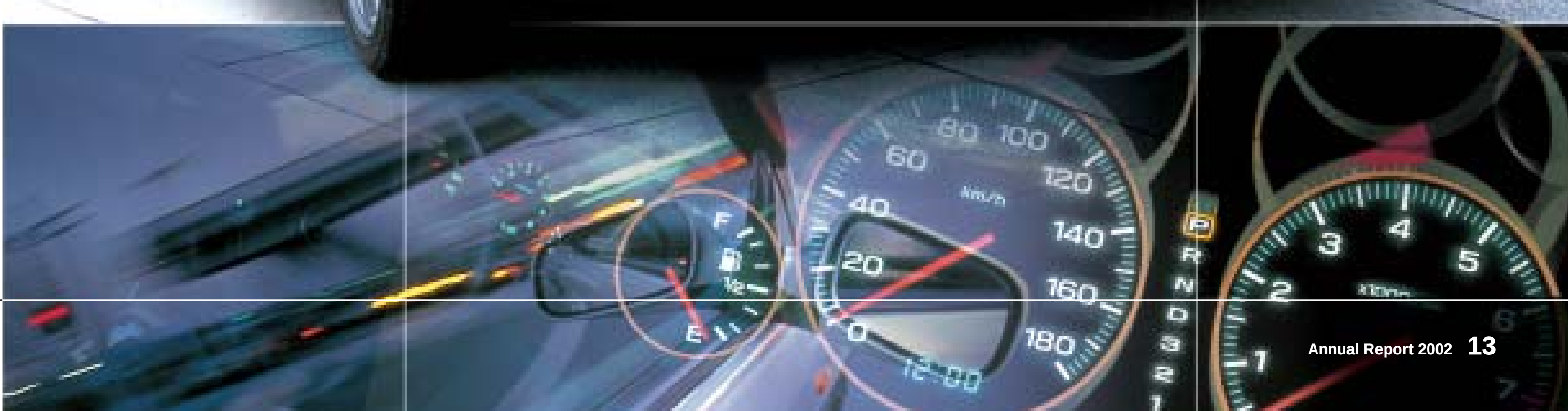
Born in Athens, Greece, in 1957. After working in the design departments of Pininfarina S.p.A., Fiat, and BMW, joined Alfa Romeo as Chief Designer in 1998. Worked on numerous design projects, including the 147 model that won the 2001 European Car of the Year and the 2001-2002 Import Car of the Year (Japan).

In order to sell customers on a brand image and to strengthen it, a company must continually provide a consistent message, encompassing not only the product itself, but also the design, advertising, promotion, storefront image, and all areas of contact with the customer. As Subaru strives to establish premium brands with global appeal, it is working at the design level—the cornerstone of all brand identity—to create brand innovation and presence.

Subaru has always maintained a policy of individuality and has established its own brand position among Japanese automobile manufacturers. However, its superb functionality and consistency has not been fully expressed in its designs. Subaru has consistently maintained its unique functions and technologies, such as all-wheel drive, horizontally opposed engines, and unparalled driving experience, as part and parcel of its vehicles. Now we must fuse these technological attributes with attractive designs and produce unique products with superb competitiveness. In our organizational reforms, this goal is illustrated by the transfer of the Design Department from the Engineering Division to the Product Planning Division. Our partnership with consulting firms that have overseas experience in our brand image building efforts and the stimulation of our overall design organization through the appointment of overseas designers is a strong indication of our design-oriented stance.

Subaru is a company that has always undertaken new challenges. By basing our efforts on clear policies and goals for our premium brand vision, we are able to pursue Subaru designs with optimum timing. In the design selection, we will adopt an extremely simple and straight process, maximize top management’s contact with designers, and clearly express Subaru’s brand philosophy in product design. The Subaru that was built on a technological foundation is now taking the first step toward the fusion of technology and design and the establishment of global brand value.

Kiyoshi Sugimoto
Corporate Vice President
Chief General Manager of Design Dept.
SUBARU Product & Portfolio Planning Division



FHI's Unique Technological Capabilities Used in the High-Speed-Flight Demonstration Project

Eiji Tanikawa
Project General Manager (High-Speed-Flight Demonstrator)
Unmanned Air Vehicles Engineering Dept.
Engineering & Development Center, Aerospace Company

Since 1999, FHI has been engaged in the development of unmanned experimental vehicles for demonstration testing, as part of the reusable space transportation system development efforts of the National Aerospace Laboratory of Japan (NAL) and the National Space Development Agency of Japan (NASDA). The purpose of these experiments is to develop the basic technology for reusable space transportation, which will enable safe space travel for all. FHI was selected from a number of domestic manufacturers that responded to the challenge of this project and is taking part in every stage, from basic design to production and testing.

FHI started producing unmanned target drones in the 1970s and succeeded in test-flying an unmanned observation aircraft in 1982 for the first time in Japan. FHI has accumulated a great many technologies and business dealings in this area, both in Japan and around the world, and is highly regarded in the field. FHI has also steadily produced results in the field of reusable space transportation testing projects, having worked together with other domestic manufacturers on the OREX (Orbital Reentry Experiment), HYFLEX (Hypersonic Flight Experiment), and ALFLEX (Automatic Landing Flight Experiment) projects.

The High-Speed-Flight Demonstration Project consists of two phases. In Phase I, various subsonic flight data are verified. Once the launch command is given, the unmanned vehicle flies completely autonomously and collects flight data, a unique exercise even on a global scale. Approximately 3.3 meters in length, the jet-engine-powered vehicle has a top speed of mach 0.6. Its automatic control uses a flight control computer and, through the application of a high-precision differential Global Positioning System (GPS), it is capable of identifying its own position within less than a meter. Phase I flight tests will be conducted in autumn 2002 by NASDA and NAL in the Republic of Kiribati, with support provided by FHI.

In Phase II, to record flight data at speeds between mach 0.8 and mach 1.2, the vehicle will be suspended from a high altitude balloon and launched from an altitude of approximately 30 km. These tests, to be conducted under a partnership with the Centre National d'Etudes Spatiales (CNES), are scheduled to start in March 2003 at the European Space Range (ESRange), which is operated by the Swedish Space Corporation (SSC). Fully autonomous control devices and advanced technologies and equipment are incorporated into the body of this compact 3.3-meter-long vehicle, and only through the use of FHI's superior system integration technology has such a test been made possible.

FHI will continue to engage itself in a wide range of developmental efforts under the policy of its Aerospace Company to develop world-leading technologies in the field of unmanned aircraft.

Courtesy of NASDA
Courtesy of NAL

Environmental Protection Efforts

Environmental Management

As a manufacturer of automobiles and other transportation machinery, FHI makes efforts to reduce environmental impact at all stages of its business activities. In May 2002, FHI formulated its new voluntary environmental plan, the Fuji Heavy Industries Environmental Protection Project (fiscal 2003 to fiscal 2007). The goals of the plan are to contribute to society through the Company's projects and attain clean operations at all stages of business, with the ultimate objective of achieving an economic system based on an activity cycle with minimal environmental impact. In environmental accounting for fiscal 2002, ended March 31, 2002, environmental costs amounted to ¥25,378 million (¥21,732 million in the previous year), with economic effects working out to ¥976 million (¥1,216 million in the previous year). FHI continues to implement environmental protection efforts on a Groupwide basis, with such efforts now being expanded to seven of the Group's consolidated subsidiaries that are involved in manufacturing operations, which are historically the greatest burden to the environment. We also widely disclose our environmental activities and have been publishing annual environmental reports since 2000, to further our stakeholders' understanding of our efforts.

Environmentally Sound Products and Technologies

New Subaru Forester

Introduced in February 2002, the New Forester achieves both superb mobility and outstanding environmental performance. Even the turbo engine manual transmission model achieves fuel economy of 13.0 km per liter in Japan's 10-15 model fuel economy. The automatic transmission model achieves the same results when in ECO mode. All models pass year 2010 fuel economy standards and have attained Japan's G-LEV certification, which requires that exhaust emissions be reduced by an additional 25% from levels approved under Japan's 2000 exhaust emission regulations. Both ease of dismantling and recyclability have been improved through the greater use of recyclable materials and greater interchangeability of components. The use of lead has been drastically reduced to meet 2005 reduction targets* well ahead of schedule.

* Voluntary Japan Automotive Manufacturers Association, Inc. (JAMA) Guidelines

Hybrid Vehicles

The Pleo Nesta Hybrid represents the culmination of all of FHI's achievements in hybrid electric minicar technology thus far. Public road fleet tests on the Pleo Nesta commenced in October 2000. Furthermore, at the 35th Tokyo Motor Show, in 2001, the Company unveiled its HM-01 hybrid AWD-system concept car, which features an idling stop & restart system and rear wheels controlled by a 42-V power source.

HM-01 hybrid AWD-system concept car

Wind Turbine Generator Systems

In November 2000, FHI introduced the Subaru Small Wind Turbine Generator System, the result of the developmental application of technologies accumulated in aircraft manufacture,

such as an aerodynamic design for blades, a structure that uses composite material, and computerized control. FHI is currently engaged in testing for the introduction of wind-power generation at small and medium-sized remote island communities. The system is the recipient of the Fiscal 2001 New Energy Award, the Director-General of Agency of Natural Resources and Energy Prize, and the 2001-2002 Good Design Award.

Subaru Small Wind Turbine Generator System

CVSR

FHI's Convenience Store Recycler (CVSR) is a refuse-collection vehicle that carries an apparatus that automatically separates the containers and organic refuse of disposed packaged food products—such as those past their expiration date—into itemized waste for disposal. Organic refuse collected by these vehicles is recycled as compost or livestock feed.

Convenience Store Recycler

Zero Emissions Efforts

FHI strives to reduce waste at all of its production plants. In fiscal 2001, the Gunma Plant (automobiles) first achieved zero emissions—the elimination of all final landfill disposal wastes. In fiscal 2002, our Utsunomiya Plant (aircraft and environment-related machinery) and Saitama Plant (general-purpose engines) also achieved zero emissions. Also, in the carrying out of these efforts, on-site incinerators at both the Utsunomiya and Saitama plants were closed, thus making all of FHI's plants entirely incinerator-free. Furthermore, in fiscal 2002 the Utsunomiya Plant stepped up its recycling cost reduction efforts by establishing a comprehensive recycling center on the premises that collects, sorts, compacts, and stores waste products.

Eco Technologies Company

In June 2002, as part of its structural reforms, FHI created the Eco Technologies Company. The new internal company will further promote environmentally compliant businesses through such efforts as the continual development of refuse collection vehicles, which command the top share of the domestic market, and the expansion of plant businesses that handle the intermediary disposal of waste and its pulverization, transport, and sorting.

Seated, from left: Kyoji Takenaka, Takeshi Tanaka, Frederick A. Henderson
Standing, from left: Hideshige Gomi, Koichi Arasawa, Teruo Hanada, Hiroshi Suzuki, Hideo Wada

Executive Officers

Board of Directors

Chairman and Chief Executive Officer

Takeshi Tanaka*

President and Chief Operating Officer

Kyoji Takenaka*

Senior Executive Vice President

Teruo Hanada*

Corporate Executive Vice Presidents

Hiroshi Suzuki
Koichi Arasawa
Hideo Wada
Hideshige Gomi

Director

Frederick A. Henderson

*Representative Director

Corporate Senior Vice Presidents

Masayoshi Nagano
Takeo Tsumuji
Takao Tsuchiya
Hiroyuki Nakatsubo
Kunitaka Nakahara
Kiyoshi Inoh
Masaru Katsurada
Takao Saito
Hiroshi Komatsu
Shunsuke Takagi
Yutaka Tsukahara
Kisaburo Wani
Hiroyuki Oikawa

Corporate Vice Presidents

Masatoshi Iwasaki
Edward Pasternak
Yoji Ishimaru
Minoru Tamura
Kazushige Okuhara
Norihisa Matsuo
Noboru Daikuhara
Toshifumi Terao
Shoichi Washizu
Kunio Ishigami
Ichiro Kudo
Kiyoshi Sugimoto
Tsunenori Hoshi
Ikuo Mori

