Commission file number 1-7628

# HONDA MOTOR CO., LTD. <br> (Translation of Registrant's name into English) 

JAPAN
(Jurisdiction of incorporation or organization)
1-1, Minami-Aoyama 2-chome, Minato-ku, Tokyo 107-8556, Japan
(Address of principal executive offices)
Securities registered pursuant to Section 12(b) of the Act.
Title of each class
Common Stock*
$\frac{\text { Name of each exchange on which registered }}{\text { The New York Stock Exchange }}$

Securities registered or to be registered pursuant to Section 12(g) of the Act.

## None

(Title of class)
Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.
None
(Title of class)
Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.
Title of each class $\quad$ Outstanding as of March 31, 2007
Common Stock
1,821,992,908**
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes $\boxtimes \quad$ No
If this report is an annual or transmission report, indicate by check mark if the registrant is not required to file reports pursuant to
Section 13 or 15 (d) of the Securities Exchange Act of 1934. Yes $\square$ No $\boxtimes$
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes $\mathbb{\text { do }} \square$

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or, a non-accelerated filer. See definition of "accelerated filer and large accelerated filer "in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer $\boxtimes \quad$ Accelerated filer $\square \quad$ Non-accelerated filer $\square$
Indicate by check mark which financial statement item the registrant has elected to follow. Item $17 \square$ Item 18 区
If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange
Act). Yes $\square$ No $\boxtimes$

* Not for trading purposes, but only in connection with the registration of American Depositary Shares, each representing one share of Common Stock.
** Shares of Common Stock include 120,199,186 shares represented by American Depositary Shares.


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## PART I

Unless the context otherwise requires, the terms "we", "us", "our", "Registrant", "Company" and "Honda" as used in this Annual Report each refer to Honda Motor Co., Ltd. and its consolidated subsidiaries.

## Item 1. Identity of Directors, Senior Management and Advisors

Not applicable.

## Item 2. Offer Statistics and Expected Timetable

Not applicable.

## Item 3. Key Information

A. Selected financial data:

The selected consolidated financial data set out below for each of the five fiscal years ended March 31, 2007 have been derived from our consolidated financial statements that were prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP).

You should read the U.S. GAAP selected consolidated financial data set out below together with "Item 5. Operating and Financial Review and Prospects" and our consolidated financial statements contained in this Annual Report.

|  | Fiscal years ended March 31,Yen (millions) |  |  |  |  | U.S. dollars (millions) |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | 2003 | 2004 | 2005 | 2006 | 2007 | 2007 |
| Income statement data: |  |  |  |  |  |  |
| Net sales and other operatingrevenue . . . . . . . . . . $¥ 77,971,499 ¥ ¥ 8,162,600 ~ ¥ 8,650,105 ¥ 9,907,996 ~ ¥ 11,087,140$ \$ 93,919 |  |  |  |  |  |  |
| Research and development | 436,863 | 448,967 | 467,754 | 510,385 | 551,847 | 4,675 |
| Operating income | 724,527 | 600,144 | 630,920 | 868,905 | 851,879 | 7,216 |
| Income before income taxes, minority interest, and equity in income of affiliates . . . . . | 619,413 | 653,680 | 668,364 | 829,904 | 792,868 | 6,716 |
| Net income | 426,662 | 464,338 | 486,197 | 597,033 | 592,322 | 5,018 |
| Balance sheet data: |  |  |  |  |  |  |
| Total assets | ¥7,821,403 | ¥8,380,549 | ¥9,368,236 | $¥ 10,631,400$ | ¥12,036,500 | \$101,961 |
| Long-term debt | 1,140,182 | 1,394,612 | 1,559,500 | 1,879,000 | 1,905,743 | 16,144 |
| Stockholders' equity | 2,629,720 | 2,874,400 | 3,289,294 | 4,125,750 | 4,482,611 | 37,972 |
| Common stock | 86,067 | 86,067 | 86,067 | 86,067 | 86,067 | 729 |
| Depreciation and capital expenditures data: |  |  |  |  |  |  |
| Depreciation excluding property on operating |  |  |  |  |  |  |
| Depreciation of property on operating leases | - | - | - | - | 9,741 | 83 |
| Total depreciation | 220,874 | 213,445 | 225,752 | 262,225 | 371,488 | 3,147 |
| Capital expenditures | 316,991 | 287,741 | 373,980 | 457,841 | 627,066 | 5,312 |
| Purchase of operating lease assets | - | - | - | - | 366,795 | 3,107 |
| Total capital expenditures | 316,991 | 287,741 | 373,980 | 457,841 | 993,861 | 8,419 |

## Weighted average number of shares outstanding

|  | (Thousands of shares) |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  | 2003 | 2004 | 2005 | 2006 | 2007 |
| Weighted average number of common shares outstanding | 1,941,905 | 1,907,276 | 1,867,535 | 1,840,799 | 1,824,675 |

## Net income per common share

| Net income per common share | (Yen) |  |  |  |  | (US\$) |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | 2003 | 2004 | 2005 | 2006 | 2007 | 2007 |
| Basic | $¥ 219.71$ | $¥ 243.45$ | ¥260.34 | $¥ 324.33$ | $¥ 324.62$ | \$2.75 |
| Diluted | 219.71 | 243.45 | 260.34 | 324.33 | 324.62 | 2.75 |

Net income per common share has been computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding during each year.

## Cash dividends declared during the period per common share

## Cash dividends declared during the period per common

 share| (Yen) |  |  |  |  | (US\$) |
| :---: | :---: | :---: | :---: | :---: | :---: |
| 2003 | 2004 | 2005 | 2006 | 2007 | 2007 |
| $¥ 15.50$ | $¥ 17.50$ | $¥ 25.50$ | $¥ 38.50$ | $¥ 77.00$ | \$0.65 |

Additionally, a year-end dividend of $¥ 20$ ( $\$ 0.17$ ) per common share aggregating $¥ 36.4$ billion ( $\$ 309$ million) relating to fiscal 2007 was determined by our board of directors in April 2007 and approved by our shareholders in June 2007. This dividend was paid in June 2007.

## Stock Split

The Company executed a two-for-one stock split for the Company's common stock effective July 1, 2006. All per share information has been adjusted retroactively for all periods presented to reflect this stock split.

## Misclassification Adjustments

As described in Note (1) (v) and Note (2) to our consolidated financial statements, certain revisions for misclassifications have been made. Also, certain reclassifications have been made to the consolidated financial statement periods presented above to conform to the presentation used for the fiscal year ended March 31, 2007.

## Exchange Rates

In this Annual Report, yen amounts have been translated into U.S. dollars for the convenience of readers. Unless otherwise noted, the rate used for these translations was $¥ 118.05=\$ 1.00$, which represents the approximate exchange rate quoted on the Tokyo Foreign Exchange Market on March 31, 2007. No representation is made that yen amounts could have been, or could be, converted into U.S. dollars at that rate or any other rate on this or any other data or at all.

The following table sets out information regarding the noon buying rates for yen in New York City as certified for customs purposes by the Federal Reserve Bank of New York expressed in yen per $\$ 1.00$ during the periods shown. On June 29,2007 , the noon buying rate was $¥ 123.39=\$ 1.00$. The average exchange rate for the period shown is the average of the month-end rates during the period.

|  | (Yen) |  |  |  |
| :---: | :---: | :---: | :---: | :---: |
| Years ended March 31, | Average | Period end | High | Low |
| 2003 | 121.10 | 118.07 | 133.40 | 115.71 |
| 2004 | 112.75 | 104.18 | 120.55 | 104.18 |
| 2005 | 107.28 | 107.22 | 114.30 | 102.26 |
| 2006 | 113.67 | 117.48 | 120.93 | 104.41 |
| 2007 | 116.55 | 117.56 | 121.81 | 110.07 |
| 2008 (through June 29, 2007) | 121.53 | 123.39 | 124.09 | 117.69 |
| Dec-2006 |  |  | 119.02 | 114.98 |
| Jan-2007 |  |  | 121.81 | 118.49 |
| Feb-2007 |  |  | 121.77 | 118.33 |
| Mar-2007 |  |  | 118.15 | 116.01 |
| Apr-2007 |  |  | 119.84 | 117.69 |
| May-2007 |  |  | 121.79 | 119.77 |
| June-2007 |  |  | 124.09 | 121.08 |

## B. Capitalization and Indebtedness

Not applicable.

## C. Reason for the Offer and Use of Proceeds

Not applicable.

## D. Risk Factors

You should carefully consider the risks described below before making an investment decision. If any of the risks described below actually occurs, Honda's business, financial condition or results of operations could be adversely affected. In that event, the trading prices of Honda's common stock and American Depositary Shares could decline, and you may lose all or part of your investment. Additional risks not currently known to Honda or that Honda now deems immaterial may also harm Honda and affect your investment.

## Relating to Honda's industry

## Honda may be adversely affected by market conditions

Honda conducts its operations in Japan and throughout the world, including North America, Europe and Asia.

A continued economic slowdown, recession or sustained loss of consumer confidence in these markets, which may be caused by rising fuel prices or other factors, could trigger a decline in demand for automobiles, motorcycles and power products that may adversely affect Honda's results of operations.

## Prices for automobiles, motorcycles and power products can be volatile

Prices for automobiles, motorcycles and power products in certain markets may experience sharp changes over short periods of time.

This volatility is caused by many factors, including fierce competition, which is increasing, short-term fluctuations in demand from underlying economic conditions, changes in import regulations, shortages of certain supplies, high material prices and sales incentives by Honda or other manufacturers or dealers. There can be no assurance that such price volatility will not continue or intensify or that price volatility will not occur in markets that to date have not experienced such volatility. Overcapacity within the industry has increased and will likely continue to increase if the economic downturn continues in Honda's major markets or worldwide, leading, potentially, to further increased price pressure. Price volatility in any or all of Honda's markets could adversely affect Honda's results of operations in a particular period.

## Risks Relating Honda's Business Generally

## Currency and Interest Rate Risks

## Honda's operations are subject to currency fluctuations

Honda has manufacturing operations throughout the world, including Japan, and exports products and components to various countries.

Honda purchases materials and sells its products in foreign currencies. Therefore, currency fluctuations may affect Honda's pricing of products sold and materials purchased. Accordingly, currency fluctuations have an effect on Honda's results of operations and financial condition, as well as Honda's competitiveness, which will over time affect its results.

Since Honda exports many products and components from Japan and generates a substantial portion of its revenues in currencies other than the Japanese yen, Honda's results of operations would be adversely affected by an appreciation of the Japanese yen against other currencies, in particular the U.S. dollar.

## Honda's hedging of currency and interest rate risk exposes Honda to other risks

Although it is impossible to hedge against all currency or interest rate risk, Honda uses derivative financial instruments in order to reduce the substantial effects of currency fluctuations and interest rate exposure on our cash flow and financial condition.

These instruments include foreign currency forward contracts, currency swap agreements and currency option contracts, as well as interest rate swap agreements. Honda has entered into, and expects to continue to enter into, such hedging arrangements. As with all hedging instruments, there are risks associated with the use of such instruments.

While limiting to some degree our risk fluctuations in currency exchange and interest rates by utilizing such hedging instruments, Honda potentially forgoes benefits that might result from other fluctuations in currency exchange and interest rates. Honda is also exposed to the risk that its counterparties to hedging contracts will default on their obligations.

Honda manages exposure to counterparty credit risk by limiting the counterparties to major international banks and financial institutions meeting established credit guidelines. However, any default by such counterparties might have an adverse effect on Honda.

## Legal and Regulatory Risks

## The automobile, motorcycle and power product industries are subject to extensive environmental and

 other governmental regulationRegulations regarding vehicle emission levels, fuel economy, noise and safety and noxious substances, as well as levels of pollutants from production plants, are extensive within the automobile, motorcycle and power product industries. These regulations are subject to change, and are often made more restrictive. The costs to comply with these regulations can be significant to Honda's operations.

## Honda is reliant on the protection and preservation of its intellectual property

Honda owns or otherwise has rights in a number of patents and trademarks relating to the products it manufactures, which have been obtained over a period of years. These patents and trademarks have been of value in the growth of Honda's business and may continue to be of value in the future. Honda does not regard any of its businesses as being dependent upon any single patent or related group of patents. However, an inability to protect this intellectual property generally, or the illegal breach of some or a large group of Honda's intellectual property rights, would have an adverse effect on Honda's operations.

## Risks Relating to Honda's Operations

## Honda's financial services business conducts business under highly competitive conditions in an industry with inherent risks

Honda's financial services business offers various financing plans designed to increase the opportunity for sales of its products and to generate financing income. However, customers can also obtain financing for the lease or purchase of Honda's products through a variety of other sources that compete with our financing services, including commercial banks and finance and leasing companies. The financial services offered by us also involve risks relating to residual value, credit risk and cost of capital. Competition for customers and/or these risks may affect Honda's results of operations in the future.

## Honda relies on various suppliers for the provision of certain raw materials and component

Honda purchases raw materials, and certain components and parts, from numerous external suppliers, and relies on some key suppliers for some items and the raw materials it uses in the manufacture of its products. Honda's ability to continue to obtain these supplies in an efficient and cost-effective manner is subject to a number of factors, some of which are not within Honda's control. These factors include the ability of its suppliers to provide a continued source of supply and Honda's ability to compete with other users in obtaining the supplies. Loss of a key supplier in particular may affect our production and increase our costs.

## Honda conducts its operations in various regions of the world

Honda conducts its businesses worldwide, and in several countries, Honda conducts businesses through joint ventures with local entities, in part due to the legal and other requirements of those countries. These businesses are subject to various regulations, including the legal and other requirements of each country. If these regulations or the business conditions or policies of these local entities change, it may have an adverse affect on Honda's business, financial condition or results of operations.

## Honda may be adversely affected by wars, use of force by foreign countries, terrorism, multinational conflicts, natural disasters, epidemics and labor strikes

Honda conducts its businesses worldwide, and its operations may variously be subject to wars, use of force by foreign countries, terrorism, multinational conflicts, natural disasters, epidemics, labor strikes and other events beyond our control which may delay or disrupt Honda's local operations in the affected regions, including the purchase of raw materials and parts, the manufacture, sales and distribution of products and the provision of services. Delays or disruptions in one region may in turn affect our global operations. If such delay or disruption occurs and continues for a long period of time, Honda's business, financial condition or results of operations may be adversely affected.

## Cautionary statement with respect to forward looking statements in this Annual Report

This Annual Report includes "forward looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. The forward-looking statements included in this Annual Report are based on the current assumptions and beliefs of Honda in light of the information currently available to it, and involve known and unknown risks, uncertainties, and other factors. Such risks, uncertainties and other factors may cause Honda's actual results, performance, achievements or financial position to be materially different from any future results, performance, achievements or financial position expressed or implied by such forward-looking statements. Such risks, uncertainties and other factors are generally set forth in Item 3.D "Risk Factors" and include, without limitation:

- the political, economic and social conditions in Japan, the United States and elsewhere, including the relevant governments' specific policies with respect to economic growth, inflation, taxation, currency conversion, imports and sources of supplies and the availability of credit, particularly to the extent such current or future conditions and policies affect the automobile, motorcycle and power product industries and markets in Japan and the United States, and the demand, sales volume and sales prices for Honda's automobiles, motorcycles and power products;
- the effects of competition in the automobile, motorcycle and power product markets on the demand, sales volume and sales prices for Honda's automobiles, motorcycles and power products;
- Honda's ability to finance its working capital and capital expenditure requirements, including obtaining any required external debt or other financing; and
- the effects of economic stagnation or recession in Honda's principal markets and exchange rate fluctuations on the Honda's results of operations.

Honda undertakes no obligation and has no intention to publicly update any forward-looking statement after the date of this Annual Report. Investors are advised to consult any further disclosures by Honda in its subsequent filings pursuant to the Securities and Exchange Act of 1934.

## Item 4. Information on the Company

## A. History and Development of the Company

Honda Motor Co., Ltd. is a limited liability, joint stock corporation incorporated on September 24, 1948 under the Commercial Code of Japan as Honda Giken Kogyo Kabushiki Kaisha. It was formed to succeed to the business of an unincorporated enterprise established in 1946 by the late Soichiro Honda to manufacture motors for motorized bicycles.

Honda develops, produces, and manufactures a variety of motor products, ranging from small generalpurpose engines to specialty sports cars that incorporate Honda's highly efficient internal combustion engine technology. Approximately 20.4 million Honda engines were sold worldwide during the fiscal year ended March 31, 2007.

Honda's principal executive office is located at 1-1, Minami-Aoyama 2-chome, Minato-ku, Tokyo, 107-8556, Japan. Its telephone number is 81-3-3423-1111.

## Principal Capital Investments

In the fiscal years ended March 31, 2005, 2006 and 2007, Honda’s capital expenditures were $¥ 373.9$ billion, $¥ 457.8$ billion, and $¥ 993.8$ billion, respectively, on an accrual basis. Also, capital expenditures excluding those with respect to property on operating leases were $¥ 373.9$ billion, $¥ 457.8$ billion, and $¥ 627.0$ billion, respectively, on an accrual basis. For further details of Honda’s capital expenditures during fiscal 2007, see "Property, Plants and Equipment" included as "Item 4.D" of this Annual Report.

## B. Business overview

## Motorcycle Business

The following table sets out unit sales for Honda's motorcycle business, including motorcycles, all-terrain vehicles (ATVs) and personal watercraft (PWC), and revenue from its motorcycle business during the fiscal years ended March 31, 2003, 2004, 2005, 2006 and 2007:

|  | Fiscal years ended March 31, |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  | 2003 | 2004 | 2005 | 2006 | 2007 |
| Units (in thousands) | 8,080 | 9,206 | 10,482 | 10,271 | 10,369 |
| Revenue in billions of Japanese yen | $¥ 978$ | $¥ 996$ | $¥ 1,097$ | $¥ 1,225$ | $\geq 1,370$ |
| Revenue as a Percentage of total sales revenue | 12\% | 12\% | 13\% | 12\% | 12\% |

Honda produces a wide range of motorcycles, ranging from the 50 cc class to the 1800 cc class in cylinder displacement. Honda's motorcycles use gasoline engines developed by Honda that are air- or water-cooled, two or four-cycle, and single, two, four or six-cylinder. Honda's motorcycle line consists of sports (including trial and moto-cross racing), business and commuter models.

Honda's motorcycles are produced at two sites in Japan: Hamamatsu and Kumamoto. In fiscal 2007, the annual production output of these sites was 567,871 units. Honda's motorcycles are also produced by subsidiaries in the United States, Italy, Spain, Brazil, Thailand, Vietnam, the Philippines and India. Annual output in those countries in fiscal 2007 was approximately $324,000,165,000,38,500,1,214,000,2,690,000,865,000,312,000$ and 713,000 units, respectively. Certain motorcycle components are manufactured in Japan and shipped to foreign plants for assembly. Each plant also buys locally made parts or manufactures parts using Honda's intellectual property and technical guidance.

## Automobile Business

The following table sets out Honda's unit sales of automobiles and revenue from its automobile business during the fiscal years ended March 31, 2003, 2004, 2005, 2006 and 2007:

|  | Fiscal years ended March 31, |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  | 2003 | 2004 | 2005 | 2006 | 2007 |
| Units (in thousands) | 2,888 | 2,983 | 3,242 | 3,391 | 3,652 |
| Revenue in billions of Japanese yen | $¥ 6,440$ | ¥6,592 | ¥6,963 | ¥8,004 | ¥8,889 |
| Revenue as a percentage of total sales revenue | 81\% | 81\% | 80\% | 81\% | 80\% |

Honda's principal automobile products include the following vehicle models:
Passenger cars:
Legend, Accord, Civic, City, Acura RL, Acura TL, Acura TSX
Multi-wagons, Minivans, Sport Utility Vehicle, Sports coupe:
Elysion, Odyssey, Step Wagon, Edix, FR-V, Stream, Mobilio, Fit, Jazz, Airwave, Pilot, Ridgeline, Element, CR-V, Crossroad, Acura MDX, Acura RDX

Mini cars:

## Life, That's, Vamos, Zest, Acty

Automobiles are produced by Honda at two sites in Japan: the Saitama factory and the Suzuka factory. Our major production sites overseas are located in Ohio (U.S.A.), Alabama (U.S.A.), Alliston (Canada), Swindon (U.K.) and Ayutthaya (Thailand).

Yachiyo Industry Co., Ltd., one of our consolidated subsidiaries, assembles the Life, Vamos and VamosHobio, Zest, Acty-Truck and Acty-Van. The automobile assembled at Yachiyo Industry undergo final tests at the Suzuka factory. For this reason, for our management purposes, those automobile products are deemed to have been produced at the Suzuka factory, instead of at Yachiyo Industry.

## Financial Services Business

The following table sets out Honda's revenue from Financial Services during the fiscal years ended March 31, 2003, 2004, 2005, 2006 and 2007:

|  | Fiscal years ended March 31, |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  | 2003 | 2004 | 2005 | 2006 | 2007 |
| Revenue in billions of Japanese yen | ¥237 | $¥ 242$ | ¥255 | $¥ 306$ | $¥ 409$ |
| Revenue as a percentage of total sales revenue | 3\% | 3\% | 3\% | 3\% | 4\% |

In our financial services business, Honda offers a variety of financial services to our customers and dealers through finance subsidiaries in Japan and abroad, with the aim of providing sales support for our products.

## Power Product and Other Businesses

The following table sets out Honda's revenue from Power Product and Other Businesses during the fiscal years ended March 31, 2003, 2004, 2005, 2006 and 2007:

|  | Fiscal years ended March 31, |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  | 2003 | 2004 | 2005 | 2006 | 2007 |
| Units (in thousands) | 4,584 | 5,047 | 5,300 | 5,876 | 6,421 |
| Revenue in billions of Japanese yen | $¥ 315$ | $¥ 331$ | $¥ 332$ | $¥ 370$ | $¥ 417$ |
| Revenue as a percentage of total sales revenue | 4\% | 4\% | 4\% | 4\% | 4\% |

Honda manufactures a variety of power products including power tillers, portable generators, generalpurpose engines, grass cutters, outboard engines, water pumps, snow throwers, power carriers, power sprayers, lawn mowers and lawn tractors (riding lawn mowers).

## Marketing and Distribution

Most of Honda's products are distributed under trademarks of Honda in Japan and/or in overseas markets. Major trademarks include HONDA, ACURA, LEGEND, INSPIRE, ACCORD, CIVIC, CITY, FIT SALOON, FIT ARIA, ACURA RL, ACURA TL, ACURA TSX, ELYSION, ODYSSEY, STEP WGN, EDIX, FR-V, STREAM, MOBILIO, FIT, JAZZ, AIRWAVE, PILOT, RIDGELINE, ELEMENT, CR-V, CROSSROAD, MDX, ACURA MDX, S2000, INSIGHT, ACURA RDX, LIFE, THAT'S, VAMOS, ZEST, ACTY, GOLD WING, WAVE, and CUB.

## Sales in Japan

Sales of Honda motorcycles, automobiles, and power products in Japan are made through different distribution networks. Honda's products are sold to consumers primarily by independent retail dealers throughout Japan.

Motorcycles are distributed through approximately 7,700 outlets, including approximately 1,000 PROS authorized dealerships. PROS dealerships sell substantially all of Honda's Japanese motorcycle models.

Honda integrated its three sales channels in Japan-Primo, Clio and Verno-into one Honda channel in March 2006. At present, 912 retail dealers operate 2,352 shops and sell Legend, Inspire, Accord, Civic, Fit Aria, Elysion, Odyssey, Step Wagon, Edix, Stream, Spike, Mobilio, Fit, Airwave, CR-V, Crossroad, S2000, Partner, Zest, Life, That's, Vamos, Zest and Acty.

Power products are distributed in Japan to approximately 1,420 retail dealers throughout Japan, including affiliates of Honda. A number of small engines are also sold to other manufacturers for use in their products.

The independent retail dealers who sell Honda's products in Japan receive payment from customers by one of four payment methods: cash, bank loans, installment payments or financing by credit companies.

## Service and parts related operations in Japan

Sales of spare parts and after sales services are mainly provided through retail dealers. Lectures on service technology are provided for dealers regularly by Honda's Automobile Sales Operations (Japan).

## Overseas sales

Approximately $96 \%$ of Honda's overseas sales are made through its principal foreign sales subsidiaries, which distribute Honda's products to local wholesalers and retail dealers.

In the United States, which is the largest market for Honda automobiles, Honda markets its products through a sales network of approximately 1,288 independent local dealers for automobiles, approximately 1,250 for motorcycles and approximately 5,700 for power products. Many of the motorcycle dealers and some of the automobile dealers also sell Honda’s power products. In 1986, Honda opened the first Acura automobile dealerships in the United States. The Acura network in the United States totaled 268 dealerships at the end of fiscal 2007. The Acura network offers $R L, T L, T S X, M D X, R S X, R D X$ and $C S X$ (Canada only) models.

With regard to exports from North America, Honda is currently exporting such North American-built models as Accord, Civic, TL, Odyssey, Pilot, Ridgeline, Element and MDX to other markets. In fiscal 2007, Honda exported approximately 35,074 units from North America to 37 countries throughout the world.

In Europe, Honda's products are distributed in the United Kingdom, Germany, France, Belgium, the Netherlands, Spain, Switzerland, Austria, Italy and other European countries through approximately 1,800 independent local dealers for automobiles, approximately 1,950 for motorcycles and approximately 7,400 for power products.

Honda Motor Co., Ltd. exports motorcycle components to 14 countries, including Indonesia, Thailand, India, Brazil and the People's Republic of China, where motorcycles are manufactured by its subsidiaries, joint venture firms and licensees. Some of the components used in the production of these vehicles are supplied locally.

Honda Motor Co., Ltd. exports automobile components to 14 countries, including the United States, Canada, the People's Republic of China, Thailand and Brazil, where automobiles are manufactured by Honda, joint venture firms and licensees. Some of the components used in the production of these vehicles are supplied locally.

Honda Motor Co., Ltd. also exports power product components to eight countries, including the United States, Thailand, Italy, the People's Republic of China, France, India, Australia, where power products are manufactured by Honda, joint venture firms and licensees. Some of the components used in the production of these products are supplied locally.

## Service and parts related operations overseas

Honda provides its overseas operations, joint venture firms, independent distributors and licensees with spare parts and necessary technical information, which they in turn supply to wholesale or retail dealers, either directly or through one or more spare parts distributors.

## Net Sales by Product Group and Region

Breakdown of Net Sales and Other Operating Revenue by Category of Activity

|  | Fiscal years ended March 31,Yen (millions) |  |  |
| :---: | :---: | :---: | :---: |
|  | 2005 | 2006 | 2007 |
| Motorcycle Business | ¥1,097,754 | $¥ 1,225,812$ | $¥ 1,370,617$ |
| Automobile Business | 6,963,635 | 8,004,694 | 8,889,080 |
| Financial Services | 255,741 | 306,869 | 409,701 |
| Power Product and Other Businesses | 332,975 | 370,621 | 417,742 |
| Total | ¥8,650,105 | ¥9,907,996 | $\underline{¥ 11,087,140}$ |

## Breakdown of Net Sales and Other Operating Revenue by Geographical Markets

|  | Fiscal years ended March 31,Yen (millions) |  |  |
| :---: | :---: | :---: | :---: |
|  | 2005 | 2006 | 2007 |
| Japan | $¥ 1,699,205$ | $¥ 1,694,044$ | $¥ 1,681,190$ |
| North America | 4,575,076 | 5,463,359 | 5,980,876 |
| Europe | 870,795 | 1,009,421 | 1,236,757 |
| Asia | 977,011 | 1,085,451 | 1,283,154 |
| Others | 528,018 | 655,721 | 905,163 |
| Total | ¥8,650,105 | ¥9,907,996 | ¥11,087,140 |

## Components and Parts, Raw Materials and Sources of Supply

Honda manufactures the major components and parts used in its products, including engines, frames and transmissions. Other components and parts, such as shock absorbers, electrical equipment and tires, are purchased from numerous suppliers. The principal raw materials used by Honda are steel plate, aluminum, special steels, steel tubes, paints, plastics and zinc, which are purchased from several suppliers. The most important raw material purchased is steel plate, accounting for approximately $41 \%$ of Honda's total purchases of raw materials.

No single supplier accounted for more than 5\% of the Company's purchases of major components and parts and principal raw materials during the fiscal year ended March 31, 2007.

Honda does not have and does not anticipate having any difficulty in obtaining its required materials from suppliers and considers its contracts and business relations with the suppliers to be satisfactory. The Company does not believe any of its domestic suppliers are substantially more dependent on foreign suppliers than are Japanese suppliers generally. However, it should be noted that Japanese industry in general is heavily dependent on foreign suppliers for substantially all of its raw materials.

## Seasonality

Honda's motorcycle and power product businesses have historically experienced some seasonality. However, this seasonality has not generally been material to our financial results.

## Environmental and Safety Regulation

## Outline of Environmental and Safety Regulation for Automobiles

## 1. Emissions

## Japan

In 2005, to limit emissions into the environment, the Central Environment Council in the Ministry of Environment created new long-term targets and comprehensive requirements for gasoline and diesel vehicles which will become effective starting from 2008. The long term targets for gasoline vehicles remain unchanged except for direct injection gasoline vehicles which will be required to meet the PM standard. Long-term emissions targets for diesel vehicles have been lowered by more than $50 \%$ from the current level of NOx and PM standards.

## The United States

Increasingly stringent emission regulations under the Clean Air Act have been enacted since the 1990s by the U.S. federal government. Under the Act, the Environmental Protection Agency (EPA) in February 2000 adopted more stringent vehicle emissions regulations applicable to passenger cars and light-duty trucks produced from model year 2004. Moreover, the new standard provides for gradual decreases in sulfur levels contained in fuel in the U.S. market.

Under the Clean Air Act, the State of California is permitted to establish its own emission control standards to the extent they are more stringent than federal standards. Pursuant to this authority, the California Air Resources Board (CARB) adopted the "California Low Emission Vehicle Program" in 1990, aiming to establish the strictest emission regulation in the world. In late 1998, CARB strengthened its regulatory standards through the introduction of new standards, known as the "California Low Emission Vehicle Program II" ("LEV II"). These new standards treat most light trucks the same as passenger cars and require both types of vehicles to meet the new emissions standards of LEV II. In January 2001, CARB approved modifications to the "Zero-Emission Vehicles" ("ZEV") requirement under LEV II, permitting gasoline SULEVs (Super Ultra Low Emission

Vehicles), hybrid vehicles (powered by gasoline engine and/or electric motor) and compressed natural gas ("CNG") vehicles to partially meet zero-emission requirements by satisfying certain additional requirements. The modified requirements also provide incentives for continued technology development.

In April 2004, CARB finalized its "ZEV" requirements. Under these requirements, from the 2005 model year, $6 \%$ of vehicles sold in California by a car manufacturer must be Partial Zero Emission Vehicles ("PZEV"), which includes SULEV's with warranties coverage up to the earlier of 15 years or 150,000 driven miles, $2 \%$ must be advanced technology PZEV's and $2 \%$ must be ZEV's. Required percentages will be gradually increased under the "Zero-Emission Vehicle" standards from the 2008 model year.

Currently, many states have adopted or proposed the California ZEV regulation. The ZEV mandate has been implemented in some states, and will be implemented in other states.

## Europe

In 1999, the European Union adopted Euro3 and Euro4 as comprehensive emissions regulations for passenger vehicles and heavy and light commercial vehicles. Euro3 was implemented in 2000 and Euro4 was implemented in 2005.

In each EU country, standards, such as those providing for preferential automobile tax treatment, have been established in respect of diesel vehicles that comply with the requirements prescribed in Euro4 for which the PM emission does not exceed $5 \mathrm{mg} / \mathrm{km}$. Honda has already introduced a considerable number of Euro4-compliant diesel models in Europe.

In 2005, the European Union created a new emission standard (Euro5 and Euro6) and comprehensive requirements for gasoline vehicles and diesel vehicles. Euro5 will become effective starting around 2009. Emission limits for gasoline vehicles and diesel vehicles will be lowered by more than the Euro level of HC, NOx and PM. Euro6 will become effective starting around 2014. Emission limits for diesel vehicles will be lowered by more than the Euro5 level HC and NOx.

Additionally, Euro5 and Euro6 will add the requirement of a PM number limit for diesel vehicles. A PM mass limit will also apply to gasoline vehicles which use lean burn direct injection engines.

## Other Regions

China adopted Step3 and Step4 emission regulations for light-duty vehicles in 2005.

These regulations are similar to Euro3 and Euro4. Step3 will be implemented in 2007 and Step4 will be implemented in 2010.

In the city of Beijing, Euro3 was implemented in December 2005.
South Korea adopted the enforcement regulation of the Special Act on Capital Region Air Quality Improvement.

Accordingly, some manufacturers shall be required to sell low emission vehicles which meet a more stringent emission standard than those meeting the national standard.

In addition, other several Asian countries adopted regulations which are similar to the European regulations (such as Euro2 and Euro3).

In Australia, Euro4-equivalent regulations will be implemented in July 2008.

## 2. Fuel Economy / CO <br> Japan

In 1998, an amendment was made to the Law Concerning Rationalization of Energy Usage that established a fuel efficiency standard based on weight class in Japan. This standard was tightened in 2005 for diesel-fueled automobiles. For gasoline automobiles, tighter standards, to be implemented in 2010, have also been established.

In light of the $\mathrm{CO}_{2}$ reduction targets promulgated under the Kyoto Protocol, the Japanese government issued a fuel regulation for an interim ethanol blending limit (less than 5\%) which became effective in 2003. The Japanese government intends to further increase this limit until the final target of $10 \%$ is achieved within a decade.

In 2005, discussions about the POST 2010 standard took place among the applicable ministries and industries.

In February 2007, the final POST 2010 target, or the "2015 standard", was announced. Fuel consumption will be reduced by $29.2 \%$ compared to the 2010 target for passenger cars.

Ethanol blended fuel is a "biomass fuel". Biomass fuel is regarded as an effective countermeasure for $\mathrm{CO}_{2}$ reduction. $\mathrm{CO}_{2}$ emissions after burning ethanol fuel produced with biomass resources (such as plants or wood) are not counted as $\mathrm{CO}_{2}$ emissions under the Kyoto Protocol.

## The United States

The Federal Motor Vehicle Information and Cost Savings Act requires automobile manufacturers to comply with the Corporate Average Fuel Economy ("CAFE") standards. Under the CAFE standards, manufacturers are subject to substantial penalties if automobiles produced by them in any model year do not meet the average standards for each category. The CAFE standard for passenger cars has been set at 27.5 miles per gallon (mpg) starting from the 1990 model year and for light trucks a 20.7 miles per gallon standard was established for the 1996-2004 model years. The standard for light trucks increased from the 2005 model year ( 21.0 miles per gallon) to the 2007 model year ( 22.2 miles per gallon). The National Highway Traffic Safety Administration ("NHTSA") reformed the CAFE standard for light trucks in 2006. The new size-based CAFE standard for light trucks will be implemented in the 2008 model year. Passenger cars are divided into the following two categories: "Domestic" and "Import", and credits earned in one category may not be applied to another.

In addition, the U.S. Senate and the House of Representatives are undergoing heated discussions on the topic of raising the CAFE standards for passenger cars.

In August 2005, CARB finalized its Green House Gas (GHG) regulation. Under the GHG regulation, which will become effective for the 2009 model year, automobile manufactures have to improve fuel economy from the current levels by more than $50 \%$ by the 2016 model year.

Many other states have adopted the GHG regulations.
In April 2007, the Supreme Court ruled that the EPA has the authority to regulate GHG emissions. In response to the Supreme Court's ruling, the President has directed his agencies to take the first steps toward regulations that would reduce gasoline consumption and GHG emissions from motor vehicles by 20 percent over the next 10 years.

## Europe

In early 1999, the European Union reached a voluntary agreement with the European Automotive Manufacturers Association for the establishment of an average emissions target of 140 grams of carbon dioxide per kilometer for new cars offered for sale in the EU in 2008. The Japan Automobile Manufacturers Association
("JAMA") and the Korean Automobile Manufacturers Association also reached a similar voluntary agreement with the European Union targeting implementation in 2009. In 2003, in an interim review, the emissions reduction efforts made by these associations were reviewed and the possibility of setting a more stringent target of above 140 grams is now being discussed. In 2003, JAMA achieved the midterm target (165-175 grams). JAMA achieved additional reduction of carbon dioxide in 2005 as compared to 2004.

In 2006, discussions about establishing targets for 2008 will begin among the European Commission, Member States and the automobile industry.

In early 2007, European Commission published "Results of the review of the Community Strategy to reduce $\mathrm{CO}_{2}$ emissions from passenger cars and light-commercial vehicles". According to this communication, the European Commission will be setting a more stringent target of 130 grams of carbon dioxide per kilometer for new cars offered for sale in the EU in 2012.

The EU is also recommending the use of biomass fuel blends.

## Other Regions

China adopted a fuel consumption regulation for passenger vehicles in 2004. Step 1 of this regulation was implemented in 2005 and Step 2 will be implemented in 2008.

South Korea adopted the regulation of Corporate Average Fuel Economy for passenger vehicles in 2005. Domestic vehicles will be required to adhere to the regulations starting from 2006 and imported vehicles will need to meet the requirement in 2010.

## 3. Recycling / End-of-Life Vehicles ("ELV")

## Japan

Japan enacted the Automobile Recycling Law in July 2002, which required manufacturers to take back air bags, fluorocarbon and shredder residue derived from end-of-life vehicles ("ELV"), which became effective on January 1, 2005. ELV processing costs are collected from owners of cars currently in use and purchasers of new cars.

## Europe

In September 2000, the European Union approved a directive requiring its member states to promulgate regulations implementing the following by April 21, 2002:

Manufacturers must be financially responsible for taking back end-of-life vehicles offered for sale after July 1, 2002 and dismantle and recycle the vehicles. Beginning on January 1, 2007, the requirement has also applied to all vehicles offered for sale in the European Union before July 1, 2002.

Manufacturers must not use specified hazardous materials in vehicles offered for sale in the European Union after July 2003; and

95\% of vehicle parts in new vehicle types sold in the European Union after December 15, 2008, must be designed to be re-usable and recoverable.

On December 30, 2006, the European Union adopted the Regulation concerning the Registration, Evaluation, Authorization and Restriction of Chemicals (REACH), which becomes effective on June 1, 2007. From June 1, 2008, any manufacturer or importer of a substance is required to submit a registration to the Agency, depending on annual production or import quantity. Also, any manufacturer or importer of an article is
required to submit a registration for the substances contained in such article this is intended to be released. Submitting a pre-registration between June 1, and December 1, 2008 will allow the manufacturer or importer to extend the deadline for submitting the registration for existing substances.

## Other Regions

Taiwan and Korea will implement automobile recycling laws from January 1, 2008 following the regulations established by the European Union and Japan. In addition, China has a plan to implement automobile recycling laws in the near future.

## 4. Safety

## Japan

In March 2005, the Ministry of Land, Infrastructure and Transport issued the world's first Seat Belt Reminders standard. Pursuant to the standard, the driver's seat in passenger vehicles must be equipped with a seat belt reminder from September 1, 2005 for new models and from September 1, 2008 for all other models.

JASIC, which is organized by MLIT and JAMA, among others, has started to review a proposal for the unification of Safety/Environment Standards, vehicle categories and certification in order to promote further internationalization of standards and certifications.

JASIC is planning to make the proposal to other contracting parties of the 58 / 98 Agreement by 2009 and aim at reaching an agreement among the contracting parties by 2015.

## The United States

In December 2003, NHTSA issued various motor vehicle safety standards, including a final rule specifying enhanced fuel system integrity requirements. For example, the rule changes the test method for rear crash impacts from a full-lap $48 \mathrm{~km} / \mathrm{h}$ test to an offset $80 \mathrm{~km} / \mathrm{h}$ test, and sets forth a phase-in compliance schedule mandating that $40 \%$ of all vehicles produced by a manufacturer meet the new safety standard by $2006,70 \%$ by 2007, and $100 \%$ by 2008.

In December 2003, vehicle manufacturers, including us, presented to the public a statement on crash vehicle compatibility, "ENHANCING VEHICLE-TO-VEHICLE CRASH COMPATIBILITY: A Set of Commitments for Progress by Automobile Manufacturers." This report describes the recommended performance criteria and research plans developed by an international group of safety experts for enhancing vehicle-to-vehicle crash compatibility in front-to-front and front-to-side crashes. By September 1, 2007, the goal is to have at least 50\% of all vehicles offered in the U.S. by participating manufacturers to meet the front-to-side performance criteria, and by September 2009, for $100 \%$ of the vehicles of participating manufacturers to meet the criteria. For the front-to-front criteria, the goal is for $100 \%$ of the vehicles of participating manufacturers to meet the criteria by September 2009, with no interim goals set. We are a participating manufacturer and intend to meet these voluntary standards.

In May 2004, NHTSA issued a proposed rule to upgrade side impact protection standards. The rule imposes a requirement to provide head protection and adopt a small adult female dummy in side crashes for the first time. Manufacturers must meet an additional performance test involving a $32-\mathrm{km} / \mathrm{h}$ vehicle side impact into a rigid pole at an approach angle of 75 degrees for $20 \%$ of all vehicles produced by a manufacturer by $2009,50 \%$ by 2010, and $100 \%$ by 2011. New dummies will be used from September 1, 2009 for the existing moving deformable barrier and new pole tests.

In December 2004, NHTSA issued a standard to require Lap/Shoulder Safety Belts for rear center seats in passenger vehicles. Manufacturers must comply with it for $50 \%$ of all vehicles produced by 2005, $80 \%$ by 2006, and $100 \%$ by 2007.

NHTSA reissued a final rule regarding a tire pressure monitoring system standard in April 2005 based on the Transportation Recall Enhancement, Accountability and Documentation Act ("TREAD Act"), which was finalized in June 2002 but vacated in November 2003 by a court decision. Manufacturers must comply with the standard for $20 \%$ of all vehicles produced by $2005,70 \%$ by 2006 , and $100 \%$ by 2007.

In August 2006, NHTSA issued a final rule revising performance requirements for advanced airbag systems. The rule upgrades the maximum speed for frontal barrier crash tests using a belted small adult female dummy. Manufacturer must comply with the upgraded requirements for $35 \%$ of all vehicles produced by $2009,65 \%$ by 2010, and $100 \%$ by 2011.

In August 2006, NHTSA issued a regulation to standardize requirements for the accuracy, collection, storage, survivability, and retrievability of onboard motor vehicle crash event data in passenger cars and other light vehicles equipped with event data recorders on or after September 2010.

In April 2007, NHTSA issued a final rule regarding an electronic stability control system standard for light vehicles to reduce rollover crashes. The new standard will require installation of electronic stability control system. Manufacturers must comply with the standard for $55 \%$ of all vehicles produced by $2008,75 \%$ by 2009 , $95 \%$ by 2010 , and $100 \%$ by 2011 .

In May 2007, NHTSA issued a final rule to revise some performance requirements for head restraints, to delay the effective date, and to set a phase-in compliance schedule. For front seat requirements, manufacturer must comply with the revised requirements for $80 \%$ of all vehicles produced by 2009 , and $100 \%$ by 2010 . For voluntarily installed rear head restraints, manufacturers also must be in compliance for $80 \%$ of all vehicles by 2010, and $100 \%$ by 2011.

## Europe

The European Commission issued a regulation and technical prescription for pedestrian protection. The regulation required M1 (Passenger vehicles up to nine passengers) and N1 (Light commercial vehicles with gross vehicle weight up to 3.5 t ) vehicles to meet standards for the protection of pedestrians in the event of a collision with the front of a motor vehicle.

The regulation consists of Phase 1, to be effective October 1, 2005 for new types of vehicles and December 31, 2012 for all vehicles, and Phase 2, to be effective September 1, 2010 for new types of vehicles and September 1, 2015 for all vehicles.

In early 2004, The European Commission issued a revised regulation relating to indirect vision to reduce "blind spots" on motor vehicles of which side and rear areas were not visible to the driver via side or rear-view mirrors. The regulation has been effective from January 29, 2006 for new types of vehicles and will be effective on January 29, 2010 for all vehicles.

Additionally, the European Commission has established a project called "eSafety" aiming at cutting road fatalities in half by 2010. The project focuses on road accident prevention. To achieve this target, such issues as the introduction of new features on automobiles are being discussed.

## 5. New Car Assessment Program (NCAP)

Programs that provide customers with assessments of car safety functions and promote the development of car safety by automobile manufacturers are conducted in countries such as the United States, Japan, Australia, the EU, Korea and China. The principal items assessed in these programs are passenger protection and braking power, which are typically assessed with stricter standards or criteria than those required by statute.

In the United States, in September 2006, NHTSA issued a final rule to require displaying specified NCAP information on a safety rating label that is part of their Monroney label. New passenger vehicles manufactured on or after September 2007 must comply with the rule.

In January 2007, NHTSA also issued a report titled, "The New Car Assessment Program Suggested Approaches for Future Program Enhancements" to encourage additional safety improvements, and to provide consumers with relevant information that will aid them in their new vehicle purchasing decisions. The future program includes detail proposals regarding not only crash worthiness assessment but also crash avoidance assessment.

## Outline of Environmental and Safety Regulation for Motorcycles

## 1. Emissions

## Japan

Japan has emissions regulations for motorcycles applicable to all classes of engine displacement. Some aspects of these requirements, such as standards for hydro-carbon levels and durability, are stricter than the current European regulations, namely the Euro1 regulations. The Central Environment Council in the Ministry of Environment issued a final report on targets for fiscal year 2006. The target level is similar to those under the Euro3 standards.

## The United States

Emissions regulations regarding off-road motorcycles and ATVs were introduced in 2006. In addition, the EPA adopted the current California emissions standards regarding on-road motorcycles on a national basis two years behind the schedule of California. The new regulations include fuel permeation requirements rather than traditional evaporative emission standards.

## Canada

The Canadian federal government has introduced emissions regulations generally equivalent to the U.S. EPA regulations for on-road motorcycles from the 2006 model year.

Currently, the Canadian federal government has proposed to introduce the emission regulations for off-road motorcycles generally equivalent to the U.S. EPA regulations.

## Europe

The EU maintains emissions regulations (Euro2) for motorcycles, as well as the "Motor Cycle (\& Moped)Whole Vehicle Type Approval", a uniform certification system for two and three-wheeled motor vehicles.

The Euro3 regulations are the most stringent standard for motorcycles. Euro3 regulations have been in effect from January 2006.

## Other Regions

Other countries, mainly in Asia, have implemented tighter emissions regulations based on European regulations.

In Thailand, a fifth stage of emissions control, which is generally equivalent to or stricter than Euro2, has been implemented. A sixth stage of emissions control, which is generally equivalent to or stricter than Euro3, will be introduced in 2008.

In Indonesia, Euro2-equivalent regulations have been in effect from January 2006.
In China, Euro2-equivalent regulations were introduced in 2004.
In Korea, Euro2-equivalent regulations were implemented in 2006. In addition, Euro3- equivalent regulations will be implemented from 2008.

In Brazil, Euro2-equivalent regulations have been in effect from the beginning of last year. Euro3equivalent regulations will be implemented in the beginning of 2009.

In India, regulations based on the Indian authorities' own test method are in effect and enhanced regulations were enacted in 2005.

## 2. Safety

## The United States

Three-wheeled all terrain vehicles, or ATVs (formerly referred to as "ATC"s) became a problem for the youth-involved accidents in 80s', and ATV regulations were about to created at that time. However, it turned out that a voluntary standard, which was agreed between the industry and regulators, was established. There was no further increase of accidents in 90s', but the rapid development of ATVs in the U.S. market from 2000 and the problem of increased youth-involved accidents became a focus again. The Consumer Product Safety Commission has been concerned about this, and is now conducting a review to make the voluntary standard for ATVs compulsory regulation.

## Europe

ATVs designed to travel on four low pressure tires on non-paved surfaces has recently increased in the EU market. Most ATVs obtained authorization by the WVTA (Whole Vehicle Type Approval) and are permitted to run on highways. As a result, there has been a problem of increasing accidents. As a result, the ATVEA (All Terrain Vehicle European industry Association) was established, and it is now are focusing on ATV standards rulemaking. It is expected that a standard will be completed in about five years at the earliest.

## Outline of Environmental and Safety Regulation for Power Products

## 1. Emissions

## The United States

The EPA enacted new engine emissions regulations applicable to model year 1997 for small non-road engines. These regulations are also applicable to engines in use from the 2001 model year. With respect to marine engines, emissions regulations for outboard engines and personal watercraft were implemented for the 1998 model year products and were gradually strengthened every year until the 2006 model year. Currently, the EPA has proposed enhanced emission regulations for non-road engines and marine engines.

In 1995, the State of California enacted new engine emissions regulations for small non-road engines. California is now gradually shifting its focus on emissions regulations for engines in use manufactured in the 2000 model year and beyond. California has introduced tighter tail-pipe emissions standards and added requirements for evaporative emissions from small non-road engines from the 2006 model year. With respect to marine engines, California enacted emissions regulations for model year 2001 outboard engines and personal watercraft that are equivalent to the U.S. federal government's 2006 model year regulations, and strengthened these regulations in the model year 2004. California plans to further strengthen the regulations for these products in the 2008 model year.

## Canada

The Canadian federal government has introduced emissions regulations generally equivalent to the U.S. EPA regulations for small non-road engines from the 2005 model year, with some exceptions.

Currently, the Canadian federal government has proposed to introduce emission regulations for marine engines generally equivalent to the U.S. EPA regulations.

## Europe

Emissions regulations regarding diesel non-road mobile machinery have been in place in the European Union. The EU has introduced regulations covering gasoline engines from 2004 based on the contents of the current EPA regulations in the United States and introduced emissions regulations targeting outboard engines and personal watercraft from 2005. In addition, with respect to marine engines, emissions regulations have been implemented since 1993 in Bodensee, which is located between Switzerland, Germany and Austria.

## 2. Safety

## Japan

The Consumer Product Safety Law, as amended, which mandates manufacturers and/or importers liable for product accidents to give a report to the Minister of the Ministry of Economy, Trade and Industry (METI), became effective on May 14, 2007.

Main points of this Law are as follows:

1. Manufacturers and importers are mandated to notify a serious product accident.
2. Distributors, retailers and repair shops are encouraged to inform manufacturers and importers.
3. Products covered by this Law include all products utilized in daily life except for products regulated by other laws (such as motor vehicles, medicines, etc.).
4. Mandatory reports are limited to serious accidents (involving fatal and serious injury accident, CO poisoning, and fire).
5. Product name, etc. are published to the public as necessary to prevent danger and hazard from occurring or expanding.

## The United States

The CPSC issued a final rule to require that portable generators bear a carbon monoxide poisoning warning label. This regulation requires that the label include pictograms and statements warning consumers that "a generator's exhaust contains poisonous carbon monoxide" and that "a generator should never be used inside the home or partially enclosed areas such as garages". This regulation became effective on May 14, 2007 and applies to any portable generator manufactured or imported on or after that date.

## Strengthening our Commitment to Reduce Our Environmental Footprint

Under the direction of "commitment for the future," Honda will continue pursuing more proactive efforts to reduce its environmental footprint, with its main focus on $\mathrm{CO}_{2}$ reduction.

## Reduction of $\mathrm{CO}_{\mathbf{2}}$ Emissions-Setting Voluntary Goals

Honda has voluntarily set global $\mathrm{CO}_{2}$ reduction goals for its products and production activities and is accelerating its efforts to achieve those goals.

In 2000, the global average of $\mathrm{CO}_{2}$ exhaust emissions among Honda automobiles was $179.5 \mathrm{~g} / \mathrm{km}$. Despite increased sales of larger-size vehicles such as SUV and minivans, average $\mathrm{CO}_{2}$ emissions were reduced by $5 \%$ during the five-year period up to 2005.

Honda now strives to achieve a further reduction of $5 \%$ or more, aiming to accomplish a total of $10 \%$ reduction by 2010 compared to the level of 2000 . Honda will also work toward a $10 \%$ reduction both for motorcycles and power products.

At Honda, the global average of $\mathrm{CO}_{2}$ emissions to produce one automobile also declined by approximately $5 \%$ during the five-year period up to 2005 . Honda is working toward a further reduction by $5 \%$ or more by 2010 to achieve a total reduction of $10 \%$ compared to the level of 2000 . For motorcycle and power product production, Honda set goals to reduce $\mathrm{CO}_{2}$ emissions by $20 \%$ in each area.

Honda is the first automaker in the world to announce global $\mathrm{CO}_{2}$ reduction goals for its products and production activities.

## New Clean Diesel

Based on the current highly successful diesel engine currently sold in Europe, Honda is now developing a cleaner next-generation four-cylinder diesel engine. This engine will meet the U.S. EPA's stringent Tier2 BIN5 emission standard requiring NOx emission levels equivalent to a gasoline-powered vehicle. Honda plans to introduce this super-clean diesel engine to market within the next three years.

Honda will also work toward development of a clean V6 diesel engine.

While improving the fuel efficiency of gasoline engines with Advanced VTEC, Advanced VCM, and other technologies, Honda will expand application of hybrid technology to smaller size vehicles and diesel technology to medium-to-large size vehicles. Thorough these comprehensive efforts leveraging the unique characteristics of each environmental technology, Honda will accelerate its efforts to reduce $\mathrm{CO}_{2}$ emissions.

## Motorcycles

Moreover, Honda will introduce new engine technologies such as super-low friction engines, which will improve fuel economy by up to $13 \%$ compared to the current level, and VCM systems for motorcycles, which will improve fuel economy by up to $30 \%$ compared to the current level.

## Preparing for the Future

Looking globally, the U.S. economy is showing signs of a moderate downturn, while European economies are expected to continue recovering and Asian economies are expected to continue expanding. Japan's economy is forecast to sustain its gradual recovery. However, the global environment in which Honda's management operates still remains uncertain because of global political and economic uncertainties, fluctuations in oil and raw material prices and currency movements. As a result, we expect the operating environment to remain difficult.