Standing Corporate Auditor

Takayoshi Yoshihashi

Corporate Auditors

Kunitake Nomura
Hiroshi Takaku
Akira Furuya

Financial Section

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
	2002	2001	2000	1999	1998	**2002**
For the Year:						
Net sales	**¥1,362,493**	¥1,311,887	¥1,330,125	¥1,352,520	¥1,303,989	**$10,225,088**
Cost of sales	**992,950**	978,841	995,131	1,067,868	1,027,782	**7,451,782**
Gross profit	**369,543**	333,046	334,994	284,652	276,207	**2,773,306**
Selling, general and administrative expenses	**281,063**	251,373	243,593	194,720	195,770	**2,109,291**
Operating income	**88,480**	81,673	91,401	89,932	80,437	**664,015**
Income before income taxes and minority interest	**56,136**	21,291	64,839	68,423	56,609	**421,283**
Net income	**30,283**	22,628	31,348	33,706	30,708	**227,265**
At Year-End:						
Shareholders' equity	**¥ 396,112**	¥ 357,455	¥ 206,404	¥ 200,220	¥ 168,833	**$ 2,972,698**
Total assets	**1,269,558**	1,168,501	1,038,558	981,256	904,571	**9,527,640**
Ratio of shareholder's equity to total assets (%)	**31.2%**	30.6%	19.9%	20.4%	18.7%	
Per Share (in yen and U.S. dollars):						
Net income:						
Basic	**¥ 40.74**	¥ 30.44	¥ 51.90	¥ 56.18	¥ 51.33	**$ 0.31**
Diluted	**38.83**	29.06	48.53	51.79	47.18	**0.29**
Shareholders' equity	**532.88**	480.86	338.75	332.41	282.09	**4.00**
Other Information:						
Depreciation and amortization	**¥ 63,964**	¥ 64,070	¥ 60,190	¥ 38,708	¥ 32,574	**$ 480,030**
Capital expenditures (addition to fixed assets)	**118,376**	102,301	103,922	57,566	56,419	**888,375**
R&D expenses	**54,903**	46,622	40,123	38,512	38,231	**412,030**
Number of shares issued at year-end (thousands of shares)	**746,506**	746,502	614,553	602,333	598,507	
Number of shareholders*	**33,094**	32,996	49,381	55,044	72,107	
Number of employees*:						
Parent only	**13,374**	13,603	13,668	13,419	13,435	
Consolidated	**26,483**	26,502	26,914	19,882	19,113	

Note: U.S. dollar figures have been translated from yen, for convenience only, at the rate of ¥133.25 to US$1.00, the approximate rate of exchange at March 31, 2002.

** As of March 31*

OVERVIEW

During the year ended March 31, 2002 ("fiscal 2002"), conditions surrounding the economy and the automotive industry both in Japan and overseas became increasingly difficult, as the corporate environment grew even more challenging. Against this backdrop, the FHI Group carried out dynamic business developments to achieve its goal of being a "global player with premium brands." These efforts included partnerships with General Motors Corporation and Suzuki Motor Corporation under the FHI New TQF21 01 Rolling Plan.

As a result, negative factors including a decline in the domestic automobile unit sales volume and an increase in expenses were compensated for by such positive factors as an increase in overseas automobile unit sales volumes as well as a favorable exchange rate and reduction of costs. Consolidated performance for the term saw increases in both sales and profit. Net sales rose a firm 3.9%, to ¥1,362.4 billion, operating income climbed 8.3%, to ¥88.4 billion, and net income surged 33.8%, to ¥30.2 billion, primarily due to the effect of the full amortization of net pension and severance obligation at transition on the prior year's results.

In free cash flow, despite the increase in cash generated from operating activities and the overall rise in income, the high level of cash used in investing activities—primarily facilities investments including the acquisition of leased property—resulted in a net cash outflow of ¥11.3 billion.

In light of the favorable consolidated performance for the fiscal year, and following its policy of long-term stable dividends, the parent company set the dividend for the term—including the interim dividend—at ¥9.00 per share, the same as for the previous year.

SEGMENT INFORMATION AND CONSOLIDATION

The FHI Group conducts business in the four segments of Automobiles, Industrial Products, Aerospace, and Other and maintains a wide-ranging product mix. In fiscal 2002, the Automobile segment accounted for 89.5% of net sales, with the other three segments accounting for the remaining 10.5%.

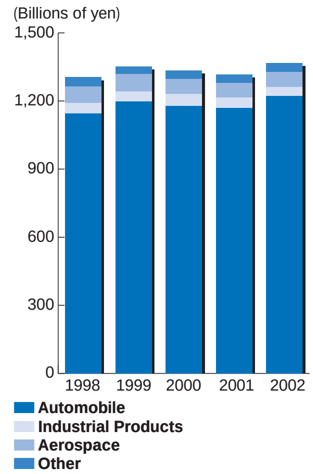
As of March 31, 2002, the FHI Group consisted of a total of 136 companies: the parent company, 121 subsidiaries, 12 affiliates, and 2 other related companies. Of these, 67 were consolidated subsidiaries and 1 was accounted for by the equity method. The remaining unconsolidated companies did not have a material impact on the consolidated financial statements as a whole and have therefore been excluded from the scope of consolidation.

REVIEW OF OPERATIONS BY SEGMENT

Automobile segment

The volume of automobile sales for the term was 543 thousand units, a decline of 17 thousand units, or 3.0%, compared with the previous term. In terms of new passenger car introductions in the Japanese market, FHI strove to expand sales by launching the Traviq seven-seater passenger wagon, adding the GT30 (six-cylinder engine touring wagon) and the RS30 (six-cylinder engine B4 sedan) to our flagship Legacy lineup, and introducing the new Forester in February 2002. However, as new introductions to our core product lines occurred near the end of the term, overall passenger car sales unfortunately slid 12.3%, to 108 thousand units.

Net Sales



In minicars, although the Sambar produced strong sales throughout the year, exceeding those of the previous fiscal year, sales of the Pleo were less than those for the previous fiscal year, having dropped off in the second half due to a string of new model introductions by FHI's competitors. Overall domestic minicar sales declined 11 thousand units, or 6.5%, to 157 thousand units. Consequently, total domestic sales fell 26 thousand units, or 9.0%, to 264 thousand units.

On the other hand, in overseas markets, strong sales were recorded in North America, increasing to 207 thousand units. Although FHI faced a weak euro and strong competition from European manufacturers, total overseas sales increased 9 thousand units, or 3.3%, to 279 thousand units.

As a result, net sales for the segment increased ¥52.3 billion, or 4.5%, to ¥1,222.7 billion, and operating income rose ¥3.4 billion, or 4.2%, to ¥85.6 billion. Also, looking at domestic and overseas net sales separately, domestic net sales declined due to the decrease in sales volume, while overseas net sales increased due to the increase in sales volume and the weakened yen.

Industrial Products segment

In the Japanese market, sales of small engines for construction machinery declined due to the economic slowdown. Overseas as well, sales of engines declined in the European market, as did sales of recreational vehicle engines in the North American market. Consequently, net sales for the segment decreased ¥4.8 billion, or 10.8%, to ¥39.5 billion. Operating income declined ¥1.0 billion and amounted to an operating loss of ¥0.2 billion.

Aerospace segment

Although the sales volume of the UH-1J utility helicopter to the Japan Defense Agency increased, the sales volume of the F-2 support fighter declined and delivery of the AH-1S anti-tank helicopter was concluded, resulting in a decline in total domestic sales volume

Consolidated Sales by Region (Number of vehicles)

	2002	2001
Japan	**264,257**	290,301
U.S.A.	**191,381**	172,686
Canada	**15,632**	15,005
Europe	**32,373**	39,951
Australia	**26,923**	27,976
Others	**12,675**	14,378
Subtotal	**543,241**	560,297
CKD* in Overseas	**3,288**	3,941
Total	**546,529**	564,238

** CKD: Complete Knocked Down*

Non-Consolidated Sales by Model (Number of vehicles)

	2002	2001	2000	1999	1998
Domestic Units:					
Legacy	**59,209**	67,424	67,972	63,499	55,001
Impreza	**24,899**	32,362	25,654	33,531	37,049
Forester	**22,922**	28,994	25,985	24,489	40,032
Others	**4,244**	297	308	1,438	2,184
Subtotal	**111,274**	129,077	119,919	122,957	134,266
Minicars	**167,265**	173,754	177,842	156,186	144,366
Total	**278,539**	302,831	297,761	279,143	278,632
Export Units:					
Legacy	**24,727**	26,254	34,304	29,530	27,857
Impreza	**75,700**	54,721	58,530	54,861	52,251
Forester	**72,629**	85,453	83,928	81,385	58,005
Others	**0**	0	0	439	819
Subtotal	**173,056**	166,428	176,762	166,215	138,932
Minicars	**22**	108	760	2,152	3,337
Total	**173,078**	166,536	177,522	168,367	142,269
CKD in Overseas	**104,234**	111,783	103,001	100,440	110,689
(SIA Portion)	**100,946**	107,842	98,861	98,464	105,237
U.S. Unit Sales*:					
Legacy	**95,291**	96,391	87,267	88,660	92,913
Impreza	**35,612**	19,220	19,356	19,041	24,242
Forester	**55,041**	56,605	50,183	40,132	15,988
Others	**—**	—	—	—	640
Total	**185,944**	172,216	156,806	147,833	133,783
U.S. Production Units*:					
Legacy	**103,010**	107,955	93,070	104,229	102,180

** U.S. Unit Sales and U.S. Production Units are the aggregate figures for the calendar year from January 2001 through December 2001.*

in the defense sector. On the other hand, in the commercial sector, despite the impact of the September 11 terrorist attacks, product sales to The Boeing Company of the United States increased. The yen-to-dollar exchange rate was also favorable. As a result, net sales increased ¥0.7 billion, or 1.1%, to ¥66.3 billion. Operating income surged ¥4.9 billion, or 200.4%, to ¥7.4 billion. This improvement in operating income was primarily the result of the increase in sales to Boeing and the favorable exchange rate.

Other segment

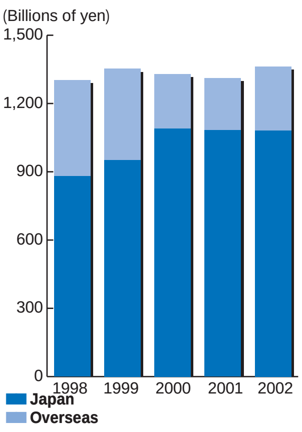
Despite an overall slow climate for demand in bus operations, net sales exceeded those for the previous fiscal year due to brisk sales of FHI's new tour bus. Amid protracted weakness in the construction industry and long-standing stagnation in demand, sales in the housing segment declined.

In transportation and ecology systems, net sales increased due to the delivery of FHI's tilting railway motor car to JR Hokkaido and firm product sales from intermediate plants, such as the Fukui Recycling Plant. As a result, net sales of this segment increased ¥3.1 billion, or 8.5%, to ¥40.6 billion. However, conditions remained severe for the Company's subsidiaries, and an operating loss of ¥4.2 billion was recorded. Moreover, after reviewing our troubled bus chassis and rail car manufacturing operations, we have decided to end new production of those product lines in fiscal 2003.

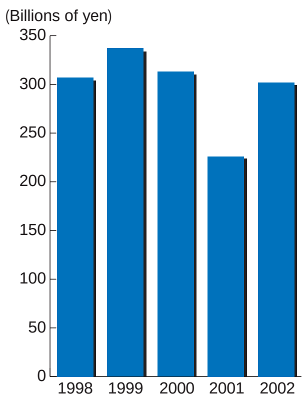
NET SALES

FHI's consolidated net sales for fiscal 2002 increased ¥50.6 billion, or 3.9%, to ¥1,362.4 billion, primarily as a result of a ¥52.3 billion increase in automobile revenues. Examining domestic and overseas net sales separately, domestic net sales declined ¥56.9 billion, or 8.3%, to ¥631.2 billion, due to the decrease in the volume of automobile sales in Japan, while overseas net sales grew a substantial ¥107.5 billion, or 17.2%, to ¥731.2 billion, due to the increased sales volume in North America and the depreciated yen. Consequently, the portion of consolidated net sales accounted for by overseas net sales climbed 6.2 percentage points, to 53.7%. Examined by individual region, North American sales climbed 7.2 percentage points, to 44.6% of the Group's total sales, and were the primary reason for the increase in the proportion of overseas net sales. For reasons stated previously, sales to the European market fell 0.9 percentage point, to 4.2%.

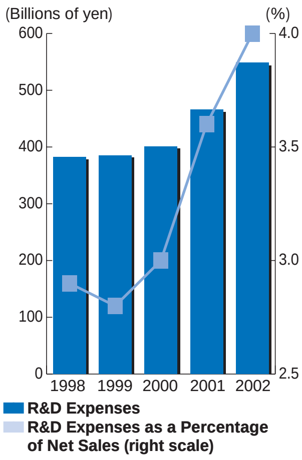
Net Sales



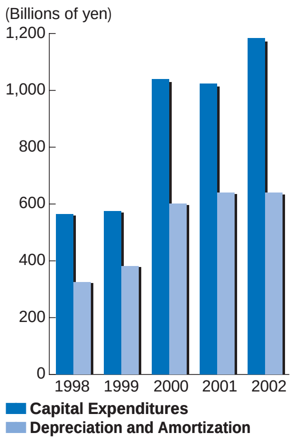
Net Income



R&D Expenses



Capital Expenditures and Depreciation and Amortization



COST, EXPENSES, AND OPERATING INCOME

In comparison to the 3.9% increase in revenue, the cost of sales increased ¥14.1 billion, or 1.4%, to ¥992.9 billion, and the cost of sales ratio declined 1.7 percentage points, from 74.6% to 72.9%. This was due to a favorable exchange rate, which accounted for approximately ¥32.6 billion in increased revenue, as well as the FHI Group's achievement of approximately ¥21.6 billion in cost reductions, which offset negative factors stemming from a deterioration of sales mix and an increase in expenditures for specified improvements in safety and other features. Hence, gross profit increased ¥36.4 billion, or 11.0%, to ¥369.5 billion, and the gross margin rate rose from 25.4%, to 27.1%.

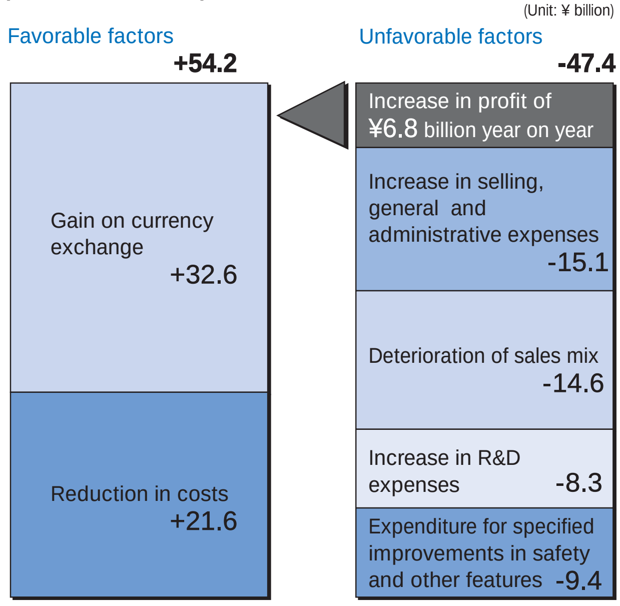
On the other hand, SG&A expenses increased a substantial ¥29.6 billion, or 11.8%, to ¥281.0 billion. This was due primarily to an ¥8.5 billion increase in overall advertising expenses as well as increases in sales promotion expenses in North America. In addition, R&D expenses increased ¥7.9 billion, mostly in new automobile development. As a result, the ratio of SG&A expenses to net sales rose 1.4 percentage points, to 20.6%. Moreover, total R&D expenses included in SG&A expenses and manufacturing expenses increased ¥8.2 billion, to ¥54.9 billion, with the ratio of R&D expenses to net sales rising 0.4 percentage point, to 4.0%.

As a result, operating income increased ¥6.8 billion, to ¥88.4 billion, mainly due to increased operating income in the Automobile and Aerospace segments. The ratio of operating income to net sales increased 0.3 percentage point, from 6.2% to 6.5%.

The following chart summarizes factors contributing to fluctuations in operating income.

Analysis of Factors Affecting in Operating Income (Consolidated Basis)

(Unit: ¥ billion)



OTHER INCOME (EXPENSES)

Other expenses, net, plummeted ¥28.0 billion, to ¥32.3 billion, thus contributing to increased income. Principal positive and negative factors were as follows.

Principal positive factors

The principal positive factor was the absence of a ¥44.5 billion provision for the one-time amortization of net pension and severance obligation at transition, implemented in the previous fiscal year.

Principal negative factors

Principal negative factors included an ¥8.4 billion increase in the loss on devaluation of securities, ¥6.8 billion in losses incurred on the liquidation of affiliated companies, and a ¥2.8 billion decrease in the gain on sales of securities.

NET INCOME

As a result, income before income taxes surged ¥34.8 billion, or 163.7%, to ¥56.1 billion. Net income climbed ¥7.6 billion, or 33.8%, to ¥30.2 billion. The effective tax rate for the previous fiscal year was an extremely low of 0.9% due to such exceptional factors as the recognition (subtraction) of deferred losses on subsidiaries based on the deferred tax accounting. With no such special factors for fiscal 2002, the effective income tax rate after the consideration of the deferred tax accounting surged 50.4%, which accounted for the large difference in the percentage of increase between income before income taxes and net income. Net income per share increased ¥10.30, from ¥30.44 to ¥40.74. As stated above, the parent company dividend for the fiscal year was set at ¥9.00 per share.

FINANCIAL POSITION

Assets

Under the severe business conditions of fiscal 2002, the FHI Group continued to strive for effective use of invested capital by concentrating its resources on priority fields in accordance with its New TQF21 financial strategy.

Total assets at year-end increased ¥101.0 billion, or 8.6%, to ¥1,269.5 billion, primarily due to the management of funds raised in preparation for bond redemption and capital expenditures in fiscal 2003. Other factors included a rise in current assets due to increased inventories as well as an increase in property, plant and equipment as a result of the relatively high level of facilities investment during the term.

Total current assets increased ¥63.4 billion, to ¥636.8 billion, primarily due to a ¥26.8 billion increase in marketable securities through surplus fund management of the above mentioned funds and a ¥22.6 billion increase in inventories due to the decline in domestic automobile demand and the increase on the currency conversion of inventories of overseas subsidiaries due to the depreciation of the yen.

A total of ¥70.6 billion was invested in property, plant and equipment during fiscal 2002, primarily in facilities in the Automobile segment. Property, plant and equipment, net, increased ¥25.1 billion, to ¥481.7 billion, after depreciation. The investment figure stated above does not include automobiles for lease and other lease assets.

Investments and other assets increased ¥12.4 billion, to ¥150.9 billion. Of this, intangible fixed assets increased ¥5.4 billion, primarily in computer software. Due to the application of the deferred tax, non-current deferred income tax assets increased ¥5.0 billion.

Liabilities and shareholders' equity

Total liabilities at year-end increased ¥64.6 billion, or 8.0%, to ¥869.9 billion. Of this, short- and long-term interest-bearing debt increased ¥31.6 billion, to ¥396.7 billion. This was due primarily to advanced fund raising through new bond issuance and long-term bank loans in preparation for bond redemption and capital investment in fiscal 2003. A portion of these funds procured was allocated to the repayment of short-term bank loans.

The net increase in liabilities through procurement and repayment on a cash flow basis amounted to ¥26.4 billion. The remaining increase of ¥5.2 billion was due to increases on the conversion of overseas consolidated subsidiaries' foreign currency denominated loans as a result of the yen's depreciation.

Operating liabilities—which consisted primarily of notes and accounts receivable—and other long-term liabilities increased ¥33.0 billion, to ¥473.2 billion. This was due primarily to ¥16.8 billion in accrued income taxes due to the increase in income and the application of accounting for income taxes and a ¥16.1 billion increase in accrued expenses due to the aforementioned increase in SG&A expenses.

Following the lump-sum amortization implemented in the previous fiscal year, accrued pension and severance liabilities declined slightly in this term.

Shareholders' equity increased ¥38.6 billion, to ¥396.1 billion, and the shareholders' equity ratio climbed 0.6 percentage points, to 31.2%. This was due primarily to a ¥23.6 billion increase as a result of increased retained earnings and a ¥11.3 billion decline in currency translation adjustments due to the yen's depreciation. Furthermore, net unrealized holding gains on securities increased ¥3.2 billion, from ¥1.7 billion, to ¥4.9 billion due mainly to an improvement in the position of investment securities previously devalued.

CAPITAL EXPENDITURES

The FHI Group's capital expenditures, which were higher in fiscal 2002 than in previous periods, increased by ¥27.0 billion compared with the prior fiscal year, to ¥70.6 billion, primarily in the Automobile segment. These expenditures were incurred mainly for production, R&D, and sales facilities in the Automobile segment. The majority of these expenditures were covered by internal reserve. Expenditures by individual segment were as follows.

Automobile segment

A total of ¥34.3 billion was invested in the parent company's streamlining initiatives in R&D facilities and efforts to enable interflowing production through flexible production lines. In addition,

¥10.6 billion was invested in FHI's manufacturing subsidiary in the United States, Subaru-Isuzu Automotive Inc., for the introduction of new models and the augmenting of engine production capacity.

Other segments

The parent company invested ¥2.4 billion in the Industrial Products segment, mostly in equipment for the launching of new products, and ¥0.7 billion in the Aerospace segment for maintenance and renewal. In other segments, a total of ¥2.2 billion was invested primarily for spare parts equipment.

The parent company's portion of these capital expenditures was ¥39.7 billion and the subsidiaries' portion was ¥30.9 billion. In addition to the aforementioned investments, ¥41.0 billion was invested in the Automobile segment in the acquisition of lease vehicles and other business assets.

CASH FLOWS

Cash and cash equivalents (hereinafter "cash") at year-end increased ¥13.2 billion, to ¥133.7 billion. However, in free cash flows, despite the increase in cash generated from operating activities and the overall rise in income, the high level of cash used in investing activities—primarily investments in facilities—resulted in a cash outflow of ¥11.3 billion. The cash level at year-end was equivalent to approximately a 1.1 month portion of FHI's average monthly sales of ¥113.5 billion, which the Company determines to be of sufficient liquidity to conduct normal business operations. Furthermore, the parent company and two overseas consolidated subsidiaries possess a balance of ¥90.8 billion in unexecuted loans on loan commitments from financial institutions, giving the Group an advantage in terms of capital mobility and efficiency.

Net cash provided by operating activities increased ¥6.6 billion, to ¥85.7 billion. Cash inflow comprising income before income taxes and minority interest, adjusted for depreciation and amortization as well as other non-cash items, and excluding expenditures for income tax, increased ¥17.4 billion, to ¥113.6 billion. This was due primarily to the increase in income coupled with a decline in such non-cash inflows as the lump-sum amortization of net pension and severance obligation at transition, which was recorded in the previous term.

However, changes in operating assets and liabilities increased ¥10.8 billion and resulted in a cash outflow of ¥27.8 billion. This was due primarily to the fact that the decline in accounts payable exceeded the decline in accounts receivable.

On the other hand, net cash used in investing activities increased ¥8.6 billion, to ¥97.0 billion. Net cash outflows for the purchase and sale of marketable securities and investment securities increased ¥2.2 billion, to ¥19.4 billion, and net cash used for the purchase and sale of property, plant and equipment (including leased assets) increased ¥2.1 billion, to ¥72.4 billion. In addition, repayments on lendings declined ¥1.7 billion, to ¥0.8 billion.

Net cash provided by financing activities increased ¥1.3 billion, to ¥19.7 billion. This was due to funds raised amounting to ¥26.4 billion as a result of the advanced fund-raising in preparation for bond redemption and capital investment in fiscal 2003, as previously mentioned. A total of ¥50.5 billion in new funds was raised during the year from bond issuance. Short- and long-term interest-bearing debt amounted to a net decline of ¥24.0 billion. Expenditures for shareholder dividends totaled ¥6.6 billion. Cash increases on currency conversions due to the yen's depreciation amounted to ¥4.7 billion.

OTHER ISSUES

Please refer to the President's interview for information on the new five-year medium-term business plan, structural reforms, and the introduction of an internal company system.

At the general meeting of shareholders held on June 26, 2002, the upper limit for buyback and retirement of stock was set at 215 million shares or ¥140.0 billion and the upper limit on the issuance of new share subscription rights for stock options was set at 1.1 million shares of the Company's common stock.

OUTLOOK

The environment surrounding corporations in fiscal 2003 is expected to remain intense, making no allowance for optimism. Against this backdrop, FHI expects increases in sales in North America and other overseas markets despite stagnation in the increasingly competitive domestic market. However, due to increases in investments for future development, while an increase in sales is expected compared with fiscal 2002, income is expected to decline. The yen to dollar exchange rate is predicted at ¥125.0 / US$1.00.

The Company predicts consolidated net sales to increase 2.0%, to ¥1,390.0 billion, and net income to decline 21.0%, to ¥24.0 billion.

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, 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.