It is under these circumstances that Honda seeks to strengthen its corporate structure quickly and flexibly to meet the requirements of our customers and society and the changes in its business environment. Also, in order to improve the competitiveness of its products, Honda will endeavor to enhance its R\&D, production and sales ability. Furthermore, Honda will continue striving to earn even more trust and understanding from society through Companywide activities. Honda recognizes that further enhancing the following specific areas is essential to its success:

## Research and Development

Along with efforts to develop even more effective safety and environmental technologies, Honda will enhance creativity in its advanced technology and products, and will create and swiftly introduce new valueadded products that meet specific needs in various markets around the world. Honda will also continue its efforts to research future technologies.

## Production Efficiency

Honda will establish efficient and flexible production systems and expand production capacity at its global production bases, with the aim of increasing its capability of supplying high quality products.

## Sales Efficiency

Honda will remain proactive in its efforts to expand product lines through the innovative use of IT and to upgrade sales and service structure, in order to further satisfy its customers.

## Product Quality

Responding to increasing consumer demand, Honda will upgrade its quality control through enhancing the functions of and coordination among the development, purchasing, production, sales and service departments.

## Safety Technologies

Honda will develop safety technologies for accident prediction and prevention, technologies to reduce injuries to passengers and pedestrians from car accidents, and technologies for reducing aggressivity, as well as expand its line-up of products incorporating such technologies. Honda will reinforce and continue to advance its contributions to traffic safety in motorized societies in Japan and overseas. Honda also intends to remain active in a variety of traffic safety programs, including advanced driving and motorcycling training schemes provided by local dealerships.

## The Environment

Honda will step up its efforts to create better, cleaner and more fuel-efficient engine technologies and to further improve recyclables throughout its product lines. The Company also plans to make further progress with fuel cells and solar cells and to promote commercialization of solar cells. In addition, Honda will further its efforts to minimize its environmental impact. To this end, we set global targets to reduce the environmental burden as measured by the Life Cycle Assessment, in all areas of business, spanning production, logistics and sales.

## Continuing to Increase Society's Trust in and Understanding toward Honda

In addition to continuing to provide products incorporating Honda's advanced safety and environmental technologies, Honda will continue striving to earn even more trust and understanding from society by, among other things, undertaking activities for corporate governance, compliance, and risk management and contributing to society.

Through these Company-wide activities, we will strive to materialize Honda's visions of "value creation (Creating New Value for our Customers)," "globalization (Expanding Regional Operations)," and "commitment to the future (Developing Safety and Environmental Solutions)," with the aim of sharing the joy with Honda's customers, thus becoming a company valued by society.

## * Life Cycle Assessment

A comprehensive system for quantifying the impact Honda's products have on the environment at different stages in their life cycles, from material procurement and energy consumption to waste disposal.

## C. Organizational Structure

As of March 31, 2007, the Company had 151 Japanese subsidiaries and 254 overseas subsidiaries. The following table sets out for each of the Company's principal subsidiaries, the country of incorporation, function and percentage ownership and voting interest held by Honda.

| Company | Country of Incorporation | Function | Percentage Ownership and Voting Interest |
| :---: | :---: | :---: | :---: |
| Honda R\&D Co., Ltd. | Japan | Research \& Development | 100.0 |
| Honda Engineering Co., Ltd. | Japan | Manufacturing and Sales of machine tools, equipment and production techniques | 100.0 |
| Yachiyo Industry Co., Ltd. | Japan | Manufacturing | 50.5 |
| Honda Lock Mfg. Co., Ltd. | Japan | Manufacturing | 100.0 |
| Yutaka Giken Co., Ltd. | Japan | Manufacturing | 69.7 |
| Asama Giken Co., Ltd. | Japan | Manufacturing | 81.7 |
| Honda Foundry Co., Ltd. | Japan | Manufacturing | 82.1 |
| Honda Motorcycle Japan Co., Ltd. | Japan | Sales | 100.0 |
| Honda Finance Co., Ltd. | Japan | Finance | 100.0 |
| Mobilityland Corporation | Japan | Others (Leisure) | 100.0 |
| Honda Trading Corporation | Japan | Others(Trading) | 100.0 |
| Honda Logistics Inc. | Japan | Others (Physical Distribution) | 100.0 |
| American Honda Motor Co., Inc. | U.S.A. | Sales | 100.0 |
| Honda North America, Inc. | U.S.A. | Coordination of Subsidiaries Operation | 100.0 |
| Honda of America Mfg., Inc. | U.S.A. | Manufacturing | 100.0 |
| American Honda Finance Corporation | U.S.A. | Finance | 100.0 |
| Honda Manufacturing of Alabama, LLC | U.S.A. | Manufacturing | 100.0 |
| Honda of South Carolina Mfg., Inc. | U.S.A. | Manufacturing | 100.0 |
| Honda Transmission Mfg. of America, Inc. | U.S.A. | Manufacturing | 100.0 |
| Honda Precision Parts of Georgia, LLC | U.S.A. | Manufacturing | 100.0 |
| Honda Power Equipment Mfg., Inc. | U.S.A. | Manufacturing | 100.0 |
| Honda R\&D Americas, Inc. | U.S.A. | Research \& Development | 100.0 |
| Cardington Yutaka Technologies Inc. | U.S.A. | Manufacturing | 100.0 |
| Celina Aluminum Precision Technology |  |  |  |
| Inc. | U.S.A. | Manufacturing | 100.0 |
| Honda Trading America Corporation | U.S.A. | Other (Trading) | 100.0 |
| Honda Engineering North America, Inc. | U.S.A. | Manufacturing and Sales of machine tools, equipment and production techniques | 100.0 |
| Honda Canada Inc. | Canada | Manufacturing and Sales | 100.0 |
| Honda Canada Finance Inc. | Canada | Finance | 100.0 |
| Honda de Mexico, S.A. de C.V. | Mexico | Manufacturing and Sales | 100.0 |
| Honda Europe NV | Belgium | Sales | 100.0 |
| Honda Motor Europe Limited | U.K. | Coordination of Subsidiaries Operation and Sales | 100.0 |
| Honda of the U.K. Manufacturing Ltd. | U.K. | Manufacturing | 100.0 |
| Honda Finance Europe plc | U.K. | Finance | 100.0 |
| Honda Motor Europe (South) S.A. | France | Sales | 100.0 |
| Honda Europe Power Equipment, S.A. | France | Manufacturing and Sales | 100.0 |
| Honda Motor Europe (North) GmbH | Germany | Sales | 100.0 |



## D. Property, Plants and Equipment

Honda's manufacturing operations are principally conducted in 32 separate factories, four of which are located in Japan. The following table sets out information, as of March 31, 2007, with respect to Honda's principal manufacturing facilities, all of which are owned by Honda:

| Location | Number of Employees | Principal Products Manufactured |
| :---: | :---: | :---: |
| Sayama, Saitama, Japan | 5,286 | Automobiles |
| Hamamatsu, Shizuoka, Japan | 3,376 | Motorcycles, power products and transmissions |
| Suzuka, Mie, Japan | 7,102 | Automobiles |
| Ohzu-machi, Kikuchi-gun Kumamoto, Japan | 2,923 | Motorcycles, all-terrain vehicles, power products and engines |
| Marysville, Ohio, U.S.A. | 6,895 | Motorcycles and automobiles |
| Anna, Ohio, U.S.A. | 2,850 | Engines |
| East Liberty, Ohio, U.S.A. | 2,596 | Automobiles |
| Lincoln, Alabama, U.S.A. | 4,563 | Automobiles |
| Swepsonville, North Carolina, U.S.A. | 566 | Power products |
| Timmonsville, South Carolina, U.S.A. | 1,603 | All-terrain vehicles |
| Alliston, Ontario, Canada | 4,585 | Automobiles |
| El Salto, Mexico | 1,487 | Motorcycles and automobiles |
| Swindon, Wiltshire, U.K. | 4,046 | Automobiles and engines |
| Ormes, France | 171 | Power products |
| Atessa, Italy | 760 | Motorcycles, power products and engines |
| Barcelona, Spain | 293 | Motorcycles |
| Guangzhou, China | 1,096 | Automobiles |
| Chongqing, China | 881 | Power products |
| Greater Noida, India | 1,331 | Automobiles |
| Gurgaon, India | 2,598 | Motorcycles |
| Karawang, Indonesia | 1,218 | Automobiles |
| Alor Gajah, Malaysia | 1,204 | Automobiles |
| Lahore, Pakistan | 587 | Automobiles |
| Manila, Philippines | 646 | Motorcycles and power products |
| Laguna, Philippines | 687 | Automobiles |
| Pingtung, Taiwan | 661 | Automobiles |
| Ayutthaya, Thailand | 2,546 | Automobiles |
| Bangkok, Thailand | 2,697 | Motorcycles and power products |
| Vinhphuc, Vietnam | 1,108 | Motorcycles and automobiles |
| Sumare, Brazil | 1,947 | Automobiles |
| Manaus, Brazil | 6,462 | Motorcycles and power products |
| Gebze, Turkey | 539 | Automobiles |

In addition to its manufacturing facilities, the Company's properties in Japan include sales offices and other sales facilities in major cities, repair service facilities, and research and development facilities.

We believe our production facilities and other properties, including the principal manufacturing facilities above, are suitable and adequate for the development, manufacture and sales of Honda's products and parts.

As of March 31, 2007, the Company’s property, with a net book value of approximately $¥ 23.6$ billion, was subject to specific mortgages securing indebtedness.

## Capital Expenditures

Capital expenditures in fiscal 2007 were applied to the expansion of manufacturing facilities, streamlining efforts, and the replacement of older equipment. Other expenditures included funds used to augment sales and R\&D facilities.

Total capital expenditures for the year amounted to $¥ 993.8$ billion, up $¥ 536.0$ billion from the previous year. Also, total capital expenditures excluding property on operating leases for the year amounted to $¥ 627.0$ billion, up $¥ 169.2$ billion from the previous year. Spending by business segment is shown below.

|  | Fiscal years ended March 31, |  |  |
| :---: | :---: | :---: | :---: |
|  | 2006 | 2007 | Increase (Decrease) |
|  | Yen (millions) |  |  |
| Motorcycle Business | ¥ 52,246 | $\geq 68,880$ | ¥ 16,634 |
| Automobile Business | 392,934 | 540,859 | 147,925 |
| Financial Services | 1,316 | 367,728 | 366,412 |
| Financial Services (Excluding Property on Operating Leases) | 1,316 | 933 | (383) |
| Power Product and Other Businesses | 11,345 | 16,394 | 5,049 |
| Total | ¥457,841 | ¥993,861 | ¥536,020 |
| Total (Excluding Property on Operating Leases) | $¥ 457,841$ | $¥ 627,066$ | $¥ 169,225$ |

In the motorcycle business, we made capital expenditures of $¥ 68.8$ billion in the fiscal year ended March 31 , 2007. Funds were allocated to the introduction of new models, as well as the improvement, streamlining and modernization of production facilities, and improvement of Sales and R\&D facilities.

In the automobile business, we made capital expenditures of $¥ 540.8$ billion in the fiscal year ended March 31, 2007. Funds were allocated to the introduction of new models, as well as the improvement, streamlining and modernization of production facilities, and improvement of Sales and R\&D facilities.

In the financial services segment, capital expenditures excluding property on operating leases amounted to $¥ 0.9$ billion in the fiscal year ended March 31, 2007, while capital expenditures for property on operating leases were $¥ 366.7$ billion. Capital expenditures in power products and other businesses in the fiscal year ended March 31, 2007, totaling $¥ 16.3$ billion, were deployed to upgrade, streamline, and modernize manufacturing facilities for power products, and to improve R\&D facilities for power products.

## Plans after fiscal 2007

Honda plans to build a new engine plant in Ogawa-machi Hiki-gun, Saitama with an investment of approximately $¥ 25,000$ million. The annual production capacity of this new plant will be approximately 200,000 units. This new plant should begin operation in 2009. The amount of this capital expenditure is included in the plan of new auto plant in Yorii-machi Oosato-gun, Saitama with an investment of approximately $¥ 70,000$ million, which was announced last fiscal year.

The estimated amount of capital expenditures in fiscal 2008 is shown below.

|  | Fiscal year ended March 31, 2008 |
| :---: | :---: |
|  | Yen (millions) |
| Motorcycle Business | $¥ 92,800$ |
| Automobile Business | 588,000 |
| Financial Services | 1,300 |
| Power Product and Other Businesses | 27,900 |
| Total | ¥710,000 |

The estimated amount of capital expenditures in fiscal 2008 for Financial Services does not include property on operating leases.

## Item 4A. Unresolved Staff Comments

We do not have any unresolved written comments provided by the staff of the Securities and Exchange Commission regarding our periodic reports under the Securities and Exchange Act of 1934.

## Item 5. Operating and Financial Review and Prospects

## A. Operating Results

## Overview

During fiscal 2007, Honda set in place a number of measures aimed at global growth and advancement. To propel ourselves forward over the medium to long term, we outlined specific measures of our three initiatives that are; developing advanced systems at our production facilities in Japan, solidifying the foundation for growth in our overseas business and working to reduce our $\mathrm{CO}_{2}$ emissions on a global level by promoting innovative products and production facilities. We also accelerated efforts to strengthen the core characteristics that make Honda unique in order to continue creating new value for our customers, such as by commercializing the HondaJet and solar cell businesses, bringing these projects a step closer to reality.

As to the economic conditions surrounding Honda during fiscal 2007, although crude oil prices became relatively more stable other raw materials prices continued to significantly increase. In the United States, despite slowing growth in personal consumption and capital investment, strong economic growth continued, albeit at a slightly slower rate, and the economies of Europe sustained a gradual recovery. Rapid economic growth also persisted in Asian countries, particularly China and India. In Japan, increases in capital investments and other factors supported a gradual economic recovery, although personal consumption was lackluster.

Tumultuous change characterized the business environment in key world markets. Amid increasingly stringent competition, we remained proactive in our efforts to launch products that create new value. These undertakings paid off in the form of higher unit sales in each of our businesses-motorcycles, automobiles and power products-and revenues grew for the seventh consecutive year as each of our businesses expanded.

Despite a demanding competitive environment, increased overseas unit sales and the currency effects caused by the depreciation of the Japanese yen rose profits, but income fell for a variety of reasons. The Company benefited from positive translation effects resulting from the depreciation in the value at yen. We experienced the negative impact of changes in our model mix, as significantly increasing gasoline prices prompted a shift in demand toward compact cars. The cost of steel, aluminium and precious metals substantially increased, and selling, general and administrative expenses accompanied the rise in unit sales. $\mathrm{R} \& \mathrm{D}$ expenses also rose, as we spent more on safety and environmental technologies and worked to improve the attractiveness of our products. Furthermore, the gain that we posted in fiscal 2006 on the return of the substitutional portion of the Employees Pension Funds to the Japanese government was absent in fiscal 2007.

In the motorcycle business, in key Asian markets, demand for motorcycles as an essential mode of transportation continued to grow. Sales in Latin America remained strong, mainly in Brazil, where economic performance was stable.

Since mid-2005, Indonesia, which is a major market for our products in Asia, has been affected by substantially increasing gasoline prices, coupled with substantially high inflation and interest rates, which depressed overall demand. However, a turnaround in this situation from mid-2006 allowed our equity method affiliate there to stage a recovery in sales.

In the automobile business, on a global basis, a sharp rise in gasoline prices spurred demand for automobiles featuring good fuel economy, leading to steady increases in sales of Honda vehicles in North America and Europe. Sales remained strong in China, India, Brazil and other emerging economies. In particular, strong worldwide sales of the new Civic, introduced in September 2005, continued in fiscal 2007. Sales of the new $C R-V$, which we launched in September 2006, also recorded strong worldwide sales results and contributed to the steady expansion of unit sales.

In power products and other businesses, unit sales in the power products business increased in all regions in fiscal 2007, mainly in North America and Europe. This rise was supported by products that play a role in customer lifestyles, such as lawn mowers and generators, as well as engines for $\mathrm{OEM}^{* 1}$ use in construction equipment and generators.

In December 2006, we established a subsidiary in Japan to manufacture and sell next-generation thin-film solar cells that we developed using proprietary technologies. Sales began in Japan on a limited regional basis in June 2007, and by autumn of 2007 we expect to commence mass production on an annual capacity of 27.5 megawatts and full-fledged sales.

Fulfilling an objective that Honda has set through research and development since the time of its establishment, in October 2004, we formed a joint venture with the General Electric Company, and in 2006, that venture secured orders to supply compact turbofan engines to two aircraft manufacturers. Furthering these efforts, in August 2006 we established a subsidiary in the United States to conduct R\&D, manufacturing and sales of compact jets. In October 2006, we began accepting orders for HondaJet, a compact business jet. Deliveries and associated revenue are scheduled to begin in 2010.

[^0]OEM refers to a manufacturing of products and components supplied for sale under a third-party brand.

## Fiscal Year 2007 Compared with Fiscal Year 2006

## Net Sales and Other Operating Revenue

Honda's consolidated net sales and other operating revenue (hereafter, "net sales") for fiscal year 2007, ended March 31, 2007, grew $11.9 \%$, compared with fiscal year 2006, to $¥ 11,087.1$ billion. Behind this increase were higher unit sales in the motorcycle business in Other regions, higher overseas unit sales in the automobile business and higher unit sales in all regions in power product and other businesses, as well as the positive impact of currency effects. Honda estimates that if the exchange rate of the Japanese yen had remained unchanged from the previous fiscal year, consolidated net sales and operating revenue for the period would have increased by approximately $7.4 \%$.

Domestic net sales decreased by $0.8 \%$ to $¥ 1,681.1$ billion, but overseas net sales were up $14.5 \%$ from fiscal year 2006, to $¥ 9,405.9$ billion.

## Cost of Sales

Despite the effects of cost reduction efforts, the cost of sales rose $12.2 \%$, to $¥ 7,865.1$ billion. The cost of sales was affected by increased unit sales, substantially increased raw materials prices, such as steel, aluminum and precious grade metals, as well as the negative impact of currency effects caused by the depreciation of the Japanese yen.

## Selling, General and Administrative Expenses / Research and Development Expenses

Selling expenses increased in line with higher unit sales, higher freight costs as the result of substantially increased crude oil prices, higher expenses related to product quality and the impact of currency effects. G\&A expenses increased due mainly to the impact of currency effects and the effects from newly consolidated subsidiaries. Total of SG\&A expenses rose $9.8 \%$ from fiscal year 2006, to $¥ 1,818.2$ billion. R\&D expenses also grew $8.1 \%$, to $¥ 551.8$ billion, as we spent more on safety and environmental technologies and worked to enhance the attractiveness of our products.

## Operating Income

Operating income declined $2.0 \%$, compared with the preceding year, to $¥ 851.8$ billion. In addition to the above mentioned factors, changes in model mix due mainly to shift of customers' demands towards more fuel efficient (compact) models especially in U.S. market negatively affected operating income.

## Other Income and Expenses

Other income and expenses, net, fell $¥ 20.0$ billion, due to an increase in losses on the valuation of interest rate swaps and other derivatives.

## Income before income taxes, minority interest and equity in income of affiliates

Income before Income Taxes, Minority Interest and Equity in Income of Affiliates fell 4.5\%, to $¥ 792.8$ billion.

## Income Tax Expense

Income tax expense decreased by $10.5 \%$, to $¥ 283.8$ billion. The effective tax rate was $35.8 \%$, a decrease by 2.4 percentage points from the previous fiscal year. Additional detailed information is described in Note (10) to the accompanying consolidated financial statements.

## Minority Interest in Income of Consolidated Subsidiaries

The amount deducted for minority interest in income of consolidated subsidiaries grew $31.6 \%$ from the previous year, to $¥ 20.1$ billion, due mainly to the impact of a newly consolidated subsidiary.

## Equity in Income of Affiliates

Equity in income of affiliates grew $3.8 \%$, to $¥ 103.4$ billion.

## Net Income

Net income was down $0.8 \%$ from the previous year, to $¥ 592.3$ billion.

In fiscal year 2006, operating income and income before income taxes, minority interest and equity in income of affiliates were impacted by the posting of a $¥ 138.0$ billion gain on the return of the substitutional portion of the Employees Pension Funds (hereafter, "gain on return") to the Japanese government, which also affected income after tax.

## Motorcycle Business

Unit sales of Honda motorcycles, all-terrain vehicles (ATVs) and personal watercraft (PWC) in fiscal 2007 amounted to $10,369,000$ units, an increase of $1.0 \%$, from the previous fiscal year. Unit sales in Japan were 337,000 units, a decrease of $8.4 \%$. Overseas unit sales in the motorcycle totaled $10,032,000$ units, an increase of $1.3 \%$, due mainly to an increase in unit sales in Other regions, especially in Latin America. Revenue from unaffiliated customers increased $11.8 \%$, to $¥ 1,370.6$ billion, from the previous fiscal year, due mainly to increased unit sales and the positive impact of currency translation effects. Operating income decreased $11.7 \%$, to $¥ 100.6$ billion, from the previous fiscal year, due mainly to increased SG\&A expenses, higher R\&D expenses and the gain on return which was recorded in the fiscal year ended March 31, 2006, offsetting the positive impact of increased profit attributable to higher revenue and positive currency effects. The Operating margin was $7.3 \%$.

## Japan

In Japan, total demand for motorcycles in fiscal year 2007, was approximately 730,000 units, down from the previous year. Demand increased for second-class motor-driven cycles ( $51 \mathrm{cc}-125 \mathrm{cc}$ ) and small-size two-wheeled motor vehicles (over 251cc), but fell for first-class motor-driven cycles (up to 50cc) and mini-size two-wheeled motor vehicles (126cc-250cc).

To meet increasingly diverse customer needs, we strengthened the Honda Dream Shop and other parts of our sales network, and strove to develop even more appealing motorcycles. Nevertheless, unit sales of motorcycles fell $8.4 \%$ in fiscal year 2007, to 337,000 units.

We adopted advanced technologies from specialized racing motorcycles in small-size two-wheeled motor vehicles, and sales of the fun-to-ride and maneuverable CBR1000RR super sports model were favorable, but sales of the CB1300 Super Bol d'Or decreased. In mini-size two-wheeled motor vehicles, sales of the Hornet, a naked sports model with refined and exciting styling, were strong. On the other hand, Forza sales declined. Sales of first- and second-class motor-driven cycles, such as the Today and the Duo, decreased.

## North America

Looking at calendar year 2006, demand in the United States for motorcycles, ATVs and personal watercraft came roughly equal to the previous year's demand. Demand for road bikes grew, but demand for ATVsparticularly utility ATVs-declined.

Of this number, Honda motorcycle sales fell $18.2 \%$, to 503,000 units, in fiscal year 2007. Sales of the CBR1000RR, a super sports model, and our new off-road model, the CRF150R, were strong, but higher interest rates and economic uncertainty impacted demand for leisure products. Particularly affected by this impact were sales of off road-models, mainly Enduro*1 models such as CRF50F and CRF70F, which dropped $15.1 \%$, to 282,000 units.

As one of our safety initiatives, we launched the world's first mass-market motorcycle with an airbag system, the GoldWing touring bike, in the United States and Canada.

Although sales of the FourTrax Rancher series of utility ATVs, which underwent a full model change in December 2006, were strong, total unit sales of ATVs and personal watercraft came to 221,000 units in fiscal year 2007, down $21.9 \%$.

## Europe

In calendar year 2006, total European motorcycle demand*2 increased from the previous year, to approximately 1,290,000 units, particularly in Spain due to changes in licensing systems as well as economic expansion, followed by increases in Italy, France and the United Kingdom.

In fiscal year 2007, unit sales decreased $6.8 \%$, to 329,000 units. Sales were strong for the SH300i, which launched in December 2006. Sales of PS125i, PS150i and Silver Wing 400 scooters were also stable, as were sales of the Deauville touring bike model. However, sales of large super sports models and models mainly in the 125 cc class declined.

## Asia

In Asia, demand for motorcycles as an essential mode of transportation has continued to grow. In fiscal year 2007, unit sales in Asia of completed products of Honda and its consolidated subsidiaries, and unit sales of parts to Honda's affiliates accounted for under the equity method for purposes of local production by such affiliates in the aggregate, declined $0.2 \%$, to $7,895,000$ units.

The Honda Group is working hard to expand local businesses in the region through its active promotion of local procurement of parts used in overseas production. In Asia, this strategy has resulted in an increase in sales of Honda-brand motorcycles that are manufactured and sold by affiliates accounted for under the equity method in India and China, but do not include any parts supplied by Honda or its consolidated subsidiaries, therefore not included in the consolidated unit sales.

Total demand in India in calendar 2006 expanded to approximately 8,390,000 units, buoyed by growing market of motorcycles which is the largest category. Hero Honda Motors Limited, an affiliate accounted for under the equity method, enjoyed strong sales of its mainstay Splendor, Splendor Plus and Super Splendor models. In December 2006, the Company launched the new CD Dawn and CD Deluxe models, which feature class-leading fuel efficiency. Honda Motorcycle and Scooter India Private Limited, a consolidated subsidiary, reported strong sales of the Shine equipped with a newly developed engine and the Activa scooter. In India in fiscal year 2007, total unit sales of completed motorcycles of Honda and its consolidated subsidiaries, and unit sales of parts to Honda's affiliates accounted for under the equity method for purposes of local production by such affiliates in the aggregate, grew $10.3 \%$, to $2,134,000$ units.

In calendar year 2006, the Indonesian market experienced increasing inflation and interest rates, caused by a sharp rise in gasoline prices, which substantially dampened consumer purchasing power in the first half of the year. Fortunately, a mid-year monetary policy relaxation helped ease the inflation rate. Companies in Indonesia responded by strengthening measures to expand sales, but total demand fell to approximately $4,630,000$ units nevertheless. P.T. Astra Honda Motors, an affiliate accounted for under the equity method, experienced strong sales of Vario, a automatic transmission (AT) equipped scooter launched in September 2006. Sales of Karizma by P.T. Astra Honda Motors, however, declined. As a result, in fiscal year 2007 total unit sales of completed motorcycles of Honda and its consolidated subsidiaries, and unit sales of parts to Honda's affiliates accounted for under the equity method for purposes of local production by such affiliates in the aggregate, fell $7.7 \%$, to $2,467,000$ units from the previous fiscal year.

In Thailand, total demand in calendar year 2006 came to approximately 2,060,000 units, down from the previous year. A maturing motorcycle market, the sharp rise in gasoline prices, political upheaval and irregular weather all had some impact on these results. Unit sales in fiscal year 2007 fell $7.5 \%$, to $1,401,000$ units from the previous year, although two AT-equipped scooters-the Click, which launched in fiscal year 2006, and the Air Blade, which went on sale in June 2006-were favorable.

Total demand for motorcycles in Vietnam in calendar year 2006 benefited greatly from the country's thorough abolition of a regulation limiting riders to one per motorcycle. This move caused the market to expand and pushed up demand to approximately $2,370,000$ units. Similarly, in fiscal year 2007, unit sales significantly increased $25.3 \%$, to 787,000 units.

China's 2005 implementation of Euro2 emission standards caused motorcycle demand to plunge, but in calendar year 2006, this demand returned to 2004 level, expanding to approximately $14,830,000$ units. Sundiro Honda Motorcycle Co., Ltd., an affiliate accounted for under the equity method, experienced strong sales of the M-Power, which launched in June 2006. Sales of the Fight Hawk, featuring a large half cowl, were also strong. Similarly, another affiliate accounted for under the equity method, Wuyang-Honda Motors (Guangzhou) Co., Ltd., introduced the SCR110-the first model in China to be equipped with programmed fuel injection (PGMFI)—in September 2006. In February 2007, the company also launched the SCR125 sports bike. Both models enjoyed favorable sales. As parts for manufacturing these new models are not supplied by Honda or its consolidated subsidiaries, their numbers are not included in Honda's consolidated unit sales. For this reason, together with the decrease in unit sales of other models, total unit sales of completed motorcycles of Honda and its consolidated subsidiaries, and unit sales of parts to Honda's affiliates accounted for under the equity method for purposes of local production by such affiliates in the aggregate, fell $39.3 \%$, to 204,000 units.

To meet increasing demand in the region, two new plants began operations-one in the Philippines in May 2006, and the other in July in Pakistan.

## Other Regions

Other regions-including Latin America, the Middle \& Near East, Africa and Oceania-unit sales grew $26.9 \%$, to $1,305,000$ units from the previous fiscal year. In Brazil, where economic performance was stable, Honda posted solid sales of such models as the Biz 125 and the CG125 Fan.

In June 2006, we began local production in Argentina to meet rising demand.
*1 Enduro
A motor sport involving long races on relatively flat off-road courses and lasting between two and 12 hours *2 Motorcycle registrations in Europe (10 countries)

## Automobile Business

Honda's unit sales of automobiles amounted to $3,652,000$ units, up $7.7 \%$ from the previous fiscal year. In Japan, unit sales decreased $3.4 \%$, to 672,000 units. Overseas unit sales increased $10.6 \%$, to 2,980,000 units, due mainly to increased unit sales in North America, Europe, Asia and other regions. Revenue from unaffiliated customers increased $11.0 \%$, to $¥ 8,889.0$ billion, from the previous fiscal year, due to increased unit sales and the positive impact of the currency translation effects. Honda estimates that if the exchange rate of the Japanese yen had remained unchanged from the previous fiscal year, consolidated net sales and operating revenue for the period would have increased by approximately $7.0 \%$. Operating income decreased $4.6 \%$, to $¥ 599.5$ billion, from the previous fiscal year, due mainly to the negative impact of changes in the model mix, substantially increased raw material costs, increased SG\&A expenses, higher R\&D expenses and the gain on return recorded in the fiscal year ended March 31, 2006, which offset the positive impacts of higher revenue attributable to the increased unit sales, continuing cost reduction effects and the currency effects caused by the depreciation of the Japanese yen. The operating margin was $6.7 \%$.

## Japan

Total automobile demand in Japan in calendar year 2006 remained largely unchanged, at around 5,740,000 units. With the number of mini cars increased and the number of registered vehicles declined.

In fiscal year 2007, unit sales declined $3.4 \%$, to 672,000 units. Although Honda's sales of the Zest and new Stream, CR-V and Crossroad models increased, sales of the Step Wagon, Life and Airwave decreased. In July 2006, Honda introduced the new Stream, a stylish model that offers powerful driving performance. In October, the new $C R-V$ also went on sale. This model features advancements in design, user-friendliness and driving performance, as well as an increased number of advanced safety features. In February 2007, Honda launched the Crossroad. This new model combines the handling ease of a compact car with the rugged exterior and versatility of an SUV.

Since integrating our sales channels in March 2006, sales have increased for mini cars and other vehicles used to be sold exclusively by each channel.

In the mini car segment, Honda strengthened its capital relationship with Yachiyo Industry Co., Ltd., strengthening its alliance with the Company. The objective of this move was to strengthen Honda's ability to develop highly competitive products and strengthen its business in this segment.

## North America

In calendar year 2006, total demand in the United States was down to approximately $16,550,000$ units. Impacted by the sharp rise in gasoline prices, demand for fuel-efficient vehicles expanded, while sales of large SUVs and pickup trucks was stagnant.

Total North American unit sales in fiscal year 2007 came to 1,788,000 units, up $6.3 \%$ from the previous year. Unit sales in the passenger car segment benefited from the April 2006 introduction of the Fit, but sales of Acura-brand cars declined, causing overall unit sales in this segment to be approximately the same level as the previous fiscal year. In the light truck segment, on the other hand, the new Acura $R D X$-an entry-premium SUV-launched in August. The $C R-V$, a compact SUV which underwent a full model change, went on sale in September, and the new Acura MDX, a premium SUV, launched in October. A favorable market response to these new models strengthened overall sales performance in this region.

To increase the local production of powertrain components, in May 2006 we started operating a new automatic transmission plant in Georgia. The Pilot, which was being manufactured on the second line of our plant in Canada, was transferred to Honda's plant in Alabama in February 2007 and the second line of our plant in Canada began manufacturing the Civic in April 2007, raising annual capacity by 60,000 units, so as to respond to heightened demand for fuel-efficient vehicles.

Honda vehicles were selected as Top Picks in three of the 10 automobile categories rated by U.S. Consumer Reports magazine for 2007 models, earning particularly high marks for their fuel efficiency and safety performance. Earning top place were the Civic in the small sedan category, the Accord in the family sedan category and the Fit in the budget car category.

## Europe

Total demand in Europe* in calendar year 2006 amounted to approximately 14,620,000 units, roughly the same level as in 2005.

Unit sales for fiscal year 2007 climbed $11.3 \%$, to 324,000 units from the previous year. Recording strong sales results were the five-door Civic and the Accord, as well as the CR-V, a compact SUV that was launched in January 2007 which underwent a full model change, and the three-door Civic.

In production, consolidated subsidiary Honda of the U.K. Manufacturing Ltd. responded to rising demand for the Civic and the CR-V, ramping up to full production in calendar year 2007 by starting two-shift production in February at its second plant. The company is strengthening its production system through the gradual transfer of diesel engine production from Japan.

## Asia

In Asia in fiscal year 2007, total unit sales of completed automobiles of Honda and its consolidated subsidiaries, and unit sales of parts to Honda's affiliates accounted for under the equity method for purposes of local production by such affiliates in the aggregate, grew $19.0 \%$, to 620,000 units from the previous fiscal year.

Total demand amounted to approximately 5,200,000 units in China in calendar year 2006, rising substantially from the previous year. Particularly strong were sales of the City by Guangzhou Honda Automobile

Co., Ltd., an affiliate accounted for under the equity method, and Civic sales by Dongfeng Honda Automobile Co., Ltd., also an equity-method affiliate. In September 2006, the Acura brand was introduced in China, in the brand's first launch outside North America, through sales of the Acura RL and the Acura TL. In fiscal year 2007, total unit sales of completed automobiles of Honda and its consolidated subsidiaries, and unit sales of parts to Honda's affiliates accounted for under the equity method for purposes of local production by such affiliates in the aggregate, significantly increased $37.6 \%$, to 361,000 units from the previous fiscal year. In production, in September 2006 operations began at the second plant of Guangzhou Honda Automobile Co., Ltd., which has an annual production capacity of 120,000 units. In March 2007, production also began at a new plant in China that manufactures automobile transmissions and other powertrain components. These advances are in line with Honda's move to strengthen its structure to meet burgeoning Chinese demand.

In India, where the market continues to expand, an Indian-made Civic model went on sale in July 2006, contributing to higher unit sales.

In Vietnam, consolidated subsidiary Honda Vietnam Co., Ltd., began local production of the Civic in July 2006.

## Other Regions

Due to expansion in Latin America, the Pacific, and the Middle \& Near East, unit sales in Other regions rose $23.4 \%$ in fiscal year 2007, to 248,000 units.

In Brazil, Honda began local production of the Civic in April 2006, and sales of this model were strong. In November 2006, we introduced the Civic FFV, a flexible-fuel vehicle that runs on $100 \%$ ethanol or any gasolineethanol mixture, followed by the launch of the Fit FFV in December. Australian sales of the Civic, Jazz and the new $C R-V$ were strong.

[^1]
## Power Products and Other Businesses

Honda's unit sales of power products totaled $6,421,000$ units, up $9.3 \%$ from the previous fiscal year. In Japan, unit sales totaled 527,000 units, an increase of $8.2 \%$. Overseas unit sales came to $5,894,000$ units, an increase of $9.4 \%$, due mainly to increased unit sales in North America and Europe. Revenue in power products and other businesses, including intersegment sales within Honda, increased $14.7 \%$, to $¥ 438.9$ billion, from the previous fiscal year, due mainly to increased unit sales of power products and the positive impact of currency translation effects. Operating income was $¥ 36.1$ billion, an increase of $0.6 \%$ from the previous fiscal year, due mainly to the positive impact of increased profit attributable to higher revenue and the currency effects caused by the depreciation of the Japanese yen, which offset the negative impact of the increased SG\&A expenses and the gain on return which was recorded in the fiscal year ended March 31, 2006. The operating margin was $8.2 \%$.

## Japan

In Japan, unit sales rose $8.2 \%$, to 527,000 units from the previous fiscal year. Sales of snowblowers, compact home-use cogeneration systems* ${ }^{*}$, the $G X$-series engines supplied to pump and generator manufacturers on an $\mathrm{OEM}^{* 2}$ basis applications increased.

## North America

In North America, sales were strong for $G C V$ series engines-mainly for OEM use in lawn mowers, as well as $G X$ - and $G C$-series engines for such OEM applications as generators and high-pressure washers. Sales of completed equipment expanded, due to Honda's introduction of the new HRR lawn mower, but sales of generators declined as a result of overall market shrinkage. As a result of these factors, unit sales from power product grew $9.8 \%$ in fiscal year 2007 , to $3,103,000$ units.

During the year, J.D. Power and Associates of the United States accorded Honda the highest ranking for the third consecutive year in the electronic fuel-injected (EFI) four-stroke outboard segment.

## Europe

In Europe, OEM sales of $G C V$-series engines for lawn mowers were favorable, as were sales of $G X$-series engines for OEM use in generators and construction equipment. As a result, unit sales grew $10.0 \%$, to $1,625,000$ units.

## Asia

Unit sales in Asia expanded $6.0 \%$, to 760,000 units, due to increased sales of pumps and other equipment in China and India.

## Other Regions

In other regions, increased unit sales of $G X$-series engines for OEM production, mainly in Latin Africa, pushed up sales $10.3 \%$, to 406,000 units from the previous fiscal year.

In fiscal year 2007, Honda introduced two four-stroke outboard engines, the BF90 and BF75 that underwent a full model change, responding to needs throughout the world by simultaneously addressing demands for high levels of both environmental performance, power performance and fuel efficiency. Honda also began sales in Japan of the EU55is generator, which employs electromagnetic inverter technology to supply a high level of power, but emit a low level of noise, and of the EU6500is generator in North America. In Japan, we introduced a compact home-use cogeneration system with improved generation efficiency which underwent a full model change. We also launched this model in the United States. In addition, Honda launched the Punch $X$ compact tiller in Japan, and the F501 and FE500 compact tillers in Europe which underwent a full model change. In China, we launched the new EM10000 high-output 10 kVA generator, which is compact and equipped with a newly developed alternator.

## *1: Compact, home-use cogeneration system

Honda has combined its original electromagnetic inverter technologies with the world's smallest ${ }^{(\mathrm{i})}$ natural gas engine (GE160V) in an efficient layout to create a small, lightweight cogeneration unit. Due to its compactness, the unit can be installed in the home and boasts an overall energy efficiency of $85 \%$. It also emits approximately $30 \%$ less carbon dioxide than conventional natural gas-powered generators or hot-water heating units using natural gas. ${ }^{(\text {ii) }}$
(i): A Honda development, the reciprocal gas enjine
(ii): Data from Honda test results. Data compares electricity from the grid with hot-water heating units that use natural gas.
*2: OEM (Original equipment manufacturing)
OEM refers to a manufacturing of products and components supplied for sale under a third-party brand.

## Financial Services Business

Honda offers a variety of financial services to its customers and dealers, with the aim of supporting sales of Honda products. These services are provided through finance subsidiaries in Japan, the United States, Canada, the United Kingdom, Germany, Brazil and Thailand.

In fiscal year 2007, net sales of our financial services business, including intersegment sales within Honda, rose $32.9 \%$, to $¥ 413.3$ billion from the previous fiscal year, due mainly to a higher loan balance accompanying the expansion of automobile business in North America, increased net sales in operating leases, as well as positive currency translation effects. Operating income also expanded $27.6 \%$, to $¥ 115.5$ billion from the previous fiscal year, due mainly to the increased profit attributable to higher revenue benefiting from a higher loan balance and positive currency translation effects, which offset the negative impact of the increased interest rates. The operating margin came to $28.0 \%$.

Our finance subsidiaries in North America have historically accounted for all leases as direct finance leases. However, starting in the year ended March 31, 2007, some of the leases which do not qualify for direct financing leases accounting treatment are accounted for as operating leases. Generally, direct financing lease revenues and interest income consist of the recognition of finance lease revenue at inception of the lease arrangement and subsequent recognition of the interest income component of total lease payments using the effective interest method. In comparison, operating lease revenues include the recognition of the gross lease payment amounts on a straight line basis over the term of the lease arrangement, and operating lease vehicles are depreciated to their estimated residual value on a straight line basis over the term of the lease. It is not anticipated that the differences in accounting for operating leases and direct finance leases will have a material net impact on the Company's results of operations overall, however, operating lease revenues and associated depreciation of leased assets do result in differing presentation and timing compared to those of direct financing leases.

Information about allowance for credit losses is provided at Item 5. Operating and Financial Review and Prospectus A. Operating Results. Information about finance subsidiaries-receivables and securitizations is described in Note (3) to the accompanying consolidated financial statements.

## Geographical Information Japan

In Japan, revenue from domestic and export sales was $¥ 4,774.1$ billion, up $7.6 \%$ compared to the previous fiscal year, due primarily to the increased revenue from exports in automobile business which offset the negative impact of the decreased unit sales in domestic automobile business. Operating income was $¥ 228.1$ billion, down $38.5 \%$, compared to the previous fiscal year, due primarily to the negative impact of the changes in the model mix, substantially increased raw material costs, increased SG\&A expenses, increased R\&D expenses and the absence of a gain on the return of the substitutional portion of the Employee Pension Funds of the Japanese government which was present in fiscal year 2006, which offset the positive impact of the increased profit attributable to higher revenue, continuing cost reduction effects and the currency effects caused by the depreciation of the Japanese yen. Operating margin was 4.8\%.

## North America

In North America, which mainly consists of the United States, revenue increased $9.9 \%$, to $¥ 6,172.6$ billion, due mainly to increased unit sales in the automobile business and the positive impact of currency translation effects. Operating income increased $29.1 \%$, to $¥ 456.8$ billion, from the previous fiscal year, due primarily to the positive impacts of increased profit attributable to higher revenue, continuing cost reduction effects, decreased SG\&A expenses and the currency effects caused by the depreciation of the Japanese yen, which offset the negative impacts of the change in model mix and substantially increased raw material costs. The operating margin was $7.4 \%$.

## Europe

In Europe, revenue increased $13.3 \%$, to $¥ 1,347.7$ billion, compared to the previous fiscal year, due primarily to increased unit sales in the automobile and power product businesses and the positive impact of currency translation effects. Operating income increased $21.6 \%$, to $¥ 31.9$ billion, from the previous fiscal year, due mainly to the positive impacts of increased profit attributable to higher revenue, continuing cost reduction and the currency effects caused by the depreciation of the Japanese yen, which offset the negative impacts of the change in model mix and increased SG\&A expenses. The operating margin was $2.4 \%$.

## Asia

In Asia, revenue increased $27.5 \%$, to $¥ 1,271.4$ billion from the previous fiscal year, due primarily to increased unit sales in the automobile business and the positive impact of currency translation effects. Operating income increased $18.7 \%$, to $¥ 77.1$ billion, from the previous fiscal year, due mainly to the positive impacts of increased profit attributable to higher revenue, which offset the negative impact of increased SG\&A expenses. The operating margin was $6.1 \%$.

## Other Regions

In other regions, revenue increased $39.5 \%$, to $¥ 797.6$ billion, compared to the previous fiscal year, due mainly to increased unit sales in all of the business segments and the positive impact of currency translation effects. Operating income rose $26.4 \%$, to $¥ 72.2$ billion, from the previous fiscal year, due mainly to the positive impact of the increased profit attributable to higher revenue, and the currency effects caused by the depreciation of the Japanese yen, offsetting the negative impact of increased SG\&A expenses. The operating margin was 9.1\%.

As described in Note (1) (v) and Note (2) to our consolidated financial statements, certain revisions for misclassifications and reclassifications have been made to the prior years' consolidated financial statements to conform to the presentation used for the fiscal year ended March 31, 2007.

## Fiscal 2006 Compared with Fiscal 2005

## Overview

## Net Sales and Other Operating Revenue

Honda's consolidated net sales and other operating revenue (hereafter "net sales") for fiscal 2006, ended March 31, 2006, amounted to $¥ 9,907.9$ billion, up $14.5 \%$ from the previous fiscal year.

Of this amount, domestic net sales decreased by $¥ 5.1$ billion, or $0.3 \%$, to $¥ 1,694.0$ billion, while overseas net sales increased by $¥ 1,263.0$ billion, or $18.2 \%$ to $¥ 8,213.9$ billion.

## Selling, General and Administrative Expenses / Research and Development Expenses

SG\&A expenses for fiscal 2006 increased by $¥ 143.1$ billion or $9.5 \%$, to $¥ 1,656.3$ billion, reflecting increased expenses from higher revenue and increased advertisement expenses and freight costs due to rising prices of crude oil which offset the positive impact of decreased in provision for credit and lease residual losses on finance subsidiaries-receivables.

R\&D expenses increased by $¥ 42.6$ billion or $9.1 \%$, to $¥ 510.3$ billion.

## Operating Income

Operating income amounted to $¥ 868.9$ billion, which was an increase by $37.7 \%$ from the previous fiscal year.

This was primarily due to positive currency effects caused by the depreciation of the Japanese yen, increased profit attributable to higher revenue, continuing cost reduction effects and gain on return, which offset the negative impact of increased SG\&A and R\&D expenses.

## Income before Income Taxes, Minority Interest and Equity in Income of Affiliates

Income before income taxes, minority interest and equity in income of affiliates was up $24.2 \%$, to $¥ 829.9$ billion. Other income \& expenses, net decreased by $¥ 76.4$ billion from the previous fiscal year, due mainly to decline in gains on derivative instruments.

## Income Tax Expense

Income tax expense increased by $18.9 \%$, to $¥ 317.1$ billion. The effective tax rate was $38.2 \%$, a decrease by 1.7 percentage points from the previous fiscal year. Additional detailed information is described in Note (10) to the accompanying consolidated financial statements. The prior year income taxes in 2005 are due to assessment by the Japanese tax authorities as a result of their transfer pricing audit relating to the Company's motorcycle business in Brazil.

## Equity in Income of Affiliates

Equity in income of affiliates increased by $3.7 \%$, to $¥ 99.6$ billion.

## Net Income

Net income amounted to $¥ 597.0$ billion, an increase of $22.8 \%$.
Basic net income per common share amounted to $¥ 324.33$, compared with $¥ 260.34$ in fiscal 2005.
The gain on "return" of $¥ 138.0$ billion which was recorded in the fiscal year ended March 31, 2006, was included in the result of consolidated operating income and consolidated income before income taxes. Accordingly, the result of amount of the relevant income after tax that was recorded by the "return" was included in the consolidated net income for the fiscal year ended March 31, 2006.

## Business segments

## Motorcycle Business

In fiscal 2006, domestic unit sales of motorcycles, all-terrain vehicles (ATVs) and personal watercraft (PWC) fell $2.6 \%$, to 368,000 units. Overseas unit sales fell $2.0 \%$, to $9,903,000$ units, mainly due to a decrease in unit sales of parts for local production at affiliates accounted for under the equity method in Asia*.

As a result, total unit sales of motorcycles amounted to $10,271,000$ units, down $2.0 \%$ compared to the previous fiscal year. Net sales from sales to unaffiliated customers in the motorcycle segment increased $11.7 \%$, to $¥ 1,225.8$ billion, due mainly to the positive impact of the currency translation effects and the change in model mix, offsetting negative impact of decreased unit sales. Operating income increased by $64.4 \%$ to $¥ 113.9$ billion, due mainly to the positive impact of currency effects caused by the depreciation of the Japanese yen, increased profit attributable to higher revenue, continuing cost reduction effects and gain on "return", offsetting the negative impact of the increase in SG\&A and R\&D expenses. The operating margin was $9.3 \%$.


#### Abstract

* Of the net sales of Honda-brand motorcycle products that are manufactured and sold by overseas affiliates accounted for under the equity method, those with respect to which parts for manufacturing were not supplied from Honda or such subsidiaries are not included in net sales and other operating revenue, in conformity with U.S. generally accepted accounting principles. Accordingly, these unit sales are not included in the financial results. Such products amounted 2,600 thousand units for the fiscal year.


## Japan

In Japan, unit sales declined $2.6 \%$, to 368,000 units. Sales of small-sized motorcycles (over 250 cc ) increased, supported by strong demand for sports bikes, as did sales of mini-sized motorcycles (126cc-250cc), which benefited from strong sales of scooters. However, sales of first-class motor-driven cycles (up to 51cc) and second-class motor-driven cycles ( $51 \mathrm{cc}-125 \mathrm{cc}$ ) fell, in market demand, and affected overall unit sales.

In the small-sized motorcycle category, the CB1300 Super Bol D'Or and the CB400 Super Bol D'Orfeaturing a newly designed half-cowl for improved riding stability-generated strong sales. With respect to minisized motorcycles, we enjoyed strong sales of the Forza series due to strong demand centered on customers in their 30's. The motor-driven cycle category, types 1 and 2, recorded declines in sales of Today and Crea Scoopy models, although sales of Zoomer bikes were favorable.

## North America

In North America, unit sales declined 4.4\%, to 615,000 units. We recorded strong sales of the VTX1300 series of cruisers and two models released at the end of the previous fiscal year: the CRF450X off-road bike and the CBR600RR sports model. Overall sales of off-road vehicles were down, however, due to substantially increased fuel prices. As a result, unit sales of models in the motorcycle segment fell $4.0 \%$, to 332,000 units.

The ATV category benefited from strong sales of the FourTrax Rincon, which underwent a full model change in October 2005, and the TRX90, which is now equipped with an easy-starting electric starter motor. However, as was the case for motorcycles, high gasoline prices affected sales of small and medium-sized ATV sales, leading to a $4.7 \%$ overall decline in combined ATV and PWC sales in North America, to 283,000 units.

## Europe

In Europe, unit sales rose $4.4 \%$, to 353,000 units.

In that region, we enjoyed strong sales of SH 150 i and $\mathrm{SH} 125 i$ scooters and the CB600F Hornet, a "naked" sports bike that underwent minor changes. Also popular was the Deauville touring bike, which underwent a full
model change in February 2006. We have already released the Forza series of large scooters, which have been well received in Japan, and in February 2006 we released the CBF1000 touring sports bike, equipped with an engine based on that found in the CBR1000RR. Both models have proven popular among European customers. In these ways, we delivered products that met the needs of customers in the intensely competitive market for commuter vehicles and in the growing market for large scooters.

## Asia

In Asia, demand for motorcycles as an essential mode of transportation has continued to grow. Total unit sales of motorcycles made by Honda and its subsidiaries, as well as of motorcycle parts sold to regional affiliates accounted for under the equity method, declined $3.5 \%$, to $7,907,000$ units.

Honda is working hard to expand local businesses in the region through its active promotion of local procurement of parts used in overseas production. This strategy has resulted in a sharp increase in $100 \%$ locally procured models made by our affiliates in India and China that are not included in Honda's unit sales.

In India, we enjoyed healthy sales of core models made by our affiliate, Hero Honda Motors Limited (HHML). These included two 125 cc models-Super Splendor, which went on sale at the end of the previous fiscal year, and Glamour, which launched in June 2005-as well as the 100cc CD Deluxe. In January 2006, HHML launched the Pleasure. Honda Motorcycle \& Scooter India (Private) Limited (HMSI), a consolidated subsidiary, recorded strong sales of the Unicorn, its first motorcycle, and the Activa scooter. Combined sales in India of completed vehicles by Honda and consolidated subsidiaries, as well as sales of unit sales of parts to Honda's affiliates accounted for under the equity method for purposes of local production by such affiliates in the aggregate, totaled $1,934,000$ units, down 865,000 from the previous fiscal year.

In Indonesia, P.T. Astra Honda Motors (AHJ), an equity-method affiliate, posted healthy sales of its Supra series, centering on the Supra X 125, which went on sale in June 2005, and the Supra Fit, which underwent a full model change in August 2005. Also popular was the Supra X 125 PGM-FI, which was added to the lineup in December 2005 and features PGM-FI for superior fuel economy and drivability. In September 2005, we commenced production at a third new plant, strengthening our annual capacity by 1 million units, to 3 million. In Indonesia, combined sales of finished vehicles by Honda and consolidated subsidiaries, as well as sales of unit sales of parts to Honda's affiliates accounted for under the equity method for purposes of local production by such affiliates in the aggregate, grew $18.0 \%$, to 2,672,000 units.

In Thailand, we enjoyed strong sales of the Wave125, which underwent a minor model change in April 2005, and the Wave100, following a full model change in April 2005. In February 2006, we launched the Click scooter with the first automatic transmission developed for the Asian market. Unit sales in Thailand of completed vehicles by Honda and consolidated subsidiaries grew $1.7 \%$, to $1,514,000$ units.

In China, Sundiro Honda Motorcycle Co., Ltd., an affiliate accounted for under the equity method, posted strong sales of the Storm, released in April 2005, and the Wiz, released in June 2005. Another equity-method affiliate, Wuyang-Honda Motors (Guangzhou) Co., Ltd., recorded strong sales of the SCR100, GL125 and other core scooter models. Due to market confusion stemming from the adoption of Euro2* emission standards, as well as suppression of purchases following the announcement of an upcoming reduction in consumption tax, combined unit sales in China of completed vehicles by Honda and consolidated subsidiaries fell 97,000 units from the previous term, to 336,000 units. However, this figure does not include sales of $100 \%$ locally procured Honda-brand vehicles manufactured and sold by affiliates accounted for under the equity method.

## Other Regions

In other regions-covering Latin America, the Middle \& Near East, Africa and Oceania—unit sales grew $10.4 \%$, to $1,028,000$ units.

In Brazil, where economic performance was stable, we posted strong sales of the core CG150 Titan and CG125 Fan models. Following a full model change in September 2005, the Biz 125, aimed at young people and women, was also popular.

In the Middle \& Near East and Africa, we enjoyed strong sales of the Chinese-made CGL125 and the Japanese-made XL125.

* Euro2 (motorcycles)

Extremely stringent exhaust emission regulations for motorcycles implemented in Europe from 2003. Euro2 regulations are relatively recent and stringent standards. China began employing Euro2 regulations from the 2005 model year, and Indonesia and Brazil are also employing these regulations. (Even more stringent Euro3 emission regulations are being implemented in Europe in 2006.)

## Automobile Business

Domestic unit sales of automobiles in fiscal 2006 fell $2.2 \%$, to 696,000 units and overseas unit sales increased by $6.5 \%$, to $2,695,000$ units. Consequently, total unit sales of automobiles grew $4.6 \%$, to $3,391,000$ units, compared to the previous fiscal year. Net sales from sales to unaffiliated customers in the automobile segment increased $14.9 \%$, to $¥ 8,004.6$ billion, due to the positive currency translation effects and increased unit sales mainly in North America and Europe. Operating income increased by $38.9 \%$ to $¥ 628.3$ billion, due mainly to the positive impact of currency effects caused by the depreciation of the Japanese yen, an increase in profit attributable to higher revenue, continuing cost reduction effects and gain on "return", which offset the negative impact of increase in SG\&A and R\&D expenses. The operating margin was $7.9 \%$.

## Japan

Total domestic automobile demand in Japan in calendar year 2005 remained largely unchanged, at around $5,860,000$ units. For Honda, however, unit sales in fiscal 2006 edged down $2.2 \%$, to 696,000 units, due to lower sales of Fit, Elysion and Odyssey models. This was despite the launch of the new Air Wave wagon and the Zest, as well as higher sales of the Step Wagon, which underwent a full model change.

In April 2005, we introduced the all-new Air Wave station wagon, featuring high utility in a compact body. In May, we released the new Step Wagon, after lowering the vehicle's floor level and center of gravity and providing a more user-friendly body size, more internal space and sedan-like driving performance and comfort. In September 2005, we launched the new Civic, featuring an innovative, monoform design and more ample interior space. In March 2006, we commenced sales of the new Zest mini car, incorporating low-floor design technology for greater cabin room, occupant access and storage space.

In addition to these and other products with new levels of value, we enhanced marketing efficiency by deploying advanced information technologies while reinforcing our sales and service capabilities. In these ways, Honda strove to maximize the lifetime satisfaction of its existing customers in Japan, whose numbers are around 9.0 million.

## North America

In calendar 2005, automobile demand in the United States remained high, at around 16,990,000 units.
In the passenger car segment, we reported an increase in unit sales of the new Civic model, which offers excellent safety features and superb fuel economy. Sales of the Acura RL and the Acura TSX, a sport sedan, were also stable. In the light truck segment, the all-new Ridgeline, a next-generation truck launched in March 2005, attracted strong demand, as did the Pilot, a mid-class SUV, and the Odyssey mini-van. As a result, overall sales in North America grew $6.8 \%$, to $1,682,000$ units.

In October, we launched a new Brazilian-made Fit model in Mexico. Further north, in November we released the Acura CSX, an Acura-brand entry model aimed designed specifically for the Canadian market.

In fiscal 2006, we received "North American Car and Truck of the Year" awards for the Civic and the Ridgeline, marking the first time in history that the same manufacturer has won both categories at the same time. In addition, Honda vehicles were selected as Top Picks in five of the 10 automobile categories rated by U.S. Consumer Reports magazine for 2006 models. These rankings reflect excellent feedback on our introduction of models in the passenger car and light truck categories that offer excellent fuel performance and safety features.

## Europe

In Europe, overall automobile demand remained almost unchanged in calendar year 2005, at around $17,660,000$ units. Nevertheless, Honda's unit sales in fiscal 2006 climbed $9.0 \%$, to 291,000 units. This was due mainly to increased sales of the five-door Civic, released in January 2006 after a full model change that resulted in a well-received sporty and sophisticated design, and the $F R-V$ series, which benefited from the addition in August 2005 of a version with the Honda-developed i-CTDi*1 diesel engine, and continued strong sales of the Jazz. To meet growing demand for diesel-powered vehicles in the region and to fortify out our manufacturing system, Honda of the U.K. Manufacturing Limited began assembling diesel engines. We included a diesel model in the new five-door Civic line, and the Accord and $C R-V$ are also available with Honda-developed diesel engines. In these ways, we enhanced our competitiveness in the extremely challenging European market.

## Asia

In Asia, total unit sales of parts to Honda's affiliates accounted for under the equity method for purposes of local production by such affiliates in the aggregate edged up $1.8 \%, 521,000$ units.

In China, the passenger car market expanded considerably, with demand reaching around 3.20 million in calendar year 2005. Guangzhou Honda, an affiliate accounted for under the equity method, recorded healthy sales of the popular Accord and Odyssey models. Another equity-method affiliate, Dongfeng Honda, enjoyed strong sales of the $C R-V$. Total unit sales in China of completed vehicles by Honda and its subsidiaries, as well as sales of component parts sets for production to equity method affiliates amounted to 263,000 units, on a par with the preceding year.

In February 2006, Dongfeng Honda expanded its capacity to 120,000 vehicles per year, in an effort to meet rapidly expanding Chinese demand. Further, in June 2005 Guangzhou Honda became the first passenger car maker in China to export vehicles to Europe from a plant that specializes in the production of export models. In these ways, Honda will continue using its accumulated China-related expertise to deliver top-level products in terms of quality and cost.

Demand continued to expand on other Asian markets, with major increases in sales of the City in Pakistan, India and elsewhere. Sales were also up in Taiwan, contributing to sales in the Asian region. In terms of manufacturing and R\&D, we expanded manufacturing capacity at our plant in India and established an R\&D location in Thailand. These are a few examples of Honda's efforts to build up its systems to respond swiftly to diversifying local needs

## Other Regions

Unit sales in other regions grew $14.2 \%$, to 201,000 units, thanks mainly to increased sales in Latin America, Oceania and the Middle \& Near East.

In Brazil, sales of the locally produced Fit increased. In Australia and the Gulf states, we posted healthy sales of the Accord, Civic and other models.
${ }^{*}$ : $\quad$ i-CTDi
This is a proprietary diesel engine developed by Honda that optimizes combustion through the adoption of a high-pressure fuel injection system, combined with a newly developed emission treatment system. The i-CTDi is also compliant with Euro4 emission standards for 2005.

## Power Product and Other Businesses

Domestic unit sales of power products in fiscal 2006 increased $12.7 \%$, to 487,000 units. Overseas unit sales increased $10.7 \%$, to $5,389,000$ units. Accordingly, total unit sales of power products rose $10.9 \%$, to $5,876,000$ units, compared to the previous fiscal year.

Net sales from power products and other businesses, including sales between segments, climbed $11.6 \%$, to $¥ 382.5$ billion, due mainly to increased unit sales. Operating income increased $86.3 \%$ to $¥ 35.9$ billion, due mainly to positive currency effects caused by the depreciation of the Japanese yen, the increased profit attributable to higher revenue and gain on "return", which offset the negative impact of the increase in SG\&A expenses. The operating margin was $9.4 \%$.

## Japan

In Japan, unit sales of power products rose $12.7 \%$, to 487,000 units, due largely to increases in sales of the $G X$ series of general-purpose engines supplied to pump manufacturers on an OEM basis, as well as higher sales of imported engines made by Honda in Thailand and China.

## North America

In North America, unit sales grew $12.5 \%$, to $2,827,000$ units. Stable demand for power generation equipment provided a strong increase in sales of both completed products and engines supplied on an $\mathrm{OEM}^{* 1}$ basis. Within the engine category, strong sales of large-scale models in the $G X$ series have enabled Honda to create a new market for completed equipment. Our North American business also benefited from healthy sales of inverter-equipped mobile generators for camping and leisure use, as well as large-scale power generation equipment.

## Europe

Unit sales in Europe grew $12.8 \%$, to $1,477,000$ units, bolstered by stable demand for GCV135/160 engines for lawn mower use, as well as construction equipment and $G X$ general-purpose engines for use in tillers. Among completed products, the new $H R X$ push lawn mower generated a considerable sales increase, encouraged by favorable weather.

## Asia

In Asia, unit sales remained mostly unchanged, at 717,000 units. In April 2005, we restructured the operations of Jialing-Honda Motors Co., Ltd., a company in China that previously manufactured and sold both power products and motorcycles. That company subsequently restarted its operations, concentrating solely on power products. This measure enabled us to better utilize our cost-competitiveness and resulted in favorable unit sales, together with Thailand-made products.

## Other Regions

In other regions, unit sales climbed $10.5 \%$, to 368,000 units. In Brazil, sales were strong for locally made $G X$ series engines, which became more price-competitive as a result of further cuts in component procurement costs.

In Australia, we posted higher sales of green products, including the environmentally friendly $H R U$ series of push lawn mowers and $U M K$ series lawn mowers.

During the year, Honda released the iGX440 general-purpose engine in Japan, United States, Europe and elsewhere. Highly friendly to the environment, the iGX440 features a new, world first electronic governor*2 technology that regulates engine speed and thus improves responsiveness to varying engine loads. In Japan, we incorporated the $i G X 440$ into the newly launched HSM1590i, a mid-sized hybrid snow plow featuring a gasoline engine for removing snow and an electric motor for travel motion. The combination of the two power units facilitates switching between work modes and enhances user-friendliness. The new product has received favorable response from customers.

In March 2006, we released the Monpal ML200, a stylish four-wheel scooter with a comfortable ride and high maneuvering stability. It is the first commercially available vehicle to feature visibility enhancement design, adapted from the Honda $\mathrm{ASV}-3^{* 3}$ advanced safety research vehicle.

Meanwhile, diffusion of our compact, home-use cogeneration system ${ }^{* 4}$ increased in Japan. In fiscal 2006, sales increased firmly in line with growing worldwide environmental awareness. Since January 2006, Tokyo Gas Co., Ltd., became a new distributor of this system.
*1: Original equipment manufacturing (OEM)
OEM refers to a manufacturing of products and components supplied for sale under a third-party brand.
*2: STR governor (electronic governor)
This system uses an electronic control unit (ECU) to constantly monitor throttle aperture and speed, so that even if the engine load changes the electronic control adjusts the throttle to maintain a pre-established speed.

STR: Self-tuning regulator
Governor: A device that regulates engine speed, maintaining a constant engine speed, regardless of load fluctuations

## *3: ASV (Advanced Safety Vehicle)

Japan's Ministry of Land, Infrastructure and Transport promotes this project for the development of advanced safety vehicles, which all manufacturers of automobiles and motorcycles join voluntarily. The first phase of this project, ASV-1 (Apr.1991-Mar.1996), studied technical possibilities. ASV-2 (Apr.1996-Mar.2001) involved research and development on practical applications, while ASV-3 (Apr.2001-Mar.2006) used technology to inter-vehicle communication technologies.

In September 2005, Honda succeeded in the creation of its ASV-3. Using inter-vehicle communication technologies to avoid collision by determining distances between vehicles, this vehicle provides features to warn of and attempt to avoid collisions, bypass collisions and minimize damage, and provide post-collision assistance.

## *4: Compact, home-use cogeneration system

By using natural gas to produce both heat and electricity, cogeneration units use energy sparingly and significantly reduce the burden that these tasks place on the environment.

## Financial Services

Honda offers a variety of financial services to its customers and dealers, with the aim of supporting sales of Honda motorcycles and automobiles. These services are provided through finance subsidiaries in the United States, Japan, Canada, the United Kingdom, Germany, Brazil and Thailand. In fiscal 2006, net sales of our financial services business, including inter-segment sales within Honda, rose $20.0 \%$, to $¥ 310.9$ billion, due mainly to stable demand for automobiles in North America, as well as the effect of increased foreign exchange
translations. Operating income edged up $0.8 \%$, to $¥ 90.5$ billion, benefiting from a higher loan balance accompanying expansion of our business, as well as a reduction in selling, general and administrative expenses, which outweighed the negative effects of increased interest rates for fund-raising purposes.

Information about allowance for credit losses is provided at Item 5. Operating and Financial Review and Prospects A. operating Results. Information about finance subsidiaries-receivables and securitizations is described in Note (3) to the accompanying consolidated financial statements.

## Geographical Information

Geographical information are based on the location of the Company and its subsidiaries.

## Japan

Net sales in Japan were $¥ 4,437.8$ billion, up by $7.2 \%$ from the previous fiscal year, due mainly to increased export sales in the automobile business and increased revenue in the motorcycle, power product and other businesses, which offset the negative impact of decreased unit sales in domestic automobile business. Operating income in Japan was $¥ 370.9$ billion, up by $100.6 \%$, due primarily to the positive impact of the currency effects caused by the depreciation of the Japanese yen, increased profit attributable to higher revenue and continuing cost reduction effects and gain on "return" of $¥ 138.0$ billion, which offset the negative impact of the increase in SG\&A and R\&D expenses.

## North America

Net sales in North America, which mainly consists of the United States, increased by $19.4 \%$ from the previous fiscal year to $¥ 5,616.3$ billion, due mainly to positive currency translation impact and the increased revenue in all of Honda’s business segments. Operating income in North America increased by $10.2 \%$ to $¥ 353.9$ billion, due primarily to the positive impact of currency effects caused by the depreciation of the Japanese yen and the increased profit attributable to higher revenue, which offset the negative impact of the increase in SG\&A expenses.

## Europe

Net sales in Europe increased by $14.0 \%$ to $¥ 1,189.5$ billion compared to the previous fiscal year, due mainly to the positive currency translation impact and the increased revenue in all of Honda's business segments. Operating income in Europe decreased by $36.2 \%$ to $¥ 26.3$ billion, due mainly to the negative impact of the changes in model mix and increased SG\&A expenses, offsetting the positive impact of the currency effects caused by the depreciation of the Japanese yen and the increased profit attributable to higher revenue.

## Asia

Net sales in Asia increased by $15.9 \%$ to $¥ 997.3$ billion from the previous fiscal year, due mainly to positive currency translation impact and the increased revenue in all of Honda's business segments. Operating income increased by $7.1 \%$ to $¥ 64.9$ billion from the same period of the previous year, due mainly to the positive impact of the currency effects caused by the depreciation of the Japanese yen, increased profit attributable to higher revenue and continuing cost reduction, which offset the negative impact of the increase in SG\&A expenses. In Asia, in addition to subsidiaries, many affiliates accounted for under the equity method manufacture and sell Honda-brand products. Operating income does not include income from these affiliates. Income from these affiliates is recorded as equity in income of affiliates and reflected in net income.

## Other Regions

Net sales in Other Regions increased by $22.7 \%$ to $¥ 571.6$ billion compared to the previous fiscal year, due mainly to positive impact of the currency translation effects and the increased revenue in all of Honda's business segments mainly in Latin America. Operating income increased by $72.2 \%$ from the same period of the previous year to $¥ 57.1$ billion, due mainly to the positive currency effects caused by the depreciation of the Japanese yen, the increased profit attributable to higher revenue and continuing cost reduction effects, offsetting the negative impact of the increase in SG\&A expenses.

As described in Note (1) (v) and Note (2) to our consolidated financial statements, certain revisions for misclassifications have been made. Also, certain reclassifications have been made to the prior years' consolidated financial statements to conform to the presentation used for the fiscal year ended March 31, 2007.

## Application of Critical Accounting Policies

Critical accounting policies are those which require us to apply the most difficult, subjective or complex judgments, often requiring us to make estimates about the effect of matters that are inherently uncertain and which may change in subsequent periods, or for which the use of different estimates that could have reasonably been used in the current period would have had a material impact on the presentation of our financial condition and results of operations.

The following is not intended to be a comprehensive list of all our accounting policies. Our significant accounting policies are more fully described in Note (1) to the accompanying consolidated financial statements.

We have identified the following critical accounting policies with respect to our financial presentation.

## Product Warranty

We warrant our products for specific periods of time.

Product warranties vary depending upon the nature of the product, the geographic location of their sales and other factors.

We recognize costs for general warranties on products we sell and product recalls. We provide for estimated warranty costs at the time products are sold to customers or the time new warranty programs are initiated. Estimated warranty costs are provided based on historical warranty claim experience with consideration given to the expected level of future warranty costs, including current sales trends, the expected number of units to be affected and the estimated average repair cost per unit for warranty claims. Our products contain certain parts manufactured by third party suppliers. Since suppliers typically warrant these parts, the expected receivables from warranties of these suppliers are deducted from our estimates of accrued warranty obligations.

We believe our accrued warranty liability is a "critical accounting estimate" because changes in the calculation can materially affect net income, and require us to estimate the frequency and amounts of future claims, which are inherently uncertain.

Our policy is to continuously monitor warranty cost accruals to determine their adequacy of the accrual. Therefore, warranty expense accruals are maintained at an amount we deem adequate to cover estimated warranty expenses.

Actual claims incurred in the future may differ from the original estimates, which may result in material revisions to the warranty expense accruals.

Additional detailed information about the changes in provisions for the product warranties for each of the years in the two-year period ended March 31,2007 is described in Note (17) to the accompanying consolidated financial statements.

## Credit Losses

Our finance subsidiaries provide wholesale financing to dealers and retail lending and direct financing leases to customers mainly in order to support sales of our products, principally in North America. We classify the receivables derived from those services as finance subsidiaries-receivables. Certain finance receivables related to sales of inventory are included in trade receivables and other assets in the consolidated balance sheets.

To determine the overall allowance for credit loss amount, receivables are segmented into pools with common characteristics such as product and collateral types, credit grades, and original loan terms. For each of these pools, we estimate losses primarily based on our historic loss experiences, delinquency rates, recovery rates and scale and composition of the portfolio, taking factors into consideration such as changing economic conditions and changes in operational policies and procedures.

We believe our allowance for credit losses is a "critical accounting estimate" because it requires us to make assumptions about inherently uncertain items such as future economic trends, quality of finance subsidiariesreceivables and other factors. We review the adequacy of the allowance for credit losses, and the allowance for credit losses is maintained at an amount that we deem sufficient to cover the estimated credit losses incurred on our owned portfolio of finance receivables. However, actual losses may differ from the original estimates as a result of actual results varying from those assumed in our estimates.

As an example of the sensitivity of the allowance calculation, the following scenario demonstrates the impact that a deviation in one of the primary factors estimated as a part of our allowance calculation would have on the provision and allowance for credit losses. If we had experienced a $10 \%$ increase in net credit losses during fiscal 2007 in our North America portfolio, the provision for fiscal 2007 and the allowance balance at the end of fiscal 2007 would have increased by approximately $¥ 5.5$ billion and $¥ 2.8$ billion, respectively. Note that this sensitivity analysis may be asymmetric, and are specific to the base conditions in fiscal 2007.

## Additional Narrative of the Change in Credit Loss as Below

The following table shows information related to our credit loss experience in our North America portfolio:

|  | Yen (billions) |  |  |
| :---: | :---: | :---: | :---: |
|  | 2005 | 2006 | 2007 |
| Charge-offs (net of recoveries) | 23.1 | 22.8 | 26.2 |
| Provision for credit losses | 31.7 | 27.4 | 25.5 |
| Allowance for credit losses | 29.2 | 30.1 | 28.7 |
| Ending receivable balance | 3,613.6 | 4,166.5 | 4,351.8 |
| Average receivable balance, net | 3,333.5 | 3,938.2 | 4,330.8 |
| Charge-offs as a \% of average receivable balance | 0.70\% | 0.58\% | 0.61\% |
| Allowance as a \% of ending receivable balance | 0.81\% | 0.72\% | 0.66\% |

## Fiscal Year 2007 Compared with Fiscal Year 2006

Net charge-offs in our North American portfolio increased by $¥ 3.4$ billion, or $15 \%$. Higher originations of finance receivables due to business expansion in fiscal year 2006 compared to fiscal year 2005 resulted in higher charge-offs in fiscal year 2007.

The provision for credit losses decreased by $¥ 1.9$ billion, or $7 \%$ and the allowance for credit losses decreased by $¥ 1.4$ billion, or $5 \%$. The decreases were due to lower estimates of losses incurred as of March 31, 2007 even though finance receivables increased.

## Fiscal Year 2006 Compared with Fiscal Year 2005

Net charge-offs in our North America portfolio decreased by $¥ 0.3$ billion, or $1 \%$. The lower loan originations during fiscal year 2005 resulted in a lower volume of defaults during fiscal year 2006, offsetting the currency translation effects. Also the difficulties experienced with the implementation of the new customer account servicing system in fiscal year 2005 has passed, which improved collection efforts.

The provision for credit losses decreased by $¥ 4.3$ billion, or $14 \%$. The allowance for credit losses increased by $¥ 0.9$ billion, or $3 \%$, due to the currency translation effects. Excluding this effect, the allowance for credit losses decreased.

## Losses on Lease Residual Values

End-customers of leased vehicles typically have an option to buy the leased vehicle for the contractual residual value of the vehicle or to return the vehicle to our finance subsidiaries through the dealer at the end of the lease term. Likewise, dealers have the option to buy the vehicle returned by the customer or to return the vehicle to our finance subsidiaries. The likelihood that the leased vehicle will be purchased varies depending on the difference between the actual market value of the vehicle at the end of the lease term and the contractual value determined at the inception of the lease. Our finance subsidiaries in North America have historically accounted for all leases as direct finance leases. However, starting in the year ended March 31, 2007, some of the leases which do not qualify for direct financing leases accounting treatment are accounted for as operating leases.

We initially determine the contract residual values by using our estimate of future used vehicle values, taking into consideration data obtained from third parties. We are exposed to risk of loss on the disposition of returned lease vehicles when the proceeds from the sale of the vehicles are less than the contractual residual values at the end of the lease term. We periodically review the estimate of residual values. Downward adjustments are made for declines in estimated residual values that are deemed to be other-than-temporary. For direct financing leases, our finance subsidiaries in North America purchase insurance to cover a portion of the estimated residual value. The adjustments on the uninsured portion of the vehicle's residual value are recognized as a loss in the period in which the estimate changed. For vehicle leases accounted for as operating leases, adjustments to estimated residual values result in changes to the remaining depreciation expense to be recognized prospectively on a straight-line basis over the remaining term of the lease.

The primary components in estimating losses on lease residual values are the expected frequency of returns, or the percentage of leased vehicles we expect to be returned by customers at the end of the lease term, and the expected loss severity, or the expected difference between the residual value and the amount we receive through sales of returned vehicles plus proceeds from insurance, if any. We estimate losses on lease residual values by evaluating several different factors, including trends in historical and projected used vehicle values and general economic measures.

We believe that our estimated losses on lease residual values is a "critical accounting estimate" because it is highly susceptible to market volatility and requires us to make assumptions about future economic trends and lease residual values, which are inherently uncertain. We believe that the assumptions used are appropriate. However, actual losses incurred may differ from original estimates.

If future auction values for all Honda and Acura vehicles in our North American direct financing lease portfolio as of March 31, 2007, were to decrease by approximately $¥ 10,000$ per unit from our present estimates, the total impact would be an increase in losses on lease residual values by about $¥ 0.8$ billion. Similarly, if future return rates for our existing portfolio of all Honda and Acura vehicles were to increase by one percentage point from our present estimates, the total impact would be an increase in losses on lease residual values by about $¥ 0.1$ billion. For operating lease portfolio as of March 31 with the same prerequisite shown above, the impacts would be immaterial. Note that this sensitivity analysis may be asymmetric, and are specific to the base conditions in fiscal 2007.

## Pension and Other Postretirement Benefits

We have various pension plans covering substantially all of our employees in Japan and certain employees in foreign countries. Benefit obligations and pension costs are based on assumptions of many factors, including the discount rate, the rate of salary increase and the expected long-term rate of return on plan assets. The discount rate and expected long-term rate of return on plan assets are determined based on our evaluation of current market conditions, including changes in interest rates. The salary increase assumptions reflect our actual experience as well as near-term outlook. Our assumed discount rate and rate of salary increase as of March 31, 2007 were $2.0 \%$ and $2.3 \%$, respectively, and our assumed expected long-term rate of return for the year ended March 31, 2007 was $4.0 \%$ for Japanese plans. Our assumed discount rate and rate of salary increase as of March 31,2007 were $5.2-6.0 \%$ and $2.9-6.4 \%$, respectively, and our assumed expected long-term rate of return for fiscal 2007 was $6.8-8.0 \%$ for foreign plans.

We believe that the accounting estimates related to our pension plans is "critical accounting estimate" because changes in these estimates can materially affect our financial condition and results of operations.

Actual results may differ from our assumptions, and the difference is accumulated and amortized over future periods. Therefore, the difference will be generally reflected as our recognized expenses and recorded obligations in future period. We believe that the assumptions currently used are appropriate, however, differences in actual expenses or changes in assumptions could affect our pension costs and obligations, including our cash requirements to fund such obligations.

The following table shows the effect of a $0.5 \%$ change in the assumed discount rate and the expected longterm rate of return on our funded status, equity, and pension expense.

## Japanese Plans

| Japane Plan |  |  | billions) |  |
| :---: | :---: | :---: | :---: | :---: |
| Assumptions | $\begin{gathered} \hline \text { Percentage } \\ \text { Point } \\ \text { Change (\%) } \end{gathered}$ | Funded status | Equity | Pension expense |
| Discount rate | +0.5/-0.5 | -88.1/+99.3 | +47.9/-59.8 | -5.2/+6.3 |
| Expected long-term rate of return | +0.5/-0.5 | - | - | -3.3/+3.3 |

## Foreign Plans

| - |  |  | billions) |  |
| :---: | :---: | :---: | :---: | :---: |
| Assumptions | $\begin{aligned} & \hline \text { Percentage } \\ & \text { Point } \\ & \text { Cange (\%) } \end{aligned}$ | Funded status | Equity | Pension expense |
| Discount rate | +0.5/-0.5 | -43.4/+49.8 | +30.7/-35.8 | -6.3/+7.3 |
| Expected long-term rate of return | +0.5/-0.5 | - | - | -1.8/+1.8 |

${ }^{(* 1)}$ Note that this sensitivity analysis may be asymmetric, and are specific to the base conditions at March 31, 2007.
(*2) Funded status for fiscal 2007 is affected by March 31, 2007 assumptions.
Pension expense for fiscal 2007 is affected by March 31, 2006 assumptions.

## New Accounting Pronouncements

In March 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 156, "Accounting for Servicing of Financial Assets". This statement amends SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities", with respect to the accounting for separately recognized servicing assets and servicing liabilities. SFAS No. 156 gives revised guidance as to when servicing assets and servicing liabilities should be recognized. It also revises guidance regarding the initial and subsequent measurement of servicing assets and liabilities. SFAS No. 156 is effective as of the beginning of an entity's first fiscal year that begins after September 15, 2006. Management is currently in process of quantifying the financial impact of adoption. It is not anticipated that adoption will have a material impact on the Company's financial position or results of operations.

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) No. 48, "Accounting for Uncertainty in Income Taxes". This Interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes". This Interpretation prescribes a two step process for the recognition and measurement in the financial statement of a tax position taken or expected to be taken in a tax return. This statement is effective as of an entity's first fiscal year that begins after December 15, 2006. Management is currently in the process of quantifying the financial impact of adoption.

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No.157, "Fair Value Measurements". This statement defines fair value, establishes
a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements and does not require any new fair value measurements. This statement is effective as of an entity's first fiscal year that begins after November 15, 2007, with early adoption encouraged. Management is currently in the process of determining whether to early adopt this statement and quantifying the financial impact of adoption. It is not anticipated that adoption will have a material impact on the Company's financial position or results of operation.

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans-an amendment of FASB Statements No. 87, 88, 106, and 132(R)". This statement amends SFAS No. 87, "Employers' Accounting for Pensions", SFAS No. 88, "Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension and for Termination Benefits", SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions", and SFAS No. 132(R), "Employers' Disclosures about Pensions and Other Postretirement Benefits". This statement requires an employer to recognize the overfunded or underfunded status as an asset or liability in its statement of financial position and to recognize changes in that funded status in comprehensive income in the year in which the changes occur. This statement replaces SFAS No. 87's requirement to report at least minimum pension liability measured as excess at the accumulated benefit obligation over the fair value at the plan assets. The Company and its consolidated subsidiaries adopted SFAS No. 158 on March 31, 2007. Detailed information about the impact of the adoption of SFAS No. 158 is provided in note 12 to the accompanying consolidated financial statements. This statement also changes the date at which benefit obligations are to be measured to the date of the year-end statement of financial position. The measurement provisions of this statement are effective for fiscal years ending after December 15, 2008.

In February 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 159, "The Fair Value Option for Financial Assets and Financial Liabilitiesincluding an amendment of SFAS No.115". This statement permits entities to choose to measure at fair value many financial instruments and certain other items that are not currently required to be measured at fair value. Subsequent changes in fair value for designated items will be required to be reported in earnings in the current period. The statement also establishes presentation and disclosure requirements for similar types of assets and liabilities measured at fair value. The statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, with early adoption being permitted. Management is currently in process of determining whether to early adopt this statement and quantifying the financial impact of adoption.

## B. Liquidity and Capital Resources

## Overview of Capital Requirements, Sources and Uses

The policy of Honda is to support its business activities by maintaining sufficient capital resources, a sufficient level of liquidity and a sound balance sheet.

Honda's main business is the manufacturing and sale of motorcycles, automobiles and power products. To support this business, it also provides retail financing and automobile leasing services for customers, as well as wholesale financing services for dealers.

In its manufacturing and sales business, Honda requires operating capital mainly to purchase parts and materials required for production, as well as to control inventory of finished products and cover receivables from dealers. Honda also requires funds for capital expenditures, mainly to introduce new models, upgrade, rationalize and renew production facilities, as well as to expand and reinforce Sales and R\&D facilities.

Honda meets its operating capital requirements mainly through cash generated by operations. Honda funds its financial programs for customers and dealers primarily from corporate bonds, medium-term notes, commercial paper, and securitization of finance receivables. The year-end balance of liabilities associated with fund-raising by finance subsidiaries was $¥ 4,470.4$ billion as of March 31, 2007.

## Cash Flows

Consolidated cash and cash equivalents amounted to $¥ 945.5$ billion as of March 31,2007 , up $¥ 228.7$ billion, or $31.9 \%$, from a year earlier, mainly owing to the increases in net cash provided by operating and financing activities, offset in part by the increase in net cash used in investing activities as described below.

Net cash provided by operating activities amounted to $¥ 904.5$ billion. Factors increasing operating cash flows included continued significant growth in sales and stable operating margins (excluding the effect of the non-cash gain on return in the prior year), accompanied by lower increases in net operating assets and liabilities in the current year.

Net cash used in investing activities totaled $¥ 1,130.7$ billion. Factors increasing net cash used in investing cash flows were mainly due to $¥ 597.9$ billion in capital expenditures associated with introducing new models, upgrading, streamlining and renewing production facilities, and the improvement of Sales and R\&D facilities. Other factors were $¥ 240.2$ billion increase in acquisition of finance subsidiaries-receivables and $¥ 365.5$ billion increase of property on operating leases associated with higher sales of automobiles in North America and elsewhere.

Net cash provided by financing activities was $¥ 423.4$ billion. During the year, Honda raised $¥ 306.0$ billion in short-term debt through the issue of commercial paper, and also raised $¥ 969.4$ billion in long-term debt through the issue of bonds and medium-term notes to meet capital requirements associated mainly with an increase in liabilities of finance subsidiaries, as well as to repay $¥ 677.5$ billion in long-term debt. By contrast, Honda also made $¥ 26.6$ billion in payments for purchase of treasury stock and $¥ 140.4$ billion in cash dividends paid.

## Liquidity

The $¥ 945.5$ billion in cash and cash equivalents at end of year corresponds to approximately 1.0 month of net sales, and Honda believes it has sufficient liquidity for its business operations. At the same time, Honda is aware of the possibility that various factors, such as recession-induced market contraction and financial and foreign exchange market volatility, may adversely affect liquidity.

For this reason, finance subsidiaries carry total short-term borrowings of $¥ 1,842.1$ billion in the form of commercial paper issued regularly to replace debt. This serves as alternative liquidity for a back-up credit line equivalent to $¥ 826.1$ billion. Honda believes it currently has sufficient credit limits, extended by prominent international banks.

Honda believes it has adequate liquidity to meet its cash obligations for the near future at least for the year ending March 31, 2008.

Honda's short- and long-term debt securities are rated by credit rating agencies, such as Moody's Investor Service, Inc., and Standard \& Poor's Rating Services. Based on major current ratings, which are shown below, Honda will be able to raise funds even if it requires more capital than its present level of liquidity would allow.

The following table shows the ratings of Honda's unsecured debt securities by Moody's and Standard \& Poor's as of the date of the filing of this Form 20-F.

|  | Credit ratings for |  |
| :---: | :---: | :---: |
|  | Short-term unsecured debt securities | Long-term unsecured debt securities |
| Moody's Investors Service | P-1 | Aa3 |
| Standard \& Poor's Rating Services | A-1 | A+ |

The above ratings are based on information provided by Honda and other information deemed credible by the rating agencies. They are also based on the agencies' assessment of credit risk associated with designated securities issued by Honda. Each rating agency uses different standards for calculating Honda's credit rating, and also makes its own assessments. Ratings can be revised or nullified by agencies at any time. These ratings are not meant to serve as a recommendation for trading in or holding debt.

## C. Research and Development

Using the most advanced technologies, Honda Motor Company and its consolidated subsidiaries conduct R\&D activities aimed at creating distinctive products that are internationally competitive. The Group's main R\&D divisions operate independently as subsidiaries, allowing technicians to pursue their tasks with significant freedom.

Product-related research and development is spearheaded by the Honda R\&D Co., Ltd., Honda R\&D Americas, Inc., in the United States and Honda R\&D Europe (Deutschland) GmbH in Germany. Research and development on production technologies centers on Honda Engineering Co., Ltd., in Japan and Honda Engineering North America, Inc. All of these entities work in close association with our other entities and business in their respective regions. Total consolidated R\&D expenditures for the year ended March 31, 2007 amounted to $¥ 551.8$ billion. Main R\&D activities conducted by each business segment are outlined below.

## Motorcycle Business

Honda is committed to developing motorcycles with new value-added features that meet the individual needs of customers around the world, and to implementing timely local development of regional products at its overseas locations. At the same time, we focus on developing industry-leading technologies that address safety and environmental issues.

Breakthroughs during fiscal 2007 include the development in the United States and Canada of the Gold Wing touring bike equipped with the world's first motorcycle airbag system. In North America and Europe, the CBR600RR underwent a full model change, achieving lower weight than the previous model through a more compact engine installed in a newly designed Fine Die-Cast aluminum frame. It also employs a newly designed compact, electrically controlled steering damper that facilitates further enhanced riding performance. In Asia, we began production and sales at an equity-method affiliate in India of the Glamour-FI 125cc motorcycle, equipped with a PGM-FI electronic fuel-injection system, which meets new demands for low fuel consumption and clean performance through exhaust emissions. In China, we commenced production and sales at an equity-method affiliate of two new models: CBF150 motorcycle, mounted with a newly developed Core 2 150cc engine with low fuel consumption and robust power achieved through substantially reduced friction loss and improved cooling performance; and SCR110 scooter, which employs PGM-FI low-friction technologies to become the first model in the country to clear Euro3 motorcycle emission gas standards.

Other technological R\&D highlights include the announced development of Honda's Variable Cylinder Management (VCM) system, which is based on high-performance Variable Valve Timing and Lift, Electronic Control (VTEC) technologies for three-phase control over the number of active cylinders, facilitating low fuel consumption and high power capacity. We also developed an engine that offers one of the world's lowest levels of friction, achieved by improving fuel efficiency through a two-plug system and reducing mechanical resistance in the engine.

Research and development expenses (which do not include research and development at equity-method affiliates described above) in the Motorcycle Business segment in fiscal 2007 totaled $¥ 90.1$ billion.

## Automobile Business

In the Automobile Business segment, we strive to develop innovative technologies and products through creativity-oriented development in response to customer needs. We also actively develop technologies that address environmental issues and provide enhanced safety performance.

Major achievements during the year include a full model change for the $C R-V$ in markets around the world. For four-wheel drive models, we introduced a new real-time 4WD system that improves rear-wheel torque transmissibility by bolstering the existing dual-pump system with a one-way cam unit. In Japan, we melded steering maneuver and voice guidance in the Honda Smart Parking Assist System, which is used on the Life. Further, we released the Crossroad, an automobile that transcends existing categories by combining the design and functionality of an SUV, the convenient size of a compact car, and the three-row, seven-seat configuration of a minivan. In North America, we commenced sales of the Acura RDX entry-premium SUV, which features a newly developed 2.3-liter i-VTEC (intelligent VTEC) turbo engine and Super-Handling All Wheel Drive (SH-AWD) to provide good fuel economy, high output and excellent driving performance. Breakthroughs in other regions included sales of flexible fuel vehicle (FFV) versions of the Civic and Fit in Brazil that can be powered by ethanol or an ethanol-gasoline mixture.

Another technology development milestone was the development of a clean diesel engine on par with a gasoline engine for environmental performance. This is achieved through a newly developed NOx catalyst that efficiently purifies NOx gases to nitrogen through a reduction reaction using ammonia produced within the catalytic converter. In addition, we have developed an evolutionary VTEC engine with high power and low fuel consumption and emissions, attained by combining VTEC and Valve Timing Control (VTC)—which dynamically controls the intake valve lift amount and aperture angle-for continuously variable control.

In the field of automotive fuel cell technologies, Honda announced the operation of its next-generation fuel-cell-powered FCX Concept, with the compact, high efficiency Honda FC STACK run through the central tunnel, to deliver radically improved performance in terms of driving, as well as environmental performance.

Research and development expenses in the Automobile Business segment in fiscal 2007 totaled $¥ 447.0$ billion.

## Power Product and Other Businesses

In the Power Products Businesses, we seek to develop products that match customers' lifestyles and needs while strengthening our lineup of offerings that address environmental issues.

In fiscal 2007, BF90 four-stroke marine outboard motor underwent a full model change. This motor features such intelligent technologies as a VTEC structure based on a 1.5-liter passenger car engine, PGM-FI, a Lean Burn Control system and the world's first air-fuel timing ignition control for a marine outboard. The BF90 is lightweight and compact, while achieving excellent drive performance and economizing on fuel consumption. We also carried out a model change for our compact, home-use cogeneration system, scoring improvements in power generation efficiency and reducing the $\mathrm{CO}_{2}$ emissions ratio. An electronic control variable jet to automatically optimize fuel flow is also employed to enhance cold-start performance.

Other technical development spawned a high-expansion-ratio engine with an original intake/compression stroke and expansion/exhaust stroke structure that was prototyped during fiscal 2007.

In other businesses, ongoing research into jet engines and HondaJet, our advanced, compact business jet, has reached fruition with development moving toward commercial production.

Research and development expenses in this segment in fiscal 2007 amounted to $¥ 14.6$ billion.

## Fundamental Research

In the area of fundamental research, Honda pursues steady and varied research activities into technologies that may lead to innovative applications in the future.

During the year, we announced a new brain-machine interface creating basic technology for manipulating robots using human brain activity as a result of joint research with Advanced Telecommunications Research Institute International. Honda has also developed a biofabric with excellent levels of durability, aesthetics and smoothness for use as an automobile interior finish. As this fabric is derived from plant materials, the material manufacturing process results in an energy savings of $10 \%$ to $15 \%$, compared with such conventional oil-based fabrics as polyester. Further, through joint research with the Research Institute of Innovative Technology for the Earth we have established a technological base for ethanol production from soft-biomass, cellulose from plant stalk and leaf matter, such as cultivated rice byproducts, that are not suitable for human consumption. This step from cellulose to bioethanol production surmounts a problem that had been thwarting progress in this field.

Expenses incurred in fundamental research are distributed among Honda's business segments.

## Patents and Licenses

At March 31, 2007, Honda owned more than 10,900 patents and 80 utility model registrations in Japan and more than 18,500 patents abroad. Honda also had applications pending for more than 18,400 patents in Japan and for more than 18,800 patents abroad. Under Japanese law, a utility model registration is a right granted with respect to inventions of less originality than those which qualify for patents. While the Company considers that, in the aggregate, Honda's patents are important, it does not consider any one of such patents, or any related group of them, to be of such importance that the expiration or termination thereof would materially affect Honda's business.

## D. Trend Information

See Item 5. A "Operating and Financial Review and Prospects" for information required by this item.

## E. Off-Balance sheet Arrangements

## (Special Purpose Entity)

For the purpose of accelerating the receipt of cash related to our finance receivables, we periodically securitize and sell pools of these receivables. In these securitizations, we sell a portfolio of finance receivables to a special purpose entity, which is established for the limited purpose of buying and reselling finance receivables. We remain as a servicer of the finance receivables and are paid a servicing fee for our services. The special purpose entity transfers the receivables to a trust or bank conduit, which issues interest-bearing asset-backed securities or commercial paper, respectively, to investors. We retain certain subordinated interests in the sold receivables in the form of subordinated certificates, servicing assets and residual interests in certain cash reserves provided as credit enhancements for investors. We apply significant assumptions regarding prepayments, credit losses and average interest rates in estimating expected cash flows from the trust or bank conduit, which affect the recoverability of our retained interests in the sold finance receivables. We periodically evaluate these assumptions and adjust them, if appropriate, to reflect the performance of the finance receivables.

## (Guarantee)

At March 31, 2007, we guaranteed $¥ 41.1$ billion of employee bank loans for their housing costs. If an employee defaults on his/her loan payments, we are required to perform under the guarantee. The undiscounted maximum amount of our obligation to make future payments in the event of defaults is $¥ 41.1$ billion. As of March 31, 2007, no amount was accrued for any estimated losses under the obligations, as it was probable that the employees would be able to make all scheduled payments.

## F. Tabular Disclosure of Contractual Obligations

The following table shows our contractual obligations at March 31, 2007:

## Contractual Obligations

|  | $\begin{aligned} & \text { At March 31, } 2007 \\ & \text { Yen (millions) } \end{aligned}$ |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  | Payments due by period |  |  |  |  |
|  | Total | Less than 1 year | $\begin{gathered} 1-3 \\ \text { years } \\ \hline \end{gathered}$ | 3-5 years | After 5 years |
| Long-term debt | 2,681,152 | 775,409 | 1,374,355 | 504,705 | 26,683 |
| Operating leases | 128,978 | 25,354 | 34,703 | 23,543 | 45,378 |
| Purchase commitments (*) | 78,027 | 78,027 | - | - |  |

(*) Honda had commitments for purchases of property, plant and equipment at March 31, 2007.
Honda expects to contribute $¥ 33,953$ million to its domestic pension plans and $¥ 37,187$ million to its foreign pension plans in the year ending March 31, 2008.

At March 31, 2007, we had no material capital lease obligations or long-term liabilities reflected on our balance sheet under U.S. GAAP other than those set forth in the table above.

## G. Safe Harbor

All information disclosed under Item 5. E and F contains "forward-looking statements" as defined in Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended.

Such statements are based on management's assumptions and beliefs taking into account information currently available to it. Therefore, please be advised that Honda's actual results could differ materially from those described in these forward-looking statements as a result of numerous factors, including general economic conditions in Honda's principal markets and foreign exchange rates between the Japanese yen and the U.S. dollar, the Euro and other major currencies, as well as other factors detailed from time to time.

## Item 6. Director, Senior Management and Employees

## A. Directors and Senior Management

Honda's Articles of Incorporation provide for a Board of Directors of not more than 30 members and for a Board of Corporate Auditors of not more than seven Corporate Auditors. Directors and Corporate Auditors are elected by resolution of the general meetings of shareholders. The Corporate Auditors are nominated by the Board of Directors as candidates for election with an approval by the Board of Corporate Auditors. The normal term of office of a Director is one year and that of a Corporate Auditor is four years. Directors and Corporate Auditors may serve any number of consecutive terms.

The Board of Directors appoints one President and Director and may appoint one Chairman of the Board of Directors and several Executive Vice Presidents and Directors, Senior Managing Directors and Managing Directors from among its members. The President represents the Company. In addition, the Board of Directors may appoint, pursuant to its resolutions, Directors who shall each represent the Company. Under the Japanese Company Law, a representative director individually has authority to represent the Company generally in the conduct of its affairs. The Board of Directors has the ultimate responsibility for the administration of the affairs of the Company.

Under the Japanese Company Law, the Corporate Auditors of the Company have the duty to audit the Director's execution of their duties. Corporate Auditors are not required to be, and the Corporate Auditors of the

Company are not, certified public accountants, and may not at the same time be Directors or employees of the Company or any of its subsidiaries. They are entitled to participate in meetings of the Board of Directors but are not entitled to vote. Corporate Auditors of the Company form the Board of Corporate Auditors, which must consist of at least three Corporate Auditors. Not less than half of the members of the Board of Corporate Auditors must be outside Corporate Auditors, each of whom has never served as a director, accounting councilor, operating officer, manager or employee of the Company or any of its subsidiaries. Corporate Auditors are required to elect from among themselves at least one Standing Corporate Auditor. Corporate Auditors also have a statutory duty to provide their report to the Board of Corporate Auditors, which must submit its audit report to the Representative Director each year. A Corporate Auditor may note his or her opinion in the audit report if his or her opinion is different from the opinion expressed in the audit report. The Board of Corporate Auditors is empowered to establish audit principles, methods of investigation by Corporate Auditors of the status of the corporate affairs and assets of the Company and other matters concerning the performance of the Corporate Auditors' duties. In addition, the Company is required to appoint independent certified public accountants as accounting auditor. Such independent certified public accountants have their primary statutory duties to audit the consolidated and non-consolidated financial statements of the Company prepared in accordance with the Japanese Company Law to be submitted by the Representative Director to general meetings of shareholders to prepare an accounting audit report thereon and to notify the contents of such report to the specified Corporate Auditor and the specified Director in charge.

The following table provides the names of all Directors and Corporate Auditors of the Company and the current positions held by such persons.

| Name <br> (Date of birth) | Current Positions and Biographies with Registrant | Term | Number of Shares Owned |
| :---: | :---: | :---: | :---: |
| Directors |  |  |  |
| Satoshi Aoki <br> (August 19, 1946) | Director of the Company from June 1995 | *3 | 15,100 |
|  | Chairman and Director of the Company, appointed in June 2007 |  |  |
|  | Executive Vice President and Director of the Company, appointed in June 2005 |  |  |
|  | Compliance Officer, appointed in April 2004 |  |  |
|  | Senior Managing Director of the Company, appointed in June 2000 |  |  |
|  | Managing Director of the Company, appointed in June 1998 |  |  |
|  | Chief Operating Officer for Business Management Operations, appointed in June 1998 |  |  |
|  | General Manager of Accounting Division for Business Management Operations, appointed in June 1996 |  |  |
|  | Director of the Company, appointed in June 1995 |  |  |
|  | General Manager of Finance Division for Business Management Operations, appointed in June 1994 |  |  |

Joined Honda in April 1969

| Name <br> (Date of birth) | Current Positions and Biographies with Registrant | Term | Number of Shares Owned |
| :---: | :---: | :---: | :---: |
| Takeo Fukui <br> (November 28, 1944) | Director of the Company from June 1988 | *3 | 22,800 |
|  | President and Director of the Company, appointed in June 2003 |  |  |
|  | Senior Managing Director of the Company, appointed in June 1999 |  |  |
|  | Motor Sports, appointed in June 1999 |  |  |
|  | President and Director of Honda R\&D Co., Ltd., appointed in June 1998 |  |  |
|  | President and Director of Honda of America Mfg., Inc., appointed in June 1996 |  |  |
|  | Managing Director of the Company, appointed in June 1996 |  |  |
|  | Executive Vice President and Director of Honda of America Mfg., Inc., appointed in June 1994 |  |  |
|  | General Manager of Hamamatsu Factory in Motorcycle Operations, appointed in June 1992 |  |  |
|  | General Manager of Development Management Division in Motorcycle Operations, appointed in March 1991 |  |  |
|  | Senior Managing Director of Honda R\&D Co., Ltd., appointed in June 1990 |  |  |
|  | Director of the Company, appointed in June 1988 |  |  |
|  | Managing Director of Honda R\&D Co., Ltd., appointed in May 1987 |  |  |
|  | President and Director of Honda Racing Corporation, appointed in May 1987 |  |  |
|  | Joined Honda in April 1969 |  |  |
| Koichi Kondo <br> (February 13, 1947) | Director of the Company from June 1997 | *3 | 8,936 |
|  | Executive Vice President and Director of the Company, appointed in June 2007 |  |  |
|  | Chairman and Director of American Honda Motor Co., Inc., appointed in April 2007 (presently held) |  |  |
|  | Chief Operating Officer for Regional Sales Operations (Japan), appointed in April 2007 (presently held) |  |  |
|  | Senior Managing Director of the Company, appointed in June 2005 |  |  |


| Name <br> (Date of birth) | Current Positions and Biographies with Registrant | Term | Number of Shares Owned |
| :---: | :---: | :---: | :---: |
|  | President and Director of Honda North America, Inc., appointed in April 2005 |  |  |
|  | Chief Operating Officer for Regional Operations (North America), appointed in April 2004 |  |  |
|  | President and Director of American Honda Motor Co., Inc., appointed in June 2003 |  |  |
|  | Executive Vice President and Director of American Honda Motor Co., Inc., appointed in April 2003 |  |  |
|  | Managing Director of the Company, appointed in June 2002 |  |  |
|  | Chief Operating Officer for Regional Operations (Latin America), appointed in April 2000 |  |  |
|  | Director of the Company, appointed in June 1997 |  |  |
|  | President and Director of Honda Automoveis do Brasil Ltda., appointed in June 1996 |  |  |
|  | President and Director of Moto Honda da Amazonia Ltda., appointed in June 1996 |  |  |
|  | President and Director of Honda Motor do Brasil Ltda. (presently Honda South America Ltda.), appointed in June 1996 |  |  |
|  | Joined Honda in April 1970 |  |  |
| Minoru Harada (January 9, 1947) | Director of the Company from June 1994 | *3 | 14,400 |
|  | Purchasing Operations Support, appointed in April 2006 (presently held) |  |  |
|  | Chief Operating Officer for Motorcycle Operations, appointed in April 2004 (presently held) |  |  |
|  | Senior Managing Director of the Company, appointed in June 1999 |  |  |
|  | President and Director of Honda Motor Europe Limited, appointed in June 1998 |  |  |
|  | Chief Operating Officer for Regional Operations (Europe, the Middle \& Near East and Africa), appointed in June 1998 |  |  |
|  | Chief Operating Officer for Power Product Operations, appointed in June 1997 |  |  |
|  | Managing Director of the Company, appointed in June 1997 |  |  |



| Name <br> (Date of birth) | Current Positions and Biographies with Registrant | Term | Number of Shares Owned |
| :---: | :---: | :---: | :---: |
|  | Chief Operating Officer for Regional Operations (Asia \& Oceania), appointed in April 2003 |  |  |
|  | President and Director of Honda Leasing (Thailand) Company Limited, appointed in June 2002 |  |  |
|  | President and Director of Honda Automobile (Thailand) Co., Ltd., appointed in December 2000 |  |  |
|  | Managing Director of the Company, appointed in June 2000 |  |  |
|  | Deputy Chief Operating Officer for Regional Operations (Asia \& Oceania), appointed in June 1999 |  |  |
|  | President and Director of Honda Cars (Thailand) Co., Ltd., appointed in June 1998 |  |  |
|  | President and Director of Asian Honda Motor Co., Ltd., appointed in May 1996 |  |  |
|  | Director of the Company, appointed in June 1995 |  |  |
|  | General Manager of Motorcycle Sales Division in Regional Operations (Asia \& Oceania), appointed in April 1995 |  |  |
|  | Joined Honda in May 1973 |  |  |
| Koki Hirashima (November 28, 1946) | Director of the Company from June 1997 | *3 | 6,000 |
|  | Senior Managing Director of the Company, appointed in June 2005 |  |  |
|  | General Supervisor, Information Systems, appointed in April 2005 (presently held) |  |  |
|  | Risk Management Officer, appointed in April 2005 (presently held) |  |  |
|  | Chief Operating Officer for Production Operations, appointed in April 2005 (presently held) |  |  |
|  | Managing Director of the Company, appointed in June 2000 |  |  |
|  | President and Director of Honda of America Mfg., Inc., appointed in June 1998 |  |  |
|  | Executive Vice President and Director of Honda of America Mfg., Inc., appointed in June 1997 |  |  |



| Name (Date of birth) | Current Positions and Biographies with Registrant | Term | Number of Shares Owned |
| :---: | :---: | :---: | :---: |
| Masaaki Kato <br> (September 16, 1949) | General Manager of Suzuka Factory of Production Operations, appointed in April 2005 |  |  |
|  | General Supervisor, Motor Sports, appointed in April 2004 |  |  |
|  | President and Director of Honda R\&D Co., Ltd., appointed in June 2003 |  |  |
|  | Motor Sports, appointed in June 2003 |  |  |
|  | Managing Director of the Company, appointed in June 2003 |  |  |
|  | Senior Managing Director of Honda R\&D Co., Ltd., appointed in June 2001 |  |  |
|  | Director of the Company, appointed in June 2000 |  |  |
|  | Executive Vice President of Honda R\&D Americas, Inc., appointed in April 1998 |  |  |
|  | Joined Honda in April 1978 |  |  |
|  | Director of the Company from June 1998 | *3 | 16,100 |
|  | Senior Managing Director of the Company, appointed in June 2007 |  |  |
|  | President and Director of Honda R\&D Co., Ltd., appointed in April 2007 (presently held) |  |  |
|  | General Supervisor, Quality appointed in April 2007 (presently held) |  |  |
|  | Managing Officer of the Company, appointed in June 2005 |  |  |
|  | President and Director of Honda of the U.K. Manufacturing Ltd., <br> Appointed in April 2005 |  |  |
|  | Executive Vice President and Director of Honda Motor Europe Ltd., appointed in April 2005 |  |  |
|  | President and Director of Honda Manufacturing of Alabama, LLC, appointed in April 2002 |  |  |
|  | Director of the Company, appointed in June 1998 |  |  |
|  | General Manager of Human Resources Division and HR Development Office for Business Support Operations appointed in January 1998 |  |  |
|  | Joined Honda in April 1974 |  |  |


| Name <br> (Date of birth) | Current Positions and Biographies with Registrant | Term | Number of Shares Owned |
| :---: | :---: | :---: | :---: |
| Toru Onda (March 18, 1949) | Director of the Company from June 1999 | *3 | 8,000 |
|  | Managing Director of the Company, appointed in June 2002 |  |  |
|  | Chief Operating Officer for Purchasing Operations, appointed in April 2000 (presently held) |  |  |
|  | Director of the Company, appointed in June 1999 |  |  |
|  | General Manager of Automobile Purchasing Division 1 in Purchasing Operations, appointed in June 1998 |  |  |
|  | Joined Honda in January 1977 |  |  |
| Akira Takano <br> (August 18, 1949) | Director of the Company from June 1996 | *3 | 9,200 |
|  | Chief Operating Officer for Customer Service Operations, appointed in April 2004 (presently held) |  |  |
|  | Managing Director of the Company, appointed in June 2003 |  |  |
|  | President and Director of Honda of the U.K. Manufacturing Ltd., appointed in June 1998 |  |  |
|  | Executive Vice President and Director of Honda Motor Europe Ltd., appointed in June 1998 |  |  |
|  | Director of the Company, appointed in June 1996 |  |  |
|  | Director of Honda R\&D Co., Ltd., appointed in June 1995 |  |  |
|  | Joined Honda in April 1972 |  |  |
| Shigeru Takagi <br> (February 4, 1952) | Director of the Company from June 1998 | *3 | 7,800 |
|  | Managing Director of the Company, appointed in June 2004 |  |  |
|  | President and Director of Honda Motor Europe Limited, appointed in April 2004 (presently held) |  |  |
|  | Chief Operating Officer for Regional Operations (Europe, the Middle \& Near East and Africa), appointed in April 2004 (presently held) |  |  |
|  | Director of the Company, appointed in June 1998 |  |  |
|  | President and Director of Honda Canada Inc., appointed in June 1998 |  |  |