Consolidated Balance Sheets

FUJI HEAVY INDUSTRIES LTD. AND CONSOLIDATED SUBSIDIARIES
As of March 31, 2002 and 2001

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars (Note 4)*
ASSETS	***2002***	*2001*	***2002***
Current assets:			
Cash and time deposits (Note 5)	**¥ 56,466**	¥ 58,610	**$ 423,760**
Marketable securities (Notes 5 and 6)	**116,461**	89,573	**874,004**
Notes and accounts receivable, trade (Note 10)	**133,688**	130,593	**1,003,287**
Allowance for doubtful accounts	**(571)**	(862)	**(4,285)**
Inventories (Note 7)	**192,548**	169,936	**1,445,013**
Short-term loans (Note 5)	**71,677**	66,519	**537,914**
Deferred tax assets (Note 12)	**34,278**	29,891	**257,246**
Other current assets (Note 10)	**32,322**	29,174	**242,566**
Total current assets	**636,869**	573,434	**4,779,505**
Property, plant and equipment (Notes 8, 9 and 10)	**1,061,179**	1,005,331	**7,963,820**
Less accumulated depreciation	**(579,422)**	(548,750)	**(4,348,383)**
Net property, plant and equipment	**481,757**	456,581	**3,615,437**
Investments and other assets:			
Investment securities (Notes 6 and 10)	**48,275**	48,185	**362,289**
Investments in non-consolidated subsidiaries and affiliates	**6,536**	7,930	**49,050**
Long-term loans	**8,351**	7,910	**62,672**
Goodwill	**22,249**	20,143	**166,972**
Intangibles, net	**15,284**	11,978	**114,702**
Deferred tax assets (Note 12)	**31,790**	26,763	**238,574**
Other assets (Note 10)	**22,256**	20,478	**167,024**
Allowance for doubtful accounts	**(3,809)**	(4,901)	**(28,585)**
	150,932	138,486	**1,132,698**
Total assets	**¥1,269,558**	¥1,168,501	**$9,527,640**

LIABILITIES AND SHAREHOLDERS' EQUITY	*Millions of yen* **2002**	*Millions of yen* 2001	*Thousands of U.S. dollars (Note 4)* **2002**
Current liabilities:			
Short-term borrowings (Note 10)	**¥ 169,807**	¥ 180,227	**$1,274,349**
Current portion of long-term debt (Note 10)	**43,845**	37,943	**329,043**
Notes and accounts payable, trade	**204,959**	207,477	**1,538,154**
Accrued expenses	**107,707**	91,574	**808,308**
Accrued income taxes (Note 12)	**23,488**	6,625	**176,270**
Other current liabilities	**36,589**	34,737	**274,589**
Total current liabilities	**586,395**	558,583	**4,400,713**
Long-term liabilities:			
Long-term debts (Note 10)	**183,090**	146,931	**1,374,034**
Accrued pension and severance liability (Note 11)	**62,579**	65,674	**469,636**
Other (Notes 9 and 12)	**37,896**	34,114	**284,398**
	283,565	246,719	**2,128,068**
Minority interest in consolidated subsidiaries	**3,486**	5,744	**26,161**
Contingent liabilities (Note 16)			
Shareholders' equity (Note 13):			
Common stock			
Authorized—1,500,000,000 shares			
Issued 2001—746,502,402 shares	**—**	144,449	**—**
2002—746,505,560 shares	**144,450**	—	**1,084,053**
Additional paid-in capital	**150,762**	150,761	**1,131,422**
Revaluation reserve for land (Notes 9 and 12)	**381**	—	**2,859**
Retained earnings	**107,328**	83,680	**805,463**
Net unrealized holding gains on securities	**4,997**	1,701	**37,501**
Translation adjustments	**(9,579)**	(20,921)	**(71,887)**
Less treasury stock, at cost	**(2,227)**	(2,215)	**(16,713)**
	396,112	357,455	**2,972,698**
Total liabilities and shareholders' equity	**¥1,269,558**	¥1,168,501	**$9,527,640**

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

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars (Note 4)*
	2002	*2001*	*2000*	***2002***
Net sales	**¥1,362,493**	¥1,311,887	¥1,330,125	**$10,225,088**
Cost of sales	**992,950**	978,841	995,131	**7,451,782**
Gross profit	**369,543**	333,046	334,994	**2,773,306**
Selling, general and administrative expenses (Note 14)	**281,063**	251,373	243,593	**2,109,291**
Operating income	**88,480**	81,673	91,401	**664,015**
Other income (expenses):				
Interest and dividend income	**2,868**	3,663	2,569	**21,523**
Interest expenses	**(3,499)**	(4,623)	(10,422)	**(26,259)**
Gain on sale of securities	**0**	2,815	12,092	**0**
Foreign exchange losses	**(4,996)**	(3,027)	(5,356)	**(37,494)**
Loss on devaluation of securities	**(8,970)**	(487)	(6,569)	**(67,317)**
Loss on sales or disposal of property, plant and equipment, net	**(3,670)**	(2,551)	(2,440)	**(27,542)**
Loss on liquidation of affiliated companies	**(6,880)**	—	—	**(51,632)**
Full amortization of net pension and severance obligation at transition	**—**	(44,520)	—	**—**
Write-down of land	**—**	—	(9,855)	**—**
Other, net	**(7,197)**	(11,652)	(6,581)	**(54,011)**
	(32,344)	(60,382)	(26,562)	**(242,732)**
Income before income taxes and minority interest	**56,136**	21,291	64,839	**421,283**
Income taxes (Note 12):				
Current	**38,325**	25,814	36,151	**287,617**
Deferred	**(10,042)**	(25,631)	(2,621)	**(75,362)**
	28,283	183	33,530	**212,255**
Income before minority interest	**27,853**	21,108	31,309	**209,028**
Minority interest in consolidated subsidiaries	**2,430**	1,520	39	**18,237**
Net income	**¥ 30,283**	¥ 22,628	¥ 31,348	**$ 227,265**

	Yen	*Yen*	*Yen*	*U.S. dollars (Note 4)*
Per share data (Note 2):				
Net income—Basic	**¥40.74**	¥30.44	¥51.90	**$0.31**
—Diluted	**38.83**	29.06	48.53	**0.29**
Cash dividends	**9.00**	9.00	9.00	**0.07**

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, 2002, 2001 and 2000

	Thousands								*Millions of yen*
	Number of shares issued	*Common stock*	*Additional paid-in capital*	*Revaluation reserve for land*	*Retained earnings*	*Net unrealized holding gains on securities*	*Accumulated translation adjustment*	*Treasury stock, at cost*	*Total shareholders' equity*
Balance, March 31, 1999	602,333	¥ 85,121	¥ 91,567	¥ —	¥ 23,535	¥ —	¥ —	¥ (3)	¥200,220
Accumulated foreign currency translation adjustment transferred from assets							(26,194)		(26,194)
Foreign currency translation adjustment							(2,060)		(2,060)
Cumulative effect of changes in accounting for income taxes					6,582				6,582
Stock class change of Subaru-Isuzu Automotive Inc.					3,495				3,495
Merger of a consolidated subsidiary	740	37	46		2,199				2,282
Cash dividends					(5,122)				(5,122)
Payment of bonuses to directors and statutory auditors					(209)				(209)
Shares issued upon conversion of convertible bonds	11,480	2,957	2,946						5,903
Accumulated deficit of subsidiaries newly included in consolidation					(8,699)				(8,699)
Treasury stock held by subsidiaries newly included in consolidation								(1,142)	(1,142)
Net income					31,348				31,348
Balance, March 31, 2000	614,553	88,115	94,559	—	53,129	—	(28,254)	(1,145)	206,404
Foreign currency translation adjustment							7,333		7,333
Retained earnings of merger of a consolidated subsidiary					14,484				14,484
Cash dividends					(6,394)				(6,394)
Payment of bonuses to directors and statutory auditors					(167)				(167)
Shares issued to GM	131,896	56,319	56,188						112,508
Shares issued upon conversion of convertible bonds	54	14	14						28
Treasury stock held by subsidiaries newly included in consolidation								(1,070)	(1,070)
Adoption of new accounting standard for financial instruments						1,701			1,701
Net income					22,628				22,628
Balance, March 31, 2001	746,502	144,449	150,761	—	83,680	1,701	(20,921)	(2,215)	357,455
Foreign currency translation adjustment							**11,342**		**11,342**
Retained earnings of merger of non-consolidated subsidiaries					**211**				**211**
Cash dividends					**(6,694)**				**(6,694)**
Payment of bonuses to directors and statutory auditors					**(152)**				**(152)**
Shares issued upon conversion of convertible bonds	**4**	**1**	**1**						**2**
Increase in treasury stock								**(12)**	**(12)**
Revaluation of land				**381**					**381**
Increase in unrealized holding gains on securities						**3,296**			**3,296**
Net income					**30,283**				**30,283**
Balance, March 31, 2002	**746,506**	**¥144,450**	**¥150,762**	**¥381**	**¥107,328**	**¥4,997**	**¥ (9,579)**	**¥(2,227)**	**¥396,112**

								Thousands of U.S. dollars (Note 4)
Balance, March 31, 2001	$1,084,045	$1,131,414	$ —	$627,992	$12,765	$(157,005)	$(16,623)	$2,682,588
Foreign currency translation adjustment						**85,118**		**85,118**
Retained earnings of merger of non-consolidated subsidiaries				**1,583**				**1,583**
Cash dividends				**(50,236)**				**(50,236)**
Payment of bonuses to directors and statutory auditors				**(1,141)**				**(1,141)**
Shares issued upon conversion of convertible bonds	**8**	**8**						**16**
Increase in treasury stock							**(90)**	**(90)**
Revaluation of land			**2,859**					**2,859**
Increase in unrealized holding gains on securities					**24,736**			**24,736**
Net income				**227,265**				**227,265**
Balance, March 31, 2002	**$1,084,053**	**$1,131,422**	**$2,859**	**$805,463**	**$37,501**	**$ (71,887)**	**$(16,713)**	**$2,972,698**

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, 2002, 2001 and 2000

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars (Note 4)
	2002	2001	2000	**2002**
Cash flows from operating activities:				
Income before income taxes and minority interest	**¥ 56,136**	¥ 21,291	¥ 64,839	**$ 421,283**
Adjustments to reconcile income before income tax and minority interest to net cash provided by operating activities:				
Depreciation and amortization	**63,964**	64,070	60,190	**480,030**
Loss on sale or disposal of property, plant and equipment, net	**3,670**	2,551	2,440	**27,542**
Increase (decrease) in provision for pension and severance liability	**(3,097)**	40,546	—	**(23,242)**
Write-down of land	**—**	—	9,855	**—**
Gain on sale of securities	**0**	(2,815)	(12,092)	**0**
Loss on devaluation of securities	**8,970**	487	6,569	**67,317**
(Increase) decrease in notes and accounts receivable, trade	**474**	(10,231)	12,719	**3,557**
(Increase) decrease in inventories	**(14,989)**	(15,053)	3,572	**(112,488)**
Increase (decrease) in notes and accounts payable, trade	**(13,378)**	8,243	(1,440)	**(100,397)**
Income taxes paid	**(21,608)**	(37,165)	(37,774)	**(162,161)**
Loss on liquidation of affiliated companies	**6,880**	—	—	**51,632**
Other, net	**(1,301)**	7,175	(13,745)	**(9,763)**
Net cash provided by operating activities	**85,721**	79,099	95,133	**643,310**
Cash flows from investing activities:				
Purchase of property, plant and equipment	**(109,117)**	(91,734)	(98,429)	**(818,889)**
Proceeds from sales of property, plant and equipment	**36,634**	21,439	21,734	**274,927**
Purchase of investment securities	**(4,754)**	(2,714)	(11,064)	**(35,677)**
Purchase of marketable securities	**(56,013)**	(50,274)	(1,171)	**(420,360)**
Proceeds from sales of investments securities	**1,832**	7,355	—	**13,748**
Proceeds from sales of marketable securities	**39,493**	28,423	12,343	**296,383**
Purchase of intangible assets	**(6,577)**	(5,992)	(3,018)	**(49,358)**
Disbursement of loans receivable	**(52,115)**	(52,216)	(56,109)	**(391,107)**
Collection of loans receivable	**52,958**	54,815	62,647	**397,433**
Other, net	**586**	2,520	(4,854)	**4,397**
Net cash used in investing activities	**(97,073)**	(88,378)	(77,921)	**(728,503)**
Cash flows from financing activities:				
Proceeds from long-term debt	**27,704**	46,443	31,670	**207,910**
Repayment of long-term debt	**(40,489)**	(63,677)	(33,816)	**(303,858)**
Issuance of bonds	**50,500**	—	10,300	**378,987**
Redemption of bonds	**—**	(10,000)	(42,474)	**—**
Repayment of commercial paper	**—**	(30,000)	30,000	**—**
Decrease in short-term borrowings	**(11,237)**	(31,831)	(65,340)	**(84,330)**
Issuance of common stock	**—**	112,224	—	**—**
Purchase of treasury stock	**(47)**	(2,249)	—	**(353)**
Proceeds from sales of treasury stock	**35**	3,901	—	**263**
Dividends paid	**(6,694)**	(6,394)	(5,122)	**(50,236)**
Net cash provided by (used in) financing activities	**19,772**	18,417	(74,782)	**148,383**
Effect of exchange rate changes on cash and cash equivalents	**4,704**	2,529	(2,218)	**35,302**
Net increase (decrease) in cash and cash equivalents	**13,124**	11,667	(59,788)	**98,492**
Cash and cash equivalents:				
Balance at beginning of year	**120,436**	108,769	145,907	**903,835**
Decrease from exclusion of a division of a subsidiary due to conversion of the subsidiary's stock	**—**	—	(10,635)	**—**
Amount applicable to subsidiaries newly included in consolidation	**—**	—	33,285	**—**
Net increase in cash and cash equivalents due to mergers	**148**	—	—	**1,110**
Balance at end of year	**¥133,708**	¥120,436	¥108,769	**$1,003,437**
Supplemental information on cash flows:				
Cash paid during the period for interest	**¥ 3,384**	¥ 4,573	¥ 11,067	**$ 25,396**
Conversion of convertible bonds	**2**	28	5,903	**15**

The accompanying notes are an integral part of these statements.

1. Basis of Presentation of the Financial Statements

Fuji Heavy Industries Ltd. (the "Company") and its subsidiaries in Japan maintain their books of account and prepare their financial statements in accordance with accounting principles and practices generally accepted in Japan, while its foreign subsidiaries maintain their books of account and prepare their financial statements in conformity with those of the countries of their domicile.

The accompanying consolidated financial statements are basically an English-translated version of those prepared in accordance with accounting principles and practices generally accepted in Japan, which are different in certain respect from the application and disclosure requirement of International Accounting Standards ("IAS"), and filed with the appropriate Local Finance Bureau of the Ministry of Finance and the Tokyo, Osaka and Nagoya Stock Exchange as required by the Securities and Exchange Law of Japan. Certain reclassifications of accounts and modifications have been made in the accompanying financial statements to facilitate understanding by readers outside of Japan. Such reclassifications and modifications had no effect on the consolidated net income. In addition, the statements of shareholders' equity and certain information in the notes to the consolidated financial statements, which are not required under accounting principles and practices generally accepted in Japan, are presented herein as additional information.

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 foreign subsidiaries are included based on their fiscal year ended December 31, significant transactions that incurred between December 31 and March 31 are reflected in the consolidated financial statements.

The consolidated financial statements include the accounts of the Company and 67 subsidiaries in the year 2002 (68 in the year ended March 31, 2001 and 72 in the year ended March 31, 2000). In addition, 1 non-consolidated affiliate in the year 2002 (2 in the year ended March 31, 2001 and 2000) are accounted for by the equity method.

Investments in insignificant non-consolidated subsidiaries and affiliates not accounted for under 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 goodwill, and is amortized over a period of five years on the straight-line basis.

All assets and liabilities of subsidiaries acquired on or after April 1, 1999, which include not only the Company's interest in the subsidiary but also the minority interest portion, are valued based on fair values at the date the Company acquires control over the subsidiary. The investment cost of the Company is allocated to the identifiable assets and liabilities of the subsidiary; the unallocated cost is recorded as goodwill.

Translation of foreign currency accounts

Effective April 1, 2000, the Company and its subsidiaries in Japan adopted the revised accounting standard for foreign currency translation, under which monetary assets and liabilities denominated in foreign currencies are translated into Japanese yen at each balance sheet date with the resulting gains or loss included in the current statements of income.

All asset and liability accounts of foreign subsidiaries and affiliates are translated into Japanese yen at the exchange rates in effect at the balance sheet date of the foreign subsidiaries, except for common stock and capital surplus, which are translated at historical rates. Revenue and expense accounts are also translated at the average exchange rates during the current year. The resulting foreign currency translation adjustments are included in shareholders' equity and minority interest.

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. Provisions for sales allowances and incentives are recognized at the time of the sale. Revenue from operating leases is recognized on a straight-line basis over the lease term.

Allowance for doubtful accounts

Allowances for doubtful accounts are provided based on the amount calculated as the actual ratio of bad debt for ordinary receivables, and an amount required for uncollectible account for specific doubtful receivables.

Marketable securities and investment securities

Prior to April 1, 2000, securities listed on stock exchanges were stated at the lower of cost or market value, cost being determined by the moving-average method. Securities not listed on stock exchanges were stated at cost, as determined by the moving-average method, after devaluation for any permanent impairment.

The Company adopted new Japanese accounting standards for financial instruments from the fiscal year ended March 31, 2001. In accordance with the new standards, securities for which fair value is available are stated at 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. Bonds and debentures held-to-maturity are stated using the amortized interest cost method.

As a result of such adoption, income before income taxes and minority interest has increased by ¥1,759 million for the year ended March 31, 2001, as compared with the amounts under the previous accounting standards. Based on the review of the purposes of holding securities at April 1, 2000, securities held-to-maturity and other securities with maturities of one year or less have been classified as marketable securities in current assets and all other securities as investment securities. As a result, marketable securities in current assets decreased by ¥21,894 million and investment securities increased by the same amount as of April 1, 2000. Also, from the year ended March 31, 2001, impairment losses of ¥5,226 million for investment securities previously recorded in a separate allowance account have been directly offset against investment securities balance.

Derivative financial instruments and hedge accounting

The new accounting standard for financial instruments, effective from the year ended March 31, 2001, requires companies 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.

If derivative financial instruments are used as hedges and meet certain hedging criteria, the Companies defer recognition of gains or losses resulting from changes in fair value of derivative financial instruments until the related losses or gains on the hedged items are recognized.

Also, if interest rate swap contracts are used as hedges and 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 was executed.

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

Financial Instrument	Transaction, Assets and Liabilities
Forward exchange contracts	Future foreign exchange transactions
Interest swaps	Borrowings

The risk exposures to movements in the exchange rates and interest rates are hedged according to the Company's 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 the exchange rates and interest rates at their inception as well as during their term.

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 and repairs, and minor renewals and improvements are charged to statement of income as incurred.

Depreciation of property, plant and equipment is principally computed using the declining-balance method for the Company and subsidiaries in Japan, and using the straight-line method for foreign subsidiaries at rates based on the estimated useful lives of the assets according to general class, type of construction and use.

Accounting for leases

Under Japanese accounting standards for leases, finance leases are, in principle, accounted for on a similar basis to sales by lessors or purchases by lessees. However, finance leases which do not transfer ownership of leased assets to lessees as stipulated in lease contracts can be accounted for as an operating lease if certain "as if capitalized" information is disclosed in the notes to the financial statements. Therefore, as a lessee, the Company has accounted for those leases as operating lease and has charged periodic lease payments to expenses when paid.

Intangible assets

Goodwill are principally amortized by the straight-line method based on the accounting records maintained in conformity with generally accepted accounting principles and practices prevailing in the respective countries of domicile.

Computer software used internally by the Company is amortized by the straight-line method over the economic useful lives (three or five years).

Accrued pension and severance liability

On terminating employment, employees of the Company and 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 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.

Prior to April 1, 2000, the Company and subsidiaries in Japan recorded the accrued severance indemnities for employees, which represented 40% of the liability which would have been payable if all employees voluntarily terminated their services at the balance sheet date.

Effective April 1, 2000, new Japanese accounting standards for pension and severance benefits were adopted. In accordance with the new accounting standards, accrued pension and severance liability for employees has been provided based on the estimated amounts of projected benefit obligation and fair value of plan assets at the end of the fiscal year. Actuarial gains and losses will be amortized from the next fiscal year by the straight-line method over the periods (5–18 years); which are less than the estimated remaining service periods of employees. As a result of such adoption, pension costs have increased by ¥40,591 million, and income before income taxes and minority interest has decreased by ¥40,934 million for the year ended March 31, 2001, as compared with the amounts under the previous accounting standards.

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

Retirement benefits to directors and statutory auditors are subject to approval at a meeting of shareholders. Previously, severance and retirement benefits for directors were recorded as expense when paid. However, for the purpose of more accurately matching them with the period in which they arise, an accrual method of recording such expenses has been employed from the beginning of current year. The impact of such change on statements of income has not been significant and is also stated in Note 18.

Research and development costs

Research and development costs are expensed as incurred and amounted to ¥54,903 million (US$412,030 thousand), ¥46,622 million and ¥40,123 million for the years ended March 31, 2002, 2001 and 2000, respectively.

Other costs

The Company provides for accrued warranty claims on its products sold based on past experience of warranty services performed on actual claims and estimated warranty costs to be incurred in the future at the time of sale.

Loss on liquidation of affiliated companies

Loss on liquidation of affiliated companies provides for potential losses from liquidation and guarantees based on the reasonable estimation of the liquidation of the affiliated companies.

Income taxes

Deferred tax accounting, similar to IAS 12, was adopted from the beginning of the fiscal year ended March 31, 2000 in accordance with the new Japanese accounting standards. 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. The cumulative effect, as of April 1, 1999, of the accounting change resulting from the adoption of deferred tax accounting was directly credited to retained earnings in the amount of ¥6,582 million.

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 years ended March 31, 2000 and 2001 have been made to conform to the presentation for the year ended March 31, 2002.

3. Effect of Bank Holiday on March 31, 2002 and 2001

As financial institutions in Japan were closed on March 31, 2002 and 2001, ¥1,647 million (US$12,360 thousand) and ¥2,065 million of notes receivable and ¥209 million (US$1,568 thousand) and ¥238 million of notes payable maturing on March 31, 2002 and 2001, respectively, were settled on the following business day, April 1, 2002 and April 2, 2001 and accounted for accordingly.

4. U.S. Dollar Amounts

The U.S. dollar amounts included in the accompanying consolidated financial statements and the related notes represent a translation using the exchange rate of ¥133.25 to US$1, the approximate exchange rate at March 31, 2002. The U.S. dollar amounts are included solely for the convenience of the reader, and these translations should not be construed as a representation that the yen amounts actually represent, or have been or could be converted into U.S. dollars at the above or any other rate.

5. Additional Cash Flow Information

(a) Cash and cash equivalents as of March 31, 2002 and 2001 consisted of the following:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2002	*2001*	***2002***
Cash and time deposits	**¥ 56,466**	¥ 58,610	**$ 423,760**
Marketable securities	**116,461**	89,573	**874,004**
Short-term loans	**71,677**	66,519	**537,914**
	244,604	214,702	**1,835,678**
Less maturity over three months	**(110,896)**	(94,266)	**(832,241)**
Cash and cash equivalents	**¥133,708**	¥120,436	**$1,003,437**

(b) Assets and liabilities of subsidiaries merged into the Company:

Assets and liabilities of Subaru Research Center Co., Ltd. and Technical Association Center Subaru Limited, which have been merged into the Company during the year ended March 31, 2002, were as follows:

There is no increase in common stock or additional paid-in capital due to these mergers.

	Millions of yen
Current assets	¥739
Fixed assets	70
Total assets	809
Current liabilities	265
Long-term liabilities	22
Total liabilities	¥287

Cash and cash equivalents included in the above current assets figures amounted to ¥148 million.