Joined Honda in April 1974

| Name <br> (Date of birth) | Current Positions and Biographies with Registrant | Term | Number of Shares Owned |
| :---: | :---: | :---: | :---: |
| Tetsuo Iwamura (May 30, 1951) | Director of the Company from June 2000 | *3 | 6,200 |
|  | President and Director of American Honda Motor Co., Inc., appointed in April 2007 (presently held) |  |  |
|  | President and Director of Honda North America, Inc., appointed in April 2007 (presently held) |  |  |
|  | Chief Operating Officer for Regional Operations (North America), appointed in April 2007 (presently held) |  |  |
|  | Managing Director of the Company, appointed in June 2006 |  |  |
|  | President and Director of Honda Automoveis do Brasil Ltda., appointed in April 2003 |  |  |
|  | President and Director of Moto Honda da Amazonia Ltda., appointed in April 2003 |  |  |
|  | President and Director of Honda South America Ltda., appointed in April 2003 |  |  |
|  | Chief Operating Officer for Regional Operations (Latin America), appointed in April 2003 |  |  |
|  | Director of the Company, appointed in June 2000 |  |  |
|  | Chief Operating Officer for Parts Operations, appointed in April 2000 |  |  |
|  | Joined Honda in April 1978 |  |  |
| Tatsuhiro Oyama (July 9, 1950) | Director of the Company from June 2001 | *3 | 9,000 |
|  | Managing Director of the Company, appointed in June 2006 |  |  |
|  | President and Director of Asian Honda Motor Co., Ltd., appointed in April 2006 (presently held) |  |  |
|  | Chief Operating Officer for Regional Operations (Asia \& Oceania), appointed in April 2006 (presently held) |  |  |
|  | Chief Operating Officer for Parts Operations, appointed in April 2003 |  |  |
|  | President and Director of Honda Motorcycle Japan Co., Ltd., appointed in August 2001 |  |  |
|  | Director of the Company, appointed in June 2001 |  |  |



| Name <br> (Date of birth) | Current Positions and Biographies with Registrant | Term | Number of Shares Owned |
| :---: | :---: | :---: | :---: |
|  | Executive Vice President and Director of the Company, appointed in June 1992 |  |  |
|  | Senior Managing Director of the Company, appointed in June 1990 |  |  |
|  | President and Director of Honda of America Mfg., Inc., appointed in June 1988 |  |  |
|  | Managing Director of the Company, appointed in June 1988 |  |  |
|  | General Manager of Suzuka Factory, appointed in March 1987 |  |  |
|  | Director of the Company, appointed in May 1983 |  |  |
|  | Executive Vice President and Director of Honda R\&D Co., Ltd., appointed in May 1983 |  |  |
|  | Director of Honda R\&D Co., Ltd., appointed in March 1977 |  |  |
|  | Joined Honda R\&D Co., Ltd. in April 1963 |  |  |
| Minekawa ober 27, 1954) | Director of the Company from June 2007 | *3 | 7,100 |
|  | Director of the Company, appointed in June 2007 |  |  |
|  | President and Director of Honda Automoveis do Brasil Ltda., appointed in April 2007 (presently held) |  |  |
|  | President and Director of Moto Honda da Amazonia Ltda., appointed in April 2007 (presently held) |  |  |
|  | President and Director of Honda South America Ltda., appointed in April 2007 (presently held) |  |  |
|  | Chief Operating Officer for Regional Operations (Latin America), appointed in April 2007 (presently held) |  |  |
|  | Operating Officer of the Company, appointed in June 2005 |  |  |
|  | Director of the Company, appointed in June 2004 |  |  |
|  | President of Guangzhou Honda Automobile Co., Ltd., appointed in April 2004 |  |  |
|  | Joined Honda in April 1978 |  |  |


| Name <br> (Date of birth) | Current Positions and Biographies with Registrant | Term | Number of Shares Owned |
| :---: | :---: | :---: | :---: |
| Corporate Auditors |  |  |  |
| Hiroshi Okubo <br> (October 30, 1945) | Corporate Auditor (full-time), appointed in June 2004 | *4 | 13,600 |
|  | Senior Managing Director of the Company, appointed in June 2003 |  |  |
|  | Compliance Officer, appointed in April 2003 |  |  |
|  | Managing Director of the Company, appointed in June 1999 |  |  |
|  | Chief Operating Officer for Business Support Operations and Chief Officer of Driving Safety Promotion Center in Business Support Operations, appointed in June 1999 |  |  |
|  | Director of the Company, appointed in June 1996 |  |  |
|  | General Manager of Executive Office in Business Support Operations, appointed in June 1994 |  |  |
|  | Joined Honda in April 1970 |  |  |
| Koji Miyajima (June 10, 1948) | Corporate Auditor of the Company (full-time), appointed in June 2003 | *4 | 7,000 |
|  | Corporate Auditor of the Company, appointed in June 2001 |  |  |
|  | General Manager of Overseas Operations Office No. 1 in Regional Operations (North America), appointed in April 2000 |  |  |
|  | Joined Honda in April 1971 |  |  |
| Shinichi Sakamoto <br> (August 3, 1950) | Corporate Auditor of the Company (full-time), appointed in June 2005 | *5 | 6,000 |
|  | Regional Operating Officer of the Company, appointed in April 2004 |  |  |
|  | Joined in April 1969 |  |  |
| Koukei Higuchi (March 14, 1936) | Corporate Auditor of the Company, appointed in June 2003 | *6 | None |
|  | Advisor of the Board of The Tokio Marine \& Fire Insurance Co., Ltd. (presently Tokio Marine \& Nichido Fire Insurance Co., Ltd.), appointed in June 2003 (presently held) |  |  |
|  | Chairman of The Tokio Marine \& Fire Insurance Co., Ltd. (presently Tokio Marine \& Nichido Fire Insurance Co., Ltd.), appointed in June 2001 |  |  |


*1. Mr. Satoru Kishi and Mr. Kensaku Hogen satisfy the required conditions for the outside director provided for in Article 2, Paragraph 1, Item 15 of the Company Law.
*2. Corporate Auditors Mr. Koukei Higuchi, Mr. Fumihiko Saito and Mr. Yuji Matsuda are outside corporate auditors as provided for in Article 2, Paragraph 1, Item 16 of the Company Law.
*3. The term of office of a Director is one year after his/her election to office at the close of the ordinary general meeting of shareholders on June 22, 2007.
*4. The term of a Corporate Auditor is four years after his/her election to office at the close of the ordinary general meeting of shareholders on June 23, 2004.
*5. The term of a Corporate Auditor is four years after his/her election to office at the close of the ordinary general meeting of shareholders on June 23, 2005.
*6. The term of a Corporate Auditor is four years after his/her election to office at the close of the ordinary general meeting of shareholders on June 22, 2007.
*7. The Company has introduced an operating officer system to facilitate transfer of authority to regions and local workplaces and effectively separate the supervisory and executive roles, while also making the Board of Directors more versatile. Managing Officers and Operating Officers under operating officer system are not statutory positions under the Japanese Company Law and do not conform to the definition of "Directors and Senior Management" as defined in Form 20-F. The Company's Managing Officers and Operating Officers, as voluntarily disclosed in Japan, are listed below.

## Managing Officers

| Akio Hamada | President and Director of Honda of America Mfg., Inc. |
| :--- | :--- |
| Takashi Yamamoto | General Manager of Saitama Factory of Production Operations |
| Suguru Kanazawa | Executive Vice President and Director of Honda Motor Europe Ltd. |
|  | President and Director of Honda of the U.K. Manufacturing Ltd. |

## Operating Officers

| Manabu Nishimae | Deputy Chief Operating Officer for Regional Sales Operations (Japan) |
| :---: | :---: |
|  | General Manager of Automobile Sales Operations for Regional Sales Operations (Japan) |
|  | General Manager of Aftermarket Operations in Regional Sales Operations (Japan) |
|  | General Manager of Asimo Business Office in Regional sales Operations (Japan) |
| Masaya Yamashita | General Manager of Kumamoto Factory of Production Operations |
| Hiroshi Kobayashi | President and Director of Honda Canada Inc. |
| Hiroshi Oshima | Corporate Communications, Motor Sports General Manager of Corporate Communications Division |
| Tsutomu Saka | General Manager of Hamamatsu Factory of Production Operations |
| Hidenobu Iwata | General Manager of Suzuka Factory of Production Operations |
| Gen Tsujii | Production for Production Opertions |
|  | General Manager of Automobile Production |
|  | Planning Office in Production Operations |
|  | President and Director of Honda Engineering Co., Ltd. |
| Koichi Fukuo | Quality, Certification \& Regulation Compliance |
| Hiroshi Soda | Executive Vice President and Director of Honda North America, Inc. |
|  | Executive Vice President and Director of American Honda Motor Co., Inc. |
| Takuji Yamada | President and Director of Honda Motor Europe (North) GmbH |
| Hideki Okada | General Manager of Regional Operation Planning Office in Regional Operations (North America) |
|  | Executive Vice President and Director of American Honda Motor Co., Inc. |
| Masahiro Takedagawa | President and Director of Honda Siel Cars India Ltd. |
|  | President and Director of Honda Motor India Private Ltd. |
| Yoichi Hojo | General Manager of Automobile Purchasing Division 2 in Purchasing Operations |
| Tsuneo Tanai | Executive Vice President and Director of Honda of America Mfg., Inc. |
| Yoshiyuki Matsumoto | Automobile Products for Automobile Operations |
| Eiji Okawara | Production in China in Production Operations |
|  | President of Guangzhou Honda Automobile Co., Ltd. |
| Ko Katayama | Manufacturing of Honda Canada Inc. |
| Masahiro Yoshida | Human Resources and Associate Relations for Business Support Operations |
|  | General Manager of Human Resources Division for Business Support Operations |
| Seiji Kuraishi | Vice President of Honda Motor (China) Investment Corporation, Ltd. |
| Takashi Nagai | Executive Vice President and Director of Asian Honda Motor Co., Ltd. |

There is no family relationship between any director or executive officer and any other director or executive officer.

## B. Compensation

Directors and Corporate Auditors receive monthly remuneration, the aggregate maximum monthly amount of which is approved at the annual general meeting of shareholders. Also, Directors and Corporate Auditors receive bonuses, the aggregate amount of which is approved at the annual general meeting of shareholders and is based on the Company's performance for the fiscal year. The amounts of the remuneration and bonuses approved to pay to Directors and Corporate Auditors are allocated among them at meetings of the Board of Directors and Corporate Auditors.

In accordance with customary Japanese business practice, when a Director or Corporate Auditor retires, a proposal to pay a lump sum retirement allowance is submitted at the general meeting of shareholders for approval. The amount of retirement allowance for a Director or Corporate Auditor generally reflects his or her position at the time of retirement, the length of his service as a Director or Corporate Auditor and other factors, as appropriate under Honda's internal regulations.

The total amount of remuneration paid to the Company's directors and corporate auditors during the fiscal year ended March 31, 2007 was $¥ 879$ million, including $¥ 772$ million paid to 21 directors (who include a director who retired during that fiscal year) and $¥ 106$ million paid to six corporate auditors. The amount of remuneration paid to the directors includes amount of wages paid to those directors who were also employees of the Company or directors of subsidiaries of the Company.

The total amount of bonuses that were paid during the year ended March 31, 2007 was $¥ 590$ million, including $¥ 513$ million to our 21 directors as of the end of the year ended March 31, 2006 and $¥ 77$ million to our six corporate auditors as of the end of the year ended March 31, 2006.

The amount of retirement allowances paid to three retired directors (including two managing officers who were directors in the past) was $¥ 330$ million, in accordance with a resolution of the Ordinary General Meeting of Shareholders held in June 2006.

## C. Board Practices

See Item 6.A "Director and Senior Management" for information concerning the Company's Directors and Corporate Auditors required by this item.

## Corporate Governance

Companies listed on the New York Stock Exchange (the "NYSE") must comply with certain standards regarding corporate governance under Section 303A of the NYSE Listed Company Manual.

However, listed companies that are foreign private issuers, such as Honda, are permitted to follow home country practice in lieu of certain provisions of Section 303A.

The following table shows the significant differences between the corporate governance practices followed by U.S. listed companies under Section 303A of the NYSE listed Company Manual and those followed by Honda.

## Corporate Governance Practices Followed by

 NYSE-listed U.S. CompaniesA NYSE-listed U.S. company must have a majority of directors meeting the independence requirements under Section 303A of the NYSE Listed Company Manual.

A NYSE-listed U.S. company must have an audit committee composed entirely of independent directors, and the audit committee must have at least three members.

## Corporate Governance Practices Followed by Honda

For Japanese companies, which employ a corporate governance system based on a board of corporate auditors (the "board of corporate auditors system"), including Honda, Japan's company law has no independence requirement with respect to directors. The task of overseeing management and, together with the accounting audit firm, accounting is assigned to the corporate auditors, who are separate from the company's management and meet certain independence requirements under Japan's company law.

In the case of Japanese companies which employ the board of corporate auditors system, including Honda, at least half of the corporate auditors must be "outside" corporate auditors who must meet additional independence requirements under Japan's company law. An outside corporate auditor is defined as a corporate auditor who has not served as a director, accounting councilor, executive officer, manager or any other employee of the company or any of its subsidiaries.

Currently, Honda has three outside corporate auditors which constitute $50 \%$ of Honda's corporate auditors.

Like a majority of Japanese listing companies, Honda employs the board of corporate auditors system as described above. Under this system, the board of corporate auditors is a legally separate and independent body from the board of directors. The main function of the board of corporate auditors is similar to that of independent directors, including those who are members of the audit committee, of a U.S. company: to monitor the performance of the directors, and review and express opinion on the method of auditing by the company's accounting audit firm and on such accounting audit firm's audit reports, for the protection of the company's shareholders.

Japanese companies which employ the board of corporate auditors system, including Honda, are required to have at least three corporate auditors. Currently, Honda has six corporate auditors. Each corporate auditor has a four-year term. In contrast, the term of each director of Honda is one year.

A NYSE-listed U.S. company must have a nominating/ corporate governance committee entirely of independent directors.

A NYSE-listed U.S. company must have a compensation committee composed entirely of independent directors.

A NYSE-listed U.S. company must generally obtain shareholder approval with respect to any equity compensation plan.

Corporate Governance Practices Followed by Honda
With respect to the requirements of Rule 10A-3 under the U.S. Securities Exchange Act of 1934 relating to listed company audit committees, Honda relies on an exemption under that rule which is available to foreign private issuers with boards of corporate auditors meeting certain criteria.

Honda's directors are elected at a meeting of shareholders. Its Board of Directors does not have the power to fill vacancies thereon.

Honda's corporate auditors are also elected at a meeting of shareholders. A proposal by Honda's Board of Directors to elect a corporate auditor must be approved by a resolution of its Board of Corporate Auditors. The Board of Corporate Auditors is empowered to request that Honda's directors submit a proposal for election of a corporate auditor to a meeting of shareholders. The corporate auditors have the right to state their opinion concerning election of a corporate auditor at the meeting of shareholders.

Maximum total amounts of compensation for Honda directors and corporate auditors are proposed to, and voted on, by a meeting of shareholders. Once the proposals for such maximum total amounts of compensation are approved at the meeting of shareholders, each of the Board of Directors and Board of Corporate Auditors determines the compensation amount for each member within the respective maximum total amounts.

Currently, Honda does not adopt stock option compensation plans. When Honda adopts it, Honda must obtain shareholder approval for stock options only if the stock options are issued with specifically favorable conditions or price concerning the issuance and exercise of the stock options.

## D. Employees

The following tables list the number of Honda full-time employees as of March 31, 2007, 2006 and 2005.

As of March 31, 2007

| Total | Motorcycle Business | Automobile Business | Financial Services | Power Product And Other Businesses |
| :---: | :---: | :---: | :---: | :---: |
| 167,231 | 33,137 | 121,691 | 1,988 | 10,415 |

At March 31, 2007, Honda had 167,231 full-time employees, including 98,493 local nationals employed in its overseas operations.

## As of March 31, 2006

| Total | Motorcycle Business | Automobile Business | Financial Services | Power Product And Other Businesses |
| :---: | :---: | :---: | :---: | :---: |
| 144,785 | 28,783 | 105,623 | 1,921 | 8,458 |

At March 31, 2006, Honda had 144,785 full-time employees, including 83,088 local nationals employed in its overseas operations.

## As of March 31, 2005

| Total | Motorcycle Business | Automobile Business | Financial Services | Power Product And Other Businesses |
| :---: | :---: | :---: | :---: | :---: |
| 137,827 | 27,991 | 99,525 | 1,787 | 8,524 |

At March 31, 2005, Honda had 137,827 full-time employees, including 76,763 local nationals employed in its overseas operations.

Most of the Company's regular employees in Japan, except management personnel, are required by the terms of the Company's collective bargaining agreement with its labor union to become members of the Federation of All Honda Workers' Union (AHWU), which is affiliated with the Japan Council of the International Metal Workers Federation. Approximately $85 \%$ of the employees of the Company and its Japanese subsidiaries were members of AHWU at March 31, 2007.

In Japan, basic wages are negotiated annually and the average increases in wages of the Company's employees in fiscal 2005, 2006 and 2007 were $2.0 \%, 2.0 \%$ and $2.0 \%$, respectively. In addition, in accordance with Japanese custom, each employee is paid a semi-annual bonus. Bonuses are negotiated during wage negotiations and are based on the overall performance of the Company or the applicable subsidiary in the previous year, the outlook for the current year and other factors.

The Company has had labor contracts with its labor union in Japan since 1970. These contracts are renegotiated with respect to basic wages and other working conditions. The regular employees of the Company's domestic subsidiaries are covered by similar contracts. Since 1957, neither the Company nor any of its subsidiaries has experienced any strikes or other labor disputes that materially affected its business activities. The Company considers labor relations with its employees to be very good.

## E. Share ownership

The total amount of the Company's voting securities owned by its officers, directors and corporate auditors as a group as of June 22, 2007 is as follows.

| $\frac{\text { Title of Class }}{\text { Common Stock }}$ | $\frac{\text { Amount Owned }}{242,236 \text { shares }}$ | $\frac{\text { \% of Class }}{0.013 \%}$ |
| :--- | :--- | :--- |

The Company's full-time employees are eligible to participate in the Honda Employee Shareholders' Association, whereby participating employees contribute a portion of their salaries to the Association and the Association purchases shares of the Company's Common Stock on their behalf. As of March 31, 2007, the Association owned 4,595,083 shares of the Company's common stock.

## Item 7. Major shareholders and Related Party Transactions

## A. Major Shareholders

As of March 31, 2007, 1,834,828,430 shares of Honda's Common Stock were issued and 1,821,992,908 shares were outstanding.

According to a report filed under the Securities and Exchange Law of Japan by Mitsubishi UFJ Financial Group, Inc., as of April 9, 2007, Mitsubishi UFJ Financial Group, Inc. directly and indirectly held 133,010,880 shares of Honda's common stock, or $7.30 \%$ of the total number of shares of Honda's outstanding stock. Mitsubishi UFJ Financial Group, Inc. does not have any voting rights that are different from those of our other shareholders.

ADS representing American Depositary Shares are issued by JPMorgan Chase Bank, N.A., as Depositary. The normal trading unit is 100 American Depositary Shares. Total issued shares of Honda as of the close of business on March 31, 2007 were 1,834,828,430 shares of Common Stock, of which 120,199,186 shares represented by ADS and 195,330,697 shares not represented by ADS were owned by residents of the United States. The number of holders of record of the Company's shares of Common Stock in the United States was 229 at March 31, 2007.

To the knowledge of Honda, it is not directly or indirectly owned or controlled by any other corporation, by any government, or by any other natural or legal person or persons severally or jointly. As far as is known to the Company, there are no arrangements, the operation of which may at a subsequent date, result in a change in control of the Company.

## B. Related Party Transactions

Honda purchases materials, supplies and services from numerous suppliers throughout the world in the ordinary course of business, including firms with which Honda is affiliated.

During the fiscal year ended March 31, 2007, Honda had sales of $¥ 329.3$ billion and purchases of $¥ 1,083.6$ billion with equity affiliates accounted under the equity method. As of March 31, 2007, Honda had receivables of $¥ 77.3$ billion from affiliated companies, and had payables of $¥ 155.6$ billion to affiliated companies.

Honda does not consider the amounts involved in such transactions to be material to its business.

## C. Interest of Experts and Counsel

Not applicable.

## Item 8. Financial Information

## A. Consolidated Statements and Other Financial Information

1 - 3. Consolidated Financial Statements
Honda's audited consolidated financial statements are included under "Item 18-Financial Statements". Except for Honda's consolidated financial statements included under Item 18, no other information in this Annual Report has been audited by independent auditors.
4. Not applicable.
5. Not applicable.

## 6. Export Sales.

See "Information on the Company - Marketing and Distribution - Overseas Sales".

## 7. Legal Proceedings.

Various legal proceedings are pending against us. We believe that such proceedings constitute ordinary routine litigation incidental to our business. With respect to product liability, personal injury claims or lawsuits, we believe that any judgment that may be recovered by any plaintiff for general and special damages and court costs will be adequately covered by our insurance and reserves. Punitive damages are claimed in certain of these lawsuits. We are also subject to potential liability by other various lawsuits and claims.

75 purported class actions on behalf of all purchasers of new motor vehicles in the United States since January 1, 2001, have been filed in various state and federal courts against American Honda Motor Co., Inc., Honda Canada, Inc., General Motors, Ford, Daimler Chrysler, Toyota, Nissan, and Volkswagen and their Canadian affiliates, the National Automobile Dealers Association and the Canadian Automobile Dealers Association. Several of the state court actions also name Honda Motor Co., Ltd. as a defendant, as well as other Japanese and German parent companies of United States based subsidiaries. The federal court actions have been consolidated for coordinated pretrial proceedings in federal court in Maine and 37 California cases have been consolidated in the state court in San Francisco. Additionally, there are pending cases in seven other states.

The nearly identical complaints allege that the manufacturer defendants, aided by the association defendants, conspired among themselves and with their dealers to prevent United States citizens from purchasing vehicles produced for the Canadian market and sold by dealers in Canada. The complaints allege that new vehicle prices in Canada are 10 to $30 \%$ lower than those in the United States and that preventing the sale of these vehicles to United States citizens resulted in the payment of supracompetitive prices by United States consumers. The complaints seek treble damages under the antitrust laws, but do not specify damages. The federal court has certified a class for injunctive relief and damages. We believe our actions have been lawful and are vigorously defending these cases.

In accordance with Statement of Financial Accounting Standards (SFAS) No. 5, "Accounting for Contingencies", Honda has recorded a contingent liability when it is probable that an obligation has been incurred and the amount of loss can be reasonably estimated. After consultation with legal counsel, and taking into account all known factors pertaining to existing lawsuits and claims, we believe that the overall results of all lawsuits and pending claims should not result in liability to us that would be likely to have an adverse material effect on our consolidated financial position and results of operations.

## 8. Profit Redistribution Policy

The Company strives to carry out its operations from a global perspective and to increase its corporate value. With respect to the redistribution of profits to our shareholders, which we consider to be one of the most
important management issues, and its basic policy for dividends is to make distributions after taking into account its long-term consolidated earnings performance.

The Company may determine dividends from surplus by a resolution of the Board of Directors based on Article 459 of the Company Law as provided by the article of Incorporation. Also, please note that the year-end cash dividends for the year ended March 31, of each year are matters to be resolved at general meeting of shareholders.

The Company will also acquire its own shares at the optimal timing with the goal of improving efficiency of the Company's capital structure. The present goal is to maintain a shareholders return ratio (i.e. the ratio of the total of the dividend payment and the repurchase of the Company's own shares to consolidated net income) of approximately $30 \%$. Retained earnings will be allocated toward financing R\&D activities that are essential for the future growth of the Company and capital expenditures and investment programs that will expand its operations for the purpose of improving business results and strengthening the Company's financial condition.

The Company distributed year-end cash dividends of $¥ 20$ per share for the year ended March 31, 2007. As a result, total cash dividends for the year ended March 31, 2007, together with the interim cash dividends of $¥ 30$ and the third quarter cash dividends of $¥ 17$, were $¥ 67$ per share.

The Company executed a two-for-one stock split for the Company's common stock effective July 1, 2006. Had the stock split not been carried out, annual dividends would have corresponded to $¥ 134$, an increase of $¥ 34$ per share from the annual dividends paid for the year ended March 31, 2006.

The Company plans to distribute quarterly cash dividends of $¥ 20$ per share for each quarter for the year ending March 31, 2008. As a result, total cash dividends for the year ending March 31, 2008 are planned to be $¥ 80$ per share, an increase of $¥ 13$ from the annual dividends paid for the year ended March 31, 2007.

Details of Distribution of Surplus ( Record dates of the fiscal year ended March 31, 2007 )

|  | Resolution of the Board of Directors | Resolution of the Board of Directors | Resolution at General Meeting of Shareholders |
| :---: | :---: | :---: | :---: |
|  | October 25, 2006 | January 31, 2007 | June 22, 2007 |
| Dividend per Share of Common Stock (yen) | 30.00 | 17.00 | 20.00 |
| Total Amount of Dividends Yen(millions) | 54,710 | 30,987 | 36,456 |

## B. Significant Changes

Except otherwise disclosed in this Annual Report on Form 20-F, no significant change has occurred since the date of the annual financial statements.

## Item 9. The Offer and Listing

## A. The Offer and Listing

Honda's shares have been listed on the Tokyo Stock Exchange (TSE) since 1957 and as of March 31, 2007, Honda's shares were traded over five stock exchanges in Japan.

Since February 11, 1977, American Depositary Shares (each representing one share of Common Stock and evidenced by American Depositary Receipts (ADRs)) have been listed and traded on the New York Stock Exchange (the NYSE), having been traded on the over-the-counter markets in the United States since 1962. In addition, European Shares (each representing ten shares of Common Stock and evidenced by European Depositary Receipts (EDRs)) have been traded in bearer form on the over-the-counter markets in several European countries since 1963. In June 1981, the shares of Common Stock were admitted to the official list of The Stock Exchange of London. In May 1983, the Company listed its shares on the stock exchanges in Zurich, Geneva and Basel in the form of Swiss Bearer Depositary Receipts. In June 1985, the shares of Common Stock were admitted to trading on the Paris Stock Exchange. As for the stock exchanges in Switzerland, the floor
exchanges in Zurich, Basel and Geneva were consolidated to form a single national bourse-the Swiss Exchange, in 1995. The Paris Stock Exchange was merged with the exchanges in Amsterdam and Brussels and created Euronext in September 2000. The Company, in June 2007, applied for delisting from Euronext Paris and SWX Swiss Exchange and for terminating European Depositary Receipts.

The monthly average turnover of Honda's shares of Common Stock and American Depositary Shares for the fiscal year ended March 31, 2007 was approximately 138,976,000 shares of Common Stock on the TSE and approximately 8,057,500 American Depositary Shares on the NYSE.

The following table sets out, for the periods indicated, the reported high and low sales prices of Honda's shares on the TSE in yen and its American Depositary Shares on the NYSE in the U.S. dollars.

| Fiscal year | Yen per share of Common Stock on the TSE* |  | U.S. dollars per American Depositary Share on the NYSE |  |
| :---: | :---: | :---: | :---: | :---: |
|  | High | Low | High | Low |
| 2003 | 2,995 | 1,920 | 23.85 | 16.40 |
| 2004 | 2,755 | 1,785 | 23.59 | 15.47 |
| 2005 | 2,850 | 2,185 | 27.30 | 19.25 |
| 2006 |  |  |  |  |
| 1st quarter | $¥ 2,835$ | $¥ 2,510$ | \$26.00 | \$23.75 |
| 2nd quarter | 3,310 | 2,690 | 29.08 | 24.06 |
| 3 rd quarter | 3,570 | 3,070 | 29.70 | 26.50 |
| 4th quarter | 3,750 | 3,050 | 31.74 | 27.10 |
| 2007 |  |  |  |  |
| 1st quarter | $¥ 4,285$ | $¥ 3,270$ | \$37.95 | \$29.13 |
| 2nd quarter | 4,030 | 3,410 | 35.00 | 29.43 |
| 3 rd quarter | 4,740 | 3,910 | 39.87 | 33.49 |
| 4th quarter | 4,940 | 4,050 | 40.82 | 34.64 |
| Jan - 2007 | $¥ 4,920$ | $¥ 4,490$ | \$40.70 | \$37.62 |
| Feb | 4,940 | 4,330 | 40.82 | 36.37 |
| Mar | 4,420 | 4,050 | 37.36 | 34.64 |
| Apr | 4,270 | 3,950 | 36.19 | 33.62 |
| May | 4,280 | 4,010 | 35.39 | 33.30 |
| June | 4,520 | 4,150 | 36.59 | 34.15 |

* The reported high and low sales prices of Honda's shares on the TSE in yen from 2003 to 2006 have been adjusted based on the shares after stock split.


## B. Plan of distribution

Not applicable.

## C. Markets

See Item 9.A, "Offer and Listing Details"

## D. Selling Shareholders

Not applicable.

## E. Dilution

Not applicable.

## F. Expenses of The Issue

Not applicable.

## Item 10. Additional Information

## A. Share Capital

Not applicable

## B. Memorandums and Article of Association

Set forth below is information relating to Honda's common stock, including brief summaries of the relevant provisions of Honda's articles of incorporation and share handling regulations as currently in effect, and of the Company Law of Japan, which has become effective as of May 1, 2006, and related legislation.

## General

Honda's authorized share capital as of the date of the filing of this Form 20-F is 7,086,000,000 shares of common stock, of which $1,834,828,430$ shares were issued. Effective as of July 1, 2006, Honda implemented a two for one stock split. Under the Company Law, shares must be registered and are transferable by delivery of share certificates. In order to assert shareholders' rights against Honda, a shareholder must have its name and address registered on Honda's register of shareholders, in accordance with Honda's share handling regulations. The registered beneficial holder of shares underlying the ADSs is the depositary for the ADSs. Accordingly, holders of ADSs will not be able directly to assert shareholders' rights.

A holder of shares may choose, at its discretion, to participate in the central clearing system for share certificates under the Law Concerning Central Clearing of Share Certificates and Other Securities of Japan. Participating shareholders must deposit certificates representing all of the shares to be included in this clearing system with the Japan Securities Depository Center, Inc. (the "Securities Center"). If a holder of shares is not a participating institution in the Securities Center, it must participate through a participating institution, such as a securities company or a bank having a clearing account with the Securities Center. All shares deposited with the Securities Center will be registered in the name of the Securities Center on Honda's register of shareholders. Each participating shareholder will in turn be registered on Honda's register of beneficial shareholders and be treated in the same way as shareholders registered on Honda's register of shareholders. For the purpose of transferring deposited shares, delivery of share certificates is not required. Entry of the share transfer in the books maintained by the Securities Center for participating institutions, or in the book maintained by a participating institution for its customers, has the same effect as delivery of share certificates. The registered beneficial owners may exercise the rights attached to the deposited shares, such as voting rights, and will receive dividends (if any) and notices to shareholders directly from Honda. The shares held by a person as a registered shareholder and those held by the same person as a registered beneficial owner are aggregated for these purposes. Beneficial owners may at any time withdraw and receive their share certificates from the Securities Center.

A law to establish a new central book entry clearing system for shares of listed companies and to eliminate the issuance and use of certificates for such shares was promulgated in June 2004 and the part of such law that is relevant to the shares of Honda will come into effect on a date within five years of the date of the promulgation which will be determined by a Cabinet Order. On the effective date, a new book entry central clearing system will be established and will become responsible for handling the shares of all Japanese companies listed on any Japanese stock exchange, including the shares of Honda. On the same day, all existing share certificates will become null and void. The transfer of shares will be effected by book-entry in the accounts maintained under the new central clearing system.

## Objects and Purposes

Article 2 of the articles of incorporation of Honda states that its purpose is to engage in the following businesses:

- Manufacture, sale, lease and repair of motor vehicles, ships and vessels, aircrafts and other transportation machinery and equipment.
- Manufacture, sale, lease and repair of prime movers, agricultural machinery and appliances, generators, processing machinery and other general machinery and apparatus, electric machinery and apparatus and precision machinery and apparatus.
- Manufacture and sale of fiber products, paper products, leather products, lumber products, rubber products, chemical industry products, ceramic products, metal products and other products.
- Overland transportation business, marine transportation business, air transportation business, warehousing business, travel business and other transport business and communication business.
- Sale of sporting goods, articles of clothing, stationary, daily sundries, pharmaceuticals, drink and foodstuffs and other goods.
- Financial business, nonlife insurance agency business, life insurance agency business, construction business including building construction work and real estate business including real estate brokerage.
- Publishing business, advertising business, translation business, interpretation business, management consultancy business, information services including information processing, information and communication and information provision, industrial planning and design, comprehensive security business and labor dispatch services.
- Management of parking garages, driving schools, training and education facilities, racecourses, recreation grounds, sporting facilities, marina facilities, hotels, restaurants and other facilities.
- Manufacture, sale and licensing of equipment, parts and supplies and all other relevant business activities and investments relating to each of the foregoing items.


## Dividends

Under its articles of incorporation, Honda's financial accounts will be closed on March 31 of each year. The record date for dividends is June 30, September 30, December 31 and March 31 of each year. In addition, the Company may distribute dividends from surplus by determining any record date.

Under the Company Law, a company is permitted to make distributions of surplus to the shareholders any number of times per fiscal year pursuant to resolutions of a general meeting of shareholders, subject to certain limitations provided by the Law and the Ordinances of the Ministry of Justice thereunder. Distributions of surplus are required, in principle, to be authorized by a resolution of a general meeting of shareholders. However, if the articles of incorporation so provide and certain other requirements under the Company Law are met, distributions of surplus may be made pursuant to a board resolution. Pursuant to the provisions of the Company Law and its articles of incorporation, the board of directors of Honda may determine distributions of its surplus.

Distributions of surplus may be made in cash or in-kind in proportion to the number of shares held by each shareholder. If a distribution of surplus is to be made in-kind, a special resolution of a general meeting of shareholders is required, except in the case that a right to receive cash distribution instead of distribution in-kind is granted to shareholders. If such right is granted, distributions in-kind may be made pursuant to an ordinary resolution of a general meeting of shareholders or, as the case may be, a board resolution.

Under the Company Law, Honda is permitted to prepare non-consolidated extraordinary financial statements consisting of a balance sheet as of any date subsequent to the end of the previous fiscal year and an
income statement for the period from the first day of the current fiscal year to the date of such balance sheet. If such extraordinary financial statements are prepared and approved in accordance with the provisions of the Company Law and the Ordinances of the Ministry of Justice thereunder, the results of such extraordinary financial statements may be considered in the calculation of distributable amount.

Under its articles of incorporation, Honda is not obligated to pay any dividends which are left unclaimed for a period of three full years after the date on which they first became payable.

## Capital and Reserves

The entire amount of the issue price of the shares to be issued in the future will generally be required to be accounted for as stated capital. However, Honda may account for an amount not exceeding one-half of such issue price as additional paid-in capital by resolution of the board of directors in accordance with the Company Law. Honda may at any time reduce the whole or any part of its additional paid-in capital or transfer them to stated capital by resolution of a general meeting of shareholders. The whole or any part of surplus may also be transferred to stated capital, additional paid-in capital or legal reserve by resolution of a general meeting of shareholders.

## Stock Splits

Honda may at any time split its shares into greater number of shares by resolution of the board of directors. When the board of directors approves a stock split, it may also amend the articles of incorporation of Honda without approval of shareholders to increase the number of its authorized shares in proportion to the stock split, so long as Honda does not issue more than one class of shares.

Upon stock splits, shareholders will not be required to exchange share certificates held by them for new share certificates. In respect of deposited shares, new shares resulting from the stock split will be deposited with the Securities Center, and shareholders who directly possess share certificates will receive additional certificates representing the additional shares resulting from the stock split.

## Consolidation of Shares

Honda may at any time consolidate the shares into a smaller number of shares by a special resolution of the general meeting of shareholders. A representative director of Honda must disclose the reason for the consolidation of the shares at the general meeting of shareholders.

## Japanese Unit Share System

Consistent with the requirements of the Company Law, the articles of incorporation of Honda adopts unit share system called as "tan-gen-kabu", under which 100 shares constitute one voting unit of shares. The board of directors of Honda by itself may reduce, but not to increase, the number of shares that constitute a voting unit or abolish the unit share system entirely by a board resolution. An increase in the number of shares that constitute one voting unit requires a resolution of a general shareholders' meeting. In any case, the number of shares constituting one voting unit may not exceed 1,000 shares.

The articles of incorporation of Honda provide that Honda may not issue share certificates for a number of shares not constituting an integral number of voting units. Because the transfer of shares normally requires delivery of the share certificates for the shares being transferred, shares constituting a fraction of a voting unit and for which no share certificates are issued may not be transferable, however, the holder of shares constituting less than one voting unit may at any time require Honda to purchase or sell such shares to constitute a voting unit at the market price in accordance with the Company's share handling regulations (see below). Because the transfer of ADRs does not require changes in the ownership of the underlying shares, holders of ADRs evidencing ADSs that constitute less than one voting unit of shares are not affected by these restrictions in their
ability to transfer the ADRs. However, because transfers of less than one voting unit of the underlying shares are normally prohibited under the unit share system, under the deposit agreement, the right of ADR holders to surrender their ADRs and withdraw the underlying shares for sale in Japan may only be exercised as to whole voting units.

## Right of a Holder of Shares Representing Less Than One Voting Unit to Require Honda to Purchase or Sell Its Shares

A holder of shares representing less than one voting unit may at any time require Honda to purchase its shares. These shares will be purchased at (a) the closing price of the shares reported by the Tokyo Stock Exchange on the day when the request for purchase reaches the share handling agent, or (b) if no sale takes place on the Tokyo Stock Exchange on that day, then the price at which the first sale of shares is effected on the Tokyo Stock Exchange thereafter. In each case, Honda will request the payment of an amount determined by Honda as an amount equal to the brokerage commission required for the sale and purchase of the shares. A holder of shares representing less than one voting unit may, in accordance with the provisions of the share handling regulations, also make a request to the effect that such number of shares should be sold to it that will, when added to the shares less than one voting unit already held by that shareholder, constitute one voting unit. However, because holders of ADSs representing less than one unit are not able to withdraw the underlying shares from deposit, these holders will not be able to exercise many shareholder rights as a practical matter.

## Other Rights of a Holder of Shares Representing Less Than One Voting Unit

A holder of shares representing less than one voting unit has the following rights and these rights may not be restricted by the articles of incorporation:

- rights to receive any consideration for acquisition by a corporation of special shares all of which may be acquired by such corporation (zembu shutoku joukou tsuki shurui kabushiki) as provided by Article 171, paragraph 1, item 1 of the Company Law,
- rights to receive any cash or other consideration for acquisition by a corporation of shares which may be acquired by such corporation on occurrence of certain event (shutoku joukou tsuki shurui kabushiki) as provided by Article 107, paragraph 1, item 3 of the Company Law,
- rights to be allocated any shares without consideration as provided by Article 185 of the Company Law,
- rights to receive distribution of any residual assets of a corporation, and
- any other rights provided in the relevant Ordinance of the Ministry of Justice, including rights to receive cash an other distribution derived from consolidation of shares, stock split, allocation of stock acquisition rights without consideration, distribution of surplus or reorganization of a corporation.

Other rights of a holder of shares constituting less than one voting unit may be restricted if the articles of incorporation so provide.

## Voting rights under the unit share system

Under the unit share system, the shareholders shall have one voting right for each voting unit of shares that they hold. A shareholder who owns shares representing less than one voting unit will not be able to exercise voting rights and any other rights relating thereto, including the right to examine Honda's accounting books and records.

## Voting Rights

Honda holds its ordinary general meeting of shareholders in June of each year. In addition, Honda may hold an extraordinary general meeting of shareholders whenever necessary by giving at least two weeks' advance
notice. Under the Company Law, notice of any shareholders' meeting must be given to each shareholder having voting rights or, in the case of a non-resident shareholder, to his resident proxy or mailing address in Japan in accordance with Honda's share holding regulations, at least two weeks prior to the date of the meeting.

A shareholder is generally entitled to one vote per voting unit of shares as described in this paragraph and under "Japanese Unit Share System" above. In general, under the Company Law and the articles of incorporation of Honda, a resolution may be adopted at a meeting of shareholders by a majority of the shares having voting rights represented at the meeting. The Company Law and Honda's articles of incorporation require a quorum for the election of directors and corporate auditors of not less than one-third of the total number of voting rights of all shareholders and the resolution shall be adopted by majority voting. Honda's shareholders are not entitled to cumulative voting in the election of directors. A corporate shareholder whose voting rights are in turn more than one-quarter directly or indirectly owned by Honda does not have voting rights.

Shareholders may exercise their voting rights through proxies, provided that those proxies are also shareholders who have voting rights. Shareholders who intend to be absent from a general meeting of shareholders may exercise their voting rights in writing. In addition, they may exercise their voting rights by electronic means if the board of directors decides to accept such means.

Under the Company Law, in order to approve certain significant matters of a corporation, more strict requirement for the quorum or the number of voting rights to approve is provided. The articles of incorporation of Honda provide that such resolution may be adopted at a meeting of shareholders by two thirds of the voting rights of the shareholders representing at least one third of all the shareholders having voting rights. Such significant matters include, but not limited to:

- the determination of the matters relating to acquisition of its own shares from a specific shareholder,
- the determination as to acquisition of special shares all of which may be acquired by a corporation (zembu shutoku joukou tsuki shurui kabushiki),
- the determination of consolidation of the shares,
- the determination of discharge of a part of responsibilities of directors, corporate auditors or accounting auditors,
- the determination of the matters concerning distribution of surplus by property other than cash (only in the case that no cash distribution is allowed to shareholders),
- the determination of the matters concerning amendments to the articles of incorporation, transfer of business or dissolution of a corporation,
- the determination of the matters concerning reorganization of a corporation.

Pursuant to the terms of the Deposit Agreement, upon receipt of notice of any meeting of holders of Common Shares of the Registrant, the Depositary will mail to the record holders of ADRs and publish a notice which will contain the information in the notice of the meeting. The record holders of ADRs at the close of business on a date specified by the Depositary will be entitled to instruct the Depositary as to the exercise of the voting rights pertaining to the amount of Common Stock of the Registrant represented by their respective Depositary Receipts. The Depositary will endeavor, in so far as practicable, to vote the amount of Common Stock of the Registrant represented by such Depositary Receipts in accordance with such instructions, and the Registrant has agreed to take all action which may at any time be deemed necessary by the Depositary in order to enable the Depositary to so vote such Common Stock. In the absence of such instructions, the Depositary has agreed to use its best efforts to give a discretionary proxy to a person designated by the Registrant. However, such proxy may not be given with respect to any proposition of which the Depositary has knowledge regarding any contest related to the action to be taken at the meeting, or the purpose of which is to authorize a merger, consolidation or any other matter which may substantially affect the rights or privileges of the Common Stock of the Registrant or other securities, property or cash received by the Depositary or the Custodian in respect thereof.

## Subscription Rights and Stock Acquisition Rights

Holders of shares have no preemptive rights under Honda's articles of incorporation. Under the Company Law, the board of directors may, however, determine that shareholders be given subscription rights in connection with a particular issue of new shares. In this case, such rights must be given to all shareholders as of a specified record date by at least two weeks' prior public notice to shareholders of the record date. In addition, individual notice must be given to each of these shareholders at least two weeks prior to the date of expiration of the subscription rights.

Honda also may decide to grant the stock acquisition rights (shinkabu-yoyakuken), with or without bonds, to any person including shareholders, by resolution of its board of directors unless issued under specially favorable conditions. The holder of such rights may exercise its rights within the exercise period by paying subscription moneys all as prescribed in the terms of such rights.

## Liquidation Rights

In the event of a liquidation of Honda, the assets remaining after payment of all debts, liquidation expenses and taxes will be distributed among the shareholders in proportion to the number of shares they own.

## Liability to Further Calls or Assessments

All of Honda's currently issued shares, including shares represented by the ADSs, are fully paid and nonassessable.

## Shareholders' Register Manager

The Chuo Mitsui Trust and Banking Company, Limited is the Shareholders' Register Manager for the shares. Chuo Mitsui's office is located at 33-1, Shiba 3-chome, Minato-ku, Tokyo, 105-8574, Japan. Chuo Mitsui maintains Honda's register of shareholders and records transfers of record ownership upon presentation of share certificates.

## Record Date

As mentioned above, the record date for Honda's dividends is June 30, September 30, December 31 and March 31, if paid. A holder of shares constituting one or more whole voting units who is registered as a holder on Honda's register of shareholders at the close of business as of March 31 is entitled to exercise shareholders' voting rights at the ordinary general meeting of shareholders with respect to the fiscal year ended on March 31. In addition, Honda may set a record date for determining the shareholders entitled to other rights and for other purposes by giving at least two weeks' prior public notice.

The shares generally trade ex-dividend or ex-rights on the Japanese stock exchanges on the third business day before a record date (or if the record date is not a business day, the fourth business day prior thereto), for the purpose of dividends or rights offerings.

## Acquisition by Honda of Shares

Under the Company Law, Honda is generally required to obtain authorization for any acquisition of its own shares by means of:
(i) a resolution at a general meeting of shareholders, which is effective for one year from the date thereof;
(ii) a resolution of the board of directors if the acquisition is in accordance with its articles of incorporation; or
(iii) a resolution of the board of directors if the acquisition is to purchase its shares from a subsidiary.

Honda may only dispose of shares so acquired in accordance with the procedures applicable to a new share issuance under the Company Law.

Upon due authorization, Honda may acquire its own shares:

- in the case of (i) and (ii) above, from stock markets or by way of tender offer;
- in the case of (i) above, from a specific person, but only if its shareholders approve such acquisition by special resolution; and
- in the case of (iii) above, from such subsidiary.

In the event Honda is to acquire its own shares from a specific person other than its subsidiary at a price which is higher than the higher of (i) the final market price on the market trading such shares as of the date of such request or (ii) in the event that such shares are subject to a tender offer, etc., the price set in the contract regarding such tender offer, any shareholder may request that Honda includes such shareholder's shares in the proposed purchase.

Acquisitions described in (i) through (iii) above must satisfy certain other requirements, including the restriction of the source of consideration in which the total amount of the purchase price of such own shares may not exceed the distributable amount of the corporation.

## Reports to Shareholders

Honda currently furnishes shareholders with notices of shareholders' meetings, business reports, including financial statements, and notices of resolutions adopted at the shareholders' meetings, all of which are in Japanese. Such notices as described above may be furnished by electronic means to those shareholders who have approved such way of furnishing notices. Pursuant to its articles of incorporation, Honda must publish notices to shareholders in Japanese in the Nihon Keizai Shimbun, a Japanese newspaper of general circulation.

## Report of Substantial Shareholdings

The Securities and Exchange Law of Japan and regulations under the Law require any person who has become a holder (together with its related persons) of more than $5 \%$ of the total issued shares of a corporation listed on any Japanese stock exchange or whose shares are traded on the over-the-counter market (including ADSs representing such shares) to file with the Director of a competent Local Finance Bureau, within five business days, in general, a report concerning those shareholdings. A similar report must also be filed to reflect any change of $1 \%$ or more in any shareholding or any change in material matters set out in reports previously filed. Copies of any report must also be furnished to the corporation and to all Japanese stock exchanges on which the corporation's shares are listed or in the case of shares traded on the over-the-counter market, the Japan Securities Dealers Association. For this purpose, shares issuable or transferable to such person upon exercise of exchangeable securities, conversion of convertible securities or exercise of warrants or stock acquisition rights are taken into account in determining both the number of shares held by that holder and the corporation's total issued share capital.

## Daily Price Limits under Japanese Stock Exchange Rules

Share prices on Japanese stock exchanges are determined on a real-time basis by the equilibrium between bids and offers. These exchanges set daily price limits, which limit the maximum range of fluctuation within a single trading day. Daily price limits are set in absolute yen according to the previous day's closing price or special quote. Although transactions may continue at the upward or downward limit price if the limit price is reached on a particular trading day, no transactions may take place outside these limits. Consequently, an investor wishing to sell at a price above or below the relevant daily limit may not be able to sell his shares at such price on a particular trading day, or at all.

## C. Material Contracts

All contracts concluded by Honda during the two years preceding this filing were entered into in the ordinary course of business.

## D. Exchange Controls

There are no laws, decrees, regulations or other legislation which materially affect our ability to import or export capital for our use or our ability to pay dividends to nonresident holders of our shares.

## E. Taxation

## Japanese Taxes

The following is a summary of the principal Japanese tax consequences to owners of our shares or ADSs who are non-resident individuals or non-Japanese corporations without a permanent establishment in Japan to which income from our shares is attributable. The tax treatment is subject to possible changes in the applicable Japanese laws or double taxation conventions occurring after that date. This summary is not exhaustive of all possible tax considerations that may apply to a particular investor. Potential investors should consult their own tax advisers as to:

- the overall tax consequences of the acquisition, ownership and disposition of shares or ADSs, including specifically the tax consequences under Japanese law;
- the laws of the jurisdiction of which they are resident; and
- any tax treaty between Japan and their country of residence.

Generally, a non-resident of Japan or a non-Japanese corporation is subject to Japanese withholding tax on dividends paid by Japanese corporations.

In the absence of any applicable tax convention or agreement reducing the maximum rate of withholding tax, the rate of Japanese withholding tax applicable to dividends paid by Japanese corporations to a non-resident or a non-Japanese corporation is $20 \%$. With respect to dividends paid on listed shares issued by Japanese corporations (such as our shares) to any corporate or individual shareholder (including non-resident shareholders), the aforementioned $20 \%$ withholding tax rate is reduced to (i) $7 \%$ for dividends to be paid between January 1, 2004 and March 31, 2009, and (ii) $15 \%$ for dividends to be paid thereafter, except for dividends paid to any individual shareholder who holds $5 \%$ or more of the issued shares of us. Japan has entered into income tax treaties, conventions or agreements, whereby the maximum withholding tax rate is generally set at $15 \%$ for portfolio investors with, among others, Australia, Belgium, Canada, Denmark, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, New Zealand, Norway, Singapore, Spain, Sweden, Switzerland, the United Kingdom and, prior to July 1, 2004, the United States. In the case of the Japan-U.S. tax treaty, as a result of its recent amendment, the maximum withholding tax rate was reduced to $10 \%$ for portfolio investors with effect from July 1, 2004. Under Japanese tax law, the maximum rate applicable under the tax treaties, conventions or agreements shall be applicable except when such maximum rate is more than the Japanese statutory rate.

With effect from July 1, 2004, a new "Convention Between the United States of America and Japan for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income" (the "New Treaty") entered into force and replaced an old treaty. Under the New Treaty, a portfolio investor that is a U.S. holder is generally subject to Japanese withholding tax on dividends on our shares or ADSs at a rate of $10 \%$.

To obtain the benefits of the reduced withholding rate on dividends under the New Treaty, a U.S. holder must file an application for reduced withholding with the Japanese tax authorities at least one day before the date of the dividend distribution. A U.S. holder of our ADSs must file, through the depositary, one application for exemption from withholding tax for eight months for the purpose of investigating tax status of the holder one day before the dividend payment and a second one for reduced withholding in accordance with the New Treaty within eight months after the end of our fiscal year in which the annual dividend is paid or, in the case of interim dividend, within eight months after the record date for such interim dividend. For this purpose, a U.S. holder must file proof of its taxpayer status, its residence and its beneficial ownership of the shares or ADSs. The
depositary may require the U.S. holder also to provide other information in accordance with the Japanese tax laws and regulations. A U.S. holder that does not submit an application for reduced withholding before a dividend is paid can file a claim for refund of the Japanese tax withheld in excess of the reduced tax under the New Treaty with the Japanese tax authorities.

Gains derived from the sale outside Japan of common stock or Depositary Receipts by a non-resident of Japan or a non-Japanese corporation, or from the sale of common stock within Japan by a non-resident of Japan or by a non-Japanese corporation not having a permanent establishment in Japan, are in general not subject to Japanese income or corporation taxes. Japanese inheritance and gift taxes at progressive rates may be payable by an individual who has acquired common stock or Depositary Receipt as a legatee, heir or donee, even if the individual is not a Japanese resident.

## United States Taxes

This section describes the material U.S. federal income tax consequences of the ownership of shares or ADSs by U.S. holders, as defined below. It applies only to persons who hold shares or ADSs as capital assets for tax purposes.