6. Marketable Securities and Investment Securities

Information as to the value of marketable securities and investment securities at March 31, 2002 and 2001 is presented below according to the disclosure requirements applicable to the respective year:

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

(a) As of March 31, 2002:

	Millions of yen		
	Book value	*Fair value*	*Difference*
Fair value exceeding book value:			
Government bonds	**¥ 5**	**¥ 5**	**¥ 0**
Sub-total	**5**	**5**	**0**
Fair value not exceeding book value:			
Corporate bonds	**5,000**	**4,860**	**(140)**
Sub-total	**5,000**	**4,860**	**(140)**
Total	**¥5,005**	**¥4,865**	**¥(140)**

	Thousands of U.S. dollars		
	Book value	*Fair value*	*Difference*
Fair value exceeding book value:			
Government bonds	**$ 38**	**$ 38**	**$ 0**
Sub-total	**38**	**38**	**0**
Fair value not exceeding book value:			
Corporate bonds	**37,523**	**36,472**	**(1,051)**
Sub-total	**37,523**	**36,472**	**(1,051)**
Total	**$37,561**	**$36,510**	**$(1,051)**

(b) As of March 31, 2001:

			Millions of yen
	Book value	Fair value	Difference
Fair value exceeding book value:			
Government bonds	¥ 4	¥ 5	¥ 1
Sub-total	4	5	1
Fair value not exceeding book value:			
Corporate bonds	5,000	4,930	(70)
Sub-total	5,000	4,930	(70)
Total	¥5,004	¥4,935	¥(69)

(2) Other securities (available for sale securities) with fair value:

(a) As of March 31, 2002:

			Millions of yen
	Acquisition cost	Book value	Difference
Book value exceeding acquisition cost:			
Equity securities	**¥10,215**	**¥19,906**	**¥ 9,691**
Bonds			
Government and municipal bonds	**1,068**	**1,074**	**6**
Corporate bonds	**674**	**677**	**3**
Other	**2,636**	**2,637**	**1**
Other	**6,505**	**6,575**	**70**
Sub-total	**21,098**	**30,869**	**9,771**
Book value not exceeding acquisition cost:			
Equity securities	**14,714**	**13,624**	**(1,090)**
Bonds			
Government and municipal bonds	**1,998**	**1,972**	**(26)**
Corporate bonds	**15,955**	**15,921**	**(34)**
Other	**4,450**	**4,445**	**(5)**
Other	**198**	**172**	**(26)**
Sub-total	**37,315**	**36,134**	**(1,181)**
Total	**¥58,413**	**¥67,003**	**¥ 8,590**

	Thousands of U.S. dollars		
	Acquisition cost	*Book value*	*Difference*
Book value exceeding acquisition cost:			
Equity securities	**$ 76,661**	**$149,388**	**$72,727**
Bonds			
Government and municipal bonds	**8,015**	**8,060**	**45**
Corporate bonds	**5,058**	**5,081**	**23**
Other	**19,782**	**19,790**	**8**
Other	**48,818**	**49,343**	**525**
Sub-total	**158,334**	**231,662**	**73,328**
Book value not exceeding acquisition cost:			
Equity securities	**110,424**	**102,244**	**(8,180)**
Bonds			
Government and municipal bonds	**14,994**	**14,799**	**(195)**
Corporate bonds	**119,737**	**119,482**	**(255)**
Other	**33,396**	**33,359**	**(37)**
Other	**1,486**	**1,291**	**(195)**
Sub-total	**280,037**	**271,175**	**(8,862)**
Total	**$438,371**	**$502,837**	**$64,466**

(b) As of March 31, 2001:

	Millions of yen		
	Acquisition cost	*Book value*	*Difference*
Book value exceeding acquisition cost:			
Equity securities	¥ 8,558	¥15,595	¥7,037
Bonds			
Government and municipal bonds	1,847	1,849	2
Other	11,160	11,166	6
Other	4,874	4,930	56
Sub-total	26,439	33,540	7,101
Book value not exceeding acquisition cost:			
Equity securities	23,916	19,804	(4,112)
Bonds			
Government and municipal bonds	1	0	(1)
Other	10,098	10,097	(1)
Other	2,551	2,542	(9)
Sub-total	36,566	32,443	(4,123)
Total	¥63,005	¥65,983	¥2,978

(3) Other securities (available for sale securities) sold during the years ended March 31, 2002 and 2001:

(a) For the year ended March 31, 2002:

Sales amount	*Total gains*	*Total losses*
¥815,133 million	¥49 million	¥136 million
US$6,117,321 thousand	US$368 thousand	US$1,021 thousand

(b) For the year ended March 31, 2001:

Sales amount	*Total gains*	*Total losses*
¥ 35,773 million	¥ 2,815 million	¥ 14 million

(4) Book value of major securities without available fair value (except for held-to-maturity debt securities stated in (1)) as of March 31, 2002 and 2001:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2002	*2001*	***2002***
Money management fund	**¥31,897**	¥31,272	**$239,377**
Commercial paper	**20,174**	21,819	**151,400**
Free financial fund	**17,806**	—	**133,629**
Medium-term note	**8,000**	—	**60,038**
Medium-term government bond fund	**7,103**	—	**53,306**
Unlisted stocks (excluding over-the-counter stocks)	**6,523**	6,622	**48,953**

Note: The Company recognized loss on devaluation of securities of ¥8,970 million (US$67,317 thousand) in the current year in which loss on devaluation of securities with fair value was ¥7,577 million (US$56,863 thousand).

The Company treated the above loss by separately recognizing the decline in fair value of the securities worth more than fifty percent of the acquisition cost and for the decline in fair value of the securities between thirty and fifty percent of the acquisition cost. Where the loss was between thirty and fifty percent, an analysis of recoverability of fair value was performed for each security.

(5) Schedule of redemption for other securities with maturity (available for sale securities) and held-to-maturity debt securities as of March 31, 2002 and 2001:

(a) As of March 31, 2002:

	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*
1) Debt securities								
Government and municipal bonds	**¥ 750**	**¥1,483**	**¥671**	**¥147**	**$ 5,628**	**$11,129**	**$5,036**	**$1,103**
Corporate bonds	**24,200**	**115**	**243**	**28**	**181,613**	**863**	**1,823**	**210**
Other	**27,109**	**5,147**	**—**	**—**	**203,445**	**38,627**	**—**	**—**
2) Other	**1,190**	**202**	**—**	**—**	**8,931**	**1,516**	**—**	**—**
Total	**¥53,249**	**¥6,947**	**¥914**	**¥175**	**$399,617**	**$52,135**	**$6,859**	**$1,313**

(b) As of March 31, 2001:

	Millions of yen	
	Within 1 year	1 to 5 years
1) Debt securities		
Government and municipal bonds	¥ 1,099	¥ 753
Corporate bonds	1,499	5,001
Other	41,570	10
2) Other	4,100	202
Total	¥48,268	¥5,966

7. Inventories

Inventories at March 31, 2002 and 2001 consisted of the following:

	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2002	*2001*	***2002***
Finished products	**¥119,925**	¥106,061	**$ 900,000**
Work in process	**53,364**	53,244	**400,480**
Raw materials	**17,157**	8,672	**128,758**
Supplies	**2,102**	1,958	**15,775**
	¥192,548	¥169,936	**$1,445,013**

8. Property, Plant and Equipment

Property, plant and equipment at March 31, 2002 and 2001 are summarized as follows:

	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2002	*2001*	***2002***
Buildings and structures	**¥239,229**	¥227,437	**$1,795,340**
Machinery and vehicles	**459,791**	457,931	**3,450,589**
Other	**189,630**	168,521	**1,423,114**
	888,650	853,889	**6,669,043**
Less accumulated depreciation	**(579,422)**	(548,750)	**(4,348,383)**
Land	**150,649**	140,810	**1,130,574**
Construction in progress	**21,880**	10,632	**164,203**
Total	**¥481,757**	¥456,581	**$3,615,437**

9. Revaluation Reserve for Land

In accordance with the Law to Partially Revise the Land Revaluation Law (Law No. 34, enacted on March 31, 1998), land owned by a consolidated subsidiary for business use was revalued. The unrealized gains from the revaluation are included in shareholders' equity as "Revaluation reserve for land", net of deferred taxes. The deferred taxes of the unrealized gains are included in long-term liabilities other. The land was revalued as of March 31, 2002 as follows:

	Millions of yen	*Thousands of U.S. dollars*
Book value of land for business use before revaluation	¥ 592	$ 4,443
Book value of land for business use after revaluation	1,704	12,788

The fair value of land is determined based on official notice prices that are assessed and published by the Commissioner of the National Tax Administration, as stipulated in Article 2, paragraph 3 of the Ordinance Implementing the Law Concerning Land Revaluation. Reasonable adjustments, including those for the timing of assessment, are made to the official notice prices.

10. Short-Term Borrowings and Long-Term Debts

Short-term borrowings at March 31, 2002 and 2001 consisted of the following:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2002	*2001*	***2002***
Bank loans with an average interest rate of 1.6% per annum	**¥169,807**	¥180,227	**$1,274,349**

Long-term debts at March 31, 2002 and 2001 consisted of the following:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2002	*2001*	***2002***
Loans principally from banks and insurance companies due through 2019 with average interest rate of 4.3% per annum	**¥105,325**	¥113,762	**$ 790,431**
Unsecured 1.8% convertible bonds due in 2003, convertible currently at ¥633.3 ($4.75) for one common share, redeemable before due date	**2,033**	2,035	**15,257**
Unsecured 0.9% convertible bonds due in 2003, convertible currently at ¥513 ($3.85) for one common share, redeemable before due date	**18,777**	18,777	**140,916**
Unsecured 2.25% bonds due July 31, 2002	**20,000**	20,000	**150,094**
Unsecured 2.10% bonds due August 29, 2003	**10,000**	10,000	**75,047**
Unsecured 2.30% bonds due September 30, 2005	**10,000**	10,000	**75,047**
Unsecured 1.76% bonds due April 30, 2004	**10,000**	10,000	**75,047**
Unsecured 0.97% bonds due April 15, 2006	**20,000**	—	**150,094**
Unsecured 1.22% bonds due September 30, 2008	**30,000**	—	**225,141**
Secured 1.8% bonds of a consolidated subsidiary due July 7, 2005	**300**	300	**2,251**
Secured 0.93% bonds of a consolidated subsidiary due February 15, 2007	**500**	—	**3,752**
	226,935	184,874	**1,703,077**
Less—Portion due within one year	**(43,845)**	(37,943)	**(329,043)**
	¥183,090	¥146,931	**$1,374,034**

Annual maturities of long-term debts at March 31, 2002 were as follows:

	Millions of yen	Thousands of U.S. dollars
2003	¥ 43,845	$ 329,043
2004	55,802	418,777
2005	41,393	310,642
2006	24,101	180,870
2007	29,452	221,028
2008 and thereafter	32,342	242,717
	¥226,935	$1,703,077

The following assets as of March 31, 2002 and 2001 were pledged as collateral for certain loans:

	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2002	*2001*	***2002***
Notes and accounts receivable, trade	**¥ 22,934**	¥ 2,746	**$ 172,112**
Other current assets	**784**	1,690	**5,884**
Property, plant and equipment	**116,311**	135,247	**872,878**
Investment securities	**206**	234	**1,546**
Other assets	**376**	—	**2,822**
	¥140,611	¥139,917	**$1,055,242**

Unsecured lines of credits for borrowings by the Company and subsidiaries (Subaru of America, Inc. and Subaru Europe N.V./S.A.) at March 31, 2002 were as follows:

	Millions of yen	Thousands of U.S. dollars
Total commitments	¥105,906	$794,792
Less amounts executed	15,053	112,968
Net balance	¥ 90,853	$681,824

11. Pension and Severance Plans

The Company and certain subsidiaries in Japan 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 fifty or over. Foreign subsidiaries primarily have defined contribution plans.

Reconciliation between the projected pension and severance obligation and allowance for pension and severance liability as of March 31, 2002 and 2001 were as follows:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2002	*2001*	***2002***
Projected pension and severance obligation	**¥127,801**	¥122,929	**$959,107**
Plan assets	**(49,856)**	(50,333)	**(374,154)**
Unfunded pension and severance obligations	**77,945**	72,596	**584,953**
Unamortized actuarial gain/loss	**(13,779)**	(6,933)	**(103,407)**
Unamortized prior service cost	**(2,172)**	—	**(16,300)**
Net amount recorded in balance sheet	**61,994**	65,664	**465,246**
Prepaid pension cost	**(19)**	(10)	**(142)**
Allowance for pension and severance liability	**¥ 62,013**	¥ 65,674	**$465,388**

Notes: 1. The above amounts include the government pension plan funded by social security taxes paid by employees and employer.
2. Certain insignificant subsidiaries calculate the liability using a simplified method.
3. In addition to the above plan assets, there are plan assets for the multi-employer pension plan amounted to ¥18,001 million (US$135,092 thousand) and ¥18,213 million for the years ended March 31, 2002 and 2001, 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.
4. Unrealized prior service cost arose from the change of accounting policy by certain consolidated subsidiaries.

Periodic pension and severance costs for the year ended March 31, 2002 and 2001 consisted of the following:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2002	*2001*	***2002***
Service cost	**¥ 7,813**	¥ 8,405	**$58,634**
Interest cost	**3,284**	3,187	**24,646**
Expected return on plan assets	**(1,856)**	(1,886)	**(13,929)**
Amortization of transition liability	**—**	44,520	**—**
Amortization of actuarial gain/loss	**422**	—	**3,167**
Amortization of prior service cost	**—**	—	**—**
Pension and severance cost	**¥9,663**	¥54,225	**$72,518**

Notes: 1. The above amounts do not include the social security taxes paid by employees.
2. Service costs of subsidiaries using the simplified method are included in Service cost above.
3. Service cost above includes service cost for the multi-employer pension plan amounted to ¥846 million (US$6,349 thousand) and ¥704 million for the years ended March 31, 2002 and 2001, respectively, in which plan assets could not be allocated to each specific participating employer.
4. Service cost above includes contributions for the defined contribution plans of foreign subsidiaries amounted to ¥1,286 million (US$9,651 thousand) and ¥1,046 million for the years ended March 31, 2002 and 2001, respectively.