This section is based on the Internal Revenue Code of 1986, as amended (the "Code"), its legislative history, existing and proposed regulations, published rulings and court decisions, all as currently in effect, as well as on the Old Treaty and the New Treaty. These laws are subject to change, possibly on a retroactive basis. In addition, this section is based in part upon the representations of the Depositary and the assumption that each obligation in the Deposit Agreement and any related agreement will be performed in accordance with its terms.

For purposes of the New Treaty and the Code, U.S. holders of ADRs evidencing ADSs will be treated as the owners of the Shares represented by those ADRs. Exchanges of shares for ADRs and ADRs for shares, generally will not be subject to U.S. federal income tax. For purposes of this discussion, a "U.S. holder" is a beneficial owner of shares or ADSs that is for United States federal income tax purposes, (i) a citizen or resident individual of the United States, (ii) a domestic corporation, (iii) an estate whose income is subject to United States federal income tax regardless of its source, or (iv) a trust if a United States court can exercise primary supervision over the trust's administration and one or more United States persons are authorized to control all substantial decisions of the trust; and that, for purposes of the New Treaty, as (i) the shares and ADSs do not form part of the business property of a permanent establishment through which the beneficial owner carries on or has carried on business and (ii) is not otherwise ineligible for benefits under the New Treaty, as the case may be, with respect to income and gain from the shares or ADSs.

This section does not apply to a person who is a member of a special class of holders subject to special rules, including a dealer in securities, a trader in securities that elects to use a mark-to-market method of accounting for its securities holdings, a tax-exempt organization, a life insurance company, a person liable for alternative minimum tax, a person that actually or constructively owns $10 \%$ or more of the voting stock of Honda, a person that holds shares or ADSs as part of a straddle or a hedging or conversion transaction, or a person whose functional currency is not the U.S. dollar.

This summary is not a comprehensive description of all the tax considerations that may be relevant with respect to a U.S. holder's shares or ADSs. Each beneficial owner of shares or ADSs should consult its own tax advisor regarding the U.S. federal, state and local and other tax consequences of owning and disposing of shares and ADSs in its particular circumstances.

## Taxation of Dividends

Under the U.S. federal income tax laws and subject to the passive foreign investment company, or PFIC, rules discussed below, the gross amount of any dividend paid by Honda out of its current or accumulated
earnings and profits (as determined for U.S. federal income tax purposes) is subject to United States federal income taxation. A U.S. holder must include any Japanese tax withheld from the dividend payment in this gross amount even though it does not in fact receive it.

Dividends paid to a noncorporate U.S. holder in taxable years beginning before January 1, 2011 that constitute qualified dividend income will be taxable to such holder at a maximum tax rate of $15 \%$ provided that the noncorporate U.S. holder holds shares or ADSs for more than 60 days during the 121 day period beginning 60 days before the ex-dividend date and meets other holding period requirements. Dividends that Honda pays with respect to the shares or ADSs generally will be qualified dividend income. A U.S. holder must include the dividend in its taxable income when the holder, in the case of shares, or the Depositary, in the case of ADSs, receives the dividend, actually or constructively. The dividend will not be eligible for the dividends-received deduction generally allowed to U.S. corporations in respect of dividends received from other U.S. corporations. The amount of the dividend distribution that a U.S. holder must include in its income will be the U.S. dollar value of the Japanese yen payments made, determined at the spot Japanese yen/U.S. dollar rate on the date of the dividend distribution, regardless of whether the payment is in fact converted into U.S. dollars. Generally, any gain or loss resulting from currency exchange fluctuations during the period from the date the U.S. holder includes the dividend payment in income to the date it converts the payment into U.S. dollars will be treated as ordinary income or loss and will not be eligible for the special tax rate applicable to qualified dividend income. The gain or loss generally will be income or loss from sources within the U.S. for foreign tax credit limitation purposes. Distributions in excess of current and accumulated earnings and profits, as determined for U.S. federal income tax purposes, will be treated as a non-taxable return of capital to the extent of U.S. holder's basis in the shares or ADSs and thereafter as capital gain.

Subject to certain limitations, the Japanese tax withheld in accordance with the Old Treaty or the New Treaty, as applicable, and paid over to Japan will be creditable against a U.S. holder's United States federal income tax liability. Special rules apply in determining the foreign tax credit limitation with respect to dividends that are subject to the maximum $15 \%$ tax rate. To the extent a refund of the tax withheld is available to a U.S. holder under Japanese law or under the Old Treaty or the New Treaty, the amount of tax withheld that is refundable will not be eligible for credit against the U.S. holder United States federal income tax liability. Please see "Japanese Taxation," above, for the procedures for obtaining a reduced rate of withholding under a treaty or a tax refund.

Dividends will be income from sources outside the United States, but dividends paid in taxable years beginning before January 1, 2007 generally will be "passive income" or "financial services income, and dividends paid in taxable years beginning after December 31, 2006 will, depending on your circumstances, be "passive" or "general" income which in either case, is treated separately from other types of income for purposes of computing the foreign tax credit allowable to a U.S. holder.

## Taxation of Capital Gains

Subject to the PFIC rules discussed below, if a U.S. holder sells or otherwise disposes of its shares or ADSs, it will recognize capital gain or loss for U.S. federal income tax purposes equal to the difference between the U.S. dollar value of the amount that it realizes and its tax basis, determined in U.S. dollars, in its shares or ADSs. Capital gain of a noncorporate U.S. holder that is recognized before January 1, 2011 will generally be taxed at a maximum rate of $15 \%$ where the property is held for more than one year. The gain or loss will generally be income or loss from sources within the U.S. for foreign tax credit limitation purposes.

## Passive Foreign Investment Company (PFIC) Rules

Honda believes it was not a PFIC for United States federal income tax purposes in 2006, and that it will not be a PFIC in 2007. Honda's shares and ADRs are not stock of a PFIC for United States federal income tax purposes. This conclusion is a factual determination that is made annually and thus may be subject to change.

In general, Honda will be a PFIC with respect to a U.S. holder if for any taxable year in which it held our ADRs or shares:

- at least $75 \%$ of Honda's gross income for the taxable year is passive income; or
- at least $50 \%$ of the value, determined on the basis of a quarterly average, of Honda's assets is attributable to assets that produce or are held for the production of passive income.

Passive income generally includes dividends, interest, royalties, rents (other than certain rents and royalties derived in the active conduct of a trade or business), annuities and gains from assets that produce passive income. If a foreign corporation owns at least $25 \%$ by value of the stock of another corporation, the foreign corporation is treated for purposes of the PFIC tests as owning its proportionate share of the assets of the other corporation, and as receiving directly its proportionate share of the other corporation's income.

If Honda is treated as a PFIC, and a U.S. holder does not make a mark-to-market election, as described below, that U.S. holder will be subject to special rules with respect to:

- any gain it realizes on the sale or other disposition of its shares or ADRs; and
- any excess distribution that Honda makes to it (generally, any distributions to it during a single taxable year that are greater than $125 \%$ of the average annual distributions received by it in respect of the shares or ADRs during the three preceding taxable years or, if shorter, its holding period for the shares or ADRs).

Under these rules:

- the gain or excess distribution will be allocated ratably over its holding period for the shares or ADSs,
- the amount allocated to the taxable year in which it realized the gain or excess distribution will be taxed as ordinary income,
- the amount allocated to each prior year, with certain exceptions, will be taxed at the highest tax rate in effect for that year, and
- the interest charge generally applicable to underpayments of tax will be imposed in respect of the tax attributable to each such year.

Special rules apply for calculating the amount of the foreign tax credit with respect to excess distributions by a PFIC.

If a U.S. holder owns shares or ADRs in a PFIC that are treated as marketable stock, it may make a mark-to-market election. If it makes this election, it will not be subject to the PFIC rules described above. Instead, in general, it will include as ordinary income each year the excess, if any, of the fair market value of its shares or ADSs at the end of the taxable year over its adjusted basis in its shares or ADSs. These amounts of ordinary income will not be eligible for the favorable tax rates applicable to qualified dividend income or longterm capital gains. It will also be allowed to take an ordinary loss in respect of the excess, if any, of the adjusted basis of its shares or ADSs over their fair market value at the end of the taxable year (but only to the extent of the net amount of previously included income as a result of the mark-to-market election). Its basis in the shares or ADSs will be adjusted to reflect any such income or loss amount.

In addition, notwithstanding any election that a U.S. holder makes with regard to the shares or ADSs, dividends that a U.S. holder receives from Honda will not constitute qualified dividend income to such holder if Honda is a PFIC either in the taxable year of the distribution or the preceding taxable year. Moreover, shares or ADSs held by a U.S. holder will be treated as stock in a PFIC if Honda was a PFIC at any time during the U.S. holder's holding period in its shares or ADSs, even if Honda is not currently a PFIC. For purposes of this rule, if a U.S. holder makes a mark-to-market election with respect to its shares or ADSs, the U.S. holder will be treated
as having a new holding period in its shares or ADSs beginning on the first day of the first taxable year beginning after the last taxable year for which the mark-to-market election applies. Dividends that a U.S. holder receives that do not constitute qualified dividend income are not eligible for taxation at the $15 \%$ maximum rate applicable to qualified dividend income. Instead, the U.S. holder must include the gross amount of any such dividend paid by Honda out of our accumulated earnings and profits (as determined for United States federal income tax purposes) in the U.S. holder's gross income, and it will be subject to tax at rates applicable to ordinary income.

If a U.S. holder owns shares or ADSs during any year that Honda is a PFIC with respect to such U.S. holder, it must file Internal Revenue Service Form 8621. U.S. holder should consult their own tax advisors regarding the PFIC rules and potential filing and other requirements.

## F. Dividends and Paying Agents

Not applicable.

## G. Statement by Experts

Not applicable.

## H. Documents on Display

Honda is subject to the information requirements of the Securities Exchange Act of 1934 and, in accordance therewith, it will file annual reports on Form 20-F within six months of its fiscal year-end and furnish other reports and information on Form 6-K with the Securities and Exchange Commission. These reports and other information can be inspected without charge at the public reference room at the Securities and Exchange Commission at 100 F Street, N.E., Washington, D.C. 20549. You can also obtain copies of such material by mail from the public reference room of the Securities and Exchange Commission at prescribed fees. You may obtain information on the operation of the Securities and Exchange public reference room by calling the Securities and Exchange Commission in the United States at 1-800-SEC-0330. The Securities and Exchange Commission also maintains a web site at www.sec.gov that contains reports, proxy statements and other information regarding registrants that file electronically with the Securities and Exchange Commission. Also, as a foreign private issuer, Honda is exempt from the rules under the Securities Exchange Act of 1934 prescribing the furnishing and content of proxy statements to shareholders.

## I. Subsidiary Information

Not applicable.

## Item 11. Quantitative and Qualitative Disclosure About Market Risk

Honda is exposed to market risks, which are changes in foreign currency exchanges rates, in interest rates and in prices of marketable equity securities. Honda is a party to derivative financial instruments in the normal course of business in order to manage risks associated with changes in foreign currency exchange rates and in interest rates. Honda does not hold any derivative financial instruments for trading purposes.

## Foreign Currency Exchange Rate Risk

Foreign currency forward exchange contracts and purchased option contracts are normally used to hedge sale commitments denominated in foreign currencies (principally U.S. dollars).

Foreign currency written option contracts are entered into in combination with purchased option contracts to offset premium amounts to be paid for purchased option contracts.

The tables below provide information about our derivatives related to foreign currency exchange rate risk as of March 31, 2006 and 2007. For forward exchange contracts and currency options, the table presents the contract amounts and fair value. All forward exchange contracts and currency options to which we are a party have original maturities of less than one year.

## Foreign Exchange Risk

| Forward Exchange Contract | 2006 |  |  | 2007 |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Yen (millions) |  | Averagecontractualrate | Yen (millions) |  | $\qquad$ |
|  | Contract amounts | Fair value |  | Contract amounts | Fair value |  |
| To sell US\$ | $¥ 270,070$ | $(1,771)$ | 115.88 | $¥ 336,005$ | 1,299 | 117.84 |
| To sell EUR | 132,694 | $(3,333)$ | 138.57 | 60,305 | (963) | 154.35 |
| To sell CA\$ | 19,225 | (1) | 100.59 | 16,548 | (67) | 100.88 |
| To sell GBP | 82,546 | (984) | 201.67 | 173,894 | $(1,352)$ | 228.48 |
| To sell other foreign currencies | 82,985 | 310 | various | 36,344 | (670) | various |
| To buy US\$ | 5,535 | 45 | 115.78 | 9,864 | (122) | 114.93 |
| To buy other foreign currencies | 992 | 22 | various | 11,358 | (85) | various |
| Cross-currencies | 304,078 | 2,228 | various | 334,676 | $(1,533)$ | various |
| Total | ¥898,125 | $(3,484)$ |  | ¥978,994 | $(3,493)$ |  |
|  | Yen (millions) |  |  | Yen (millions) |  |  |
| Currency Option | Contract amounts | $\underline{\text { Fair value }}$ | Average contractual rate | Contract amounts | $\underline{\text { Fair value }}$ | Average contractual rate |
| Option purchased to sell US\$ | $\geq 58,446$ | 520 | various | ¥ | - | - |
| Option written to sell US\$ | 104,576 | (323) | various | - | - | - |
| Option purchased to sell other currencies | 4,982 | 19 | various | 2,317 | 24 | various |
| Option written to sell other currencies | 8,544 | (85) | various | 3,476 | (42) | various |
| Total | ¥176,548 | 131 |  | $\underline{¥} 5,793$ | (18) |  |

## Interest Rate Risks

Honda is exposed to market risk for changes in interest rates related primarily to its debt obligations and finance receivables. In addition to short-term financing such as commercial paper, Honda has long-term debt with both fixed and floating rates. Our finance receivables are primarily fixed rate. Interest rate swap agreements are mainly used to convert floating rate financing (normally three-five years) to fixed rate financing in order to match financing costs with income from finance receivables. Foreign currency and interest rate swap agreements used among different currencies, also serve to hedge foreign currency exchange risk as well as interest rate risk.

The following tables provide information about Honda's financial instruments that were sensitive to changes in interest rates at March 31, 2006 and 2007. For finance receivables and long-term debt, these tables present principal cash flows, fair value and related weighted average interest rates. For interest rate swaps and currency \& interest rate swaps, the table presents notional amounts, fair value and weighted average interest rates. Variable interest rates are determined using formulas such as LIBOR $+\alpha$ and an index.

## Interest Rate Risk

## Finance Subsidiaries-Receivables

|  | 2006 |  | 2007 |  |  |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Yen (millions) |  | Yen (millions) |  |  |  |  |  |  |  | Average interest rate |
|  |  |  |  |  |  | Expect | ted matur | rity date |  |  |  |
|  | Total | Fair value | Total | Within 1 year | $\begin{gathered} 1-2 \\ \text { year } \end{gathered}$ | $\begin{gathered} \hline 2-3 \\ \text { year } \end{gathered}$ | $\begin{gathered} \hline 3-4 \\ \text { year } \end{gathered}$ | $\begin{gathered} \hline \text { 4-5 } \\ \text { year } \end{gathered}$ | Thereafter | Fair value |  |
| Direct Finance Leases : |  |  |  |  |  |  |  |  |  |  |  |
| US \$ | 1,846,959 | * | 1,426,173 | 558,263 | 531,211 | 309,651 | 27,039 | 9 | - | * | 4.75\% |
| Other | 348,691 | * | 439,499 | 127,160 | 97,709 | 108,119 | 102,209 | 4,285 | 17 | * | 4.52\% |
| Total—Direct <br> Finance Leases . . . . | $¥ 2,220,100$ | * | ¥1,892,566 | 701,234 | 634,491 | 421,017 | 130,713 | 5,094 | 17 | * |  |
| Other Finance |  |  |  |  |  |  |  |  |  |  |  |
| JP¥ | $¥ 412,415$ | 377,036 | ¥ 402,970 | 135,176 | 103,753 | 75,794 | 48,250 | 25,086 | 14,911 | 398,869 | 4.82\% |
| US \$ | 1,982,413 | 1,935,956 | 2,485,210 | 876,988 | 525,019 | 466,471 | 350,458 | 210,906 | 55,368 | 2,545,210 | 7.03\% |
| Other | 428,934 | 405,397 | 487,922 | 265,085 | 94,556 | 67,451 | 40,621 | 17,573 | 2,636 | 411,955 | 7.48\% |

Total—Other
Finance
Receivables
Receivables .... $¥ 2,823,762 \underline{2,718,389} ¥ 3,376,102 \underline{1,277,249} \underline{723,328} \underline{609,716} \underline{439,329} \underline{253,565} \underline{\underline{72,915}} \underline{\underline{3,356,034}}$
Retained interest in the
sold pools of finance
receivables **.... 94,634 94,634 88,110 88,110
Total $* * * \ldots \ldots \ldots \nexists 5,138,496 \quad ¥ 5,356,778$
*: Under U.S. generally accepted accounting principles, disclosure of fair values of direct finance leases is not required.
** : The retained interest in the sold pools of finance receivables is accounted for as "trading" securities and is reported at fair value.
***: The finance subsidiaries-receivables include finance subsidiaries-receivables included in trade receivables and other assets in the consolidated balance sheets. Additional detailed information is described in Note (3) to the accompanying consolidated financial statements.

## Long-Term Debt (including current maturities)

|  | 2006 |  | 2007 |  |  |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Yen (millions) |  | Yen (millions) |  |  |  |  |  |  |  | Average interest rate |
|  | Total | Fair value | Total | Expected maturity date |  |  |  |  |  | Fair value |  |
|  |  |  |  | $\begin{aligned} & \text { Within } \\ & 1 \text { year } \end{aligned}$ | $\begin{gathered} 1-2 \\ \text { year } \end{gathered}$ | $\begin{gathered} 2-3 \\ \text { year } \end{gathered}$ | $\begin{gathered} \hline 3-4 \\ \text { year } \end{gathered}$ | $\begin{gathered} 4-5 \\ \text { year } \end{gathered}$ | Thereafter |  |  |
| Japanese yen bonds | $¥ 231,200$ | 228,555 | $¥ 230,129$ | 50,050 | 30,048 | 60,049 | 59,992 | 29,990 | - | 229,379 | 0.89\% |
| Japanese yen medium-term notes (Fixed rate) | 374,624 | 374,887 | 367,900 | 114,000 | 103,400 | 70,500 | 62,000 | 18,000 | - | 368,425 | 0.80\% |
| Japanese yen medium-term notes <br> (Floating rate) | 100,696 | 101,328 | 85,200 | 24,500 | 38,000 | 19,700 | - | 3,000 | - | 85,525 | 0.77\% |
| U.S. dollar medium-term notes (Fixed rate) | 336,512 | 334,377 | 354,500 | 35,409 | 107,539 | 88,147 | 58,764 | 41,135 | 23,506 | 357,121 | 4.52\% |
| U.S. dollar medium-term notes (Floating rate) | 986,010 | 995,905 | 1,171,527 | 444,023 | 480,341 | 153,140 | 35,259 | 58,764 | - | 1,183,041 | 5.38\% |
| U.S. dollar commercial paper | 204,893 | 204,893 | - | - | - | - | - | - | - | - | - |
| Loans and others-primarily fixed rate | 302,710 | 303,969 | 471,896 | 107,427 | 129,322 | 94,169 | 101,964 | 35,837 | 3,177 | 471,384 | 4.14\% |
| Total | ¥2,536,645 | 2,543,914 | ¥2,681,152 | 775,409 | 888,650 | 485,705 | 317,979 | 186,726 | 26,683 | 2,694,875 |  |

## Interest Rate Swaps

| Notional principal currency | Receive/Pay | 2006 |  | 2007 |  |  |  |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  |  | Yen (millions) |  | Yen (millions) |  |  |  |  |  |  |  | Average receive rate | Average pay rate |
|  |  | Contract amounts | Fair value | Contract amounts | Expected maturity date |  |  |  |  |  | Fair value |  |  |
|  |  |  |  |  | Within 1 year | $\begin{aligned} & 1-2 \\ & \text { year } \end{aligned}$ | $\begin{gathered} 2-3 \\ \text { year } \end{gathered}$ | $\begin{gathered} 3-4 \\ \text { year } \end{gathered}$ | $\begin{gathered} \hline \text { 4-5 } \\ \text { year } \end{gathered}$ | Thereafter |  |  |  |
| JP¥ | Float/Fix | $¥ \quad 1,455$ | (3) | $¥ \quad 5,858$ | 150 | 4,582 | 326 | 800 | - | - | - | 1.01\% | 1.45\% |
| US\$ | Float/Fix | 2,712,564 | 39,965 | 2,933,563 | 1,195,922 | 964,636 | 633,560 | 120,409 | 19,036 | - | 8,661 | 5.35\% | 4.65\% |
|  | Fix/Float | 337,726 | $(6,426)$ | 355,921 | 35,414 | 108,016 | 88,538 | 59,025 | 41,318 | 23,610 | $(1,878)$ | 4.52\% | 5.50\% |
|  | Float/Float | 52,274 | (311) | 90,899 | 32,464 | 49,581 | 8,854 | - | - | - | (205) | 5.20\% | 5.36\% |
| CA\$ | Float/Fix | 433,089 | 4,445 | 490,691 | 126,528 | 134,859 | 116,808 | 89,792 | 22,704 | - | 2,186 | 4.09\% | 3.94\% |
|  | Fix/Float | 71,663 | $(1,067)$ | 75,961 | 6,817 | 18,832 | 18,677 | 6,373 | 25,196 | 66 | (346) | 3.95\% | 4.44\% |
|  | Float/Float | 185,057 | (303) | 195,325 | 74,134 | 64,383 | 37,207 | 14,701 | 4,834 | 66 | (302) | 4.04\% | 4.13\% |
| GBP | Float/Fix | 54,927 | 32 | 48,314 | 16,408 | 10,321 | 11,377 | 10,208 | - | - | 333 | 4.81\% | 4.90\% |
|  | Fix/Float | 8,993 | - | 1,931 | 1,563 | 368 | - | - | - | - | - | 5.11\% | 5.62\% |
| Total |  | $¥ 3,857,748$ | 36,332 | $¥ 4,198,463$ | 1,489,400 | 1,355,578 | 915,347 | 301,308 | 113,088 | 23,742 | 8,449 |  |  |

## Currency \& Interest Rate Swap

|  |  |  | 200 |  |  |  |  |  | 200 |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  |  |  | Yen (m | lions) |  |  |  | Yen (mi | lions) |  |  |  |  |  |
|  |  |  |  |  |  |  |  | Expected m | aturity dat |  |  |  |  |  |
| side currency | side currency | Receive/ Pay | Contract amounts | Fair value | Contract amounts | Within 1 year | $\begin{gathered} 1-2 \\ \text { year } \end{gathered}$ | $\begin{gathered} \hline 2-3 \\ \text { year } \end{gathered}$ | $\begin{gathered} \hline 3-4 \\ \text { year } \end{gathered}$ | $\begin{gathered} \hline 4-5 \\ \text { year } \end{gathered}$ | Thereafter | Fair value | receive rate | Average pay rate |
| JP¥ | US\$ | Fix/Float | ¥393,389 | $(22,996)$ | $¥ 386,064$ | 117,555 | 109,379 | 76,071 | 64,740 | 18,319 | - | $(21,728)$ | 0.80\% | 5.61\% |
|  |  | Float/Float | 103,823 | $(5,520)$ | 87,414 | 25,374 | 40,496 | 18,516 | 3,028 | - | - | $(4,940)$ | 0.77\% | 5.58\% |
| JP¥ | CA\$ | Fix/Float | 2,772 | (610) | 2,790 | - | - | 2,790 | - | - | - | (628) | 0.95\% | 4.75\% |
| Other | Other | Fix/Float | 70,041 | 736 | 70,387 | - | - | - | 70,387 | - | - | 6,425 | 3.75\% | 5.50\% |
|  |  | Float/Float | 14,333 | 241 | 61,879 | - | 22,471 | 39,408 | - | - | - | 3,334 | 3.99\% | 5.42\% |
|  | Total |  | ¥584,358 | $(28,149)$ | $¥ 608,534$ | 142,929 | 172,346 | 136,785 | 138,155 | 18,319 | - | $(17,537)$ |  |  |

## Equity Price Risk

Honda is exposed to equity price risk as a result of its holdings of marketable equity securities. Marketable equity securities included in Honda's investment portfolio are held for purposes other than trading, and are reported at fair value, with unrealized gains or losses, net of deferred taxes included in accumulated other comprehensive income (loss) in the stockholders' equity section of the consolidated balance sheets. At March 31, 2006 and 2007, the estimated fair value of marketable equity securities was $¥ 141.8$ billion and $¥ 169.2$ billion, respectively.

## Item 12. Description of Securities Other than Equity Securities

Not applicable.

## Item 13. Defaults, Dividend Arrearages and Delinquencies

None.

## Item 14. Material Modifications to the Rights of Security Holders and Use Proceeds

Effective July 1, 2006, we effected (1) a one to two split of our shares of common stock and (2) a change in the ratio of our American Depositary Receipt to Honda's underlying shares of common stock from 1:0.5 to 1:1. See Item 3.A. for further information.

## Item 15. Controls and Procedures

## Disclosure Controls and Procedures

Under the supervision and participation of our management, including our Chief Executive Officer and Chief Operating Officer for Business Management Operations (who is our principal financial officer), we performed an evaluation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the U.S. Securities Exchange Act of 1934) as of March 31, 2007. Based on that evaluation, our Chief Executive Officer and Chief Operating Officer for Business Management Operations concluded that our disclosure controls and procedures were effective as of that date.

## Management's Report on Internal Control over Financial Reporting

The management of Honda is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the U.S. Securities Exchange Act of 1934). The Company's internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles and includes those policies and procedures that (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or because the degree of compliance with policies or procedures may deteriorate.

Our management, including our Chief Executive Officer and Chief Operating Officer for Business Management Operations(who is our principal financial officer), assessed the effectiveness of internal control over financial reporting as of March 31, 2007 based on the criteria established in "Internal Control-Integrated Framework" published by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based on that assessment, our management concluded that our internal control over financial reporting was effective as of March 31, 2007.

Management's assessment of the effectiveness of internal control over financial reporting has been audited by KPMG AZSA \& Co., an independent registered public accounting firm, as stated in their report which is included herein.

## Changes in Internal Control over Financial Reporting

No significant changes were made in our internal control over financial reporting during the fiscal year ended March 31, 2007 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## Item 16A. Audit Committee Financial Expert

Honda's Board of Auditors has determined that Mr. Shinichi Sakamoto is qualified as an "audit committee financial expert" as defined by the rules of the SEC. He was elected as one of Honda's corporate auditors at the general meeting of shareholders held on June 23 2005. See Item 6.A. for additional information regarding

Mr. Sakamoto. Mr. Sakamoto meets the independence requirements imposed on corporate auditors under the Company law of Japan. See Item 6.C. for an explanation of such independence requirements

## Item 16B. Code of Ethics

Honda has adopted a code of ethics that applies to its principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions. A copy of Honda's code of ethics is attached as an exhibit to this annual report on Form 20-F.

## Item 16C. Principal Accountant Fees and Services

Principal Accountant, who conducted audits of our consolidated financial statements under U.S. generally accepted accounting principles or its affiliates, is independent auditor under applicable SEC rules and billed the following fees to us for professional services:

|  | Yen (millions) |  |
| :---: | :---: | :---: |
|  | 2006 | 2007 |
| Audit Fees | 1,119 | 2,708 |
| Audit-Related Fees | 45 | 38 |
| Tax Fees | 350 | 176 |
| All Other Fees | - | - |
| Total | 1,514 | 2,922 |

"Audit fees" means fees for audit services, which are professional services provided by independent auditors for the audit of our annual financial statements or for services that are normally provided by independent auditors with respect to any submissions required under applicable laws and regulations.
"Audit-related fees" means fees for audit-related services, which are assurance services provided by independent auditors that are reasonably related to the carrying out of auditing or reviewing of our financial reports and other related services. This category includes fees for agreed-upon or expanded audit procedures related to accounting and/or other records.
"Tax fees" means fees for tax services, which are services provided by independent auditors related to tax compliance, tax advice and tax planning.
"All other fees" means fees for all other services, which are any services provided by independent auditors other than the audit services, audit-related services and tax services set forth above. This category includes fees for training and other miscellaneous support services.

## Pre-approval policies and procedures of the Board of Auditors

Under applicable SEC rules, our Board of Corporate Auditors must pre-approve audit services, audit-related services, tax services and other services to be provided by principal accountant to ensure that the independence of principal accountant under such rules is not impaired as a result of the provision of any of these services.

While, as a general rule, specific pre-approval must be obtained for these services to be provided, our Board of Corporate Auditors has adopted pre-approval policies and procedures which list particular audit and non-audit services that may be provided without specific pre-approval. Our Board of Corporate Auditors reviews this list of services on an annual basis, and is informed of each such service that is actually provided.

All services to be provided to us by principal accountant and its affiliates those are not specifically set forth in this list must be specifically pre-approved by our Board of Corporate Auditors.

None of the services described above in this Item 16C were waived from the pre-approval requirements pursuant to Rule 2-01(c)(7)(i)(C) of Regulation S-X.

## Item 16D. Exemption from the Listing Standards for Audit Committees

With respect to the requirements of Rule 10A-3 under the Securities Exchange Act of 1934 relating to listed company audit committees, which apply to us through Section 303A. 06 of the New York Stock Exchange's Listed Company Manual, we rely on an exemption provided by paragraph (c)(3) of that Rule available to foreign private issuers with boards of corporate auditors meeting certain requirements. For a New York Stock Exchangelisted Japanese company with a board of corporate auditors, the requirements for relying on paragraph (c)(3) of Rule 10A-3 are as follows:

- The Board of Corporate Auditors must be established, and its members must be selected, pursuant to Japanese law expressly requiring such a board for Japanese companies that elect to have a corporate governance system with corporate auditors.
- Japanese law must and does require the board of corporate auditors to be separate from the Board of Directors.
- None of the members of the board of corporate auditors may be elected by management, and none of the listed company's executive officers may be a member of the board of corporate auditors.
- Japanese law must and does set forth standards for the independence of the members of the board of corporate auditors from the listed company or its management.
- The board of corporate auditors, in accordance with Japanese law or the listed company's governing documents, must be responsible, to the extent permitted by Japanese law, for the appointment, retention and oversight of the work of any registered public accounting firm engaged (including, to the extent permitted by Japanese law, the resolution of disagreements between our management and the auditor regarding financial reporting) for the purpose of preparing or issuing an audit report or performing other audit, review or attest services for the listed company, including its principal accountant which audits its consolidated financial statements included in its annual reports on Form 20-F.
- To the extent permitted by Japanese law:
- the board of corporate auditors must established procedures for (i) the receipt, retention and treatment of complaints received by us regarding accounting, internal accounting controls, or auditing matters, and (ii) the confidential, anonymous submission by our employees of concerns regarding questionable accounting or auditing matters;
- the board of corporate auditors must have the authority to engage independent counsel and other advisers, as it determines necessary to carry out its duties; and
- the listed company must provide for appropriate funding, as determined by its board of corporate auditors, for payment of (i) compensation to any registered public accounting firm engaged for the purpose of preparing or issuing an audit report or performing other audit, review or attest services for us, (ii) compensation to any advisers employed by the board of corporate auditors, and (iii) ordinary administrative expenses of the board of corporate auditors that are necessary or appropriate in carrying out its duties.

In our assessment, our Board of Corporate Auditors, which meets the requirements for reliance on the exemption in paragraph (c)(3) of Rule 10A-3 as described above, is not materially less effective than an audit committee meeting all the requirements of paragraph (b) of Rule 10A-3 (without relying on any exemption provided by at acting independently of management and performing the functions of an audit committee as contemplated therein.

## Item 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchasers

The following table sets forth certain information with respect to purchases by Honda of its own shares during the year ended March 31, 2007. There were no purchases of Honda's shares by its affiliated purchasers during that year.

| Period | (a) Total Number of Shares Purchased ${ }^{(1)}$ | (b) Average Price Paid per Share | (c) Total <br> Number of Shares Purchased as Part of Publicly Announced Plans or Programs | (d) Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs ${ }^{(2)}$ |
| :---: | :---: | :---: | :---: | :---: |
| April 1 to April 30, $2006{ }^{(3)}$ | 1,926,974 | $¥ 3,817$ | 1,922,000 | 0 |
| May 1 to May 31, $2006{ }^{(3)}$ | 2,269,054 ${ }^{(4)}$ | ¥3,909 | 0 | 0 |
| June 1 to June 30, $2006{ }^{(3)}$ | 1,638 | ¥3,649 | 0 | 0 |
| July 1 to July 31, 2006 | 956 | ¥3,606 | 0 | 0 |
| August 1 to August 31, 2006 | 1,911,938 | $¥ 3,881$ | 1,909,500 | 4,090,500 |
| September 1 to September 30, 2006 | 1,812,770 | $¥ 3,886$ | 1,807,400 | 2,283,100 |
| October 1 to October 31, 2006 | 868,720 | $¥ 4,115$ | 866,200 | 0 |
| November 1 to November 30, 2006. | 2,690 | $¥ 4,171$ | 0 | 0 |
| December 1 to December 31, 2006 | 817,340 ${ }^{(5)}$ | $¥ 4,629$ | 0 | 0 |
| January 1 to January 31, 2007 | 1,313 | $¥ 4,701$ | 0 | 0 |
| February 1 to February 28, 2007 | 870 | $¥ 4,702$ | 0 | 0 |
| March 1 to March 31, 2007 | 1,296 | $¥ 4,310$ | 0 | 0 |
| Total | 9,615,559 | ¥3,961 | 6,505,100 |  |

(1) For each month, the number of shares shown in column (a) in excess of the number of shares shown in column (c) represents the aggregate number of shares representing less than one unit that Honda purchased from the holders thereof upon their request. For an explanation of the right of such holders, see "Japanese Unit Share System—Right of a Holder of Shares Representing Less Than One Unit to Require Honda to Purchase or Sell Its Shares" under Item 10.B of this Annual Report.
(2) During the year ended March 31, 2007, the following share repurchase programs were in effect:

Share repurchase approved by the Board of Directors pursuant to the Articles of Incorporation Date of announcement: January 31, 2006
Maximum number of shares authorized to be repurchased: 5,800,000
Maximum yen amount authorized to be used for repurchase: $¥ 32,000,000,000$
Repurchase period: from February 6, 2006 to April 14, 2006
(This program expired on the last day of the repurchase period referred to above.)
Share repurchase approved by the Board of Directors pursuant to the Articles of Incorporation
Date of announcement: July 26, 2006
Maximum number of shares authorized to be repurchased: 6,000,000
Maximum yen amount authorized to be used for repurchase: $¥ 18,000,000,000$
Repurchase period: from August 2, 2006 to October 13, 2006
(This program expired on the last day of the repurchase period referred to above.)
(3) Honda conducted a two-for-one stock split for the Company's common stock effective July 1, 2006.

Numbers for April, May and June 2006 have been adjusted based on the number of shares after the stock split.
(4) The number of shares shown in May 2006 includes shares the Company repurchased from the following subsidiaries, pursuant to a resolution of the Board of Directors at its meeting on May 16, 2006 and pursuant to Article 163 of the Company Law. Numbers for the followings have adjusted based on the number of shares after the stock split.

1. Honda Express Co., Ltd.
2. Name of Subsidiary: Honda Express Co., Ltd.
3. Details of Acquisition
(1) Type of shares acquired: Shares of common stock
(2) Aggregate number of shares acquired: $1,926,750$ shares ( $0.11 \%$ of total outstanding shares)
(3) Aggregate price of acquisition: $¥ 7,531,665,750$
(4) Date of Acquisition : May 31, 2006
4. Reason for Acquisition

The Company purchased its own shares held by Honda Express Co., Ltd., which recently became a subsidiary of the Company, as a result of a summary share exchange effected on April 28,2006.
2. Honda Kaihatsu Co., Ltd.

1. Name of Subsidiary: Honda Kaihatsu Co., Ltd.
2. Details of Acquisition
(1) Type of shares acquired: Shares of common stock
(2) Aggregate number of shares acquired: 193,200 shares ( $0.01 \%$ of total outstanding shares)
(3) Aggregate price of acquisition: $¥ 755,218,800$
(4) Date of acquisition : May 31, 2006
3. Reason for Acquisition

The Company purchased its own shares held by Honda Kaihatsu Co., Ltd., which recently became a subsidiary of the Company as a result of the Company Law coming into effect on May 1, 2006.
3. Atsumitec Co., Ltd.

1. Name of Subsidiary: Atsumitec Co., Ltd.
2. Details of Acquisition
(1) Type of shares acquired: Shares of common stock
(2) Aggregate number of shares acquired: 143,600 shares ( $0.01 \%$ of total outstanding shares)
(3) Aggregate price of acquisition: $¥ 561,332,400$
(4) Date of acquisition: May 31, 2006
3. Reason for Acquisition

The Company purchased its own shares held by Honda Atsumitec Co., Ltd., which recently became a subsidiary of the Company as a result of the Company Law coming into effect on May 1, 2006.
(5) Yachiyo Industry Co., Ltd. became a consolidated subsidiary of the Company as of December 27, 2006. As a result, 814,717 shares, or $50.45 \%$ of the total number of Honda shares held by Yachiyo, are now included in the Company's treasury stock in its consolidated balance sheet, reflecting Honda' percentage of voting rights in Yachiyo.

## Item 17. Financial Statements

Not applicable.

## Item 18. Financial Statements

See Consolidated Financial Statements attached hereto.

## Item 19. Exhibits

1.1 Articles of Incorporation of the registrant (English translation)
1.2 Share Handling Regulations of the registrant (English translation)
1.3 Regulations of Board of Directors of the registrant (English translation)
1.4 Regulations of the Board of Corporate Auditors of the registrant (English translation)
2.1 Specimen common stock certificates of the registrant (English translation) (1)
2.2 Deposit Agreement dated as of December 19, 1962, as amended and restated as of October 1, 1982 (including changes from Amendment to Deposit Agreement dated as of April 1, 1989) among the registrant, Morgan Guaranty Trust Company of New York (now JP Morgan Chase Bank), as Depositary, and all owners and holders from time to time of American Depositary Receipts and European Depositary Receipts, including the form of American Depositary Receipt (2)
2.3 Form of Amendment No. 2 to Deposit Agreement dated as of April, 1995, among the parties referred to in Exhibit 2.2 above (2)
2.4 Form of Amendment No. 3 to Deposit Agreement dated as of January, 2002, among the parties referred to in Exhibit 2.2 above (3)
2.5 Form of Amendment No. 4 to Deposit Agreement dated as of June, 2006 among the parties referred to in Exhibit 2.2 above (4)
2.6 Form of Amendment No. 5 to Deposit Agreement dated as of June, 2007 among the parties referred to in Exhibit 2.2 above (5)
8.1 List of Significant Subsidiaries (See "Organizational Structure" in Item 4.C. of this Form 20-F)
11.1 Code of Ethics (6)
12.1 Certification of the principal executive officer required by 17 C.F.R. 240. 13a-14(a)
12.2 Certification of the principal executive officer required by 17 C.F.R. 240. 13a-14(a)
13.1 Certification of the chief executive officer required by 18 U.S.C. Section 1350
13.2 Certification of the chief financial officer required by 18 U.S.C. Section 1350
(1) Incorporated by reference to the registrant's annual report on Form 20-F filed on September 27, 2001.
(2) Incorporated by reference to the Registration Statement on Form F-6 (File No. 33-91842) filed on May 1, 1995.
(3) Incorporated by reference to the Registration Statement on Form F-6 (File No. 333-14228) filed on December 20, 2001.
(4) Incorporated by reference to the Registration Statement on Form F-6 (File No. 333-114874) filed on June 28, 2006.
(5) Incorporated by reference to the Registration Statement on Form F-6 (File No. 333-143589) filed on June 8, 2007.
(6) Incorporated by reference to the registrant's annual report on Form 20-F filed on July 9, 2004.

The Company has not included as exhibits certain instruments with respect to its long-term debt, the amount of debt authorized under each of which does not exceed $10 \%$ of its total assets, and it agrees to furnish a copy of any such instrument to the Securities and Exchange Commission upon request.

HONDA MOTOR CO., LTD.
(Honda Giken Kogyo Kabushiki Kaisha)
(A Japanese Company)
AND SUBSIDIARIES
Consolidated Financial Statements and
Report of Independent Registered
Public Accounting Firm
March 31, 2007

To be Included in
The Annual Report
Form 20-F
Filed with
The Securities and Exchange Commission
Washington, D.C., U.S.A.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

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Financial statements of affiliates are omitted because such affiliates are not individually significant.

## Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Honda Motor Co., Ltd.:
We have audited the accompanying consolidated balance sheets of Honda Motor Co., Ltd. and subsidiaries as of March 31, 2006 and 2007, and the related consolidated statements of income, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended March 31, 2007, expressed in Japanese yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Honda Motor Co., Ltd. and subsidiaries as of March 31, 2006 and 2007, and the results of their operations and their cash flows for each of the years in the three-year period ended March 31, 2007 in conformity with U.S. generally accepted accounting principles.

As described in Note 12 to the consolidated financial statements, the Company adopted the provisions of Statement of Financial Accounting Standards No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - an amendment of FASB Statements of No. 87,88,106 and 132(R) as of March 31, 2007. As described in Note 1(u) to the consolidated financial statements, the Company changed its method of quantifying errors as of March 31, 2007. Also as further described in Note 2, the Company made certain classification adjustments to its consolidated financial statements as of and for the years ended March 31, 2006 and 2005.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of March 31, 2007, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated July 17, 2007 expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

## /S/ KPMG AZSA \& Co.

Tokyo, Japan
July 17, 2007

## Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Honda Motor Co., Ltd.:
We have audited management's assessment, included in the accompanying Management's Report on Internal Control over Financial Reporting, that Honda Motor Co., Ltd. and subsidiaries maintained effective internal control over financial reporting as of March 31, 2007, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Honda Motor Co., Ltd. and subsidiaries maintained effective internal control over financial reporting as of March 31, 2007, is fairly stated, in all material respects, based on the criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Also, in our opinion, Honda Motor Co., Ltd. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of March 31, 2007, based on the criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Honda Motor Co., Ltd. and subsidiaries as of March 31, 2006 and 2007, and the related consolidated statements of income, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended March 31, 2007, expressed in Japanese yen, and our report dated July 17, 2007 expressed an unqualified opinion on those consolidated financial statements.
/S/ KPMG AZSA \& Co.
Tokyo, Japan
July 17, 2007

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Consolidated Balance Sheets

## March 31, 2006 and 2007



[^2]See accompanying notes to consolidated financial statements.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Consolidated Statements of Income

Years ended March 31, 2005, 2006 and 2007

|  | Yen (millions) |  |  |
| :---: | :---: | :---: | :---: |
|  | 2005* | 2006* | 2007 |
| Net sales and other operating revenue (note 3) | $¥ 8,650,105$ | ¥9,907,996 | ¥ $11,087,140$ |
| Operating costs and expenses: |  |  |  |
| Cost of sales (note 3) | 6,038,172 | 7,010,357 | 7,865,142 |
| Selling, general and administrative | 1,513,259 | 1,656,365 | 1,818,272 |
| Research and development | 467,754 | 510,385 | 551,847 |
|  | 8,019,185 | 9,177,107 | 10,235,261 |
| Gain on transfer of the substitutional portion of the Employees' |  |  |  |
| Pension Funds (note 12) . . . . . . . . . . . . . . . . . . . . . . . . . . | - | 138,016 | - |
| Operating income . | 630,920 | 868,905 | 851,879 |
| Other income (notes $1(\mathrm{q})$ and 6 ): |  |  |  |
| Interest | 10,696 | 27,363 | 42,364 |
| Other | 60,541 | 2,214 | 13,243 |
|  | 71,237 | 29,577 | 55,607 |
| Other expenses (notes 1(q) and 6): |  |  |  |
| Interest | 11,655 | 11,902 | 12,912 |
| Other | 22,138 | 56,676 | 101,706 |
|  | 33,793 | 68,578 | 114,618 |
| Income before income taxes, minority interest and equity in income of affiliates | 668,364 | 829,904 | 792,868 |
| Income tax (benefit) expense (note 10): |  |  |  |
| Current | 151,146 | 319,945 | 300,294 |
| Deferred | 115,519 | $(2,756)$ | $(16,448)$ |
|  | 266,665 | 317,189 | 283,846 |
| Income before minority interest and equity in income of affiliates | 401,699 | 512,715 | 509,022 |
| Minority interest in income of consolidated subsidiaries | $(11,559)$ | $(15,287)$ | $(20,117)$ |
| Equity in income of affiliates (note 5) | 96,057 | 99,605 | 103,417 |
| Net income | ¥ 486,197 | $\ddagger$ 597,033 | ¥ 592,322 |
|  | Yen |  |  |
|  | 2005 | 2006 | 2007 |
| Basic net income per common share (note 1(o)) | $¥ 260.34$ | $¥ \quad 324.33$ | $¥ \quad 324.62$ |

[^3]See accompanying notes to consolidated financial statements.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Consolidated Statements of Stockholders' Equity and Comprehensive Income

Years ended March 31, 2005, 2006 and 2007


## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

Consolidated Statements of Stockholders' Equity and Comprehensive Income-(Continued)
Years ended March 31, 2005, 2006 and 2007

|  | Yen (millions) |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | $\begin{gathered} \text { Common } \\ \text { stock } \\ \hline \end{gathered}$ | Capital surplus | $\begin{gathered} \text { Legal } \\ \text { reserves } \end{gathered}$ | Retained earnings | Accumulated other comprehensive income (loss), net | Treasury stock | Total stockholders' equity |
| Cumulative effect of adjustments resulting from the adoption of SAB No. 108, net of tax (note 1(u)) | - | - | - | $(62,640)$ | 18,149 | - | $(44,491)$ |
| Adjusted balances as of March 31,2006 | 86,067 | 172,529 | 35,811 | 4,205,246 | $(389,038)$ | $(29,356)$ | 4,081,259 |
| Transfer to legal reserves |  |  | 1,919 | $(1,919)$ |  |  | - |
| Cash dividends |  |  |  | $(140,482)$ |  |  | $(140,482)$ |
| Comprehensive income (loss): |  |  |  |  |  |  |  |
| Net income |  |  |  | 592,322 |  |  | 592,322 |
| Other comprehensive income (loss), net of tax (note 14) |  |  |  |  |  |  |  |
| Adjustments from foreign currency translation |  |  |  |  | 96,775 |  | 96,775 |
| Unrealized gains (losses) on marketable securities: |  |  |  |  |  |  |  |
| Unrealized holding gains (losses) |  |  |  |  | 1,004 |  | 1,004 |
| Reclassification adjustments for losses (gains) realized in net income |  |  |  |  | $(5,575)$ |  | $(5,575)$ |
| Unrealized gains (losses) on derivative instruments: |  |  |  |  |  |  |  |
| Unrealized holding gains (losses) |  |  |  |  | (337) |  | (337) |
| Reclassification adjustments for losses (gains) realized in net income . . . . . . . . . |  |  |  |  | 421 |  | 421 |
| Minimum pension liabilities adjustment |  |  |  |  | 8,908 |  | 8,908 |
| Total comprehensive income |  |  |  |  |  |  | 693,518 |
| Adjustment for initially applying SFAS No. 158, net of tax (note 12) |  |  |  |  | $(139,324)$ |  | $(139,324)$ |
| Purchase of treasury stock |  |  |  |  |  | $(30,974)$ | $(30,974)$ |
| Reissuance of treasury stock |  |  |  | (277) |  | 18,891 | 18,614 |
| Retirement of treasury stock |  |  |  |  |  |  | - |
| Balance at March 31, 2007 | ¥86,067 | ¥172,529 | $¥ 37,730$ | $¥ 4,654,890$ | $¥(427,166)$ | $¥(41,439)$ | $¥ 4,482,611$ |

See accompanying notes to consolidated financial statements.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Consolidated Statements of Cash Flows

Years ended March 31, 2005, 2006 and 2007

|  | Yen (millions) |  |  |
| :---: | :---: | :---: | :---: |
|  | 2005* | 2006* | 2007 |
| Cash flows from operating activities (note 13): |  |  |  |
| Net income | ¥ 486,197 | ¥ 597,033 | $\geq 592,322$ |
| Adjustments to reconcile net income to net cash provided by operating activities: |  |  |  |
| Depreciation excluding property on operating leases | 225,752 | 262,225 | 361,747 |
| Depriciation of property on operating leases | - | - | 9,741 |
| Deferred income taxes | 115,519 | $(2,756)$ | $(16,448)$ |
| Minority interest in income | 11,559 | 15,287 | 20,117 |
| Equity in income of affiliates | $(96,057)$ | $(99,605)$ | $(103,417)$ |
| Dividends from affiliates | 35,824 | 64,055 | 54,849 |
| Provision for credit and lease residual losses on finance subsidiaries-receivables | 50,638 | 36,153 | 44,128 |
| Loss (gain) on derivative instruments, net | $(60,432)$ | 10,351 | 56,836 |
| Gain on transfer of the substitutional portion of the Employees' Pension Funds (note 12) | - | $(138,016)$ | - |
| Decrease (increase) in assets: |  |  |  |
| Trade accounts and notes receivable | $(70,145)$ | $(113,259)$ | $(49,529)$ |
| Inventories | $(79,483)$ | $(109,661)$ | $(96,839)$ |
| Other current assets | 10,280 | $(59,484)$ | $(15,206)$ |
| Other assets | $(78,130)$ | $(81,796)$ | $(5,523)$ |
| Increase (decrease) in liabilities: |  |  |  |
| Trade accounts and notes payable | 66,488 | 21,420 | 38,186 |
| Accrued expenses | 41,101 | 51,653 | 41,898 |
| Income taxes payable | 33,704 | 39,900 | $(37,282)$ |
| Other current liabilities | 19,973 | 6,126 | 1,103 |
| Other liabilities | 66,621 | 80,410 | 14,274 |
| Other, net | 5,761 | 604 | $(6,432)$ |
| Net cash provided by operating activities | 785,170 | 580,640 | 904,525 |
| Cash flows from investing activities: |  |  |  |
| Increase in investments and advances | $(25,661)$ | $(17,314)$ | $(9,874)$ |
| Decrease in investments and advances | 15,985 | 3,711 | 3,829 |
| Payment for purchase of available-for-sale securities | $(96,829)$ | $(158,011)$ | $(141,902)$ |
| Proceeds from sales of available-for-sale securities | 154,253 | 129,496 | 172,806 |
| Payment for purchase of held-to-maturity securities | $(20,856)$ | $(63,395)$ | $(13,614)$ |
| Proceeds from redemption of held-to-maturity securities | - | 55,990 | 41,109 |
| Capital expenditures | $(373,980)$ | $(460,021)$ | $(597,958)$ |
| Proceeds from sales of property, plant and equipment | 14,216 | 39,951 | 20,641 |
| Acquisitions of finance subsidiaries-receivables | (2,710,520) | $(3,031,644)$ | $(2,857,024)$ |
| Collections of finance subsidiaries-receivables | 1,561,299 | 1,870,675 | 2,138,875 |
| Proceeds from sales of finance subsidiaries-receivables | 684,308 | 930,595 | 477,927 |
| Purchase of operating lease assets | - | - | $(366,795)$ |
| Proceeds from sales of operating lease assets | - | - | 1,276 |
| Net cash used in investing activities | $(797,785)$ | $(699,967)$ | (1,130,704) |
| Cash flows from financing activities: |  |  |  |
| Increase (decrease) in short-term debt, net | 20,244 | $(124,941)$ | 306,063 |
| Proceeds from long-term debt | 704,433 | 865,677 | 969,491 |
| Repayment of long-term debt | $(495,238)$ | $(568,605)$ | $(677,539)$ |
| Cash dividends paid (note 11) | $(47,797)$ | $(71,061)$ | $(140,482)$ |
| Cash dividends paid to minority interests | $(2,722)$ | $(4,083)$ | $(7,434)$ |
| Payment for purchase of treasury stock, net | $(84,147)$ | $(77,064)$ | $(26,689)$ |
| Net cash provided by financing activities | 94,773 | 19,923 | 423,410 |
| Effect of exchange rate changes on cash and cash equivalents | 12,394 | 43,406 | 31,527 |
| Net change in cash and cash equivalents | 94,552 | $(55,998)$ | 228,758 |
| Cash and cash equivalents at beginning of year * | 678,234 | 772,786 | 716,788 |
| Cash and cash equivalents at end of year | $¥ \quad 772,786$ | $¥ 716,788$ | $¥ \quad 945,546$ |

[^4]See accompanying notes to consolidated financial statements.

# HONDA MOTOR CO., LTD. AND SUBSIDIARIES 

## Notes to Consolidated Financial Statements

## (1) General and Summary of Significant Accounting Policies

## (a) Description of Business

Honda Motor Co., Ltd. (the "Company") and its subsidiaries (collectively "Honda") develop, manufacture, distribute and provide financing for the sale of its motorcycles, automobiles and power products. Honda's manufacturing operations are principally conducted in 32 separate factories, four of which are located in Japan. Principal overseas manufacturing facilities are located in the United States of America, Canada, Mexico, the United Kingdom, France, Italy, Spain, China, India, Indonesia, Malaysia, Pakistan, the Philippines, Taiwan, Thailand, Vietnam, Brazil and Turkey.

## (b) Basis of Presenting Consolidated Financial Statements

The Company and its domestic subsidiaries maintain their books of account in conformity with financial accounting standards of Japan, and its foreign subsidiaries generally maintain their books of account in conformity with those of the countries of their domicile.

The consolidated financial statements presented herein have been prepared in a manner and reflect the adjustments which are necessary to conform them with U.S. generally accepted accounting principles.

## (c) Consolidation Policy

The consolidated financial statements include the accounts of the Company, its subsidiaries and those variable interest entities where the Company is the primary beneficiary under the Financial Accounting Standard Boards (FASB) Interpretation (FIN) No. 46 (revised December 2003), "Consolidation of Variable Interest Entities". All significant intercompany balances and transactions have been eliminated in consolidation.

Investments in affiliates in which the Company has the ability to exercise significant influence over their operating and financial policies, but where the Company does not have a controlling financial interest are accounted for using the equity method.

## (d) Use of Estimates

Management of Honda has made a number of estimates and assumptions relating to the reporting of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements in conformity with U.S. generally accepted accounting principles. Significant items subject to such estimates and assumptions include, but are not limited to, allowance for credit losses, losses on lease residual values, realizable values of inventories, realization of deferred tax assets, impairment of longlived assets, product warranty obligations, and the fair values of assets and obligations related to employee benefits. Actual results could differ from those estimates.

## (e) Revenue Recognition

Sales of manufactured products are recognized when persuasive evidence of an arrangement exists, delivery has occurred, title and risk of loss have passed to the customers, the sales price is fixed or determinable, and collectibility is probable.

Honda provides dealer incentives passed on to the end customers generally in the form of below-market interest rate loans or lease programs. The amount of interest or lease subsidies paid is the difference between the amount offered to retail customers and a market-based interest or lease rate. Honda also provides dealer

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

incentives retained by the dealer, which generally represent discounts provided by Honda to the dealers. These incentives are classified as a reduction of sales revenue as the consideration is paid in cash and Honda does not receive an identifiable benefit in exchange for this consideration. The estimated costs are accrued at the time the product is sold to the dealer.

Operating lease revenues are recorded on a straight-line basis over the term of the lease.
Interest income from finance receivables is recognized using the interest method. Finance receivable origination fees and certain direct origination costs are deferred, and the net fee or cost is amortized using the interest method over the contractual life of the finance receivables.

Finance subsidiaries of the Company periodically sell finance receivables. Gain or loss is recognized equal to the difference between the cash proceeds received and the carrying value of the receivables sold and is recorded in the period in which the sale occurs. Honda allocates the recorded investment in finance receivables between the portion(s) of the receivables sold and portion(s) retained based on the relative fair values of those portions on the date the receivables are sold. Honda recognizes gains or losses attributable to the change in the fair value of the retained interests, which are recorded at estimated fair value and accounted for as "trading" securities. Honda determines the fair value of the retained interests by discounting the future cash flows. Those cash flows are estimated based on prepayments, credit losses and other information as available and are discounted at a rate which Honda believes is commensurate with the risk free rate plus a risk premium. A servicing asset or liability is amortized in proportion to and over the period of estimated net servicing income. Servicing assets and servicing liabilities at March 31, 2006 and 2007 were not significant.

## (f) Cash Equivalents

Honda considers all highly liquid debt instruments with an original maturity of three months or less to be cash equivalents. Cash equivalents consist of money market funds and commercial paper, and amount to ¥96,325 million and $¥ 117,182$ million as of March 31, 2006 and 2007, respectively.

## (g) Inventories

Inventories are stated at the lower of cost, determined principally by the first-in, first-out method, or market.

## (h) Investments in Securities

Honda classifies its debt and equity securities in the following categories: available-for-sale, trading, or held-to-maturity. Debt securities that are classified as "held-to-maturity" securities are reported at amortized cost. Debt and equity securities classified as "trading" securities are reported at fair value, with unrealized gains and losses included in earnings. Other marketable debt and equity securities are classified as "available-for-sale" securities and are reported at fair value, with unrealized gains or losses, net of deferred taxes included in accumulated other comprehensive income (loss) in the stockholders' equity section of the consolidated balance sheets. Honda did not hold any "trading" securities at March 31, 2006 and 2007, except for retained interests in the sold pools of finance receivables, which are accounted for as "trading" securities and included in finance subsidiaries-receivables.

Honda periodically compares the fair value of investment securities with their cost basis. If the fair value of investment securities has declined below our cost basis and such decline is judged to be other-than-temporary, Honda recognizes the impairment of the investment securities and the carrying value is reduced to its fair value through a charge to income. The determination of other-than-temporary impairment is based upon an assessment

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

of the facts and circumstances related to each investment security. In determining the nature and extent of impairment, Honda considers such factors as financial and operating conditions of the issuer, the industry in which the issuer operates, degree and period of the decline in fair value and other relevant factors.

Non-marketable equity securities are carried at cost, and are examined the possibility of impairment periodically.

## (i) Goodwill

Honda accounts for goodwill in accordance with Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets". Goodwill, all of which is allocated to Honda's reporting units, is not amortized but instead is tested for impairment at least annually. Honda completed its annual tests for March 31, 2005, 2006, and 2007 and concluded no impairment needed to be recognized. The carrying amount of goodwill at March 31, 2006 and 2007 was $¥ 27,951$ million and $¥ 30,590$ million, respectively.

## (j) Property on Operating Leases

Property on operating leases is reported at cost, less accumulated depreciation. Depreciation of the vehicles is generally provided on a straight-line basis to an estimated residual value over the lease term. The residual values of the vehicles related to the operating leases are estimated at inception by using our estimate of future used vehicle values, taking into consideration data obtained from third parties.

## (k) Depreciation

Depreciation of property, plant and equipment is calculated principally by the declining-balance method based on estimated useful lives and salvage values of the respective assets.

The estimated useful lives used in computing depreciation of property, plant and equipment are as follows:

|  | Asset | Life |
| :---: | :---: | :---: |
| Buildings |  | 3 to 50 years |
| Machinery and equipment |  | 2 to 20 years |

## (l) Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of

Honda's long-lived assets and identifiable intangible assets other than goodwill having finite useful lives are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows (undiscounted and without interest charges) expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. Assets to be disposed of by sale are reported at the lower of the carrying amount or estimated fair value less costs to sell.

## (m) Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in earnings in the period that includes the enactment date.

## (n) Product-Related Expenses

Advertising and sales promotion costs are expensed as incurred. Advertising expenses for each of the years in the three-year period ended March 31,2007 were $¥ 246,997$ million, $¥ 287,901$ million and $¥ 308,409$ million, respectively. Provisions for estimated costs related to product warranty are made at the time the products are sold to customers or new warranty programs are initiated. Estimated warranty expenses are provided based on historical warranty claim experience with consideration given to the expected level of future warranty costs as well as current information on repair costs. Included in warranty expenses accruals are costs for general warranties on vehicles Honda sells and product recalls.

## (o) Basic Net Income per Common Share

Basic net income per common share has been computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding during each year. The weighted average number of common shares outstanding for the years ended March 31, 2005, 2006 and 2007 was $1,867,535,957,1,840,799,671$ and $1,824,675,228$ respectively. There were no potentially dilutive shares outstanding during the years ended March 31, 2005, 2006 or 2007.

The Company executed a two-for-one stock split for the Company's common stock effective July 1, 2006. All per share information has been adjusted retroactively for all periods presented to reflect this stock split.

## (p) Foreign Currency Translation

Foreign currency financial statement amounts are translated into Japanese yen on the basis of the year-end rate for all assets and liabilities and the weighted average rate for the year for all income and expense amounts. The resulting translation adjustments are included in accumulated other comprehensive income (loss) in the stockholders' equity section of the consolidated balance sheets.

Foreign currency receivables and payables are translated at the applicable current rates on the balance sheet date. All revenues and expenses associated with foreign currencies are converted at the rates of exchange prevailing when such transactions occur. The resulting exchange gains or losses are reflected in other income (expense) in the consolidated statements of income.

Foreign currency transaction gains (losses) included in other income (expenses) - other for each of the years in the three-year period ended March 31, 2007 are as follows:

|  | Yen <br> (millions) |  |  |
| :---: | :---: | :---: | :---: |
| $\mathbf{2 0 0 5}$ | $\mathbf{2 0 0 6}$ | $¥(38,880)$ | $\mathbf{2 0 0 7}$ |
| $¥(17,146)$ |  | $¥(48,261)$ |  |

## (q) Derivative Financial Instruments

Honda has entered into foreign exchange agreements and interest rate agreements to manage currency and interest rate exposures. These instruments include foreign currency forward contracts, currency swap agreements, currency option contracts and interest rate swap agreements.

Honda recognizes at fair value of all derivative financial instruments in its consolidated balance sheet.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Honda applies hedge accounting for certain foreign currency forward contracts related to forecasted foreign currency transactions between the Company and its subsidiaries. These are designated as cash flow hedges on the date derivative contracts entered into. The Company has a currency rate risk management policy documented. In addition, it documents all relationships between derivative financial instruments designated as cash flow hedges and the relevant hedged items to identify the relationship between them. The Company assesses, both at the hedge's inception and on an ongoing basis, whether the derivative financial instruments designated as cash flow hedge are highly effective to offset changes in cash flows of hedged items.

When it is determined that a derivative financial instrument is not highly effective as a cash flow hedge, when the hedged item matures, is sold or is terminated, or when it is identified that the forecasted transaction is no longer probable, the Company discontinues hedge accounting. To the extent derivative financial instruments are designated as cash flow hedges and have been assessed as being highly effective, changes in their fair value are recognized in other comprehensive income (loss). The amounts are reclassified into earnings in the period when forecasted hedged transactions affect earnings. When these cash flow hedges prove to be ineffective, changes in the fair value of the derivatives are immediately recognized in earnings.

Changes in the fair value of derivative financial instruments not designated as accounting hedges are recognized in earnings in the period of the change.

The amount recognized in earnings included in other income (expenses) - other during the year ended March $31,2005,2006$ and 2007 are $¥ 44,905$ million gain, $¥ 55,516$ million loss and $¥ 48,485$ million loss, respectively. In relation to this, the Company included gains and losses on translation of debts of finance subsidiaries denominated in foreign currencies intended to be hedged of $¥ 10,667$ million gain, $¥ 45,046$ million gain and $¥ 8,351$ million loss in other income (expenses) - other during the years ended March 31, 2005, 2006 and 2007, respectively. In addition, net realized gains and losses on interest rate swap contracts not designated as accounting hedges by mainly finance subsidiaries of $¥ 28,000$ million loss, $¥ 827$ million gain and $¥ 3,309$ million gain are included in other income (expenses) - other during the years ended March 31, 2005, 2006 and 2007, respectively. These gains and losses are presented on a net basis.

Honda doesn't hold any derivative financial instruments for trading purposes.

## (r) Shipping and Handling Costs

Shipping and handling costs included in selling, general and administrative expenses for each of the years in the three-year period ended March 31, 2007 are as follows:

| $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |  |
| :---: | :---: | :---: |
| 2005 | 2006 | 2007 |
| $\ddagger 159,472$ | $¥ 181,675$ | 219,361 |

## (s) Asset Retirement Liability

Honda applies Financial Accounting Standards Board (FASB) Interpretation (FIN) No. 47, "Accounting for Conditional Asset Retirement Obligations - an interpretation of FASB Statement No.143". FIN47 clarifies the term conditional asset retirement obligation as used in SFAS No. 143 and requires a liability to be recorded if the fair value of the obligation can be reasonably estimated. Asset retirement obligations covered by this Interpretation include those for which an entity has a legal obligation to perform an asset retirement activity, however the timing and (or) method of settling the obligation are conditional on a future event that may or may not be within the control of the entity.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## (t) New Accounting Pronouncements

In March 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 156, "Accounting for Servicing of Financial Assets". This statement amends SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities", with respect to the accounting for separately recognized servicing assets and servicing liabilities. SFAS No. 156 gives revised guidance as to when servicing assets and servicing liabilities should be recognized. It also revises guidance regarding the initial and subsequent measurement of servicing assets and liabilities. SFAS No. 156 is effective as of the beginning of an entity's first fiscal year that begins after September 15, 2006. Management is currently in process of quantifying the financial impact of adoption. It is not anticipated that adoption will have a material impact on the Company's financial position or results of operations.

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) No. 48, "Accounting for Uncertainty in Income Taxes". This Interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes". This Interpretation prescribes a two step process for the recognition and measurement in the financial statement of a tax position taken or expected to be taken in a tax return. This statement is effective as of an entity's first fiscal year that begins after December 15, 2006. Management is currently in the process of quantifying the financial impact of adoption.

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No.157, "Fair Value Measurements". This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements and does not require any new fair value measurements. This statement is effective as of an entity's first fiscal year that begins after November 15, 2007, with early adoption encouraged. Management is currently in the process of determining whether to early adopt this statement and quantifying the financial impact of adoption. It is not anticipated that adoption will have a material impact on the Company's financial position or results of operation.

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - an amendment of FASB Statements No. 87, 88, 106, and 132(R)". This statement amends SFAS No. 87, "Employers' Accounting for Pensions", SFAS No. 88, "Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension and for Termination Benefits", SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions", and SFAS No. 132(R), "Employers' Disclosures about Pensions and Other Postretirement Benefits". This statement requires an employer to recognize the overfunded or underfunded status as an asset or liability in its statement of financial position and to recognize changes in that funded status in comprehensive income in the year in which the changes occur. This statement replaces SFAS No. 87's requirement to report at least minimum pension liability measured as excess at the accumulated benefit obligation over the fair value at the plan assets. The Company and its consolidated subsidiaries adopted SFAS No. 158 on March 31, 2007. Detailed information about the impact of the adoption of SFAS No. 158 is provided in note 12 to the accompanying consolidated financial statements.

This statement also changes the date at which benefit obligations are to be measured to the date of the year-end statement of financial position. The measurement provisions of this statement are effective for fiscal years ending after December 15, 2008.

In February 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 159, "The Fair Value Option for Financial Assets and Financial

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Liabilities - including an amendment of SFAS No.115". This statement permits entities to choose to measure at fair value many financial instruments and certain other items that are not currently required to be measured at fair value. Subsequent changes in fair value for designated items will be required to be reported in earnings in the current period. The statement also establishes presentation and disclosure requirements for similar types of assets and liabilities measured at fair value. The statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, with early adoption being permitted. Management is currently in process of determining whether to early adopt this statement and quantifying the financial impact of adoption.

## (u) Cumulative Effect of Prior Year Adjustments

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB No. 108"). SAB No. 108 provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying current year misstatements for the purpose of materiality assessment. SAB No. 108 requires that registrants quantify a current year misstatement using an approach that considers both the impact of prior year misstatements that remain on the balance sheet and those that were recorded in the current year income statement. The Company historically quantified misstatements and assessed materiality based on a current year income statement approach. The transition provisions of SAB No. 108 permit the Company to adjust for the cumulative effect on retained earnings of immaterial errors related to prior years.

The Company adopted SAB No. 108 effective beginning of the fiscal year ended March 31, 2007, and adjusted the items described below in the accompanying consolidated financial statements as of the beginning of the fiscal year ended March 31, 2007 to correct the prior year misstatements, which were considered to be immaterial to the consolidated statements of income and consolidated balance sheets in prior years under the income statement approach. The net impact of these adjustments decreased the Company's beginning retained earnings and beginning accumulated other comprehensive loss for 2007 by $¥ 62,640$ million, net of tax effect of $¥ 31,235$ million, and $¥ 18,149$ million, respectively, for the items described below and incremental effects on the consolidated balance sheet are shown in the table below:

1. The Company and its certain domestic subsidiaries in Japan historically calculated depreciation of property, plant and equipment, using a salvage value determined as $5 \%$ of the acquisition cost. However, since the sales proceeds received for the liquidated assets and their economical value at the end of its useful life historically have been nominal, the Company and its certain domestic subsidiaries assessed the adequacy of the salvage value and concluded that they should have calculated depreciation using the salvage value of $¥ 1$ for its properly, plant and equipment. The Company and its certain domestic subsidiaries recalculated depreciation expenses retrospectively considering the corrected salvage value. The reassessment indicated that an accumulated overstatement of property, plant and equipment in the consolidated financial statements had occured.
2. Equity in income of affiliates should be recognized based on affiliates' consolidated financial statements in accordance with U.S. generally accepted accounting principles. However, the Company historically recognized equity in income of affiliates based on the results of operations of the parent-only financial statements of the affiliates, as the Company assessed that the difference between the total amounts of equity in income on the consolidation basis and those on the parent-only basis had been immaterial to the Company's consolidated financial statements under the income statement approach. This misstatement resulted in an accumulated understatement of equity in income of affiliates and the carrying value of the investments in affiliates in the consolidated financial statements.
3. The Company reclassified the residual tax effect of minimum pension liabilities included in accumulated other comprehensive income during the year ended March 31, 2006, which related to corporate

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

tax rate changes in the past based on the proportional allocation over the expiration of unrecognized obligation. However, the residual tax effect should have been reclassified only when the pension plan is liquidated or dissolved under the portfolio approach. This misstatement resulted in an understatement of accumulated other comprehensive loss and corresponding overstatement in income tax benefit.

The impact of the affected line items in the consolidated balance sheet at the beginning of fiscal year ended March 31, 2007 is as follows.

## Consolidated Balance Sheet

| Assets | Yen (millions) |  |  |  |
| :---: | :---: | :---: | :---: | :---: |
|  | 1 | 2 | 3 | Cumulative Effect of Prior Year Adjustment as of April 1, 2006 |
| Investments and advances: |  |  |  |  |
| Investments in and advances to affiliates | $(4,546)$ | 36,274 | - | 31,728 |
| Total investments and advances | $(4,546)$ | 36,274 | - | 31,728 |
| Property, plant and equipment, at cost: |  |  |  |  |
| Less accumulated depreciation and amortization | 109,308 | - | - | 109,308 |
| Net property, plant and equipment | $\underline{(109,308)}$ | - | - | $(109,308)$ |
| Other assets | 43,722 | - | - | 43,722 |
| Total assets | $(70,132)$ | 36,274 | - | $(33,858)$ |
|  | Yen (millions) |  |  |  |
| Liabilities, Minority Interests and Stockholders' Equity | 1 | 2 | 3 | Cumulative effect of Prior Year Adjustment as of April 1, 2006 |
| Other liabilities | $(1,818)$ | 14,305 | - | 12,487 |
| Total liabilities | $(1,818)$ | 14,305 | - | 12,487 |
| Minority interests in consolidated subsidiaries | $(1,854)$ | - | - | $(1,854)$ |
| Stockholders' equity: |  |  |  |  |
| Retained earnings | $(66,460)$ | 21,969 | $(18,149)$ | $(62,640)$ |
| Accumulated other comprehensive income (loss), net . | - | - | 18,149 | 18,149 |
| Total stockholders' equity | $(66,460)$ | 21,969 | - | $(44,491)$ |
| Total liabilities, minority interests and stockholders' equity | $(70,132)$ | 36,274 | - | $(33,858)$ |

## (v) Reclassifications and Revisions of Classifications

Certain revisions for misclassifications and reclassifications have been made to the prior years' consolidated financial statements to conform to the presentation used for the fiscal year ended March 31, 2007. Detailed information is provided in note 2 .

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## (2) Revisions of Classifications

Certain revisions for misclassifications have been made to the prior years' consolidated financial statements.
(a) Minority interest and minority interest in income, which were included in other liabilities and other expenses-other, respectively, have been revised to be disclosed independently in consolidated balance sheets and consolidated statements of income. Minority interest in income and cash dividends paid to minority interests, which were included in other liabilities and other, net, in cash flows from operating activities, have been revised to be disclosed independently in cash flows from operating activities and cash flows from financing activities, respectively, in the consolidated statements of cash flows.
(b) Auction rate securities, which were classified as cash equivalents, have been revised to be classified as available-for-sale securities due within one year, which are included in other current assets in the consolidated balance sheets. Payment for purchase of auction rate securities and proceeds from sales of auction rate securities have been revised to be classified in payment for purchase of available-for-sale securities and proceeds from sales of available-for-sale securities in the consolidated statements of cash flows, respectively.
(c) The long-term portion of deferred tax liabilities and deferred tax assets related to the lease transactions of finance subsidiaries, which were classified in other current liabilities and deferred income taxes, have been revised to be classified in other liabilities and other assets, respectively.
(d) The long-term portion of accrued expenses and prepaid expenses related to pension benefit plans, which were included in accrued expenses and other current assets have been revised to be classified in other liabilities and other assets, respectively. The long-term portion of deferred tax liabilities, which were included in other current liabilities, and deferred tax assets, have also been revised to classified in other liabilities and other assets.
(e) The long-term portion of prepaid expenses, deferred income and accrued expenses related to extended vehicle service contracts of the subsidiaries in the United States, which were included in other current assets, trade payables accounts and accrued expenses, respectively, have been revised to be classified in other liabilities and other assets. The long-term portion of related deferred tax liabilities, which were included in other current liabilities, and deferred income taxes have also been revised to be classified in other liabilities and other assets.
(f) Certain consolidated subsidiaries' assets, which were classified in investment and advances - other, have been revised to be classified in other assets.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

The impact of the affected line items in the consolidated balance sheet at March 31, 2006 and in the consolidated statements of income and the consolidated statements of cash flows for the years ended March 31, 2005 and 2006 are as follows:

## Consolidated Balance Sheet

| Assets | Yen (millions) |  |  |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | $\begin{gathered} \hline 2006 \\ \text { Previously } \\ \text { reported } \end{gathered}$ | (a) | (b) | (c) | (d) | (e) | (f) | Total | $\begin{gathered} \hline 2006 \\ \begin{array}{c} \text { After } \\ \text { revised } \end{array} \end{gathered}$ |
| Cash and cash equivalents | 747,327 |  | $(30,539)$ |  |  |  |  | $(30,539)$ | 716,788 |
| Deferred income taxes | 198,033 |  |  | 80,859 | $(33,845)$ | $(23,753)$ |  | 23,261 | 221,294 |
| Other current assets | 450,002 |  | 30,539 |  | $(22,097)$ | $(51,459)$ |  | $(43,017)$ | 406,985 |
| Total current assets | 4,625,898 | - | - | 80,859 | (55,942) | (75,212) | - | (50,295) | 4,575,603 |
| Investments and advances: |  |  |  |  |  |  |  |  |  |
| Other, including marketable equity securities | 286,092 |  |  |  |  |  | 12,368 | 12,368 | 298,460 |
| Total investments and advances | 695,085 | - | - | - | - | - | 12,368 | 12,368 | 707,453 |
| Other assets | 453,006 |  |  |  | 22,097 | 87,917 | (12,368) | 97,646 | 550,652 |
| Total assets | 10,571,681 | - | - | 80,859 | $(33,845)$ | 12,705 | - | 59,719 | 10,631,400 |
|  | Yen (millions) |  |  |  |  |  |  |  |  |
| Liabilities, Minority Interests and Stockholders' Equity | 2006Previously <br> reported | (a) | (b) | (c) | (d) | (e) | (f) | Total | $\begin{gathered} 2006 \\ \begin{array}{c} \text { After } \\ \text { revised } \end{array} \end{gathered}$ |
| Trade payables: |  |  |  |  |  |  |  |  |  |
| Accounts | 1,099,902 |  |  |  |  | $(84,493)$ |  | $(84,493)$ | 1,015,409 |
| Accrued expenses | 930,115 |  |  |  | $(105,605)$ | $(37,538)$ |  | $(143,143)$ | 786,972 |
| Other current liabilities | 466,332 |  |  | $(268,106)$ |  |  |  | $(268,106)$ | 198,226 |
| Total current liabilities | 3,989,409 | - | - | (268,106) | $\overline{(105,605)}$ | $\overline{(122,031)}$ | - | (495,742) | 3,493,667 |
| Other liabilities | 577,522 | $(87,460)$ |  | 348,965 | 71,760 | 134,736 |  | 468,001 | 1,045,523 |
| Total liabilities | 6,445,931 | (87,460) | - | 80,859 | $(33,845)$ | 12,705 | - | (27,741) | 6,418,190 |
| Minority interests in consolidated subsidiaries | - | 87,460 |  |  |  |  |  | 87,460 | 87,460 |
| Total liabilities, minority interests and stockholders' equity | 10,571,681 | - | - | 80,859 | $\stackrel{(33,845)}{ }$ | 12,705 | - | 59,719 | $\underline{\underline{10,631,400}}$ |

## Consolidated Statements of Income



## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## Consolidated Statements of Cash Flows

|  | Yen (millions) |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | $\begin{gathered} 2006 \\ \begin{array}{c} \text { Previously } \\ \text { reported } \end{array} \end{gathered}$ | (a) | (b) | (d) | (e) | Total |  |
| Cash flows from operating activities <br> Adjustments to reconcile net income to net cash provided by operating activities: |  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |  |
| Minority interest in income | - | 15,287 |  |  |  | 15,287 | 15,287 |
| Decrease (increase) in assets: |  |  |  |  |  |  |  |
| Other current assets | $(75,771)$ |  |  | 7,765 | 8,522 | 16,287 | $(59,484)$ |
| Other assets | $(61,482)$ |  |  | $(7,765)$ | $(12,549)$ | $(20,314)$ | $(81,796)$ |
| Increase (decrease) in liabilities: |  |  |  |  |  |  |  |
| Trade accounts and notes payable | 41,360 |  |  |  | $(19,940)$ | $(19,940)$ | 21,420 |
| Accrued expenses | 98,273 |  |  | $(36,426)$ | $(10,194)$ | $(46,620)$ | 51,653 |
| Other liabilities | 5,740 | 4,083 |  | 36,426 | 34,161 | 74,670 | 80,410 |
| Other, net | 15,891 | $(15,287)$ |  |  |  | $(15,287)$ | 604 |
| Net cash provided by operating activities | 576,557 | 4,083 | - | - | - | 4,083 | 580,640 |
| Cash flows from investing activities: |  |  |  |  |  |  |  |
| Payment for purchase of available-for-sale securities | $(6,915)$ |  | $(151,096)$ |  |  | $(151,096)$ | $(158,011)$ |
| Proceeds from sales of available-for-sale securities | 5,666 |  | 123,830 |  |  | 123,830 | 129,496 |
| Net cash used in investing activities | (672,701) | - | $(27,266)$ | - | - | $(27,266)$ | (699,967) |
| Cash flows from financing activities: |  |  |  |  |  |  |  |
| Cash dividends paid to minority interests | - | $(4,083)$ |  |  |  | $(4,083)$ | $(4,083)$ |
| Net cash provided by financing activities | 24,006 | $(4,083)$ | - | - | - | $(4,083)$ | 19,923 |
| Effect of exchange rate changes on cash and cash equivalents | 45,927 |  | $(2,521)$ |  |  | $(2,521)$ | 43,406 |
| Net change in cash and cash equivalents | $(26,211)$ | - | $(29,787)$ | - | - | $(29,787)$ | $(55,998)$ |
| Cash and cash equivalents at beginning of year | 773,538 |  | (752) |  |  | (752) | 772,786 |
| Cash and cash equivalents at end of year | 747,327 | - | $(30,539)$ | - | - | $(30,539)$ | 716,788 |

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

|  | Yen (millions) |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | 2005 Previously reported | (a) | (b) | (d) | (e) | Total |  |
| Cash flows from operating activities <br> Adjustments to reconcile net income to net cash provided by operating activities: |  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |  |
| Minority interest in income | - | 11,559 |  |  |  | 11,559 | 11,559 |
| Decrease (increase) in assets: |  |  |  |  |  |  |  |
| Other current assets | $(11,797)$ |  |  | 14,332 | 7,745 | 22,077 | 10,280 |
| Other assets | $(52,198)$ |  |  | $(14,332)$ | $(11,600)$ | $(25,932)$ | $(78,130)$ |
| Increase (decrease) in liabilities: |  |  |  |  |  |  |  |
| Trade accounts and notes payable | 76,338 |  |  |  | $(9,850)$ | $(9,850)$ | 66,488 |
| Accrued expenses | 71,469 |  |  | $(26,239)$ | $(4,129)$ | $(30,368)$ | 41,101 |
| Other liabilities | 19,826 | 2,722 |  | 26,239 | 17,834 | 46,795 | 66,621 |
| Other, net | 17,320 | $(11,559)$ |  |  |  | $(11,559)$ | 5,761 |
| Net cash provided by operating activities | 782,448 | 2,722 | - | - | - | 2,722 | 785,170 |
| Cash flows from investing activities: |  |  |  |  |  |  |  |
| Payment for purchase of available-for-sale securities | $(1,608)$ |  | $(95,221)$ |  |  | $(95,221)$ | $(96,829)$ |
| Proceeds from sales of available-for-sale securities | 13,140 |  | 141,113 |  |  | 141,113 | 154,253 |
| Net cash used in investing activities | $(843,677)$ | - | 45,892 | - | - | 45,892 | $(797,785)$ |
| Cash flows from financing activities: |  |  |  |  |  |  |  |
| Cash dividends paid to minority interests | - | $(2,722)$ |  |  |  | $(2,722)$ | $(2,722)$ |
| Net cash provided by financing activities | 97,495 | $(2,722)$ | - | - | - | $(2,722)$ | 94,773 |
| Effect of exchange rate changes on cash and cash equivalents | 12,851 |  | (457) |  |  | (457) | 12,394 |
| Net change in cash and cash equivalents | 49,117 | - | 45,435 | - | - | 45,435 | 94,552 |
| Cash and cash equivalents at beginning of year | 724,421 |  | $(46,187)$ |  |  | $(46,187)$ | 678,234 |
| Cash and cash equivalents at end of year | 773,538 | - | (752) | - | - | (752) | 772,786 |

## (3) Finance Subsidiaries-Receivables and Securitizations

Finance subsidiaries-receivables represent finance receivables generated by finance subsidiaries. Certain finance receivables related to sales of inventory are included in trade receivables and other assets in the consolidated balance sheets. Finance receivables include wholesale financing to dealers and retail financing and direct financing leases to consumers.

The allowance for credit losses is maintained at an amount management deems adequate to cover estimated losses on finance receivables. The allowance is based on management's evaluation of many factors, including current economic trends, industry experience, inherent risks in the portfolio and the borrower's ability to pay.

Finance subsidiaries of the Company purchase insurance to cover a substantial amount of the estimated residual value of vehicles leased to customers. The allowance for losses on lease residual values is maintained at an amount management deems adequate to cover estimated losses on the uninsured portion of the vehicles' lease residual values. The allowance is also based on management's evaluation of many factors, including current economic conditions, industry experience and the finance subsidiaries' historical experience with residual value losses.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Finance subsidiaries-receivables, net, consisted of the following at March 31, 2006 and 2007:

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |
| :---: | :---: | :---: |
|  | 2006 | 2007 |
| Direct financing leases | $¥ 2,220,100$ | $¥ 1,892,566$ |
| Retail | 2,405,926 | 2,923,944 |
| Wholesale | 403,499 | 437,242 |
| Term loans to dealers | 14,337 | 14,916 |
| Total finance receivables | 5,043,862 | 5,268,668 |
| Retained interests in the sold pools of finance receivables . | 94,634 | 88,110 |
|  | 5,138,496 | 5,356,778 |
| Less: |  |  |
| Allowance for credit losses | 35,316 | 35,020 |
| Allowance for losses on lease residual values | 37,774 | 33,928 |
| Unearned interest income and fees | 224,901 | 143,131 |
|  | 4,840,505 | 5,144,699 |
| Less: |  |  |
| Finance receivables included in trade receivables, net | 470,002 | 509,697 |
| Finance receivables included in other assets, net | 157,166 | 168,952 |
| Finance subsidiaries-receivables, net | 4,213,337 | 4,466,050 |
| Less current portion | 1,230,912 | 1,426,224 |
| Noncurrent finance subsidiaries-receivables, net | $\underline{¥ 2,982,425}$ | $\underline{¥ 3,039,826}$ |

The following schedule shows the contractual maturities of finance receivables for each of the five years following March 31, 2007 and thereafter:

| Years ending March 31 | $\underset{\text { Yen }}{\text { (millions) }}$ |
| :---: | :---: |
| 2008 | $¥ 1,978,483$ |
| 2009 | 1,357,819 |
| 2010 | 1,030,733 |
| 2011 | 570,042 |
| 2012 | 258,659 |
| After five years | 72,932 |
|  | 3,290,185 |
| Total | ¥5,268,668 |

Net sales and other operating revenue and cost of sales include finance income and related cost of finance subsidiaries for each of the years in the three-year period ended March 31, 2007 as follows:

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |  |
| :---: | :---: | :---: | :---: |
|  | 2005 | 2006 | 2007 |
| Finance income | ¥259,188 | $¥ 310,937$ | ¥413,334 |
| Finance cost | 54,815 | 115,636 | 188,844 |

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Finance subsidiaries of the Company periodically sell finance receivables. Finance subsidiaries sold retail finance receivables subject to limited recourse provisions totaling approximately $¥ 731,508$ million, $¥ 930,629$ million and $¥ 562$, 488 million to investors in fiscal years 2005 , 2006 and 2007 , respectively. Pre-tax net gains or losses on such sales resulted in losses of $¥ 4,291$ million, $¥ 11,849$ million and a gain of $¥ 1,175$ million in fiscal years 2005, 2006 and 2007, respectively, which are included in loss on sale of receivables.

Finance subsidiaries sold direct financing lease receivables subject to limited recourse provisions totaling approximately $¥ 100,374$ million in fiscal year 2006 . Pre-tax net gains or losses on such sales resulted in a net gain of $¥ 483$ million is included in loss on sale of receivables for fiscal year 2006. The leases sold during fiscal year 2006 had $100 \%$ insurance coverage of the residual value of the vehicles collateralizing those leases. Finance subsidiaries did not sell any direct financing lease receivable in fiscal year 2007.

Retained interests in securitizations were comprised of the following at March 31, 2006 and 2007:

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |
| :---: | :---: | :---: |
|  | 2006 | 2007 |
| Subordinated certificates | ¥52,572 | $¥ 44,198$ |
| Residual interests | 42,062 | 43,912 |
| Total | ¥94,634 | $¥ 88,110$ |

Key economic assumptions used in initially estimating the fair values at the date of the securitizations during each of the years in the three-year period ended March 31, 2007 are as follows:

|  | 2005 | 2006 | 2007 |
| :---: | :---: | :---: | :---: |
| Weighted average life (years) | 1.64 to 1.77 | 1.60 to 1.75 | 1.66 to 1.77 |
| Prepayment speed | 1.25\% to $1.30 \%$ | $1.00 \%$ to $1.30 \%$ | 1.25\% to $1.30 \%$ |
| Expected credit losses | 0.30\% to 0.70\% | 0.35\% to 0.55\% | $0.23 \%$ to $0.27 \%$ |
| Residual cash flows discount | 6.55\% to $12.00 \%$ | $6.53 \%$ to $12.00 \%$ | $5.43 \%$ to $12.00 \%$ |

At March 31, 2007, the significant assumptions used in estimating the retained interest in the sold pools of finance receivables are as follows:

|  | Weighted average assumption |
| :---: | :---: |
| Prepayment speed | 1.27\% |
| Expected credit losses | 0.24\% |
| Residual cash flows discount rate | 8.80\% |

The sensitivity of the current fair value to immediate $10 \%$ and $20 \%$ adverse changes from expected levels for each significant assumption above mentioned were immaterial.

The following illustration presents quantitative information about balances of outstanding securitized portfolios as of March 31, 2006 and 2007.

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |
| :---: | :---: | :---: |
|  | 2006 | 2007 |
| Securitized receivables |  |  |
| Retail | $¥ 1,402,552$ | ¥1,208,409 |
| Direct finance leases | 97,711 | 67,758 |
| Total securitized receivables | $\underline{\underline{¥ 1,500,263}}$ | $\underline{\underline{¥ 1,276,167}}$ |

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## (4) Inventories

Inventories at March 31, 2006 and 2007 are summarized as follows:

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |
| :---: | :---: | :---: |
|  | 2006 | 2007 |
| Finished goods | $¥ 687,230$ | $¥ 772,917$ |
| Work in process | 28,218 | 34,970 |
| Raw materials | 320,856 | 375,229 |
|  | $¥ 1,036,304$ | ¥1,183,116 |

## (5) Investments and Advances-Affiliates

Investments in affiliates are accounted for using the equity method. Differences between the cost of investments in affiliates and the amount of underlying equity in net assets of the affiliates principally represent investor level goodwill.

Honda considers whether the fair value of any of its equity method investments have declined below their carrying value whenever adverse events or changes in circumstances indicate that recorded values many not be recoverable. If Honda considered any such decline to be other than temporary based on various factors, then a write-down would be recorded to estimated fair value.

Significant investments in affiliates accounted for under the equity method at March 31, 2006 and 2007 are Showa Corporation (33.5\%), Keihin Corporation(42.2\%), Guangzhou Honda Automobile Co., Ltd.(50.0\%), Dongfeng Honda Engine Co., Ltd.(50.0\%), and P.T. Astra Honda Motor(50.0\%).

Certain adjustments were recorded to investments and advances to affiliates as of April 1, 2006, please refer to note $1(\mathrm{u})$ for further information.

The difference between the carrying amount of investment in affiliates and the amount of underlying equity in net assets is not material as of March 31, 2006 and 2007.

Investments in affiliates include equity securities which have quoted market values at March 31, 2006 and 2007 compared with related carrying amounts as follows;

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |
| :---: | :---: | :---: |
|  | 2006 | 2007 |
| Carrying amount | $¥ 130,802$ | $¥ 184,879$ |
| Market value | 444,250 | 412,892 |

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Certain combined financial information in respect of affiliates accounted for under the equity method at March 31, 2006 and 2007, and for each of the years in the three-year period ended March 31, 2007 is shown below:

|  |  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |
| :---: | :---: | :---: | :---: |
|  |  | 2006 | 2007 |
| Current assets |  | $¥ 1,056,428$ | $¥ 1,434,855$ |
| Other assets, principally property, plant and equipment |  | 1,063,235 | 1,317,057 |
| Total assets |  | 2,119,663 | 2,751,912 |
| Current liabilities |  | 762,660 | 1,038,968 |
| Other liabilities |  | 182,503 | 306,418 |
| Total liabilities |  | 945,163 | 1,345,386 |
| Stockholders' equity |  | $\xlongequal{¥ 1,174,500}$ | $\xlongequal{¥ 1,406,526}$ |
|  |  | $\underset{\text { (millions) }}{\text { Yen }}$ |  |
|  | 2005 | 2006 | 2007 |
| Net sales | $¥ 3,039,751$ | $¥ 3,426,348$ | $¥ 4,598,573$ |
| Net income | 220,596 | 229,640 | 268,577 |
| Cash dividends received by Honda during the year | 35,824 | 64,055 | 54,849 |

Sales to affiliates by the Company and its subsidiaries and sales among such affiliates are made on the same basis as sales to unaffiliated parties.

Honda's equity in undistributed income of affiliates at March 31, 2006 and 2007 included in retained earnings was $¥ 275,874$ million and $¥ 354,552$ million, respectively.

Honda mainly purchases materials, supplies and services from affiliates, and sells parts used in its products, equipment and services to affiliates.

Trade receivables and trade payables include the following balances with affiliates at March 31, 2006 and 2007, and purchases and sales include the following transactions with affiliates for each of the years in the threeyear period ended March 31, 2007:


Mr. Minekawa, a Director of the Company, served as the President of Guangzhou Honda Automobile Co., Ltd., one of our affiliates in China until June 23, 2005. In fiscal year 2006 from April to June, Honda sold automobile

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

parts, equipment and services to the affiliated company in the amount of $¥ 10,008$ million. In fiscal year 2005, Honda sold automobile parts, equipment and services to the affiliated company in the amount of $¥ 37,023$ million.

## (6) Investments and Advances

Investments and advances at March 31, 2006 and 2007 consisted of the following:

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |
| :---: | :---: | :---: |
|  | 2006* | 2007 |
| Current |  |  |
| Auction rate securities | ¥ 30,539 | ¥ 41,318 |
| Corporate debt securities | 13,100 | 311 |
| U.S. government and agency debt securities | 18,733 | 2,993 |
| Commercial paper | 5,998 | - |
| Advances | 829 | 581 |
|  | $¥$ 69,199 | $\ddagger$ 45,203 |

[^5]Investments and advances due within one year are included in other current assets.

|  |  |  |
| :---: | :---: | :---: |
|  | 2006* | 2007 |
| Noncurrent |  |  |
| Marketable equity securities | $¥ 141,846$ | ¥169,280 |
| Convertible preferred stocks | 22,934 | - |
| Convertible notes | 56,635 | - |
| Government bonds | 2,999 | 2,999 |
| U.S. government and agency debt securities | 2,937 | 10,034 |
| Non-marketable equity securities accounted |  |  |
| Non-marketable preferred stocks | 6,000 | 2,000 |
| Other | 13,357 | 11,639 |
| Guaranty deposits | 30,110 | 30,847 |
| Advances | 2,209 | 2,481 |
| Other | 19,433 | 25,330 |
|  | $¥ 298,460$ | ¥254,610 |

[^6]
## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Certain information with respect to marketable securities at March 31, 2006 and 2007 is summarized below:

|  | $\underset{\text { Yen }}{\text { (millions) }}$ |  |
| :---: | :---: | :---: |
|  | 2006 | 2007 |
| Available-for-sale |  |  |
| Cost | $¥ 60,905$ | $¥ 107,573$ |
| Fair value | 172,385 | 210,598 |
| Gross unrealized gains | 111,540 | 103,113 |
| Gross unrealized losses | 60 | 88 |
| Held-to-maturity |  |  |
| Amortized cost | $¥ 43,767$ | ¥ 16,337 |
| Fair value | 43,428 | 16,348 |
| Gross unrealized gains | 1 | 26 |
| Gross unrealized losses | 340 | 15 |

Maturities of debt securities classified as held-to-maturity at March 31, 2007 were as follows:

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |
| :---: | :---: |
| Due within one year | $¥ 3,304$ |
| Due after one year through five years | 11,035 |
| Due after five years through ten years | 1,998 |
| Total | $¥ 16,337$ |

Realized gains and losses from available-for-sale securities included in other expenses (income) - other for each of the years in the three-year period ended March 31,2007 , were, $¥ 2,206$ million net gains, $¥ 462$ million net losses and $¥ 10,463$ million net gains, respectively.

Gross unrealized losses on marketable securities and fair value of the related securities, aggregated by length of time that individual securities have been in a continuous unrealized loss position at March 31, 2007 were as follows:

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |
| :---: | :---: | :---: |
|  | Fair value | $\begin{gathered} \hline \text { Unrealized } \\ \text { losses } \\ \hline \end{gathered}$ |
| Available-for-sale |  |  |
| Less than 12 months | $¥ 329$ | $¥(88)$ |
| 12 months or longer | - | - |
|  | $¥ 329$ | $¥(88)$ |
| Held-to-maturity |  |  |
| Less than 12 months | $¥ 3,540$ | $¥$ (1) |
| 12 months or longer | 3,938 | (14) |
|  | ¥7,478 | $¥(15)$ |

Honda judged this decline in fair value of investment securities to be temporary, with considering such factors as financial and operating conditions of the issuer, the industry in which the issuer operates, degree and period of the decline in fair value and other relevant factors.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## (7) Property on Operating Leases

Future minimum lease rentals expected to be received from property on operating leases at March 31, 2007 are as follows:

| Years ending March 31 | $\underset{\text { (millions) }}{\text { Yen }}$ |
| :---: | :---: |
| 2008 | $¥ 61,045$ |
| 2009 | 60,168 |
| 2010 | 46,470 |
| 2011 | 6,885 |
| 2012 | 112 |
| Total future minimum lease rentals | ¥174,680 |

Future minimum rentals as shown above should not necessarily be considered indicative of future cash collections.

## (8) Short-term and Long-term Debt

Short-term debt at March 31, 2006 and 2007 is as follows:

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |
| :---: | :---: | :---: |
|  | 2006 | 2007 |
| Short-term bank loans | $¥ 314,124$ | $¥ 311,117$ |
| Medium-term notes | 152,246 | 182,355 |
| Commercial paper | 227,187 | 772,396 |
|  | ¥693,557 | $\underline{¥ 1,265,868}$ |

The weighted average interest rates on short-term debt outstanding at March 31, 2006 and 2007 were $3.21 \%$ and $4.00 \%$, respectively.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Long-term debt at March 31, 2006 and 2007 is as follows:
$\left.\begin{array}{llll}\text { Yen } \\ \text { (millions) }\end{array}\right]$

The loans maturing through 2031 and through 2030 are either secured by property, plant and equipment or subject to collateralization upon request, and their interest rates range from $0.69 \%$ to $16.17 \%$ per annum at March 31, 2007 and weighted average interest rate on total outstanding long-term debt at March 31, 2006 and 2007 is $4.35 \%$ and $3.96 \%$, respectively. Property, plant and equipment with a net book value of approximately $¥ 22,592$ million and $¥ 23,654$ million at March 31, 2006 and 2007, respectively, were subject to specific mortgages securing indebtedness. Furthermore, finance subsidiaries-receivables of approximately $¥ 8,993$ million and $¥ 1,931$ million at March 31, 2006 and 2007 respectively, were pledged as collateral by a financial subsidiary for certain loans.

At March 31, 2006, $¥ 205,573$ million of commercial paper borrowings were classified as long-term, as it is the respective finance subsidiary's intention to refinance them on a long-term basis and it has established the necessary credit facilities to do so. During fiscal year 2007, management decided not to classify the commercial paper as long term since management has no intention of refinancing them on a long-term basis. The weighted average interest rate on commercial paper at March 31, 2006 was approximately $4.32 \%$.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Medium-term notes are unsecured, and their interest rates range from $0.63 \%$ to $4.66 \%$ at March 31, 2006 and from $0.77 \%$ to $5.38 \%$ at March 31, 2007.

The following schedule shows the maturities of long-term debt for each of the five years following March 31, 2007 and thereafter:

| Years ending March 31: | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |
| :---: | :---: |
| 2008 | $¥ 775,409$ |
| 2009 | 888,650 |
| 2010 | 485,705 |
| 2011 | 317,979 |
| 2012 | 186,726 |
| After five years | 26,683 |
|  | 1,905,743 |
| Total | $\underline{\underline{¥ 2,681,152}}$ |

Certain of the Company's subsidiaries have entered into currency swap and interest rate swap agreements for hedging currency and interest rate exposures resulting from the issuance of long-term debt. Fair value of contracts related to currency swaps and interest rate swaps is included in other assets/liabilities and/or other current assets/liabilities in the consolidated balance sheets, as appropriate (see note 15). Unless a right of setoff exists, the offsetting of assets and liabilities is not made in the consolidated balance sheets.

At March 31, 2007, Honda had unused line of credit facilities amounting to $¥ 1,127,722$ million, of which $¥ 390,278$ million related to commercial paper programs and $¥ 737,444$ million related to medium-term notes programs. Honda is authorized to obtain financing at prevailing interest rates under these programs.

At March 31, 2007, Honda also had committed lines of credit amounting to $¥ 840,889$ million, none of which was in use. The committed lines are used to back up the commercial paper programs. Borrowings under those committed lines of credit generally are available at the prime interest rate.

As is customary in Japan, both short-term and long-term bank loans are made under general agreements which provide that security and guarantees for present and future indebtedness will be given upon request of the bank, and that the bank shall have the right to offset cash deposits against obligations that have become due or, in the event of default, against all obligations due to the bank. Certain debenture trust agreements provide that Honda must give additional security upon request of the trustee.

## (9) Other Liabilities

Other liabilities at March 31, 2006 and 2007 are summarized as follows:

|  | $\underset{\text { (millions) }}{\text { Yen }}$ |  |  |
| :---: | :---: | :---: | :---: |
|  | 2006* |  | 2007 |
| Accrued liabilities for product warranty, excluding current portion | $¥ 137,503$ | ¥ | 153,409 |
| Additional minimum pension liabilities (note 12) | 171,773 |  | - |
| Pension and other postretirement benefits (note 12) | 117,286 |  | 524,457 |
| Deferred income taxes | 406,727 |  | 316,048 |
| Other | 212,234 |  | 243,798 |
|  | $\underline{¥ 1,045,523}$ |  | ,237,712 |

[^7]
## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## (10) Income Taxes

Total income taxes for each of the years in the three-year period ended March 31, 2007 were allocated as follows:

|  |  | $\underset{\text { Yen }}{\text { (millions) }}$ |  |
| :---: | :---: | :---: | :---: |
|  | 2005 | 2006 | 2007 |
| Income from continuing operations | ¥266,665 | $¥ 317,189$ | ¥283,846 |
| Other comprehensive income (note 14) | 12,718 | 154,370 | 935 |
|  | ¥279,383 | ¥471,559 | ¥284,781 |

Income before income taxes and equity in income of affiliates by domestic and foreign source and income tax expense (benefit) for each of the years in the three-year period ended March 31, 2007 consisted of the following:

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |  |  |
| :---: | :---: | :---: | :---: | :---: |
|  | Income before income taxes | Income taxes |  |  |
|  |  | Current | Deferred | Total |
| 2005*: |  |  |  |  |
| Japanese | ¥148,860 | ¥ 57,066 | $\geq 24,134$ | ¥ 81,200 |
| Foreign | 519,504 | 94,080 | 91,385 | 185,465 |
|  | ¥668,364 | $¥ 151,146$ | $¥ 115,519$ | $¥ 266,665$ |
| 2006*: |  |  |  |  |
| Japanese | $¥ 317,997$ | ¥103,697 | $¥ 38,225$ | $¥ 141,922$ |
| Foreign | 511,907 | 216,248 | $(40,981)$ | 175,267 |
|  | ¥829,904 | ¥319,945 | $\geq$ ¥ $(2,756)$ | ¥317,189 |
| 2007: |  |  |  |  |
| Japanese | ¥182,433 | ¥ 89,155 | $\geq(13,798)$ | $¥ 75,357$ |
| Foreign | 610,435 | 211,139 | $(2,650)$ | 208,489 |
|  | $\stackrel{\text { ¥792,868 }}{\underline{\underline{0}}}$ | $\stackrel{\text { ¥300,294 }}{\underline{\underline{0}}}$ | $\underline{\underline{¥(16,448)}}$ | $\underline{\underline{¥ 283,846}}$ |

[^8]The statutory income tax rate is approximately $40 \%$ for each of the years in the three-year period ended March 31, 2007. The foreign subsidiaries are subject to taxes based on income at rates ranging from $16 \%$ to $40 \%$.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

The effective tax rate for Honda for each of the years in the three-year period ended March 31, 2007 differs from the Japanese statutory income tax rate for the following reasons:

|  | 2005 | 2006 | 2007 |
| :---: | :---: | :---: | :---: |
| Statutory income tax rate | 40.0\% | 40.0\% | 40.0\% |
| Valuation allowance provided for current year operating losses of subsidiaries | 0.5 | 0.3 | 0.4 |
| Difference in statutory tax rates of foreign subsidiaries | (1.9) | (2.3) | (3.7) |
| Reversal of valuation allowance due to utilization of operating loss carryforwards | (1.1) | (0.8) | (0.2) |
| Research and development credit | (2.3) | (3.0) | (3.3) |
| Tax authority assessment relating to prior years * | 1.8 | - | - |
| Other adjustments relating to prior years | - | 3.1 | - |
| Other | 2.9 | 0.9 | 2.6 |
| Effective tax rate | 39.9\% | 38.2\% | 35.8\% |

* The prior year income taxes in 2005 are due to assessment by the Japanese tax authorities as a result of their transfer pricing audit relating to the Company's motorcycle business in Brazil.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at March 31, 2006 and 2007 are presented below:

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |
| :---: | :---: | :---: |
|  | 2006 | 2007 |
| Deferred tax assets: |  |  |
| Inventories | $¥ 30,012$ | $\geq 35,114$ |
| Allowance for dealers and customers | 141,141 | 153,328 |
| Accrued bonus | 35,968 | 40,628 |
| Property, plant and equipment | 17,817 | 61,409 |
| Foreign tax credit | 9,267 | 10,427 |
| Operating loss carryforwards | 75,131 | 39,781 |
| Minimum pension liabilities adjustment | 68,566 | - |
| Pension and other postretirement benefits | 62,829 | 210,378 |
| Other | 121,951 | 141,104 |
| Total gross deferred tax assets | 562,682 | 692,169 |
| Less valuation allowance | 70,239 | 35,447 |
| Net deferred tax assets | 492,443 | 656,722 |
| Deferred tax liabilities: |  |  |
| Inventories | $(11,018)$ | $(13,650)$ |
| Prepaid pension expenses | $(29,019)$ | $(34,422)$ |
| Property, plant and equipment, excluding lease transactions | $(67,263)$ | $(59,680)$ |
| Lease transactions | $(357,578)$ | $(405,516)$ |
| Undistributed earnings of subsidiaries and affiliates | $(81,675)$ | $(106,273)$ |
| Net unrealized gains on marketable securities | $(44,580)$ | $(41,039)$ |
| Other | $(52,059)$ | $(27,262)$ |
| Total gross deferred tax liabilities | $(643,192)$ | $(687,842)$ |
| Net deferred tax (liability) asset | $\underline{¥(150,749)}$ | $\geq(31,120)$ |

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Deferred income tax assets and liabilities at March 31, 2006 and 2007 are reflected in the consolidated balance sheets under the following captions:

|  | $\underset{\text { Yen }}{\text { (millions) }}$ |  |
| :---: | :---: | :---: |
|  | 2006* | 2007 |
| Current assets-Deferred income taxes | ¥ 221,294 | $\geq 215,172$ |
| Other assets | 37,686 | 71,583 |
| Other current liabilities | $(3,002)$ | $(1,827)$ |
| Other liabilities | $(406,727)$ | $(316,048)$ |
| Net deferred tax (liability) asset | $\geq(150,749)$ | $\geq(31,120)$ |

## * See note 2.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income over the periods in which those temporary differences become deductible and operating loss carryforwards utilized. Management considered the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods which the deferred tax assets are deductible, management believes it is more likely than not that Honda will realize the benefits of these deductible differences and operating loss carryforwards, net of the existing valuation allowances at March 31, 2006 and 2007. The net change in the total valuation allowance for the years ended March 31, 2005 was decrease of $¥ 11,989$ million, for the year ended March 31, 2006 was increase of $¥ 10,502$ million, and for the year ended March 31,2007 was decrease of $¥ 34,792$ million. The valuation allowance primarily relates to deferred tax assets associated with net operating loss carryforwards incurred by certain foreign subsidiaries.