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

a. Attribution of expected benefit obligation	Straight-line method
b. Discount rate	Primarily 3.0%
c. Expected rate of return on plan assets	Primarily 4.0%
d. Amortization of actuarial gain/loss	Primarily 18 years (will be amortized by the straight-line method starting from the next fiscal year based on periods less than the estimated average remaining service period of employees)
e. Amortization of prior service cost	Primarily 18 years (will be amortized by the straight-line method based on periods less than estimated average remaining service period of employees)
f. Amortization of transition liability	One year

12. Income Taxes

The Company is subject to a number of taxes based on income, which in aggregate, resulted in normal statutory tax rates of approximately 41.8% for the years ended March 31, 2002, 2001 and 2000.

A reconciliation of the statutory tax rate in Japan to the Company's effective income tax rate for the years ended March 31, 2002, 2001 and 2000 was as follows:

	2002	*2001*	*2000*
Statutory tax rate	**41.8%**	41.8%	41.8%
Increase (reduction) in taxes resulting from:			
Valuation allowance provided	**6.8**	(35.3)	9.0
Non-deductible expenses	**1.4**	2.1	0.9
Adjustment of past corporation taxes	**1.4**	—	—
Effect of lower taxes on foreign income	**(0.7)**	(2.3)	(0.3)
Tax credit	**—**	(4.0)	—
Other	**(0.3)**	(1.4)	0.3
Effective income tax rate	**50.4%**	0.9%	51.7%

Significant components of the deferred tax assets and liabilities at March 31, 2002 and 2001 were as follows:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2002	*2001*	***2002***
Deferred tax assets:			
Deficit carry forwards	**¥ 4,190**	¥ 4,308	**$ 31,445**
Unrealized gain on sales of inventories	**9,078**	7,489	**68,128**
Accrued pension and severance liabilities	**22,428**	20,419	**168,315**
Accrued expenses	**3,858**	6,556	**28,953**
Accrued enterprise taxes	**1,676**	697	**12,578**
Accrued employees bonuses	**5,008**	4,093	**37,583**
Warranty claims	**7,843**	6,392	**58,859**
Loss on valuation of investment securities	**4,067**	2,006	**30,522**
Unrealized gain on sales of property, plant and equipment	**7,417**	5,683	**55,662**
Loss on valuation of inventories	**1,842**	1,774	**13,824**
Allowance for doubtful accounts	**1,383**	1,838	**10,379**
Unearned revenue	**—**	2,294	**—**
Foreign tax credit	**1,377**	1,343	**10,334**
Loss on liquidation of affiliated companies	**2,876**	—	**21,583**
Other	**13,539**	5,991	**101,606**
Total deferred tax assets	**86,582**	70,883	**649,771**
Valuation allowance	**(10,378)**	(7,464)	**(77,884)**
Total deferred tax assets, net of valuation allowance	**76,204**	63,419	**571,887**
Deferred tax liabilities:			
Depreciation and amortization	**(12,442)**	(10,027)	**(93,373)**
Net unrealized holding gains on investment securities	**(3,619)**	(1,462)	**(27,159)**
Revaluation reserve for land	**(457)**	—	**(3,430)**
Other	**(146)**	(351)	**(1,096)**
Total deferred tax liabilities	**(16,664)**	(11,840)	**(125,058)**
Net deferred tax assets	**¥59,540**	¥51,579	**$446,829**

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*
	2002	*2001*	***2002***
Current assets—Deferred tax assets:	**¥34,278**	¥29,891	**$257,246**
Investments and other assets—Deferred tax assets:	**31,790**	26,763	**238,574**
Long-term liabilities—Deferred tax liabilities on revaluation of land:	**(457)**	—	**(3,430)**
Long-term liabilities—Other:	**(6,071)**	(5,075)	**(45,561)**
Total net deferred tax assets	**¥59,540**	¥51,579	**$446,829**

13. Shareholders' Equity

The Japanese Commercial Code provides that an amount equal to at least 10% of cash dividends and other distributions from retained earnings paid by the parent company and its subsidiaries in Japan is appropriated as a legal reserve. No further appropriation is required when the legal reserve equals 25% of stated capital. The Japanese Commercial Code, amended effective on October 1, 2001, provides that an amount equal to at least 10% of appropriations paid in cash be appropriated as a legal reserve until an aggregated amount of additional paid-in capital and the legal reserve equals 25% of common stock, and this legal reserve and additional paid-in capital excess 25% of common stock may be reduced by resolution of the shareholders. Legal reserve included in retained earnings as of March 31, 2002 and 2001 were ¥7,901 million (US$59,295 thousand) and ¥7,555 million, respectively, and are restricted to be used as dividends.

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, 2002 include amounts representing final cash dividends of ¥3,346 million (US$25,111 thousand), ¥9 (US$0.07) per share, and director's bonuses of ¥110 million (US$826 thousand), which were approved at the shareholders' meeting held on June 26, 2002.

14. Selling, General and Administrative Expenses

Selling, general and administrative expenses for the years ended March 31, 2002, 2001 and 2000 consisted of the following:

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars*
	2002	*2001*	*2000*	***2002***
Transportation and packing expenses	**¥ 14,171**	¥ 14,578	¥ 13,495	**$ 106,349**
Advertising cost	**51,196**	42,633	41,265	**384,210**
Sales incentives	**22,182**	15,248	16,696	**166,469**
Salaries and bonuses	**55,298**	54,026	55,840	**414,994**
Research and development cost	**53,735**	45,780	40,123	**403,265**
Others	**84,481**	79,108	76,174	**634,004**
	¥281,063	¥251,373	¥243,593	**$2,109,291**

15. Leases

(1) Information as lessee

As allowed under Japanese accounting standards, the Company and subsidiaries in Japan account for finance leases, which do not transfer ownership of leased assets to lessees as stipulated in lease contracts, as an operating lease. 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*
	2002	*2001*	***2002***
Machinery and vehicles	**¥1,159**	¥1,702	**$ 8,698**
Tools and other	**4,556**	6,116	**34,191**
Intangibles assets	**659**	797	**4,946**
	6,374	8,616	**47,835**
Accumulated depreciation	**(3,785)**	(5,480)	**(28,405)**
Net	**¥2,589**	¥3,136	**$19,430**

Information related to finance leases for the years ended March 31, 2002, 2001 and 2000 was as follows:

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars*
	2002	*2001*	*2000*	***2002***
Lease expenses	**¥1,331**	¥1,879	¥2,017	**$9,989**
Depreciation expense	**1,246**	1,725	1,757	**9,351**
Interest expense portion	**73**	111	141	**548**

Future minimum lease payments, excluding the portion of interest thereon, as of March 31, 2002 and 2001 were as follows:

	Millions of yen	*Millions of yen*	*Thousands of U.S. dollars*
	2002	*2001*	***2002***
Finance leases:			
One year or less	**¥ 1,026**	¥ 1,325	**$ 7,700**
More than one year	**1,518**	1,977	**11,392**
	¥ 2,544	¥ 3,302	**$ 19,092**
Operating leases:			
One year or less	**¥ 3,317**	¥ 2,558	**$ 24,893**
More than one year	**36,779**	34,215	**276,015**
	¥40,096	¥36,773	**$300,908**

(2) Information as lessor

Capitalized lease assets for finance leases at March 31, 2002 and 2001 were as follows:

	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2002	2001	**2002**
Machinery and vehicles	**¥11,961**	¥13,062	**$ 89,764**
Tools and other	**7,781**	5,515	**58,394**
Intangible assets	**213**	215	**1,598**
	19,955	18,792	**149,756**
Accumulated depreciation	**(8,867)**	(6,818)	**(66,544)**
	¥11,088	¥11,974	**$ 83,212**

Information related to finance leases for the years ended March 31, 2002, 2001 and 2000 was as follows:

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2002	2001	2000	**2002**
Lease income	**¥7,832**	¥5,086	¥ 8,852	**$58,777**
Depreciation expense	**5,894**	3,901	10,420	**44,233**
Interest income portion	**1,153**	1,286	1,163	**8,653**

Future minimum lease income, excluding the portion of interest thereon, as of March 31, 2002 and 2001 was as follows:

	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2002	2001	**2002**
Finance leases:			
One year or less	**¥ 5,624**	¥ 4,159	**$ 42,207**
More than one year	**10,710**	7,949	**80,375**
	¥16,334	¥12,108	**$122,582**
Operating leases:			
One year or less	**¥ 9,086**	¥ 8,490	**$ 68,187**
More than one year	**6,962**	7,263	**52,248**
	¥16,048	¥15,753	**$120,435**

16. Contingent Liabilities

Contingent liabilities at March 31, 2002 were as follows:

	Millions of yen	Thousands of U.S. dollars
Trade notes discounted with banks	¥ 203	$ 1,523
As guarantor of indebtedness from financial institutes	39,904	299,467
As guarantor of indebtedness of affiliated companies	15,164	113,801

17. Derivative Financial Instruments

In the normal course of business, the Company and its consolidated subsidiaries employ derivative financial instruments, including foreign exchange forward contracts 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 at March 31, 2002 and 2001 is summarized below according to the disclosure requirements applicable to the respective year:

(1) Foreign currency contracts:

(a) As of March 31, 2002:

			Millions of yen			*Thousands of U.S. dollars*
	Contract amount	*Fair value*	*Unrealized gains (losses)*	*Contract amount*	*Fair value*	*Unrealized gains (losses)*
Foreign currency options contracts:						
Sell—						
Call U.S. dollar	**¥2,648**			**$19,872**		
	[22]	**¥48**	**¥ (26)**	**[165]**	**$360**	**$(195)**
Buy—						
Put U.S. dollar	**2,522**			**18,927**		
	[22]	**6**	**(16)**	**[165]**	**45**	**(120)**

(b) As of March 31, 2001:

			Millions of yen
	Contract amount	*Fair value*	*Unrealized gains (losses)*
Foreign currency options contracts:			
Sell—			
Call U.S. dollar	¥29,172		
	[442]	¥926	¥(484)
Buy—			
Put U.S. dollar	27,931		
	[433]	240	(193)

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, 2002:

	Millions of yen			Thousands of U.S. dollars		
	Contract amount	*Fair value*	*Unrealized gains (losses)*	*Contract amount*	*Fair value*	*Unrealized gains (losses)*
Interest swap contracts:						
Receive floating rate						
pay fixed rate	¥3,000	¥(34)	¥(34)	$22,514	$(255)	$(255)

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

Derivative financial instruments, principally forward exchange contracts and currency and interest swaps, 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.

18. Segment Information

Information by industry segment

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

A summary of net sales, operating income, assets, depreciation and capital expenditures by industry segments for the years ended March 31, 2002, 2001 and 2000 are shown below:

Net sales:

	Millions of yen	*Millions of yen*	*Millions of yen*	*Thousands of U.S. dollars*
	2002	*2001*	*2000*	***2002***
Net sales:				
Automobiles—				
Outside customers	**¥1,219,766**	¥1,167,209	¥1,175,471	**$ 9,153,966**
Inter-segment	**2,970**	3,131	4,474	**22,289**
Total	**1,222,736**	1,170,340	1,179,945	**9,176,255**
Industrial products—				
Outside customers	**39,419**	44,224	51,847	**295,827**
Inter-segment	**136**	140	150	**1,021**
Total	**39,555**	44,365	51,997	**296,848**
Aerospace—				
Outside customers	**66,276**	65,504	66,144	**497,381**
Inter-segment	**53**	118	185	**398**
Total	**66,329**	65,622	66,329	**497,779**
Other—				
Outside customers	**37,032**	34,951	36,663	**277,914**
Inter-segment	**3,658**	2,555	2,172	**27,452**
Total	**40,690**	37,505	38,835	**305,366**
Elimination	**(6,817)**	(5,944)	(6,981)	**(51,160)**
Consolidated total	**¥1,362,493**	¥1,311,887	¥1,330,125	**$10,225,088**

Segment profit or loss:

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2002	2001	2000	**2002**
Operating income (loss):				
Automobiles	**¥85,649**	¥82,211	¥92,314	**$642,769**
Industrial products	**(290)**	784	1,283	**(2,176)**
Aerospace	**7,412**	2,467	2,034	**55,624**
Other	**(4,209)**	(4,100)	(4,411)	**(31,587)**
Total	**88,562**	81,362	91,220	**664,630**
Corporate and elimination	**(82)**	312	181	**(615)**
Consolidated operating income	**¥88,480**	¥81,673	¥91,401	**$664,015**

Assets:

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2002	2001	2000	**2002**
Total assets:				
Automobiles	**¥1,053,708**	¥ 956,131	¥ 849,046	**$7,907,752**
Industrial products	**62,126**	57,372	49,478	**466,236**
Aerospace	**110,156**	106,955	98,064	**826,687**
Other	**70,233**	74,851	47,993	**527,077**
Total	**1,296,223**	1,195,309	1,044,581	**9,727,752**
Corporate and elimination	**(26,665)**	(26,808)	(6,023)	**(200,112)**
Consolidated total	**¥1,269,558**	¥1,168,501	¥1,038,558	**$9,527,640**