At March 31, 2007, certain of the Company's subsidiaries have operating loss carryforwards for income tax purposes of $¥ 128,162$ million, which are available to offset future taxable income, if any. Periods available to offset future taxable income vary in each tax jurisdiction and range from one year to an indefinite period as follows:

|  | $\underset{\text { Yen }}{\text { (millions) }}$ |
| :---: | :---: |
| Within 1 year | $¥ \quad 528$ |
| 1 to 5 years | 10,599 |
| 5 to 15 years | 11,947 |
| Indefinite periods | 105,088 |
|  | ¥128,162 |

At March 31, 2006 and 2007, Honda did not recognize deferred tax liabilities of $¥ 60,703$ million and $¥ 78,252$ million, respectively, for certain portions of the undistributed earnings of the Company’s foreign subsidiaries because such portions were considered permanently reinvested. At March 31, 2006 and 2007, the undistributed earnings not subject to deferred tax liabilities were $¥ 2,676,892$ million and $¥ 2,995,170$ million, respectively.

## (11) Dividends and Legal Reserves

The Company law of Japan enforced on May 1, 2006 provides that earnings in an amount equal to $10 \%$ of dividends of retained earnings shall be appropriated as a capital surplus or a legal reserve on the date of

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

distribution of retained earnings until an aggregated amount of capital surplus and a legal reserve equals $25 \%$ of stated capital. The Japanese Commercial Code, effective until the enforcement of the Company law of Japan, provided that earnings in an amount equal to at least $10 \%$ of appropriations of retained earnings that were paid in cash shall be appropriated as a legal reserve until an aggregated amount of capital surplus and the legal reserve equaled $25 \%$ of stated capital. Certain foreign subsidiaries are also required to appropriate their earnings to legal reserves under the laws of the respective countries.

Dividends and appropriations to the legal reserves charged to retained earnings during the years in the threeyear period ended March 31, 2007 represent dividends paid out during those years and the related appropriations to the legal reserves. Dividends per share for each of the years in the three-year period ended March 31, 2007 were $¥ 25.5, ¥ 38.5$ and $¥ 77$, respectively. The accompanying consolidated financial statements do not include any provision for the dividend of $¥ 20$ per share aggregating $¥ 36,456$ million proposed and resolved in the general stockholders' meeting held in June 2007.

The Company executed a two-for-one stock split for the Company's common stock effective July 1, 2006. Information pertaining to dividends per share has been adjusted retroactively for all periods presented to reflect this stock split.

## (12) Pension and Other Postretirement Benefits

The Company and its subsidiaries have various pension plans covering substantially all of their employees in Japan and certain employees in foreign countries. Benefits under the plans are primarily based on the combination of years of service and compensation. The funding policy is to make periodic contributions as required by applicable regulations. Plan assets consist primarily of listed equity securities and bonds.

Retirement benefits for directors, excluding certain benefits, are provided in accordance with management policy. There are occasions where officers other than directors receive special lump-sum payments at retirement. Such payments are charged to income as paid since amounts vary with circumstances and it is impractical to compute a liability for future payments.

In January 2003, the Emerging Issues Task Force (EITF) reached a final consensus on Issue No. 03-2 "Accounting for the Transfer to the Japanese Government of the Substitutional Portion of Employee Pension Fund Liabilities" ("EITF 03-2"). EITF 03-2 addresses accounting for a transfer to the Japanese government of a substitutional portion of an Employees' Pension Fund ("EPF") plan, which is a defined benefit pension plan established under the Welfare Pension Insurance Law. EITF 03-2 requires employers to account for the separation process of the substitutional portion from the entire EPF plan (which includes a corporation portion) upon completion of the transfer to the government of the substitutional portion of the benefit obligation and related plan assets. The separation process is considered the culmination of a series of steps in a single settlement transaction. Under this approach, the difference between the fair value of the obligation and the assets required to be transferred to the government should be accounted for and separately disclosed as a subsidy.

As stipulated in the Japanese Welfare Pension Insurance Law, the "Honda Employees' Pension Fund (a confederated welfare pension fund, the "Fund")", of which the Company and a part of its domestic subsidiaries and affiliates accounted for under the equity method were members, has obtained approval from the Japanese Minister of Health, Labor and Welfare for exemption from benefits obligations related to past employee service with respect to the substitutional portion of the Fund on July 1, 2005 and completed its transfer on March 9, 2006. Previously on April 1, 2004, the Company received approval of exemption from the obligation for benefits related to future employee services with respect to the fund. As a result, the Company recognized a gain of $¥ 228,681$ million, which is the difference between the settled accumulated benefit obligation and the assets

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

transferred to the government; a gain of $¥ 56,448$ million for the derecognition of previous accrued salary progression; and settlement loss of $¥ 147,113$ million for the related unrecognized loss. Collectively, the Company recognized a net gain of $¥ 138,016$ million for the fiscal year ended March 31, 2006.

The Company and its consolidated subsidiaries adopted SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - an amendment of FASB Statements No. 87, 88, 106, and 132(R)" on March 31, 2007, recognized its overfunded or underfunded status as an asset or liability in its consolidated balance sheets.

The incremental effect of applying SFAS No. 158 at March 31, 2007, on balance sheet items is as follows:

|  | Yen (millions) |  |  |
| :---: | :---: | :---: | :---: |
|  | Before Application of SFAS158 | Adjustments | After <br> Application of SFAS 158 |
| Other assets | $¥ 575,851$ | ¥ 11,347 | $¥ 587,198$ |
| Total assets | 12,025,153 | 11,347 | 12,036,500 |
| Accrued expenses | 847,008 | $(39,667)$ | 807,341 |
| Total current liabilities | 4,327,194 | $(39,667)$ | 4,287,527 |
| Other liabilities | 1,047,374 | 190,338 | 1,237,712 |
| Total liabilities | 7,280,311 | 150,671 | 7,430,982 |
| Accumulated other comprehensive loss, net | $(287,842)$ | $(139,324)$ | $(427,166)$ |
| Total stockholder's equity | 4,621,935 | $(139,324)$ | 4,482,611 |

The incremental effect of applying SFAS No. 158 on Accumulated other comprehensive loss, net, includes tax effect of $¥ 72,881$ million.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Reconciliations of beginning and ending balances of the pension benefit obligations and the fair value of the plan assets are as follows:


## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Pension expense for each of the years in the three-year period ended March 31, 2007 included the following:
$\left.\begin{array}{lllllll} & & & \\ \text { Yen } \\ \text { (millions) }\end{array}\right]$

The estimated actuarial loss (gain), net transition obligation and prior service benefit for all domestic defined pension plans that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are $¥ 14,290$ million, $¥ 1,741$ million and $¥ 7,289$ million, respectively. And the estimated actuarial loss (gain), net transition obligation and prior service cost for all foreign defined pension plans that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are $¥ 4,341$ millions, $¥ 41$ million and $¥ 772$ million, respectively.

Weighted-average assumptions used to determine benefit obligation at March 31, 2006 and 2007 were as follows:

|  | 2006 | 2007 |
| :---: | :---: | :---: |
| Japanese plans: |  |  |
| Discount rate | 2.0\% | 2.0\% |
| Rate of salary increase | 2.2\% | 2.3\% |
| Foreign plans: |  |  |
| Discount rate | 4.9 ~ 5.8\% | $5.2 \sim 6.0 \%$ |
| Rate of salary increase | $3.5 \sim 5.2 \%$ | $2.9 \sim 6.4 \%$ |

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Weighted-average assumptions used to determine net periodic benefit cost for each of the years in the threeyear period ended March 31, 2007 were as follows:

|  | 2005 | 2006 | 2007 |
| :---: | :---: | :---: | :---: |
| Japanese plans: |  |  |  |
| Discount rate | 2.0\% | 2.0\% | 2.0\% |
| Rate of salary increase | 2.3\% | 2.3\% | 2.2\% |
| Expected long-term rate of return | 4.0\% | 4.0\% | 4.0\% |
| Foreign plans: |  |  |  |
| Discount rate | $5.8 \sim 6.8 \%$ | $5.4 \sim 6.3 \%$ | $4.9 \sim 5.8 \%$ |
| Rate of salary increase | $3.5 \sim 6.7 \%$ | $3.5 \sim 6.7 \%$ | $3.5 \sim 5.2 \%$ |
| Expected long-term rate of return | $6.8 \sim 8.5 \%$ | $6.8 \sim 8.0 \%$ | 6.8~8.0\% |

Honda determines the expected long-term rate of return based on the expected long-term return of the various asset categories. Honda considers the current expectations for future returns and the actual historical returns of each plan asset category.

## Measurement date

Honda uses a March 31 measurement date for their plans excluding certain foreign subsidiaries which use a December 31 measurement date for their plans.

## Plan Assets

Honda's domestic and foreign pension plan weighted-average asset allocations at March 31, 2006 and 2007, by asset category are as follows:

|  | 2006 | 2007 |
| :---: | :---: | :---: |
| Japanese plans: |  |  |
| Equity securities | 48\% | 43\% |
| Debt securities | 37\% | 36\% |
| Other | 15\% | 21\% |
|  | 100\% | 100\% |
| Foreign plans: |  |  |
| Equity securities | 65\% | 70\% |
| Debt securities | 24\% | 27\% |
| Other | 11\% | 3\% |
|  | 100\% | 100\% |

Honda investment policies for the domestic and foreign pension benefit are designed to maximize total returns that are available to provide future payments of pension benefits to eligible participants under accepted risks. Honda sets target assets allocations for the individual asset categories based on the estimated returns and risks in the long future. Plan assets are invested in individual equity and debt securities using the target assets allocation.

## Obligations

The accumulated benefit obligations for all domestic defined benefit plans at March 31, 2006 and 2007 were $¥ 1,019,764$ million and $¥ 1,088,890$ million, respectively. The accumulated benefit obligations for all foreign defined benefit plans at March 31, 2006 and 2007 were $¥ 303,509$ million and $¥ 340,527$ million, respectively.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## Cash flows

Honda expects to contribute $¥ 33,953$ million to its domestic pension plans and $¥ 37,187$ million to its foreign pension plans in the year ending March 31, 2008.

## Estimated future benefit Payment

The following table presents estimated future gross benefit payments:

|  | $\underset{\text { Yen }}{\text { (millions) }}$ |  |
| :---: | :---: | :---: |
|  | Japanese plans | Foreign plans |
| 2008 | $¥ 40,130$ | $\geq 4,540$ |
| 2009 | 42,885 | 5,138 |
| 2010 | 45,546 | 6,144 |
| 2011 | 43,660 | 7,178 |
| 2012 | 45,339 | 8,582 |
| 2013-2017 | 250,746 | 74,946 |

Certain of the Company's subsidiaries in North America provide certain health care and life insurance benefits to retired employees. Such benefits have no material effect on Honda's financial position and results of operations.

## (13) Supplemental Disclosures of Cash Flow Information

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |  |
| :---: | :---: | :---: | :---: |
|  | 2005 | 2006 | 2007 |
| Cash paid during the year for: |  |  |  |
| Interest | ¥ 99,475 | ¥134,609 | ¥187,268 |
| Income taxes | 159,041 | 282,986 | 351,225 |

During the fiscal year ended March 31, 2005, the Company retired shares totaling 46,000,000 shares at a cost of $¥ 216,371$ million by offsetting with capital surplus of $¥ 190$ million and unappropriated retained earnings of $¥ 216,181$ million based on the resolution of board of directors.

During the year ended March 31, 2006, the Company reissued certain of its treasury stock at fair value of $¥ 802$ million to the minority shareholder of subsidiary, which the Company made a wholly owned subsidiary, and the Company retired shares totaling $11,000,000$ shares at a cost of $¥ 66,224$ million by offsetting with capital surplus of $¥ 2$ million and unappropriated retained earnings of $¥ 66,221$ million based on the resolution of board of directors.

During the year ended March 31, 2007, the Company reissued certain of its treasury stock at fair value of $¥ 18,521$ million to the outside shareholder of affiliates to obtain $100 \%$ share of these companies.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## (14) Accumulated Other Comprehensive Income (Loss)

The components and related changes in accumulated other comprehensive income (loss) for each of the years in the three-year period ended March 31, 2007 are as follows:

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |  |
| :---: | :---: | :---: | :---: |
|  | 2005 | 2006 | 2007 |
| Adjustments from foreign currency translation: |  |  |  |
| Balance at beginning of year | $¥(665,413)$ | ¥ $(624,937)$ | $¥(375,777)$ |
| Adjustments for the year | 40,476 | 249,160 | 96,775 |
| Balance at end of year | $(624,937)$ | $(375,777)$ | $(279,002)$ |
| Net unrealized gains on marketable securities: |  |  |  |
| Balance at beginning of year | 36,066 | 33,744 | 62,710 |
| Reclassification adjustments for realized (gain) loss on marketable |  |  |  |
| Increase (decrease) in net unrealized gains on marketable securities | $(3,668)$ | 29,807 | 1,004 |
| Balance at end of year | 33,744 | 62,710 | 58,139 |
| Net unrealized gains (losses) on derivative instruments: |  |  |  |
| Balance at beginning of year | - | - | (64) |
| Reclassification adjustments for realized (gain) loss on derivative |  |  |  |
| instruments | - | (38) | 421 |
| Increase (decrease) in net unrealized gains on derivative instruments | - | (26) | (337) |
| Balance at end of year | - | (64) | 20 |
| Minimum pension liabilities adjustment: |  |  |  |
| Balance at beginning of year | $(225,226)$ | $(202,741)$ | $(94,056)$ |
| Cumulative effect of adjustments resulting from the adoption of SAB |  |  |  |
| No. 108, net of tax (note 1(u)) | - | - | 18,149 |
| Adjusted balances at beginning of year | $(225,226)$ | $(202,741)$ | $(75,907)$ |
| Adjustments for the year | 22,485 | 108,685 | 8,908 |
| Adjustment for initially applying SFAS No. 158, net of tax (note 12) | - | - | 66,999 |
| Balance at end of year | $(202,741)$ | $(94,056)$ | - |
| Pension and other postretirement benefits adjustment |  |  |  |
| Adjustment for initially applying SFAS No. 158, net of tax (note 12) | - | - | $(206,323)$ |
| Balance at end of year | - | - | (206,323) |
| Total accumulated other comprehensive income (loss): |  |  |  |
| Balance at beginning of year | $(854,573)$ | $(793,934)$ | $(407,187)$ |
| Cumulative effect of adjustments resulting from the adoption of SAB No. 108, net of tax (note 1(u)) | - | - | 18,149 |
| Adjusted balances at beginning of year | $(854,573)$ | $(793,934)$ | $(389,038)$ |
| Adjustments for the year | 60,639 | 386,747 | 101,196 |
| Adjustment for initially applying SFAS No. 158, net of tax (note 12) | - | - | $(139,324)$ |
| Balance at end of year | $\underline{¥(793,934)}$ | $¥(407,187)$ | $¥(427,166)$ |

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

The tax effects allocated to each component of other comprehensive income (loss) and reclassification adjustments are as follows:

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |  |
| :---: | :---: | :---: | :---: |
|  | Before-tax amount | Tax (expense) or benefit (note 10) | Net-of-tax amount |
| 2005: |  |  |  |
| Adjustments from foreign currency translation . . | ¥ 39,469 | $¥ 1,007$ | $¥ 40,476$ |
| Unrealized gains (losses) on marketable securities: |  |  |  |
| Unrealized holding gains (losses) arising during the year | $(6,104)$ | 2,436 | $(3,668)$ |
| Reclassification adjustments for losses (gains) realized in net income | 2,114 | (768) | 1,346 |
| Net unrealized gains (losses) | $(3,990)$ | 1,668 | $(2,322)$ |
| Minimum pension liabilities adjustment | 37,878 | $(15,393)$ | 22,485 |
| Other comprehensive income (loss) | ¥ 73,357 | $\ddagger(12,718)$ | $¥ 60,639$ |
| 2006: |  |  |  |
| Adjustments from foreign currency translation . . | $¥ 301,737$ | $¥(52,577)$ | $\geq 249,160$ |
| Unrealized gains (losses) on marketable securities: |  |  |  |
| Unrealized holding gains (losses) arising during the year | 49,675 | $(19,868)$ | 29,807 |
| Reclassification adjustments for losses (gains) realized in net income | $(1,395)$ | 554 | (841) |
| Net unrealized gains (losses) | 48,280 | $(19,314)$ | 28,966 |
| Unrealized gains (losses) on derivative instruments |  |  |  |
| Unrealized holding gains (losses) arising during the year | (43) | 17 | (26) |
| Reclassification adjustments for losses (gains) realized in net income | $¥ \quad(64)$ | 26 | (38) |
| Net unrealized gains (losses) | (107) | 43 | (64) |
| Minimum pension liabilities adjustment | 191,207 | $(82,522)$ | 108,685 |
| Other comprehensive income (loss) | 541,117 | $¥(154,370)$ | $¥ 386,747$ |
| 2007: |  |  |  |
| Adjustments from foreign currency translation . . | ¥ 95,275 | $¥ \quad 1,500$ | $¥ 96,775$ |
| Unrealized gains (losses) on marketable securities: |  |  |  |
| Unrealized holding gains (losses) arising during the year | 1,408 | (404) | 1,004 |
| Reclassification adjustments for losses (gains) realized in net income | $(9,520)$ | 3,945 | $(5,575)$ |
| Net unrealized gains (losses) | $(8,112)$ | 3,541 | $(4,571)$ |
| Unrealized gains (losses) on derivative instruments |  |  |  |
| Unrealized holding gains (losses) arising during the year | (562) | 225 | (337) |
| Reclassification adjustments for losses (gains) realized in net income | 703 | (282) | 421 |
| Net unrealized gains (losses) | 141 | (57) | 84 |
| Minimum pension liabilities adjustment | 14,827 | $(5,919)$ | 8,908 |
| Other comprehensive income (loss) | ¥102,131 | $\pm$ (935) | ¥101,196 |

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## (15) Fair Value of Financial Instruments

The estimated fair values of significant financial instruments at March 31, 2006 and 2007 are as follows:

|  | $\underset{\text { (millions) }}{\text { Yen }}$ |  |  |  |
| :---: | :---: | :---: | :---: | :---: |
|  | 2006 |  | 2007 |  |
|  | Carrying amount | Estimated fair value | Carrying amount | Estimated fair value |
| Finance subsidiaries-receivables (a) | $¥ 2,843,819$ | $¥ 2,813,023$ | $¥ 3,434,721$ | $¥ 3,444,144$ |
| Marketable securities | 172,385 | 172,385 | 210,598 | 210,598 |
| Held-to-maturity securities | 43,767 | 43,428 | 16,337 | 16,348 |
| Convertible preferred stocks |  |  |  |  |
| Host contracts | 8,943 | 8,943 | - | - |
| Embedded derivatives | 13,991 | 13,991 | - | - |
|  | 22,934 | 22,934 | - | - |
| Convertible notes (b) |  |  |  |  |
| Host contracts | 8,156 | 8,156 | - | - |
| Embedded derivatives | 48,479 | 48,479 | - | - |
| Debt | $\begin{array}{r} 56,635 \\ (3,230,202) \end{array}$ | $\begin{array}{r} 56,635 \\ (3,237,471) \end{array}$ | (3,947, - ${ }^{\text {220 }}$ ) | $(3,960, \overline{743})$ |
| Foreign exchange instruments (c) |  |  |  |  |
| Asset position . . . . . . . . . . | $\geq$ 4,477 | $\geq \quad 4,477$ | $\geq \quad 3,735$ | $\geq \quad 3,735$ |
| Liability position | $(35,979)$ | $(35,979)$ | $(24,783)$ | $(24,783)$ |
| Net | $\geq$ (31,502) | $\geq$ (31,502) | $¥ \quad(21,048)$ | $\geq{ }^{¥}(21,048)$ |
| Interest rate instruments (d) |  |  |  |  |
| Asset position | ¥ 36,334 | ¥ 36,334 | $¥ \quad 10,866$ | $\geq 10,866$ |
| Liability position | (2) | (2) | $(2,417)$ | $(2,417)$ |
| Net | ¥ 36,332 | ¥ 36,332 | $\pm$$¥ \quad 8,449$ | ¥ 8,449 |

(a) The carrying amounts of finance subsidiaries-receivables at March 31, 2006 and 2007 in the table exclude $¥ 1,996,686$ million and $¥ 1,709,978$ million of direct financing leases, net, classified as finance subsidiariesreceivables in the consolidated balance sheets, respectively. The carrying amounts of finance subsidiariesreceivables at March 31, 2006 and 2007 in the table also include $¥ 627,168$ million and $¥ 678,649$ million of finance receivables classified as trade receivables and other assets in the consolidated balance sheets.
(b) A subsidiary had a forward sale contract in relation to a portion of the above convertible notes. The carrying amount and estimated fair value of the derivative financial instrument as of March 31, 2006 is $¥ 5,462$ million, asset position. In the year ended March 31, 2007, the subsidiary exercised the forward sale contract, and there was no balance of the derivative financial instrument as of March 31, 2007.
(c) The fair values of foreign currency forward exchange contracts, foreign currency option contracts and foreign currency swap agreements are included in other liabilities and other current assets/liabilities in the consolidated balance sheets as follows (see note 8 ):

|  | $\begin{aligned} & \text { Yen } \\ & \text { (millions) } \end{aligned}$ |  |
| :---: | :---: | :---: |
|  | 2006 | 2007 |
| Other current assets | $¥ 4,477$ | $¥ 3,735$ |
| Other current liabilities | $(35,113)$ | $(24,783)$ |
| Other liabilities | (866) | - |
|  | $\ddagger(31,502)$ | $¥(21,048)$ |

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

(d) The fair values of interest rate swap agreements are included in other assets/liabilities and other current assets/liabilities in the consolidated balance sheets as follows (see note 8):

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |
| :---: | :---: | :---: |
|  | 2006 | 2007 |
| Other current assets | $¥ 3,101$ | $¥ 3,890$ |
| Other assets | 33,233 | 6,976 |
| Other current liabilities | - | $(2,417)$ |
| Other liabilities | (2) | - |
|  | $\underline{¥ 36,332}$ | $\underline{¥ 8,449}$ |

The estimated fair values have been determined using relevant market information and appropriate valuation methodologies. However, these estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. The effect of using different assumptions and/or estimation methodologies may be significant to the estimated fair values.

The methodologies and assumptions used to estimate the fair values of financial instruments are as follows:

## Cash and cash equivalents, trade receivables and trade payables

The carrying amounts approximate fair values because of the short maturity of these instruments.

## Finance subsidiaries-receivables

The fair values of retail receivables and term loans to dealers were estimated by discounting future cash flows using the current rates for these instruments of similar remaining maturities. Given the short maturities of wholesale receivables, the carrying amount of such receivables approximates fair value. The fair value of the retained interest in the sold pools of finance receivables were estimated by calculating the present value of the future cash flows using a discount rate commensurate with the risks involved.

## Marketable securities

The fair value of marketable securities was estimated using quoted market prices.

## Held-to-maturity securities

The fair value of held-to-maturity security was estimated using quoted market prices.

## Convertible notes and convertible preferred stock investment

Convertible instruments were bifurcated into two portions for accounting purposes. The note and preferred stock portions of these convertible instruments were treated as available-for-sale and were marked-to-market through other comprehensive income (loss). The fair value was determined based on an analysis of interest rate movements and an assessment of credit worthiness. The embedded derivative was marked-to-market through the statement of income and fair value was estimated using a trinomial convertible bond pricing model.

## Debt

The fair values of bonds and notes were estimated based on the quoted market prices for the same or similar issues. The fair value of long-term loans was estimated by discounting future cash flows using rates currently available for loans of similar terms and remaining maturities. The carrying amounts of short-term bank loans and commercial paper approximate fair values because of the short maturity of these instruments.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## Foreign exchange and interest rate instruments

The fair values of foreign currency forward exchange contracts and foreign currency option contracts were estimated by obtaining quotes from banks. The fair values of currency swap agreements and interest rate swap agreements were estimated by discounting future cash flows using rates currently available for these instruments of similar terms and remaining maturities.

## (16) Risk Management Activities and Derivative Financial Instruments

Honda is a party to derivative financial instruments in the normal course of business to reduce their exposure to fluctuations in foreign exchange rates and interest rates. Currency swap agreements are used to convert long-term debt denominated in a certain currency to long-term debt denominated in other currencies. Foreign currency forward exchange contracts and purchased option contracts are normally used to hedge sale commitments denominated in foreign currencies (principally U.S. dollars). Foreign currency written option contracts are entered into in combination with purchased option contracts to offset premium amounts to be paid for purchased option contracts. Interest rate swap agreements are mainly used to convert floating rate financing, such as commercial paper, to (normally three-five years) fixed rate financing in order to match financing costs with income from finance receivables. These instruments involve, to varying degrees, elements of credit, exchange rate and interest rate risks in excess of the amount recognized in the consolidated balance sheets.

The aforementioned instruments contain an element of risk in the event the counterparties are unable to meet the terms of the agreements. However, Honda minimizes the risk exposure by limiting the counterparties to major international banks and financial institutions meeting established credit guidelines. Management of Honda does not expect any counterparty to default on its obligations and, therefore, does not expect to incur any losses due to counterparty default. Honda generally does not require or place collateral for these financial instruments.

Foreign currency forward contracts and currency swap agreements are agreements to exchange different currencies at a specified rate on a specific future date. Foreign currency option contracts are contracts that allow the holder of the option the right but not the obligation to exchange different currencies at a specified rate on a specific future date. Foreign currency forward exchange contracts, foreign currency option contracts and currency swap agreements outstanding at March 31,2006 were $¥ 898,125$ million, $¥ 176,548$ million and $¥ 584,358$ million, respectively and totaled $¥ 1,659,031$ million. At March 31, 2007, foreign currency forward exchange contracts, foreign currency option contracts and currency swap agreements outstanding were $¥ 978,994$ million, $¥ 5,793$ million and $¥ 608,534$ million, respectively and totaled $¥ 1,593,321$ million.

## Cash flow hedge

The Company applies hedge accounting for certain foreign currency forward exchange contracts related to forecasted foreign currency transactions between the Company and its subsidiaries. Changes in the fair value of derivative financial instruments designated as cash flow hedges are recognized in other comprehensive income (loss). The amounts are reclassified into earnings in the same period when forecasted hedged transactions affect earnings. The amount recognized in accumulated other comprehensive income (loss) was $¥ 64$ million loss in the fiscal year ended March 31, 2006 and $¥ 20$ million gain in the fiscal year ended March 31, 2007, respectively. All amounts recorded in accumulated other comprehensive income (loss) as year-end are expected to be recognized in earnings within the next twelve months. The period that hedges the changes in cash flows related to the risk of foreign currency rate is at most around two months.

There are no derivative financial instruments where hedge accounting has been discontinued due to the forecasted transaction no longer being probable. The Company excludes financial instruments' time value component from the assessment of hedge effectiveness, of which amount was $¥ 421$ million loss for the year

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

ended March 31,2006 , and $¥ 1,187$ million loss for the year ended March 31,2007 , respectively. There are no derivative financial instruments that have been assessed as being ineffectiveness.

## Derivative financial instruments not designated as accounting hedges

Changes in the fair value of derivative financial instruments not designated as accounting hedges are recognized in earnings in the period of the change.

Interest rate swap agreements generally involve the exchange of fixed and floating rate interest payment obligations without the exchange of the underlying principal amount. At March 31, 2006 and 2007, the notional principal amounts of interest rate swap agreements were $¥ 3,857,748$ million and $¥ 4,198,463$ million, respectively.

## (17) Commitments and Contingent Liabilities

At March 31, 2007, Honda had commitments for purchases of property, plant and equipment of approximately $¥ 78,027$ million.

Honda has entered into various guarantee and indemnification agreements. At March 31, 2006 and 2007, Honda has guaranteed $¥ 46,737$ million and $¥ 41,151$ million of bank loan of employees for their housing costs, respectively. If an employee defaults on his/her loan payments, Honda is required to perform under the guarantee. The undiscounted maximum amount of Honda's obligation to make future payments in the event of defaults is $¥ 46,737$ million and $¥ 41,151$ million, respectively, at March 31, 2006 and 2007. At March 31, 2007, no amount has been accrued for any estimated losses under the obligations, as it is probable that the employees will be able to make all scheduled payments.

Honda warrants its vehicles for specific periods of time. Product warranties vary depending upon the nature of the product, the geographic location of its sale and other factors.

The changes in provisions for those product warranties for each of the years in the two-year period ended March 31, 2007 are as follow:

|  | $\begin{aligned} & \text { Yen } \\ & \text { (millions) } \end{aligned}$ |  |
| :---: | :---: | :---: |
|  | 2006 | 2007 |
| Balance at beginning of year | $¥ 268,429$ | $¥ 283,947$ |
| Warranty claims paid during the period | $(126,834)$ | $(113,454)$ |
| Liabilities accrued for warranties issued during the period | 125,732 | 143,280 |
| Changes in liabilities for pre-existing warranties during the period | 332 | 605 |
| Foreign currency translation | 16,288 | 2,725 |
|  | $¥ 283,947$ | ¥ 317,103 |

With respect to product liability, personal injury claims or lawsuits, Honda believes that any judgment that may be recovered by any plaintiff for general and special damages and court costs will be adequately covered by Honda's insurance and reserves. Punitive damages are claimed in certain of these lawsuits. Honda is also subject to potential liability under other various lawsuits and claims. In accordance with Statement of Financial Accounting Standards (SFAS) No. 5, "Accounting for Contingencies", Honda has recorded a contingent liability when it is probable that an obligation has been incurred and the amount of loss can be reasonably estimated.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Honda reviews these pending lawsuits and claims periodically and adjusts the amounts recorded for these contingent liabilities, if necessary, by considering the nature of lawsuits and claims, the progress of the case and the opinions of legal counsel. Honda does not record liabilities for lawsuits or potential claims that it believes will not result in an unfavorable outcome or when a reasonable estimate of the amount of probable loss cannot be determined. After consultation with legal counsel, and taking into account all known factors pertaining to existing lawsuits and claims, Honda believes that the ultimate outcome of such lawsuits and pending claims should not result in liability to Honda that would be likely to have an adverse material effect on its consolidated financial position, results of operations or cash flows.

## (18) Leases

Honda is the lessee under several operating leases, primarily for office and other facilities, and certain office equipment.

Future minimum lease payments under noncancelable operating leases that have initial or remaining lease terms in excess of one year at March 31, 2007 are as follows:

| Years ending March 31: | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |
| :---: | :---: |
| 2008 | $¥ 25,354$ |
| 2009 | 19,349 |
| 2010 | 15,354 |
| 2011 | 12,752 |
| 2012 | 10,791 |
| After five years | 45,378 |
| Total minimum lease payments | ¥128,978 |

Rental expenses under operating leases for each of the years in the three-year period ended March 31, 2007 were $¥ 44,619$ million, $¥ 46,102$ million and $¥ 46,910$ million, respectively.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## (19) Allowances for Trade Receivable and Finance Subsidiaries-receivables

The allowances for trade receivable and finance subsidiaries-receivables for the years ended March 31, 2005, 2006 and 2007 are set forth in the following table:

March 31, 2005:
Trade accounts and notes receivable


Finance subsidiaries-receivables

| Allowance for credit losses | $¥ 24,411$ | $¥ 33,365$ | $¥ 27,575$ | $¥ 725$ | $¥ 30,926$ |
| :---: | :---: | :---: | :---: | :---: | :---: |
| Allowance for losses on lease residual values | 26,124 | 17,273 | 10,156 | 784 | 34,025 |
|  | $¥ 50,535$ | ¥50,638 | $¥ 37,731$ | $¥ 1,509$ | $¥ 64,951$ |

March 31, 2006:
Trade accounts and notes receivable
Allowance for doubtful accounts $\ldots \ldots . \quad \xlongequal{¥ 9,710} \quad \xlongequal{¥ 3,825} \quad \xlongequal{¥ 3,320} \quad \xlongequal{¥ 474} \quad \xlongequal{¥ 10,689}$

Finance subsidiaries-receivables
Allowance for credit losses $\ldots \ldots \ldots \ldots$
Allowance for losses on lease residual

| values | 34,025 | 7,998 | 7,974 | 3,725 | 37,774 |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  | $¥ 64,951$ | ¥36,153 | $¥ 37,347$ | ¥6,967 | $¥ 70,724$ |

March 31, 2007:
Trade accounts and notes receivable
Allowance for doubtful accounts $\ldots \ldots \ldots \quad \xlongequal{¥ 10,689} \quad \xlongequal{¥ 2,918} \quad \xlongequal{¥ 5,850} \quad \xlongequal{¥ 442} \quad \xlongequal{¥ 8,199}$

Finance subsidiaries-receivables

| Allowance for credit losses | $¥ 32,950$ | $¥ 27,286$ | $¥ 27,273$ |  | 549 | $¥ 33,512$ |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Allowance for losses on lease residual |  |  |  |  |  |  |
|  | $¥ 70,724$ | $¥ 44,128$ | $¥ 48,080$ | ¥ | 668 | $¥ 67,440$ |

## (20) Segment Information

Honda has four reportable segments: the Motorcycle business, the Automobile business, the Financial services business and the Power product and other businesses, which are based on Honda's organizational structure and characteristics of products and services. Operating segments are defined as components of Honda's about which separate financial information is available that is evaluated regularly by management in deciding how to allocate resources and in assessing performance. The accounting policies used for these reportable segments are consistent with the accounting policies used in Honda's consolidated financial statements.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

Principal products and functions of each segment are as follows:

| Segment | Principal products <br> and services | Functions |
| :--- | :--- | :--- |$|$| Motorcycle business | Motorcycles, all-terrain vehicles <br> (ATVs), personal watercrafts and <br> relevant parts | Research \& Development <br> Manufacturing <br> Sales and related services |
| :--- | :--- | :--- |
| Automobile business | Automobiles and relevant parts | Research \& Development <br> Manufacturing <br> Sales and related services |
| Financial services business | Financial, insurance services | Retail loan and lease related to Honda <br> products |
| Others |  |  |

## Segment Information

As of and for the year ended March 31, 2005

|  | Yen (millions) |  |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Motorcycle | Automobile Business |  | Financial Services Business | Power Product and Other Businesses | Segment Total | Reconciling Items | Consolidated |
| Net sales and other operating revenue: |  |  |  |  |  |  |  |  |
| External customers | $¥ 1,097,754$ | $¥ 6,963,635$ | ¥ | 255,741 | $¥ 332,975$ | $¥ 8,650,105$ | - | $¥ 8,650,105$ |
| Intersegment | - | - | $\underline{\square}$ | 3,447 | $\geq$ ¥ 9,869 | $\pm 13,316$ | $\underline{\geq(13,316)}$ |  |
| Total | $¥ 1,097,754$ | $¥ 6,963,635$ | $¥$ | 259,188 | $¥ 342,844$ | $¥ 8,663,421$ | ¥ $(13,316)$ | $¥ 8,650,105$ |
| Cost of sales, |  |  |  |  |  |  |  |  |
| SG\&A and R\&D expenses | $\underline{¥ 1,028,422}$ | $\underline{¥ 6,511,253}$ | $\underline{\square}$ | 169,287 | ¥323,539 | $\underline{¥ 8,032,501}$ | $\underline{¥(13,316)}$ | $¥ 8,019,185$ |
| Gain on transfer of the substitutional portion of the Employee's Pension Funds |  |  |  |  |  |  |  |  |
| Segment income | ¥ 69,332 | ¥ 452,382 | $\underline{\square}$ | 89,901 | ¥ 19,305 | ¥ 630,920 | - | $¥$ 630,920 |
| Equity in income of affiliates | ¥ 29,921 | $¥ 65,183$ |  | - | ¥ 953 | ¥ 96,057 | - | $¥ 96,057$ |
| Assets | ¥ 848,671 | $¥ 4,265,636$ |  | ,333,605 | $¥ 261,843$ | ¥9,709,755 | $¥(341,519)$ | ¥9,368,236 |
| Investments in affiliates | $\geq 79,143$ | $\geq 249,876$ |  | - | $\geq 17,279$ | $\geq 346,298$ | - | $\geq 346,298$ |
| Depreciation and amortization | ¥ 28,606 | ¥ 189,150 | ¥ | 419 | ¥ 7,577 | ¥ 225,752 | - | ¥ 225,752 |
| Capital expenditures | $\geq 41,845$ | $\geq 317,271$ | $¥$ | 1,941 | $\geq 12,923$ | $\geq 373,980$ | - | $\geq 373,980$ |
| Provision for credit and lease residual losses on finance subsidiaries- receivables | - | - |  | 50,638 | - | ¥ 50,638 | - | $¥ 50,638$ |

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## As of and for the year ended March 31, 2006



## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

Notes to Consolidated Financial Statements-(Continued)
As of and for the year ended March 31, 2007


## Explanatory notes:

1. Segment income is measured in a consistent manner with consolidated operating income, which is net income before other income, other expenses, income tax (benefit) expense, minority interest in income, and equity in income of affiliates. Expenses not directly associated with specific segments are allocated based on the most reasonable measures applicable.
2. Assets of each segment are defined as total assets, including derivative financial instruments, investments in affiliates, and deferred tax assets. Segment assets are based on those directly associated with each segment and those not directly associated with specific segments are allocated based on the most reasonable measures applicable except for the corporate assets described below.
3. Intersegment sales and revenues are generally made at values that approximate arm's-length prices.
4. Unallocated corporate assets, included in reconciling items, amounted to $¥ 464,504$ million as of March 31, 2005, $¥ 354,903$ million as of March 31, 2006, and $¥ 377,873$ million as of March 31, 2007 respectively, which consist primarily of cash and cash equivalents and marketable securities held by the Company. Reconciling items also include elimination of intersegment transactions.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

5. Depreciation and amortization of Financial Services Business include $¥ 9,741$ million of depreciation of property on operating leases for the year ended March 31, 2007.
6. Capital expenditure of Financial Services Business includes $¥ 366,795$ million of purchase of operating lease assets for the year ended March 31, 2007.

External Sales and Other Operating Revenue by Product or Service Groups

|  | Yen (millions) |  |  |
| :---: | :---: | :---: | :---: |
|  | $\begin{gathered} \text { March } 31, \\ 2005 \end{gathered}$ | $\begin{gathered} \text { March 31, } \\ 2006 \end{gathered}$ | $\begin{gathered} \text { March 31, } \\ 2007 \end{gathered}$ |
| Motorcycles and relevant parts | $¥ 933,740$ | $¥ 1,051,855$ | $¥ 1,221,638$ |
| All-terrain vehicles (ATVs), perso relevant parts | ¥ 164,014 | ¥ 173,957 | ¥ 148,979 |
| Automobiles and relevant parts | ¥6,963,635 | $¥ 8,004,694$ | ¥ 8,889,080 |
| Financial, insurance services | ¥ 255,741 | $¥ 306,869$ | $¥ 409,701$ |
| Power products and relevant parts | ¥ 229,760 | $¥ 263,651$ | ¥ 287,302 |
| Others | $\geq 103,215$ | $¥ 106,970$ | $¥ 130,440$ |
| Total | $\underline{¥ 8,650,105}$ | ¥9,907,996 | ¥11,087,140 |

## Geographical Information

As of and for the year ended March 31, 2005

|  | Yen (millions) |  |  |  |
| :---: | :---: | :---: | :---: | :---: |
|  | Japan | United States | Other Countries | Total |
| Sales to external customers | ¥1,983,182 | $¥ 4,138,049$ | $¥ 2,528,874$ | $¥ 8,650,105$ |
| Long-lived assets | $¥$ 894,065 | $¥ 428,467$ | $¥ 360,680$ | $¥ 1,683,212$ |

## As of and for the year ended March 31, 2006

|  | Yen (millions) |  |  |  |
| :---: | :---: | :---: | :---: | :---: |
|  | Japan | United States | Others Countries | Total |
| Sales to external customers | ¥2,021,999 | $¥ 4,876,436$ | ¥3,009,561 | ¥9,907,996 |
| Long-lived assets | ¥ 949,713 | $\geq 499,599$ | $¥ 487,208$ | $¥ 1,936,520$ |

## As of and for the year ended March 31, 2007

|  | Yen (millions) |  |  |  |
| :---: | :---: | :---: | :---: | :---: |
|  | Japan | United States | Others Countries | Total |
| Sales to external customers | ¥2,061,720 | ¥5,291,683 | $¥ 3,733,737$ | $¥ 11,087,140$ |
| Long-lived assets | $¥$ 993,078 | $¥$ 929,107 | $¥ 619,544$ | ¥ 2,541,729 |

The above information is based on the location of the Company and its subsidiaries.

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## Supplemental Geographical Information

In addition to the disclosure required by U.S.GAAP, Honda provides the following supplemental information as required by Japanese Securities and Exchange Law:
(1) Overseas sales and revenues based on the location of the customer

|  | Yen (millions) |  |  |
| :---: | :---: | :---: | :---: |
|  | $\begin{gathered} \text { March 31, } \\ 2005 \end{gathered}$ | $\begin{gathered} \text { March 31, } \\ 2006 \end{gathered}$ | $\begin{gathered} \text { March } 31, \\ 2007 \end{gathered}$ |
| North America | ¥4,575,076 | ¥5,463,359 | $¥ 5,980,876$ |
| Europe | $¥ 870,795$ | $¥ 1,009,421$ | $¥ 1,236,757$ |
| Asia | $¥$ 977,011 | $¥ 1,085,451$ | $¥ 1,283,154$ |
| Other regions | $¥ 528,018$ | $¥ 655,721$ | ¥ 905,163 |

Explanatory notes:
Major countries or regions in each geographic area:

| North America | United States, Canada, Mexico |
| :--- | :--- |
| Europe | United Kingdom, Germany, France, Italy, Belgium |
| Asia | Thailand, Indonesia, China, India |
| Other Regions | Brazil, Australia |

(2) Supplemental geographical information based on the location of the Company and its subsidiaries

As of and for the year ended March 31, 2005

|  | Yen (millions) |  |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Japan | North America | Europe | Asia | Other Regions | Total | Reconciling Items | $\underline{\text { Consolidated }}$ |
| Net sales and other operating revenue: |  |  |  |  |  |  |  |  |
| External customers | $¥ 1,983,182$ | $¥ 4,585,650$ | $¥ 858,936$ | $¥ 773,753$ | $¥ 448,584$ | $\geq 8,650,105$ | - | $¥ 8,650,105$ |
| Transfers between geographic areas | ¥2,155,756 | $\geq 119,904$ | ¥ 184,136 | ¥ 86,810 | ¥ 17,373 | $\ddagger$ ¥ 2,563,979 | $\underline{¥}(2,563,979)$ |  |
| Total | $¥ 4,138,938$ | $¥ 4,705,554$ | $¥ 1,043,072$ | $¥ 860,563$ | $¥ 465,957$ | $¥ 11,214,084$ | $¥(2,563,979)$ | $¥ 8,650,105$ |
| Cost of sales, |  |  |  |  |  |  |  |  |
| SG\&A and R\&D expenses | ¥3,954,039 | $¥ 4,384,400$ | $¥ 1,001,829$ | ¥799,871 | $¥ 432,764$ | ¥10,572,903 | $\geq(2,553,718)$ | ¥8,019,185 |
| Gain on transfer of the substitutional portion of the Employees' Pension Funds . | - | - | - | - | - | - | - | - |
| Operating income | $\geq 184,899$ | $\geq 321,154$ | ¥ 41,243 | ¥ 60,692 | $\geq 33,193$ | $\geq$ 641,181 | $\geq \quad(10,261)$ | $\geq$ 630,920 |
| Assets | $¥ 2,480,052$ | $¥ 5,254,246$ | $\ddagger$ 649,547 | $¥ 541,331$ | ¥203,605 | $¥ 9,128,781$ | $¥ 239,455$ | ¥9,368,236 |
| Long-lived assets | $\ddagger 894,065$ | $¥ 502,284$ | $¥ 118,339$ | $¥ 121,095$ | $¥ 47,429$ | $¥$ 1,683,212 | - | $¥ 1,683,212$ |

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## As of and for the year ended March 31, 2006

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |  |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Japan | North America | Europe |  | Asia | Other Regions | Total | Reconciling Items | Consolidated |
| Net sales and other operating revenue: |  |  |  |  |  |  |  |  |  |
| External customers | $¥ 2,021,999$ | $¥ 5,475,261$ | $¥ 1,001,177$ | $¥$ | 856,892 | $¥ 552,667$ | ¥ 9,907,996 | - | $¥ 9,907,996$ |
| Transfers between geographic areas | ¥2,415,874 | $\pm 141,064$ | $\underline{¥ 188,341}$ | $\geq$ | 140,501 | ¥ 19,023 | $\underline{¥ 2,904,803}$ | $\underline{¥(2,904,803)}$ | - |
| Total | $¥ 4,437,873$ | $¥ 5,616,325$ | $¥ 1,189,518$ | $¥$ | 997,393 | $¥ 571,690$ | $¥ 12,812,799$ | $¥(2,904,803)$ | $¥ 9,907,996$ |
| Cost of sales, SG\&A and R\&D expenses | $\underline{¥ 4,204,939}$ | $¥ 5,262,382$ | $\underline{¥ 1,163,213}$ | $\geq$ | 932,394 | $\underline{¥ 514,527}$ | $\underline{¥ 12,077,455}$ | $\underline{¥(2,900,348)}$ | $\geq 9,177,107$ |
| Gain on transfer of the substitutional portion of the Employees' Pension Funds | $\ddagger 138,016$ | - | - |  | - | - | ¥ 138,016 | - | $¥ 138,016$ |
| Operating income | $\ddagger 370,950$ | $¥ 353,943$ | $¥ \quad 26,305$ | ¥ | 64,999 | $\ddagger 57,163$ | $\ddagger 873,360$ | $¥ \quad(4,455)$ | $¥ \quad 868,905$ |
| Assets | ¥2,695,212 | $¥ 6,128,303$ | $¥ 800,786$ | $¥$ | 717,933 | $¥ 309,209$ | $¥ 10,651,443$ | $¥ \quad(20,043)$ | $¥ 10,631,400$ |
| Long-lived assets | $¥ 949,713$ | $¥ 589,596$ | $\ddagger 157,819$ | $\pm$ | 167,148 | $¥ 72,244$ | $\ddagger 1,936,520$ | - | $¥ 1,936,520$ |

As of and for the year ended March 31, 2007

|  | $\begin{gathered} \text { Yen } \\ \text { (millions) } \end{gathered}$ |  |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Japan | North America | Europe | Asia | Other Regions | Total | Reconciling Items | Consolidated |
| Net sales and other operating revenue: |  |  |  |  |  |  |  |  |
| External customers | $¥ 2,061,720$ | $¥ 6,002,797$ | $¥ 1,228,564$ | $¥ 1,024,680$ | ¥769,379 | $¥ 11,087,140$ | - | $¥ 11,087,140$ |
| Transfers between geographic areas | ¥2,712,403 | $\underline{¥ 169,847}$ | $\underline{¥ 119,161}$ | $\ddagger$ 246,723 | $\underline{¥} 28,259$ | $\underline{¥ 3,276,393}$ | $\underline{¥(3,276,393)}$ |  |
| Total | $¥ 4,774,123$ | $¥ 6,172,644$ | $¥ 1,347,725$ | $¥ 1,271,403$ | ¥797,638 | $¥ 14,363,533$ | $¥(3,276,393)$ | $¥ 11,087,140$ |
| Cost of sales, SG\&A and R\&D expenses | $¥ 44,545,988$ | $\underline{¥ 5,715,817}$ | $\underline{¥ 1,315,736}$ | $\underline{¥ 1,194,250}$ | $\underline{¥ 725,377}$ | $\underline{¥ 13,497,168}$ | $\underline{¥(3,261,907)}$ | $\underline{¥ 10,235,261}$ |
| Gain on transfer of the substitutional portion of the Employees' Pension Funds |  |  |  |  |  |  |  |  |
| Operating income | $¥ 228,135$ | $¥ 456,827$ | $¥ \quad 31,989$ | $¥ \quad 77,153$ | ¥ 72,261 | ¥ 866,365 | $¥ \quad(14,486)$ | $¥ \quad 851,879$ |
| Assets | $¥ 2,985,123$ | $¥ 6,834,409$ | $¥ 948,922$ | $¥$ 935,963 | $¥ 414,147$ | $¥ 12,118,564$ | $¥ \quad(82,064)$ | $¥ 12,036,500$ |
| Long-lived assets | ¥ 993,078 | $¥ 1,028,132$ | ¥ 198,232 | $¥$ 228,802 | ¥ 93,485 | ¥ 2,541,729 | - | $¥ 2,541,729$ |

Explanatory notes:

1. Major countries or regions in each geographic area:

| North America | United States, Canada, Mexico |
| :--- | :--- |
| Europe | United Kingdom, Germany, France, Italy, Belgium |
| Asia | Thailand, Indonesia, China, India |
| Other Regions | Brazil, Australia |

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

2. Operating income of each geographical region is measured in a consistent manner with consolidated operating income, which is net income before other income, other expenses, income tax (benefit) expense, minority interest in income, and equity in income of affiliates.
3. Assets of each geographical region are defined as total assets, including derivative financial instruments, investments in affiliates, and deferred tax assets.
4. Sales and revenues between geographic areas are generally made at values that approximate arm's-length prices.
5. Unallocated corporate assets, included in reconciling items, amounted to $¥ 464,504$ million as of March 31 , 2005, $¥ 354,903$ million as of March 31, 2006, and $¥ 377,873$ million as of March 31, 2007 respectively, which consist primarily of cash and cash equivalents and marketable securities held by the Company. Reconciling items also include elimination of transactions between geographic areas.

## (21) Subsequent Event

The Board of Directors, at its meeting held on May 15, 2007, resolved that the Company will purchase its own shares pursuant to Article 156 of the Company Law, which applies pursuant to Article 165, Paragraph 3, of that law. The main purpose for the acquisition are enhancing its capital efficiency and enabling greater flexibility in its capital policies.
(1) Type of shares and maximum number of shares to be acquired:

Shares of Common Stock 10,000,000 shares
(2) Maximum amount of acquisition:

38 billion yen
(3) Period of acquisition:

Starting on May 16, 2007 and ending on June 12, 2007
(4) Method of acquisition:

Purchase through ToSTNet-2 (as a closing-price transaction) over the Tokyo Stock Exchange
Total number and amount of shares the Company acquired during the period were $8,204,000$ shares and $34,128,640,000$ yen .

## HONDA MOTOR CO., LTD. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements-(Continued)

## (22) Selected Quarterly Financial Data (Unaudited) *

Quarterly financial data for the years ended March 31, 2006 and 2007 are set forth in the following table:

|  | Yen (millions) |  |  | Yen |
| :---: | :---: | :---: | :---: | :---: |
|  | Net sales and other operating revenue | Operating Income | Net income | Basic net income per common share |
| Year ended March 31, 2005 : |  |  |  |  |
| First quarter | ¥ 2,073,153 | ¥159,993 | $¥ 114,262$ | $¥ 60.82$ |
| Second quarter | 2,093,578 | 172,932 | 127,122 | 67.85 |
| Third quarter | 2,133,820 | 157,636 | 150,760 | 80.89 |
| Fourth quarter | 2,349,554 | 140,359 | 94,053 | 50.71 |
|  | $¥$ ¥ $8,650,105$ | $¥ 630,920$ | $¥ 486,197$ | $¥ 260.34$ |
| Year ended March 31, 2006: |  |  |  |  |
| First quarter | $\geq 2,264,579$ | ¥170,393 | $¥ 110,666$ | ¥ 59.87 |
| Second quarter | 2,337,670 | 162,694 | 133,708 | 72.45 |
| Third quarter | 2,472,006 | 194,986 | 133,146 | 72.41 |
| Fourth quarter | 2,833,741 | 340,832 | 219,513 | 119.89 |
|  | $\underline{¥ 9,907,996}$ | ¥868,905 | $\underline{¥ 597,033}$ | $¥ 324.33$ |
| Year ended March 31, 2007: |  |  |  |  |
| First quarter | $¥ 2,599,724$ | $¥ 203,521$ | $¥ 143,402$ | $¥ 78.46$ |
| Second quarter | 2,630,874 | 193,024 | 127,909 | 70.05 |
| Third quarter | 2,768,652 | 205,110 | 144,827 | 79.45 |
| Fourth quarter | 3,087,890 | 250,224 | 176,184 | 96.70 |
|  | $¥ 11,087,140$ | $¥ 851,879$ | $¥ 592,322$ | $¥ 324.62$ |

[^9] public accounting firm.

## Signatures

Pursuant to the requirements of Section 12 of the Securities Exchange Act of 1934, the Registrant certifies that it meets all of the requirements for the filing of Form $20-\mathrm{F}$ and has duly caused this annual report to be signed on its behalf by the undersigned, thereunto duly authorized.

HONDA GIKEN KOGYO
KABUSHIKI KAISHA
(HONDA MOTOR CO., LTD.)

## By: <br> $\qquad$

Takeo Fukui
President and Representative Director

Date: July 18, 2007
Tokyo, Japan

## INDEX OF EXHIBITS

1.1 Articles of Incorporation of the registrant (English translation)
1.2 Share Handling Regulations of the registrant (English translation)
1.3 Regulations of Board of Directors of the registrant (English translation)
1.4 Regulations of the Board of Corporate Auditors of the registrant (English translation)
2.1 Specimen common stock certificates of the registrant (English translation) (1)
2.2 Deposit Agreement dated as of December 19, 1962, as amended and restated as of October 1, 1982 (including changes from Amendment to Deposit Agreement dated as of April 1, 1989) among the registrant, Morgan Guaranty Trust Company of New York (now JP Morgan Chase Bank), as Depositary, and all owners and holders from time to time of American Depositary Receipts and European Depositary Receipts, including the form of American Depositary Receipt (2)
2.3 Form of Amendment No. 2 to Deposit Agreement dated as of April, 1995, among the parties referred to in Exhibit 2.2 above (2)
2.4 Form of Amendment No. 3 to Deposit Agreement dated as of January, 2002, among the parties referred to in Exhibit 2.2 above (3)
2.5 Form of Amendment No. 4 to Deposit Agreement dated as of June, 2006 among the parties referred to in Exhibit 2.2 above (4)
2.6 Form of Amendment No. 5 to Deposit Agreement dated as of June, 2007 among the parties referred to in Exhibit 2.2 above (5)
8.1 List of Significant Subsidiaries (See "Organizational Structure" in Item 4.C. of this Form 20-F)
11.1 Code of Ethics (6)
12.1 Certification of the principal executive officer required by 17 C.F.R. 240. 13a-14(a)
12.2 Certification of the principal executive officer required by 17 C.F.R. 240. 13a-14(a)
13.1 Certification of the chief executive officer required by 18 U.S.C. Section 1350
13.2 Certification of the chief financial officer required by 18 U.S.C. Section 1350
(1) Incorporated by reference to the registrant's annual report on Form 20-F filed on September 27, 2001.
(2) Incorporated by reference to the Registration Statement on Form F-6 (File No. 33-91842) filed on May 1, 1995.
(3) Incorporated by reference to the Registration Statement on Form F-6 (File No. 333-14228) filed on December 20, 2001.
(4) Incorporated by reference to the Registration Statement on Form F-6 (File No. 333-114874) filed on June 28, 2006.
(5) Incorporated by reference to the Registration Statement on Form F-6 (File No. 333-143589) filed on June 8, 2007.
(6) Incorporated by reference to the registrant's annual report on Form 20-F filed on July 9, 2004.

The Company has not included as exhibits certain instruments with respect to its long-term debt, the amount of debt authorized under each of which does not exceed $10 \%$ of its total assets, and it agrees to furnish a copy of any such instrument to the Securities and Exchange Commission upon request.
[Translation]

## ARTICLES OF INCORPORATION

As of June 22, 2007
HONDA MOTOR CO., LTD.

## Record of Resolutions of the General Meetings of Shareholders

1. September 8, 1948
2. September 24, 1948
3. November 14, 1949
4. July 1,1951
5. October 25, 1951
6. April 10, 1952
7. August 2, 1952
8. September 20, 1952
9. December 1, 1952
10. May 20, 1953
11. August 16, 1953
12. September 27, 1953
13. December 30, 1953
14. April 17, 1955
15. October 29, 1955
16. October 29, 1956
17. April 27, 1957
18. October 29, 1957
19. April 28, 1959
20. April 28, 1960
21. October 28, 1960
22. October 30, 1961
23. April 26, 1962
24. October 26, 1962
25. December 18, 1962
26. April 28, 1964
27. October 30, 1970
28. October 29, 1973
29. April 26, 1974
30. April 24, 1975
31. May 25, 1978
32. May 22, 1980
33. May 27, 1982
34. October 1, 1982
35. August 19, 1985
36. May 28, 1987
37. June 27, 1991
38. June 29, 1994
39. June 29, 1999
40. June 28, 2001
41. June 25, 2002
42. June 24, 2003
43. June 23, 2004
44. June 23, 2005
45. June 23, 2006
46. July 1, 2006
47. June 22, 2007
(drafting for Incorporation)
(establishment)
(amendment)
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(amendment)
(amendment)
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## Chapter I. General Provisions

## Article 1. (Corporate name)

The Company is called Honda Giken Kogyo Kabushiki Kaisha, which is written in English as HONDA MOTOR CO., LTD.

## Article 2. (Objects)

The object of the Company shall be to carry on the following business:

1. Manufacture, sale, lease and repair of motor vehicles, ships and vessels, aircrafts and other transportation machinery and equipment.
2. Manufacture, sale, lease and repair of prime movers, agricultural machinery and appliances, generators, processing machinery and other general machinery and apparatus, electric machinery and apparatus and precision machinery and apparatus.
3. Manufacture and sale of fiber products, paper products, leather products, lumber products, rubber products, chemical industry products, ceramic products, metal products and other products.
4. Overland transportation business, marine transportation business, air transportation business, warehousing business, travel business and other transport business and communication business.
5. Sale of sporting goods, articles of clothing, stationary, daily sundries, pharmaceuticals, drink and foodstuffs and other goods.
6. Financial business, nonlife insurance agency business, life insurance agency business, construction business including building construction work and real estate business including real estate brokerage.
7. Publishing business, advertising business, translation business, interpretation business, management consultancy business, information services including information processing, information and communication and information provision, industrial planning and design, comprehensive security business and labor dispatch services.
8. Management of parking garages, driving schools, training and education facilities, racecourses, recreation grounds, sporting facilities, marina facilities, hotels, restaurants and other facilities.
9. Manufacture, sale and licensing of equipment, parts and supplies and all other relevant business activities and investments relating to each of the foregoing items.

## Article 3. (Location of head office)

The Company shall have its head office in Minato-ku, Tokyo.

## Article 4. (Governance components)

The Company shall have the following governance components as well as General Meetings of Shareholders and Directors, respectively.

1. Board of Directors
2. Corporate Auditors
3. Board of Corporate Auditors
4. Accounting Auditors

## Article 5. (Method of giving public notices)

The public notices of the Company shall be given by publication in the Nihon Keizai Shinbun published in Tokyo.

## Chapter II. Shares

## Article 6. (Total number of shares authorized to be issued by the Company)

The total number of shares authorized to be issued by the Company shall be $7,086,000,000$ shares.

## Article 7. (Issuance of shares)

The Company shall issue share certificates representing its issued shares.

## Article 8. (Number of shares constituting one voting unit, and non-issuance of share certificates representing less than one voting unit)

The number of shares constituting one voting unit in the Company consists of one hundred (100) shares.
Notwithstanding the preceding Article, the Company shall not issue any share certificates representing Shares Less Than One Voting Unit; provided, however, that this shall not apply to the matters otherwise provided for in the Share Handling Regulations.

## Article 9. (Request for sale of Shares Less Than One Voting Unit)

A shareholder of the Company (including a beneficial shareholder; the same applies hereinafter) may, in accordance with the provisions of the Share Handling Regulations, make a request to the effect that such number of shares should be sold to it that will, when added to the Shares Less Than One Voting Unit already held by that shareholder, constitute one voting unit of shares.

## Article 10. (Procedures relating to shares, etc.)

The denomination of the share certificates of the Company shall be provided for in the Share Handling Regulations established by the Board of Directors.

Entry of the name of the transferee of shares in the shareholders' register, purchase and request for sale of Shares Less Than One Voting Unit and other procedures and fees relating to shares shall be governed by the Share Handling Regulations established by the Board of Directors.

## Article 11. (Shareholders' Register Manager)

The Company shall have a Shareholders' Register Manager.
The Shareholders' Register Manager and its place of business shall be decided by resolution of the Board of Directors, and a public notice thereof shall be given.

Preparation and storage of the shareholders' register (which term shall also include the register of beneficial shareholders in this document) of the Company, the register of stock acquisition rights, and the register of lost share certificates and any other business relating to shares and stock acquisition rights shall be delegated to the Shareholders' Register Manager and not conducted by the Company.

## Article 12. (Record date)

The shareholders appearing or recorded on the shareholders' register as of the end of each business year shall be the shareholders entitled to exercise the rights of shareholders at the ordinary general meeting of shareholders for such business year.

If it is necessary in addition to the preceding paragraph, the shareholders or registered pledgees appearing or recorded on the shareholders' register as of a specific date of which advance public notice is given in accordance with the resolution of the Board of Directors may be deemed the shareholders or registered pledgees entitled to exercise the rights of shareholders or registered pledgees.

## Chapter III. General Meeting of Shareholders

## Article 13. (Time of convocation)

The ordinary general meeting of shareholders shall be convened within three months from the day following the end of each business year.

In addition to the above, an extraordinary general meeting of shareholders shall be convened whenever necessary.

## Article 14. (Persons to convene meeting)

Except as otherwise provided by laws or ordinances, a general meeting of shareholders shall be convened by the President and Director, based upon the resolution of the Board of Directors. If the President and Director is prevented from so doing, one of the other Directors in the order fixed in advance by the Board of Directors shall convene the meeting.

## Article 15. (Chairman)

Chairmanship of a general meeting of shareholders shall be assumed by the Chairman of the Board of Directors or the President and Director pursuant to a resolution made in advance by the Board of Directors. If both the Chairman of the Board of Directors and the President and Director are prevented from so doing, one of the other Directors shall do so in the order fixed in advance by the Board of Directors.

## Article 16. (Resolutions)

Except as otherwise provided by laws or ordinances or by the Articles of Incorporation, resolutions at a general meeting of shareholders shall be adopted by a majority vote of the shareholders present who are entitled to exercise their voting rights thereat.

The special resolution provided for in Article 309, Paragraph 2 of the Company Law shall be adopted by two-thirds or more of the votes of the shareholders present at a meeting, who must hold one-third or more of the voting rights of shareholders who are entitled to exercise their voting rights.

## Article 17. (Exercise of voting rights by proxy)

Any shareholder or the legal representative may delegate the power to exercise the voting rights to proxy, provided that such proxy shall be one shareholder of the Company who is entitled to voting rights. Such shareholder or proxy shall present to the Company a document evidencing the proxy's power of representation for each general meeting of shareholders.

## Article 18. (Minutes)

The minutes of general meetings of shareholders shall record the substance of the proceedings at the meetings, the results thereof and other matters as prescribed by laws or ordinances, and such minutes shall be kept on file for ten years at the head office of the Company and the certified copies thereof shall be kept on file for five years at each of the branches of the Company.

## Chapter IV. Directors and Board of Directors

## Article 19. (Number of Directors)

Directors of the Company shall be not more than thirty in number.

## Article 20. (Election of Directors)

Directors shall be elected by the resolution of a general meeting of shareholders. Resolution of such elections shall be adopted by a majority of the votes of the shareholders present, who must hold one-third or more of the votes of all shareholders who are entitled to exercise their voting rights. A resolution for the election of Directors shall not be made by cumulative voting.

## Article 21. (Term of Office)

The term of office of Directors shall expire at the close of the ordinary general meeting of shareholders relating to the business year ending within one year after their election to office.

## Article 22. (Directors with executive powers)

The Board of Directors shall appoint from among the Directors one President and Director and may appoint one Chairman of the Board of Directors, several Executive Vice Presidents and Directors, Senior Managing Directors and Managing Directors.

## Article 23. (Representative Directors)

The President and Director shall represent the Company.
In addition to the preceding paragraph, the Board of Directors shall appoint, pursuant to its resolutions, Directors who shall each represent the Company.

## Article 24. (Board of Directors)

Except as provided by laws or ordinances or by the Articles of Incorporation, matters relating to the Board of Directors shall be governed by the Regulations of the Board of Directors established by the Board of Directors.

## Article 25. (Notice of meetings of the Board of Directors)

Notice of convocation of a meeting of the Board of Directors shall be sent to each Director and Corporate Auditor three days prior to the date of the meeting, provided, however, that such period may be shortened in case of urgent necessity.

If the consent of all Directors and Corporate Auditors is obtained in advance, a meeting may be held without following the procedures for convening a meeting.

## Article 26. (Omission of the resolution of the Board of Directors)

The Company shall deem that there was a resolution of the Board of Directors, if the conditions of Article 370 of the Company Law are satisfied.

## Article 27. (Remuneration of Directors, etc.)

Remuneration, bonus, retirement allowance and other proprietary benefits provided by the Company as compensation for the duties of Directors shall be determined by resolution of a general meeting of shareholders.

## Chapter V. Corporate Auditors and Board of Corporate Auditors

## Article 28. (Number of Corporate Auditors)

Corporate Auditors of the Company shall be not more than seven in number.

## Article 29. (Election of Corporate Auditors)

Corporate Auditors shall be elected by resolution of a general meeting of shareholders. Resolution of such election shall be adopted by a majority of the votes of the shareholders present, who must hold one-third or more of the votes of shareholders who are entitled to exercise their voting rights.

## Article 30. (Term of Office of Corporate Auditors)

The term of office of Corporate Auditors shall expire at the close of the ordinary general meeting of shareholders relating to the last business year ending within four years after their election to office.

The term of office of a Corporate Auditor elected to fill the vacancy of a Corporate Auditor who resigned from his/her office before the expiration of his/her term shall expire at the time of expiration of the term of office of the retired Corporate Auditor.

## Article 31. (Board of Corporate Auditors)

Except as provided by laws or ordinances or by the Articles of Incorporation, matters relating to the Board of Corporate Auditors shall be governed by the Regulations of the Board of Corporate Auditors established by the Board of Corporate Auditors, provided, however, that such Regulations may not preclude the exercise of the power of any Corporate Auditor.

## Article 32. (Notice of Meetings of Board of Corporate Auditors)

Notice of convocation of a meeting of the Board of Corporate Auditors shall be sent to each Corporate Auditor three days prior to the date of the meeting, provided, however, that such period may be shortened in case of urgent necessity.

If the consent of all Corporate Auditors is obtained in advance, a meeting may be held without following the procedures for convening a meeting.

## Article 33. (Remuneration of Corporate Auditors, etc.)

Remuneration, bonus, retirement allowance and other proprietary benefits provided by the Company as compensation for the duties of Corporate Auditors shall be determined by resolution of a general meeting of shareholders.

## Chapter VI. Accounts

## Article 34. (Business year)

The business year of the Company shall commence on the first day of April each year and end on the last day of March the following year.

## Article 35. (Governance Component deciding dividends from surplus, etc.)

The Company may determine such matters which are described in each item in Paragraph 1, Article 459 of the Company Law by a resolution of the Board of Directors.

## Article 36. (Record date for dividend from surplus)

The record date for the dividends shall be June 30, September 30, December 31 and March 31 of each year.

In addition to the above, the Company may distribute dividends from surplus by determining any record date.

## Article 37. (Limitation period for dividend)

The Company shall be relieved of the obligation to pay dividend upon expiration of three full years from the day they became due and payable.
-End-
[Translation]

## SHARE HANDLING REGULATIONS

June 23, 2006
HONDA MOTOR CO., LTD.

## Record of Resolutions of the Meeting of the Board of Directors

April 27, 1953
December 30, 1953
April 27, 1957
April 28, 1960
December 1, 1962
March 31, 1967
August 19, 1968
February 28, 1972
December 19, 1977
May 28, 1981
October 1, 1982
November 14, 1991
October 1, 1999
April 1, 2000
May 12,2000
December 4, 2000
October 4, 2001
June 25,2002
April 1, 2003
June 24, 2003
June 23, 2004
January 31, 2006
May 16, 2006
June 23, 2006

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## SHARE HANDLING REGULATIONS

## CHAPTER I. GENERAL PROVISIONS

## Article 1. (Purpose)

These Regulations shall govern the denomination of share certificates of the Company and matters related to the handling of shares in accordance with the provisions of Articles 8, 9, and 10 of the Articles of Incorporation of the Company. Provided, however, that handling procedures with respect to the beneficial shareholders shall be governed by the Japan Securities Depository Center, Inc. (hereinafter referred to as the "Center") as well as these Regulations.

## Article 2. (Denomination of Share Certificates)

1. Share certificates to be issued by the Company shall be in denominations of ten thousand $(10,000)$, one thousand $(1,000)$, five hundred (500), and one hundred (100) shares. Share certificates representing less than one hundred (100) shares may also be issued.
2. Of the share certificates as described in the preceding paragraph, share certificates representing a number of shares less than one voting unit set forth in Article 8 of the Articles of Incorporation of the Company (hereinafter referred to as "Shares Less Than One Unit") shall not be issued except in the cases set forth in Articles 21 and 22 hereof.
3. Notwithstanding the provisions of Paragraph 1, with respect to the shares held in the name of the Center, the Company may issue share certificates representing a number of shares other than the denominations provided for in that Paragraph upon request by the Center.

Article 3. (Shareholders Register Manager ('Share Registrar"))
The share registrar of the Company, its place of business, its place of operations and forwarding offices shall be as follows:

Share registrar and its place of business:

Its place of operations:

Forwarding offices:

The Chuo Mitsui Trust and Banking Company, Limited. 33-1, Shiba 3-chome, Minato-ku, Tokyo

The Chuo Mitsui Trust and Banking Company, Limited. Securities Agency Department, Head Office 8-4, Izumi 2-chome, Suginami-ku, Tokyo
All branch offices in Japan of The Chuo Mitsui Trust and Banking Company, Limited, and Head Office and branch offices of Japan Securities Agency Corporation

## Article 4. (Method of Application, Offer and Notification, etc.)

1. Requests, offers, notifications and applications pursuant to these regulations and other requests, offers, notifications and applications with respect to business the Company has assigned to the share registrar shall be made to the share registrar.
2. Procedures stated in the preceding paragraph shall be made in the form prescribed by the Company, bearing the registered seal impression prescribed in the provisions set forth in Article 14 hereof.
3. If it is not possible to follow the procedures stated in the preceding paragraph, a document proving that the person in action legitimately bears the right to make such act shall be submitted to the Company.
4. If any procedure stated in the first paragraph is made by a proxy, a document proving his or her power of representation and, if such procedure requires consent of a guardian or assistant, a document proving such consent shall be submitted to the Company.

## CHAPTER II. REGISTRATION OF TRANSFER OF SHARES, ETC.

## Article 5. (Registration of Transfer of Shares)

1. In the case of an application for entry or record into shareholders register, an application in a written form shall be submitted together with the share certificates with the applicant's name entered thereon.
2. In the case of a shareholder making an application for registration of the transfer of shares acquired for any reasons other than assignment, submission of a document proving such acquisition may be required upon the request of the Company in addition to the procedures set out in the preceding paragraph.

## Article 6. (Registration of Transfer of Shares Otherwise Required by Laws and Regulations)

When procedures such as approval, permission, acquisition of consent from another person, etc. are required under laws or regulations with respect to the transfer of shares, an application in a written form shall be submitted together with the share certificates with the applicant's name entered thereon and a document proving the completion of such procedures.

## Article 7. (Entries in the Beneficial Shareholders' Register)

Entries in the beneficial shareholders' register shall be made in accordance with the notice from the Center concerning the beneficial shareholders and the beneficial shareholders' form.

## Article 8. (Beneficial Shareholder's Form)

Beneficial shareholders shall submit a beneficial shareholder's form through a Participant.

## Article 9. (Consolidation of the Shareholders' Register and Beneficial Shareholders' Register)

If a Shareholder entered in the shareholders' register is identified as the same person as a beneficial shareholder entered in the beneficial shareholders' register by way of his or her address and name, the number of shares entered in the shareholders' register and that entered in the beneficial shareholders' register shall be combined for the purposes of the execution of rights of that shareholder.

## CHAPTER III. PLEDGES AND SHARES HELD IN TRUST

## Article 10. (Registration or Cancellation of Pledges)

In the case of an application for registration, amendment or cancellation of the pledges on shares, an application in a written form jointly signed by the pledgor and pledgee shall be submitted together with the share certificates concerned with the pledgee's name entered thereon.

## Article 11. ( Recording or Cancellation of Shares Held on Trust)

In the case of an application for the recording or cancellation of shares held on trust an application in a written form shall be submitted by the trustor or the trustee together with the share certificates concerned.

## CHAPTER IV. OPTION NOT TO HOLD SHARE CERTIFICATES

## Article 12. (Notice of Intention not to Hold Share Certificates)

Any shareholder intending not to hold share certificates must submit a notice in a written form together with the share certificates concerned. Provided, however, that if the share certificates concerned have not been issued, such share certificates need not be submitted.

## Article 13. (Request for Issue of Share Certificates Which Shareholders have Intended not to Hold)

If a shareholder who has given a notice of intention not to hold share certificates requests issuance of such share certificates, an application in a written form to that effect shall be submitted by him or her. Provided, however, that any application for the issuance of share certificates for Shares Less Than One Unit may not be submitted in case that the Company intended not to issue share certificates in regard to Shares Less Than One Unit.

## CHAPTER V. NOTIFICATIONS

## Article 14. (Notification of Address, Name and Seal Impression of Shareholders)

1. Shareholders, beneficial shareholders and registered pledgees of shares or their statutory agents shall notify the Company of their addresses, names or trade names, and seal impressions. Provided, however, that non-Japanese may substitute their specimen signatures for seal impressions.
2. In case of any change in the matters notified as described in the preceding paragraph, notification to such effect shall be made.

## Article 15. (Notification of Agent for Shareholders Residing Abroad)

1. Shareholders, beneficial shareholders and registered pledgees of shares residing abroad or their statutory agents shall appoint a standing proxy in Japan and notify the Company thereof in addition to the procedures set forth in the preceding Article.
2. The provisions as described in Article 14 apply, mutatis mudandis, to the standing agent stated in the preceding paragraph.

## Article 16. (Representative of a Corporation)

1. If a shareholder, beneficial shareholder, or registered pledgee of shares, or a statutory agent thereof, is a corporation, notification of its representative shall be made.
2. In the case of any change of representative, a notification in a written form shall be submitted together with a certificate of registered matters in the commercial register.

## Article 17. (Representative of Joint Shareholders)

Shareholders and beneficial shareholders who jointly own shares must appoint one (1) representative and submit a notification in a written form jointly signed by all such co-owners. In case of any change of representative, the same procedure shall apply.

## Article 18. (Change to Information in the Shareholders' Register, the Beneficial Shareholders' Register or Matters Indicated on Share Certificates)

In the case of changes due to the reasons listed below which affect entries to the shareholders' register, beneficial shareholders' register or matters indicated on share certificates, a notification in a written form shall be submitted together with the share certificates concerned and documentation proving the relevant fact. Provided, however, that share certificates need not be submitted where they have not been issued or in the case of any change to the beneficial shareholders' register:

1. Change to family name or given name;
2. Appointment, change to, or removal of a person with parental authority, guardian or other statutory agent;
3. Change to trade name or corporate name; or
4. Change to the corporate organization.

## Article 19. (Exception in Regard to Notifications Made by Beneficial Shareholders)

Any notification to be made by a beneficial shareholder according to this chapter shall be made through a Participant. Provided, however, that where the change relates only to the registered seal impression, notification need not be made through a Participant.

## CHAPTER VI. REISSUANCE OF SHARE CERTIFICATES

## Article 20. (Reissuance Due to Split or Consolidation )

In the case of an application for the issue of new share certificates due to a split or consolidation of shares, an application in a written form shall be submitted together with the share certificates concerned.

## Article 21. (Reissuance Due to Mutilation or Defacement)

In the case of an application for the issue of new share certificates due to mutilation or defacement of share certificates, an application in a written form shall be submitted together with the share certificates concerned. Provided, however, that if the share certificates are stained or damaged to such an extent that it is difficult to ascertain their authenticity, the procedures set forth in Article 7 shall apply.

## Article 22. (Reissuance Due to Completed Column)

In the case that the column for entry of the names of shareholders on a share certificate has been completed to capacity, the Company shall take back such share certificate and issue a new share certificate.

## CHAPTER VII. REGISTRATION OF LOST SHARE CERTIFICATES

## Article 23. (Request to Register Lost Share Certificates)

Any person who requests the registration of a lost share certificate(s) shall submit a request form together with a document proving the acquisition of such certificate(s), a document proving the loss of such certificate(s), and proof of identification; provided, however, that if the person requesting the registration of the lost share certificate(s) is the registered holder of the shares relating to the lost share certificate(s) with respect to which the request is being made, such person need only submit a written document proving the loss of such share certificate(s).

## Article 24. (Application for Cancellation by Person Who Registered Lost Share Certificates)

If a person who registered lost share certificates applies to cancel the registration made under the preceding paragraph, that person shall submit an application form.

## Article 25. (Application of Cancellation by Bearer of Share Certificates)

When a person who possesses share certificates that have been registered as lost share certificate(s) is to apply for cancellation of that registration of lost share certificates, that person shall submit an application form together with share certificates and evidence of the identity of the applicant. However, if an application for cancellation is filed by a shareholder or registered pledgee of shares, evidence of the identity of the applicant is not required to be submitted.

## Article 26. (Mutatis Mutandis Application to Various Notifications)

In the case where any person who has registered a lost share certificate(s) is not a shareholder or registered pledgee of shares, and if such person desires to change the relevant entry or record in the register of lost share certificates, the provisions of Articles 14 through 18 shall apply mutatis mutandis.

## CHAPTER VIII. PURCHASE OF SHARES LESS THAN ONE UNIT

## Article 27. (Request for the Purchase of Shares Less Than One Unit)

1. In case of an application for the purchase of Shares Less Than One Unit, a request in a written form shall be submitted together with the share certificates concerned. Provided, however, that if the share certificates concerned have not been issued, such share certificates need not be submitted.
2. In the case of a beneficial shareholder requesting the purchase of Shares Less Than One Unit, such request shall be made through a Participant and the Center.

## Article 28. (Determination of Purchase Price)

In the case of a request stated in the preceding Article being made, the purchase price shall be obtained by multiplying the number of shares by the closing price per share of the Company in trading on the Tokyo Stock Exchange on the day on which the request reached the transfer agent's place of business for handling shares or forwarding offices as set out in Article 3 hereof. If there is no trading on that day, or if that day is a holiday of the Stock Exchange, the value per share taken will be that of the first trading price effected on any day subsequent to such day.

## Article 29. (Payment of Proceeds for Purchase)

1. The proceeds for purchase shall be paid to the shareholder who has requested the purchase of Shares Less Than One Unit without delay after four (4) business days from the day on which the purchase price was determined at the place of business for handling shares where the request was received, except for where the Company separately provides otherwise; provided, however, that if the proceeds for purchase is a price cum rights, such as one relating to dividends of surplus, stock split, and allotment of shares without consideration, the proceeds for purchase shall be paid by the relevant record date or allotment date.
2. At the time of paying the proceeds for purchase stated in the preceding paragraph, fees prescribed in Paragraph 3 of Article 40 shall be deducted.

## Article 30. (Transfer of Shares Purchased)

1. The title to Shares Less Than One Unit requested for purchase shall be transferred to the Company on the day on which the payment procedure of the proceeds for purchase was completed pursuant to the preceding Article. Provided, however, that in the case of a delay in receiving the proceeds by the shareholder who has requested the purchase of shares, the title to the Shares Less Than One Unit concerned shall be transferred to the Company on the day on which the Company makes a verbal notification or, in the case of delivering a reminder by mail, on the day when such mail is dispatched.
2. If it is established that the purchase price of Shares Less Than One Unit in respect of which the Company has received a request of purchase is a price cum rights, such as one relating to dividends of surplus, stock split, and allotment of shares without consideration, and the day on which shareholders entitled to execute such rights are determined passes without the purchase proceeds being received by the shareholder who requested purchase of the shares, the title to the shares concerned is deemed to be transferred to the Company at the close of business on that day, regardless of the provisions of the preceding paragraph.

## CHAPTER IX. REQUEST FOR SALE OF SHARES LESS THAN ONE UNIT

## Article 31. (Method of Requesting Sale of Shares Less Than One Unit)

1. When any shareholder or beneficial shareholder of Shares Less Than One Unit requests the sale of the number of Shares Less Than One Unit that will, when added to the Shares Less Than One Unit already held by that shareholder, constitute one unit of shares (such a request is hereinafter referred to as an "Additional Purchase Request"), such shareholder shall submit an Additional Purchase Request form together with the relevant share certificates and the estimated price for shares to be additionally purchased as set forth in the following Article; provided, however, that if the relevant share certificates have not been issued, such share certificates need not be submitted.
2. In the case of a beneficial shareholder making a request referred to in the preceding paragraph, such request shall be made through a Participant and the Center.

## Article 32. (Estimated Price for Shares to Be Additionally Purchased)

1. The estimated price for shares to be additionally purchased shall be the last price per share of the Company in trading on the Tokyo Stock Exchange on the business day immediately preceding the day on which the relevant Additional Purchase Request documents as set forth in the preceding paragraph reaches the share registrar's place of business or any of its forwarding offices as set forth in Article 3 (in the case where there is no trading effected on such business day, the last trading price effected on the day immediately preceding such business day) multiplied by the number of shares for which the application for additional purchase is made and multiplied further by 1.3 , and any fraction of such amount less than $¥ 1,000$ resulting from such calculation shall be rounded up to the nearest thousand yen.
2. The Company shall not process any Additional Purchase Request as set forth in the preceding Article if the estimated price submitted for shares to be additionally purchased is less than the amount provided for in the preceding paragraph.

## Article 33. (Additional Purchase Requests Exceeding the Balance of Treasury Shares)

If the total number of shares for which Additional Purchase Requests are made on the same day exceeds the number of the transferable treasury shares held by the Company (excluding those treasury shares held for specific purposes), any Additional Purchase Requests made on such day shall not be effective.

## Article 34. (Effective Date of Additional Purchase Requests)

An Additional Purchase Request shall become effective on the day on which both the relevant Additional Purchase Request documents as set forth in Article 31 and the estimated price for shares to be additionally purchased as set forth in Article 32 reach the share registrar's place of business for handling shares or forwarding office as set forth in Article 3.

## Article 35. (Periods during which Additional Purchase Requests are not Accepted)

1. The Company will suspend the acceptance of any Additional Purchase Requests during the period commencing on the 12th business day prior to March 31 and ending on March 31 and during the period commencing on the 12th business day prior to September 30 and ending on September 30.
2. Notwithstanding the provisions of the preceding paragraph, the Company may set other periods during which the acceptance of Additional Purchase Requests is suspended if the Company deems it necessary.

## Article 36. (Determination of the Price of Shares to be Additionally Purchased)

1. The price per share of shares to be additionally purchased shall be the last price per share of the Company in trading on the Tokyo Stock Exchange on the day on which the relevant Additional Purchase Request becomes effective. If there is no trading on such day or if such day is a holiday of the Stock Exchange, the price shall be that of the first traded price thereafter.
2. The price of shares to be additionally purchased shall be the price per share in accordance with the preceding paragraph multiplied by the number of shares for which the Additional Purchase Request has been made.
3. If the estimated price for shares to be additionally purchased as set forth in Article 32 is less than the total sum of the price for shares to be additionally purchased as set forth in the preceding paragraph and charges set forth in Article 40 (such sum is hereinafter referred to as "Additional Purchase Proceeds"), the amount of the shortfall shall be requested to be paid by the person who made the relevant Additional Purchase Request. In such case, if the shortfall is not paid within 5 business days from the day after payment is requested, such Additional Purchase Request will be cancelled.

## Article 37. (Receipt of Additional Purchase Proceeds)

1. The Company shall receive the Additional Purchase Proceeds from the estimated price for shares to be additionally purchased on a day to be specified by the Company which shall be within 6 business days from the date on which the price of the shares to be additionally purchased is determined or from the date on which the amount of the shortfall in accordance with paragraph 3 of the preceding Article is paid; provided, however, that if the price of shares to be additionally purchased is a price cum rights, such as one relating to dividends of surplus, stock split, or allotment of shares without consideration, the Additional Purchase Proceeds must be received by the relevant record date or allotment date.
2. After the Additional Purchase Proceeds as prescribed in the preceding paragraph has been deducted from the estimated price for shares to be additionally purchased, the balance shall be returned by bank transfer to a bank account specified by the shareholder who made the relevant Additional Purchase Request or by postal transfer cash payment.

## Article 38. (Transfer of Shares Additionally Purchased)

Treasury shares for which an Additional Purchase Request has been made shall be transferred to the shareholder or beneficial shareholder who made the Additional Purchase Request on the day on which the Additional Purchase Proceeds in accordance with the preceding Article is received in full.

## Article 39. (Delivery of Share Certificates)

For such shares that have come to constitute a number of shares equal to one unit due to any Additional Purchase Request, a share certificate shall, without delay, be issued and delivered to the shareholder who made the relevant Additional Purchase Request; provided, however, that this provision does not apply in the case where a beneficial shareholder made such Additional Purchase Request.

## CHAPTER X. FEES

## Article 40. (Fees)

1. When a shareholder receives share certificates pursuant to Article 13 (Request for Issue of Share Certificates Which Shareholders have Intended not to Hold), Article 20 (Reissuance Due to Split or Consolidation), or Article 21 (Reissuance Due to Mutilation or Defacement), he or she shall pay a total fee of fifty (50) yen per certificate plus applicable stamp duty.
2. When a request to register a lost share certificate is made in accordance with Article 23, a lost share certificate request fee of $¥ 8,600$ is payable per request and a fee of $¥ 500$ is payable per each lost share certificate registered.
3. When a shareholder requests the purchase of Shares Less Than One Unit pursuant to Article 27 or requests the sale of Shares Less Than One Unit pursuant to Article 31, he or she shall pay the relevant fees in respect to commission payable on the trade of shares, prescribed specifically.
[Translation]

## REGULATIONS OF THE BOARD OF DIRECTORS

 HONDA MOTOR CO., LTD.
## REGULATIONS OF THE BOARD OF DIRECTORS

## Article 1. (Purpose)

These Regulations shall govern the matters concerning the Board of Directors of the Company under Article 24 of its Articles of Incorporation.

## Article 2. (Composition)

The Board of Directors shall be composed of all of the Directors of the Company.

Corporate Auditors shall attend meetings of the Board of Directors.

## Article 3. (Timing of Convocation of Meetings of the Board of Directors)

Ordinary meetings of the Board of Directors shall be convened in January, February, April, May, June, July and October and an extraordinary meeting of the Board of Directors shall be convened whenever necessary.

## Article 4. (Persons Entitled to Convene Meetings of the Board of Directors and the Chairman)

The Chairman of the Board of Directors or the President and Director shall, as resolved at a meeting of the Board of Directors in advance, convene a meeting of the Board of Directors and act as chairman thereat. If both the Chairman of the Board of Directors and the President and Director are prevented from so doing, one of the other Directors shall take his or her place in the order established in advance by the Board of Directors. Provided, however, that in the case that laws and regulations provide otherwise, one of the other Directors or Corporate Auditors shall convene a meeting of the Board of Directors.

## Article 5. (Notice of Convocation)

1. A notice of convocation of meetings of the Board of Directors shall be dispatched to each Director and to each Corporate Auditor at least three (3) days before the date of the meeting.
2. If the unanimous consent of all of the Directors and Corporate Auditors is obtained, a meeting of the Board of Directors may be held without following the procedures for convocation.

## Article 6. (Method of Resolutions)

1. Resolutions of a meeting of the Board of Directors shall be adopted by a majority of the Directors present, who must constitute a majority of the Directors.
2. The Director who has special interests in any of the matters for resolution may not participate in the resolution as prescribed in the preceding paragraph on such matters.
3. Any Director who may not participate in a resolution under the provision of the preceding paragraph will not be counted in the number of Directors mentioned in paragraph 1 of this article.
4. If the requirements set out in Article 370 of the Company Law are satisfied, those matters that are the object of the resolution shall be deemed to have been resolved by the Board of Director.

## Article 7. (Opinions of the Corporate Auditors)

The Corporate Auditors shall state their opinions when deemed necessary at a meeting of the Board of Directors.

## Article 8. (Matters to be Resolved)

The matters to be resolved by the Board of Directors are as follows:
(1) Convocation of a general meeting of the Shareholders and determination of objectives thereof and matters to be submitted thereto;
(2) Election and discharge of Representative Directors and Directors with Executive Power;
(3) Approval of transactions between the Company and a Director, conflict of interest transactions and transactions by a Director competing with the Company's business;
(4) Issue of new shares and bonds;
(5) Approval for deliberation of financial reports and business reports, and schedules attached thereto;
(6) Determination of payment of dividends of surplus;
(7) Establishment, relocation and abolition of branch offices and other important organizations;
(8) Appointment and dismissal of managers and other important employees;
(9) Disposition and acquisition of important assets;
(10) Borrowings of a substantial amounts;
(11) Approval of basic policy for establishment of internal governance systems; and
(12) Other matters prescribed by laws and regulations or in the Articles of Incorporation.

## Article 9. (Matters to be Reported)

1. Directors shall report to the Board of Directors without delay in the case that any of the matters set forth below occurs:
(1) When a transaction between the Company and a Director, a conflict of interest transaction or a transaction by a Director competing with the Company's business is made;
(2) When a Director becomes an unlimited-liability partner, director, corporate auditor or manager of another company; and
(3) When Article 331, Paragraph 1 of the Company Law is applicable.
2. The Representative Director shall report to the Board of Directors on the state of business execution at least once in every three (3) months.
3. If a Director notifies all of the Directors and Corporate Auditors of matters that should be reported to the Board of Directors, those matters shall not be required to be reported to the Board of Directors.
4. The provision of the preceding paragraph does not apply to reports set out in paragraph 2 of this article.

## Article 10. (Minutes)

The substance of the proceedings of the meeting of the Board of Directors, the results thereof, and any matter required under laws and ordinances shall be recorded in minutes, to which the Directors and the Corporate Auditors present thereat shall affix their names and seals.

## Article 11. (Consultation)

The Senior Adviser, Executive Adviser, Special Adviser and Standing Adviser shall advise the Board of Directors and Representative Directors.

## Article 12. (Amendment)

Any amendment of these Regulations require a resolution of the Board of Directors.

## Supplementary Provision

Came into force on October 1, 1982
Partly amended on April 18, 1983
Partly amended on May 28, 1987
Partly amended on April 27, 2001
Partly amended on June 25, 2002
Partly amended on April 21, 2003
Partly amended on June 24, 2003
Partly amended on June 25, 2004
Partly amended on February 25, 2005
Partly amended on June 23, 2005
Partly amended on June 23, 2006
-End-
[Translation]

## REGULATIONS OF THE BOARD OF CORPORATE AUDITORS

Established: June 29, 1994
Amended: May 1, 2002
Amended: June 23, 2004
Amended: January 28, 2005
Amended: June 23, 2006
Amended: September 14, 2006

HONDA MOTOR CO., LTD.

## REGULATIONS OF THE BOARD OF CORPORATE AUDITORS

## Article 1. (Purport)

These Regulations shall govern the matters concerning the Board of Corporate Auditors of the Company under laws and ordinances and its Articles of Incorporation.

## Article 2. (Composition)

1. The Board of Corporate Auditors shall be composed of all of the Corporate Auditors of the Company.
2. The Board of Corporate Auditors shall have a standing Corporate Auditor.
3. In addition to the preceding paragraph, the Board of Corporate Auditors shall have a chairman of the Board of Corporate Auditors and a Specified Corporate Auditor as stipulated in Article 7 hereof.

## Article 3. (Purpose of the Board of Corporate Auditors)

The Board of Corporate Auditors shall be reported on important matters concerning audits and discusses and shall resolve those matters, but that does not preclude the Corporate Auditors from exercising their powers.

## Article 4. (Duties of the Corporate Auditors)

Corporate Auditors shall perform the duties set out below. However, the determination set out in Item 3 may not preclude any Corporate Auditor from exercising his or her powers as a Corporate Auditor.
(1) Preparation of audit report.
(2) Election and discharge of standing Corporate Auditors.
(3) Determination of audit policies, methods of investigating the state of the Company's business and assets, and other matters relating to the performance of Corporate Auditors' duties.

## Article 5. (Election and Discharge of Standing Corporate Auditor)

The Board of Corporate Auditors shall, by its resolution, elect a standing Corporate Auditor from among the Corporate Auditors and discharge the standing Corporate Auditor.

## Article 6. (Chairman)

1. The Board of Corporate Auditors shall, by its resolution, determine a chairman of the Board Corporate Auditors.
2. In addition to the duties set out in Article 9, Paragraph 1, the chairman shall also carry out the duties that are delegated by the Board of Corporate Auditors, but that does not preclude each Corporate Auditor from exercising his or her powers.

## Article 7 (Specified Corporate Auditor)

1. The Board of Corporate Auditors shall, by its resolution, determine a person to carry out the duties set out below (the "Specified Corporate Auditor"):
(1) Receive from a Director the business report and schedules attached thereto and the accounts-related documents, all of which each Corporate Auditors should receive, and submit them to other Corporate Auditors;
(2) Provide notice of the contents of the Board of Corporate Auditors' audit report relating to the business report and schedules attached thereto to the Director stipulated as the person to receive that notice (the "Specified Director");
(3) Agree with the Specified Director on a date to provide the notice set out in the preceding Item;
(4) Receive from the accounting auditor a notice on the contents of the accounting audit report and notify the other Corporate Auditors of the contents of that audit report;
(5) Agree with the accounting auditor on a date to receive the notice set out in the preceding Item;
(6) Notify the Specified Director and the accounting auditor of the contents of the Board of Corporate Auditors' audit report relating to the accounts-related documents; and
(7) Agree with the Specified Director on a date to provide the notice set out in the preceding Item.
2. The Specified Corporate Auditor shall be a standing Corporate Auditor.

## Article 8. (Timing of Meetings)

Meetings of the Board of Corporate Auditors shall be held regularly. However, meetings may be held from time to time whenever necessary.

## Article 9. (Convener)

1. The chairman of the Board of Corporate Auditors shall convene and operate the meetings of the Board of Corporate Auditors.
2. Each Corporate Auditor is entitled to request the chairman to convene a meeting of the Board of Corporate Auditors.
3. If the chairman does not convene a meeting of the Board of Corporate Auditors despite a request made under the preceding paragraph, the Corporate Auditor who made the request will be entitled to convene and operate the meeting himself or herself.

## Article 10. (Convocation Procedures)

1. To convene a meeting of the Board of Corporate Auditors, a notice of convocation shall be dispatched to each Corporate Auditor at least three (3) days before the date of the meeting. However, in case of urgent need that period may be shortened.
2. If the unanimous consent of all of the Corporate Auditors is obtained, a meeting of the Board of Corporate Auditors may be held without following the procedures for convocation.

## Article 11. (Method of Resolutions)

1. Resolutions of a meeting of the Board of Corporate Auditors shall be adopted by a majority of all the Corporate Auditors, except for cases provided otherwise in these Regulations.
2. Before adopting any resolution, Corporate Auditors shall conduct deliberations based on sufficient materials.

## Article 12. (Resolutions of Audit Policies, etc.)

1. Before starting an audit, the Board of Corporate Auditors shall resolve the audit policy, audit plan and audit method, and the allotment of audit services.
2. In addition to resolving the matters set out in the preceding paragraph, the Board of Corporate Auditors shall resolve any matters it deems necessary for performing its duties, such as the budget for audit expenses.
3. In addition to resolving the matters set out in the preceding two (2) paragraphs, the Board of Corporate Auditors shall resolve the contents of the systems set out below and request Directors establish these systems:
(1) Matters relating to employees who should assist the Corporate Auditors;
(2) Matters relating to the independence from Directors of the employees set out in the preceding Item;
(3) A system for Directors and employees to report to Corporate Auditors and other systems relating to reports to Corporate Auditors; and
(4) A system to ensure that Corporate Auditors' audits are carried out effectively.

## Article 13. (Regular Meetings with Representative Directors)

1. The Board of Corporate Auditors shall regularly meet with the Representative Directors and make efforts to strive to develop the same awareness of the Company and its business as the Representative Directors have by, for example, exchanging opinions on such matters as issues the Company is facing, the environment in which Corporate Auditors is conducting their audits, and issues that are important in audits, and making requests that it deems necessary.
2. The Board of Corporate Auditors shall, as appropriate, report to the Representative Directors and the Board of Directors on audit policies and audit plans and the progress and results of audits.
3. In addition to determining matters stipulated under law, the Board of Corporate Auditors shall, upon consultation with Directors, determine the matters on which the Board of Directors and employees should report to the Board of Corporate Auditors under the systems set out in Paragraph 3(iii) of the preceding Article, and it shall be reported such matters.

## Article 14. (Reports to the Board of Corporate Auditors)

1. Corporate Auditors shall report to the Board of Corporate Auditors on the progress of their business and shall report on that progress whenever required by the Board of Corporate Auditors.
2. A Corporate Auditor who has been reported by an accounting auditor, Director, employee of the Audit Office, or any other relevant person shall report thereon to the Board of Corporate Auditors.
3. When necessary, the Board of Corporate Auditors shall request reports from accounting auditors, Directors, employees of the Audit Office, and other relevant persons.
4. If a Corporate Auditor, accounting auditor, Director, an employee of, for example, the Audit Office, or any other person notifies all of the members of the Board of Corporate Auditors of matters that should be reported to the Board of Corporate Auditors as set out in the preceding three (3) paragraphs, those matters shall not be required to be reported to the Board of Corporate Auditors.

## Article 15. (Measures to be Taken on Receiving Reports)

If the Board of Corporate Auditors receives a report as set out below, it shall conduct the necessary investigation and take measures appropriate to the circumstances:
(1) A report from a Director that a fact has been discovered that might cause significant damage to the Company;
(2) A report from an accounting auditor that (i) a Director has acted improperly in relation to carrying out his or her duties or (ii) a material fact has been discovered such as a breach of the Articles of Incorporation or a breach of laws or regulations; or
(3) A report from a Director or an employee on matters stipulated in advance on consultation with Directors.

## Article 16. (Preparation of Audit Reports)

1. The Board of Corporate Auditors shall, after its deliberation, prepare the audit report of the Board of Corporate Auditors based on audit reports prepared by each Corporate Auditor.
2. If the contents of the Board of Corporate Auditors' audit report differ from the contents of a Corporate Auditor's audit report and that Corporate Auditor requests that the contents of his or her audit report be attached to the audit report of the Board of Corporate Auditors, then those contents shall be so attached.
3. Each Corporate Auditor shall sign the Board of Corporate Auditors' audit report. Standing Corporate Auditors and outside corporate auditors shall enter or record in the audit report that they are standing Corporate Auditors or outside corporate auditors.
4. If the Company is to prepare extraordinary financial reports or consolidated financial reports, the preceding three (3) paragraphs shall apply mutatis mutandis to the preparation of those documents.

## Article 17 (Consent etc. to, and Request a Proposal for, the Appointment of Corporate Auditors)

1. The following matters concerning the appointment of Corporate Auditors shall be resolved at a meeting of the Board of Corporate Auditors:
(1) Consent for submission of a proposal concerning the appointment of Corporate Auditors to a general meeting of shareholders;
(2) Request for deliberation on the appointment of a Corporate Auditor at a general meeting of shareholders; and
(3) Request for submission of a proposal concerning the appointment of a Corporate Auditor to a general meeting of shareholders.
2. The preceding paragraph shall also apply mutatis mutandis to the appointment of Corporate Auditors to fill vacancies of Corporate Auditors.

## Article 18. (Consent etc. Concerning Appointment of Accounting Auditors)

1. The following matters concerning appointment, non-reappointment or discharge of accounting auditors shall be resolved at a meeting of the Board of Corporate Auditors:
(1) Consent for submission of a proposal concerning appointment of accounting auditors to a general meeting of shareholders;
(2) Consent for deliberation on the non-reappointment or discharge of an accounting auditor at a general meeting of shareholders;
(3) Request for submission of a proposal concerning the appointment of an accounting auditor to a general meeting of shareholders;
(4) Request for deliberation on the appointment, non-reappointment or discharge of an accounting auditor at a general meeting of shareholders; and
(5) Appointment of the person to temporarily perform the duties of an accounting auditor in its absence.
2. The consent of all Corporate Auditors to the discharge of an accounting auditor in accordance with statutory grounds for discharge may be obtained at a meeting of the Board of Corporate Auditors. In such case, the Corporate Auditor appointed by the Board of Corporate Auditors must report on the discharge and the reasons therefor at the first general meeting of shareholders after such discharge.
3. The consent set out in the preceding paragraph may be obtained in writing or by electromagnetic record.

## Article 19. (Consent to Remuneration etc. of the Accounting Auditor)

The consent to the remuneration etc. of the accounting auditor and any person who temporarily performs the duties of an accounting auditor may be obtained by resolution of the Board of Corporate Auditors.

## Article 20. (Consent of the Board of Corporate Auditors to the Exemption of Directors from Some of their Liability, etc.)

1. The consent of all Corporate Auditors set out below may be obtained at a meeting of the Board of Corporate Auditors:
(1) Consent for submission of a proposal concerning exemption of a Director from some of his or her liability to a general meeting of shareholders;
(2) Consent for submission of a proposal concerning an amendment to the Articles of Incorporation so as to enable the exemption of Directors from some of their liability by a resolution of a meeting of the Board of Directors to a general meeting of shareholders;
(3) Consent for submission of a proposal concerning exemption of a Director from some of his or her liability to a meeting of the Board of Directors in accordance with the Articles of Incorporation; and
(4) Consent for submission of a proposal by the Board of Directors for an amendment to the Articles of Incorporation so as to enable the execution of an agreement limiting some of the liability of Outside Directors to a general meeting of shareholders.
2. The consent set out in the preceding paragraph may be obtained in writing or by electromagnetic record.

## Article 21. (Consent to Auxiliary Intervention)

1. The consent of all of the Corporate Auditors for the Company's providing auxiliary intervention for a Director defendant in a shareholder class action may be obtained at the Board of Corporate Auditors.
2. The consent set out in the preceding paragraph may be obtained in writing or by electromagnetic record.

## Article 22. (Deliberation on Exercise of Powers by Corporate Auditors)

Corporate Auditors may deliberate on the following matters in advance at a meeting of the Board of Corporate Auditors when they exercise their powers or fulfill their obligations with respect to those matters:
(1) Explanation about questions to a Corporate Auditor notified by a shareholder before a general meeting of shareholders;
(2) Report to the Board of Directors and request for convocation of a meeting of the Board of Directors, etc.;
(3) Report of opinions concerning proposals or documents or other things to be submitted to a general meeting of shareholders;
(4) Request for suspension of the acts of Directors that are beyond the scope of the Company's purpose or that breach law, ordinance, or the Company's Articles of Incorporation;
(5) Statement of opinions on appointment, discharge, resignation and remuneration etc. of Corporate Auditors at a general meeting of shareholders;
(6) Matters about lawsuits between the Company and a Director; and
(7) Any other matters concerning the bringing of lawsuits, etc.

## Article 23. (Deliberation on Remuneration etc.)

Deliberation of the remuneration etc. of Corporate Auditors may, if all Corporate Auditors have so consented, be made at a meeting of the Board of Corporate Auditors.

## Article 24. (Minutes)

1. The Board of Corporate Auditors shall prepare minutes for its meetings, the contents of the minutes being the matters set out below, and each Corporate Auditor present shall sign or affix his or her seal to the minutes.
(1) Place, date, and time of meeting (including the method of attendance of any Corporate Auditor, Director, or accounting auditor who was not at the location of the meeting but who attended the meeting of the Board of Corporate Auditors);
(2) Outline of the proceedings and the results thereof;
(3) If a Corporate Auditor stated his or her opinion or made a statement at the Board of Corporate Auditors meeting on any of the following matters, an outline of the details of the opinion or statement:
(A) A report from a Director that a fact has been discovered that might cause significant damage to the Company; and
(B) A report from an accounting auditor that (i) a Director has acted improperly in relation to carrying out his or her duties or (ii) a material fact has been discovered such as a breach of the Articles of Incorporation or a breach of laws or ordinances;
(4) The name or trade name of the Directors and the accounting auditors present at the meeting; and
(5) The name of the chairman of the meeting.
2. If the report to the Board of Corporate Auditors is not necessary pursuant to Article 14, Paragraph 4, minutes the contents of which shall be the matters set out below shall be prepared:
(1) The content of matters that do not need to be reported to the Board of Corporate Auditors;
(2) The day the report to the Board of Corporate Auditors was no longer required; and
(3) The name of the Corporate Auditors who performed their duties in connection with preparing the minutes.
3. The Company shall retain the minutes set out in the preceding two (2) paragraphs at its head office for ten (10) years.

## Article 25. (Secretariat of the Board of Corporate Auditors)

The secretariat of the Board of Corporate Auditors shall take charge of duties concerning the convocation of the meetings of the Board of Corporate Auditors, preparation of the minutes and any other general matters concerning operation of the Board of Corporate Auditors.

## Article 26. (Code of Corporate Auditors Auditing Standards)

In addition to being governed by laws, ordinances, the Articles of Incorporation, and these Regulations, matters concerning the Board of Corporate Auditors and the performance of the duties of Corporate Auditors shall be governed by the Code of Corporate Auditors Auditing Standards, which are determined by the Board of Corporate Auditors.

## Article 27. (Amendment to and Abolition of Regulations)

Any amendment to or abolition of these Regulations shall be made by a resolution of the Board of Corporate Auditors.

## (Supplementary Provision)

These amendments to the Regulations are effective as of September 14, 2006.

## CERTIFICATION

I, Takeo Fukui, certify that:

1. I have reviewed this annual report on Form 20-F of Honda Motor Co., Ltd.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the company and have:
(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.
(c) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
(d) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent functions):
(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Date: July 18, 2007

|  | /S/ $\quad$ Takeo Fukui |
| :--- | :---: |
| Name: $\quad$ Takeo Fukui |  |
| Title: | Chief Executive Officer |
|  | Honda Motor Co., Ltd. |

## CERTIFICATION

I, Fumihiko Ike, certify that:

1. I have reviewed this annual report on Form 20-F of Honda Motor Co., Ltd.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the company and have:
(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.
(c) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
(d) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent functions):
(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Date: July 18, 2007

|  | /S/ Fumihiko Ike |
| :--- | :---: |
| Name: | Fumihiko Ike |
| Title: | Chief Operating Officer for |
|  | Business Management Operations |
| Honda Motor Co., Ltd. |  |

## CERTIFICATION

Pursuant to 18 U.S.C. § 1350, the undersigned officer of Honda Motor Co., Ltd. (the "Company"), hereby certifies, to such officer's knowledge, that the Company's annual report on Form 20-F for the year ended March 31, 2007 (the "Report") fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934 and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: July 18, 2007

| By | /S/ $\quad$ Takeo Fukui |
| :--- | :---: |
| Name: | Takeo Fukui |
| Title: | Chief Executive Officer <br>  |

## CERTIFICATION

Pursuant to 18 U.S.C. § 1350, the undersigned officer of Honda Motor Co., Ltd. (the "Company"), hereby certifies, to such officer's knowledge, that the Company's annual report on Form 20-F for the year ended March 31, 2007 (the "Report") fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934 and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: July 18, 2007

| By | /S/ Fumihiko Ike |
| :--- | :---: |
| Name: | Fumihiko Ike |
| Title: | Chief Operating Officer for |
|  | Business Management Operations |
|  | Honda Motor Co., Ltd. |


[^0]:    *1: OEM (Original equipment manufacturing)

[^1]:    * Source: European Automobile Manufacturers' Association (ACEA), passenger car category (15 countries in the European Union, three countries in the European Free Trade Association)

[^2]:    * See note 2 .

[^3]:    * See note 2.

[^4]:    * See note 2.

[^5]:    * See note 2

[^6]:    * See note 2 .

[^7]:    * See note 2.

[^8]:    * See note 2.

[^9]:    * All quarterly financial data is unaudited and also has not been reviewed by our independent registered