Other significant items:

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2002	2001	2000	**2002**
Depreciation:				
Automobiles	**¥ 57,724**	¥ 57,225	¥ 53,651	**$433,201**
Industrial products	**2,055**	1,943	2,024	**15,422**
Aerospace	**2,084**	2,392	2,739	**15,640**
Other	**2,101**	2,510	1,821	**15,767**
Total	**63,964**	64,070	60,235	**480,030**
Corporate and elimination	**—**	—	(45)	**—**
Consolidated total	**¥ 63,964**	¥ 64,070	¥ 60,190	**$480,030**
Capital expenditures for segment assets:				
Automobiles	**¥109,054**	¥ 95,255	¥ 98,428	**$818,416**
Industrial products	**3,223**	2,155	2,296	**24,188**
Aerospace	**988**	1,535	1,671	**7,415**
Other	**5,111**	3,356	3,489	**38,356**
Total	**118,376**	102,301	105,884	**888,375**
Corporate and elimination	**—**	—	(1,962)	**—**
Consolidated total	**¥118,376**	¥102,301	¥103,922	**$888,375**

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	*Passenger cars, minicars*
Industrial products	*General-purpose engines, power generators*
Aerospace	*Aircraft, parts of space-related devices*
Other	*Rail cars, specialized vehicles, buses, houses, real estate*

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

4. All figures in corporate and elimination represent elimination.
5. Change of accounting policy
(Fiscal 2002)
Accrued directors' severance and retirement benefits.
Previously, severance and retirement benefits for directors were recorded as expense when paid. However, for the purpose of more accurately matching them with the period in which they arise, an accrual method of recording such expenses has been employed beginning from the current year. The impact of such change on statements of income has not been significant.
(Fiscal 2001)
None.

Information by geographic area

A summary of net sales, operating income and assets by geographic areas for the years ended March 31, 2002, 2001 and 2000 is shown below:

Net sales:

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2002	2001	2000	**2002**
Net sales:				
Japan—				
Outside customers	**¥ 801,351**	¥ 866,161	¥ 903,697	**$ 6,013,891**
Inter-segment	**280,213**	218,288	188,984	**2,102,912**
Total	**1,081,564**	1,084,448	1,092,681	**8,116,803**
North America—				
Outside customers	**557,509**	441,566	420,457	**4,183,933**
Inter-segment	**1,972**	1,645	1,799	**14,799**
Total	**559,481**	443,211	422,256	**4,198,732**
Other—				
Outside customers	**3,633**	4,161	5,971	**27,264**
Inter-segment	**85**	69	72	**638**
Total	**3,718**	4,230	6,043	**27,902**
Elimination	**(282,270)**	(220,002)	(190,855)	**(2,118,349)**
Consolidated total	**¥1,362,493**	¥1,311,887	¥1,330,125	**$10,225,088**

Segment profit or loss:

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2002	2001	2000	**2002**
Operating income:				
Japan	**¥72,393**	¥62,818	¥61,800	**$543,287**
North America	**20,705**	21,848	27,154	**155,385**
Other	**63**	62	181	**472**
Total	**93,161**	84,728	89,135	**699,144**
Corporate and elimination	**(4,681)**	(3,055)	2,266	**(35,129)**
Consolidated total	**¥88,480**	¥81,673	¥91,401	**$664,015**

Assets:

	Millions of yen	Millions of yen	Millions of yen	Thousands of U.S. dollars
	2002	*2001*	*2000*	***2002***
Assets:				
Japan	**¥1,031,129**	¥ 963,528	¥ 856,235	**$7,738,304**
North America	**282,230**	244,201	212,958	**2,118,049**
Other	**1,220**	1,281	1,918	**9,155**
Total	**1,314,579**	1,209,010	1,071,111	**9,865,508**
Corporate and elimination	**(45,021)**	(40,509)	(32,553)	**(337,868)**
Consolidated total	**¥1,269,558**	¥1,168,501	¥1,038,558	**$9,527,640**

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 expense are allocated to each segment.
4. Change of accounting policy
(Fiscal 2002)
Accrued directors' severance and retirement benefits.
Previously, severance and retirement benefits for directors were recorded as expense when paid. However, for the purpose of more accurately matching them with the period in which they arise, an accrual method of recording such expenses has been employed beginning from the current year. The impact of such change on statements of income has not been significant.
(Fiscal 2001)
None.

Overseas sales

Overseas sales for the years ended March 31, 2002, 2001 and 2000 are summarized as follows:

	Millions of yen		Millions of yen		Millions of yen		Thousands of U.S. dollars
	2002		*2001*		*2000*		***2002***
Overseas sales:							
North America	**¥ 607,630**	**44.6%**	¥ 491,068	37.4%	¥ 480,588	36.1%	**$ 4,560,075**
Europe	**56,820**	**4.2**	66,463	5.1	99,192	7.5	**426,417**
Other	**66,778**	**4.9**	66,160	5.0	63,876	4.8	**501,148**
Total	**¥ 731,228**	**53.7%**	¥ 623,691	47.5%	¥ 643,656	48.4%	**$ 5,487,640**
Consolidated net sales	**¥1,362,493**	**100.0%**	¥1,311,887	100.0%	¥1,330,125	100.0%	**$10,225,088**

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, Chile and Taiwan
3. Overseas sales are sales outside of Japan by the Company and consolidated subsidiaries.

To the Board of Directors of
FUJI HEAVY INDUSTRIES LTD.

We have audited the accompanying consolidated balance sheet of FUJI HEAVY INDUSTRIES LTD. (a Japanese corporation) and consolidated subsidiaries as of March 31, 2002 and the related consolidated statements of income, shareholders' equity and cash flows for the year then ended, expressed in Japanese yen. Our audit was made in accordance with generally accepted auditing standards in Japan and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. The financial statements of FUJI HEAVY INDUSTRIES LTD. and consolidated subsidiaries for year 2001, which are presented for comparative purposes, were audited by other auditors whose report dated June 27, 2001 expressed an unqualified opinion on those statements.

In our opinion, the consolidated financial statements referred to above present fairly the consolidated financial position of FUJI HEAVY INDUSTRIES LTD. and consolidated subsidiaries as of March 31, 2002, and the consolidated results of their operations and their cash flows for the year then ended in conformity with accounting principles generally accepted in Japan (see Note 1) applied on a consistent basis during the period, except as noted in the following paragraph.

FUJI HEAVY INDUSTRIES LTD. and consolidated subsidiaries changed the method of accounting for retirement benefit to directors and statutory auditors, effective April 1, 2001, as referred to in Notes 2 and 18 with which we concur.

Also, in our opinion, the U.S. dollar amounts in the accompanying consolidated financial statements have been translated from Japanese yen on the basis set forth in Note 4.

Tokyo, Japan
June 26, 2002

Asahi & Co.

Asahi & Co.

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. (74.0%)
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. (100.0%)
Manufacture of Subaru specially equipped automobiles and management of Subaru automobile parts distribution
http://www.kiryu-kougyo.co.jp/

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

Subaru Used Car Sales Co., Ltd. (100.0%)
Refurbishment, distribution, and sales of used Subaru cars

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

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

Yusoki Kogyo K.K. (45.6%)
Manufacture and sales of parts for car trailers, crane trucks, construction machinery, and automobiles
http://www.yusoki.co.jp/

TOKYO SUBARU INC. (100.0%)
and 40 other dealerships
Distribution, sales, and service of Subaru automobiles
http://www.sss.ne.jp/tokyo-subaru/

NIIGATA SUBARU, Inc.* (46.7%)
Distribution, sales, and service of Subaru automobiles
http://www.niigata-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.
Tel: (856) 488-8500
Fax: (856) 665-3346
Distribution and sales of Subaru automobiles
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.
Tel: (856) 488-8532
Fax: (856) 488-9279
Distribution and sales of Subaru automobiles

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

Subaru-Isuzu Automotive Inc. (51.0%)
and one subsidiary
5500 State Road 38 East, Lafayette, IN 47903, U.S.A.
Tel: (765) 449-1111
Fax: (765) 449-6952
Manufacture of Subaru and Isuzu automobiles
http://www.subaru-isuzu.com/

Subaru of Taiwan Co., Ltd. (As of May 30, 2002)
11, Lane 157, SEC. 6, Chung Shan N Rd.,
Taipei, Taiwan
Tel: 886-2-8866-6630
Fax: 886-2-2832-4021

Subaru Canada, Inc. (100.0%)
and one subsidiary
5990 Falbourne Street, Mississauga, Ontario, Canada L5R 3S7
Tel: (905) 568-4959
Fax: (905) 568-8087
Distribution and sales of Subaru automobiles
http://www.subaru.ca/

Subaru Europe N.V./S.A. (100.0%)
c/o Hermesstraat 6C, 1930 Nossegem-Zaventem, Belgium
Tel: (02) 714-0400
Fax: (02) 725-7792
Distribution and sales of automobiles, parts, and accessories

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

* Affiliates accounted for by the equity method

Head Office
Subaru Building, 7-2, Nishi-Shinjuku 1-chome, Shinjuku-ku,
Tokyo 160-8316, Japan
Tel: (03) 3347-2111
Fax (03) 3347-2338

Investor Relations Office
Subaru Building, 7-2, Nishi-Shinjuku 1-chome, Shinjuku-ku,
Tokyo 160-8316, Japan
Tel: (03) 3347-2655
Fax: (03) 3347-2295

Established
July 15, 1953

Paid-in Capital
¥144,450 million

Number of Shareholders
44,089

Number of Common Stock Issued and Outstanding
746,505,560

Domestic Manufacturing Divisions
Gunma Manufacturing Division (Automobile Division)
Utsunomiya Manufacturing Division (Aerospace Division and Transportation & Ecology Systems Division)
Isesaki Manufacturing Division (Bus Manufacturing & House Prefabricating Division)
Saitama Manufacturing Division (Industrial Products Division)

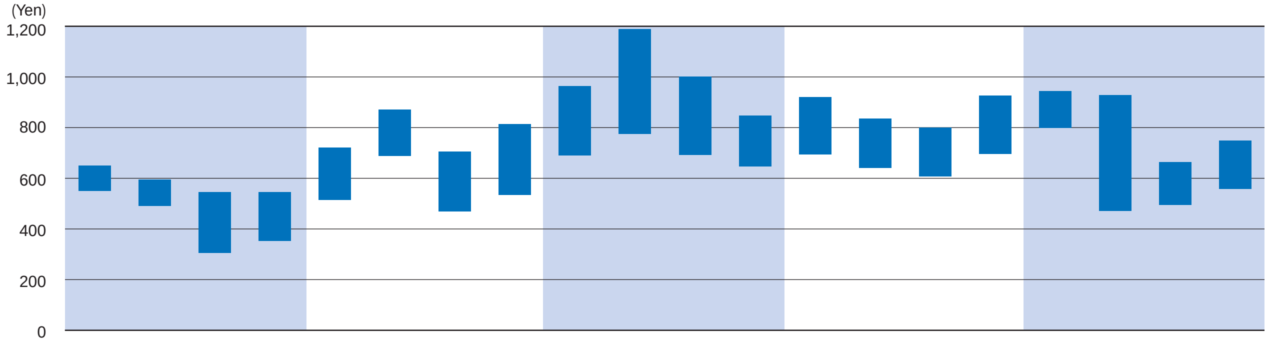
Major Shareholders
General Motors of Canada Limited
Japan Trustee Services Bank, Ltd.
The Mitsubishi Trust and Banking Corporation
The Industrial Bank of Japan, Ltd.
The Nippon Life Insurance Company
The Chase Manhattan Bank, N.A. London
Suzuki Motor Corporation
Trust & Custody Services Bank, Ltd.
UFJ Trust Bank Ltd.
J.P. Morgan Trust Bank Ltd.

Stock Listings
Tokyo Stock Exchange, Osaka Securities Exchange,
Nagoya Stock Exchange

Transfer Agent
Mizuho Trust & Banking Co., Ltd.
5-1, Marunouchi 1-chome, Chiyoda-ku, Tokyo 100-8240, Japan

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

Quarterly Common Stock Price Range (Tokyo Stock Exchange)



FY	1998	1999	2000	2001	**2002**
High	¥649	¥871	¥1,189	¥925	**¥944**
Low	305	469	647	608	**471**

FUJI HEAVY INDUSTRIES LTD.
Subaru Building, 7-2, Nishi-Shinjuku 1-chome, Shinjuku-ku, Tokyo 160-8316, Japan

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

Printed on recycled paper in Japan