2006

Financial Statements

Valeo

CONSOLIDATED STATEMENTS OF INCOME

(In millions of euros)	Notes	2006	2005 (1) Restated	2004 (1) Restated
NET SALES	*3.1*	**9,970**	**9,736**	**9,018**
Other operating revenues		116	98	62
TOTAL OPERATING REVENUES		**10,086**	**9,834**	**9,080**
Cost of sales		(8,431)	(8,177)	(7,467)
GROSS MARGIN (2)		**1,539**	**1,559**	**1,551**
% of net sales		15.4%	16.0%	17.2%
Research and development expenditure	*3.3*	(661)	(640)	(580)
Selling expenses		(195)	(191)	(182)
Administrative expenses		(458)	(452)	(431)
Other income and expenses	*3.4*	(70)	(50)	(98)
OPERATING INCOME		**271**	**324**	**322**
% of total operating revenues		2.7%	3.3%	3.5%
Cost of net debt	*3.5*	(57)	(52)	(32)
Other financial income and expenses	*3.6*	(9)	(52)	(37)
INCOME BEFORE INCOME TAXES		**205**	**220**	**253**
Income taxes	*3.7*	(75)	(66)	(18)
Equity in net earnings of associates		-	6	5
INCOME FROM CORE ACTIVITIES		**130**	**160**	**240**
% of total operating revenues		1.3%	1.6%	2.6%
Non-strategic activities (3)		36	(12)	8
NET INCOME FOR THE PERIOD		**166**	**148**	**248**
Minority interests		(5)	(6)	(8)
NET INCOME ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY		**161**	**142**	**240**
% of total operating revenues		1.6%	1.4%	2.6%
Income from core activities attributable to equity holders of the company				
• **Basic earnings per share (in euros)**		**1.62**	**1.95**	**2.82**
• Diluted earnings per share (in euros)		1.62	1.93	2.63
Net income attributable to equity holders of the company				
• **Basic earnings per share (in euros)**	*3.8.1*	**2.10**	**1.80**	**2.92**
• Diluted earnings per share (in euros)	*3.8.2*	2.09	1.79	2.71

(1) The statements of income for 2004 and 2005 have been restated from those published on February 9, 2006, as described in notes 2.1 and 3.3.

(2) Gross margin represents net sales (excluding other operating revenues) less cost of sales.

(3) See note 2.1.

The notes are an integral part of the consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

(In millions of euros)	Notes	2006	2005 (1) Restated	2004 (1) Restated
ASSETS				
Goodwill	4.1	1,415	1,484	1,158
Other intangible assets	4.2	528	522	281
Property, plant and equipment	4.3	1,918	2,041	1,945
Investments in associates	4.4	103	116	96
Non-current financial assets	4.5	24	28	14
Deferred tax assets	4.6	96	100	83
Non-current assets		**4,084**	**4,291**	**3,577**
Inventories	4.7	647	654	565
Accounts and notes receivable	4.8	1,834	1,906	1,726
Other current assets		311	243	228
Taxes recoverable		64	51	58
Other current financial assets	5.2.5	10	24	-
Assets held for sale	4.3	20	11	-
Cash and cash equivalents	4.11	618	949	868
Current assets		**3,504**	**3,838**	**3,445**
TOTAL ASSETS		**7,588**	**8,129**	**7,022**
LIABILITIES AND EQUITY				
Share capital		233	233	251
Additional paid-in capital		1,387	1,385	1,617
Retained earnings		94	56	(87)
Stockholders' equity		**1,714**	**1,674**	**1,781**
Minority interests		38	43	57
Stockholders' equity including minority interests	4.9	**1,752**	**1,717**	**1,838**
Provisions - non-current portion	4.10	937	1,123	1,000
Long-term debt	4.11	1,274	1,303	1,027
Deferred tax liabilities	4.6	1	9	13
Non-current liabilities		**2,212**	**2,435**	**2,040**
Accounts and notes payable		1,955	1,925	1,685
Provisions - current portion	4.10	418	431	298
Taxes payable		76	82	83
Other liabilities		836	792	715
Current maturities of long-term debt	4.11	54	581	188
Other current financial liabilities	5.2.5	11	9	-
Short-term debt	4.11	274	157	175
Current liabilities		**3,624**	**3,977**	**3,144**
TOTAL LIABILITIES AND EQUITY		**7,588**	**8,129**	**7,022**

(1) The balance sheets for 2004 and 2005 have been restated from those published on February 9, 2006, as described in note 6.

The notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In millions of euros)	Notes	2006	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES [1]				
Net income for the period		166	148	248
Equity in net earnings of associates		-	(6)	(5)
Net dividends received from associates		4	4	3
Expenses (income) with no cash effect	*4.12*	411	518	516
Cost of net debt		59	54	33
Income taxes (current and deferred)		77	60	17
Gross operating cash flows		**717**	**778**	**812**
Income taxes paid		(85)	(65)	(28)
Changes in working capital	*4.12*	48	107	45
Net cash provided by operating activities		**680**	**820**	**829**
CASH FLOWS FROM INVESTING ACTIVITIES [1]				
Outflows relating to acquisitions of intangible assets		(165)	(145)	(122)
Outflows relating to acquisitions of property, plant and equipment		(494)	(441)	(413)
Inflows relating to disposals of property, plant and equipment		17	41	19
Net change in non-current financial assets		32	(3)	-
Impact of changes in scope of consolidation	*2.6*	124	(466)	(73)
Net cash used in investing activities		**(486)**	**(1,014)**	**(589)**
CASH FLOWS FROM FINANCING ACTIVITIES [1]				
Dividends paid to parent company stockholders		(84)	(91)	(85)
Dividends paid to minority interests in consolidated subsidiaries		(5)	(5)	(5)
Equalization tax on dividends		-	-	(101)
Issuance of share capital		4	1	33
Sale (purchase) of treasury shares		4	8	-
Issuance of long-term debt		3	826	26
Grants and contributions received		48	39	26
Net outflows related to capital reductions		-	(252)	-
Net interest paid		(60)	(33)	(28)
Repayment in long-term debt		(553)	(196)	(36)
Net cash provided by (used in) financing activities		**(643)**	**297**	**(170)**
Effect of exchange rate changes on cash		1	28	(1)
NET CHANGE IN CASH AND CASH EQUIVALENTS		**(448)**	**131**	**69**
Cash and cash equivalents at beginning of year		**792**	**661** [2]	**624**
Cash and cash equivalents at end of year		**344**	**792**	**693** [2]
Of which : • Cash and cash equivalents		618	949	868
• Short-term debt		(274)	(157)	(175)

(1) The impact of the sale of the Electric Motors & Actuators business is described in note 2.1.

(2) The difference between net cash and cash equivalents at December 31, 2004 and at January 1, 2005 is due to the application of IAS 32 at January 1, 2005 (treasury shares are now deducted from stockholders' equity).

The notes are an integral part of the consolidated financial statements.

STATEMENTS OF RECOGNIZED INCOME AND EXPENSES

(In millions of euros)	2006	2005 [1] Restated	2004 [1] Restated
Exchange differences on translation of foreign operations	(69)	135	6
Actuarial gains (losses) on defined benefit plans	27	(50)	(42)
Cash flow hedges:			
• Gains (losses) taken to equity	7	23	-
• Transferred to profit and loss for the period	(19)	(8)	-
Net investment hedges:			
• Gains (losses) taken to equity	-	(3)	-
Remeasurement of available-for-sale financial assets	-	-	-
Income taxes on items recognized directly in equity	(1)	5	1
Income and expenses recognized directly through equity	**(55)**	**102**	**(35)**
Net income for the period	**166**	**148**	**248**
Total recognized income and expenses for the period	**111**	**250**	**213**
Attributable to:			
• Equity holders of the company	109	240	208
• Minority interests	2	10	5
Corrections of errors [2]	**-**	**-**	**(9)**
Attributable to:			
• Equity holders of the company	-	-	(9)
• Minority interests	-	-	-

(1) The statements of recognized income and expenses for the periods to December 31, 2004 and December 31, 2005 have been restated from those published on February 9, 2006, as described in note 6.

(2) See note 6.

The notes are an integral part of the consolidated financial statements.

STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

Number of shares	(In millions of euros)	Share capital	Additional paid-in capital	Translation adjustment	Retained earnings	Stockholders' equity	Minority interests	Stockholders' equity including minority interests
82 133 728	**Stockholders' equity at January 1, 2004 (Restated)** [1]	**246**	**1,589**	**-**	**(90)**	**1,745**	**97**	**1,842**
	Dividends	-	-	-	(85)	(85)	(7)	(92)
	Equalization tax on dividends [2]	-	-	-	(101)	(101)	-	(101)
1 575 296	Employee share issue	5	28	-	-	33	-	33
	Share-based payments	-	-	-	5	5	-	5
	Income and expenses recognized directly through equity	-	-	9	(41)	(32)	(3)	(35)
	Net income	-	-	-	240	240	8	248
	Other movements [3]	-	-	-	(24)	(24)	(38)	(62)
83 709 024	**Stockholders' equity at December 31, 2004 (Restated)** [1]	**251**	**1,617**	**9**	**(96)**	**1,781**	**57**	**1,838**
(1 037 804)	Total impact of financial instruments (IAS32, IAS39)	-	-	-	27	27	-	27
82 671 220	**Stockholders' equity at January 1, 2005 (Restated)**	**251**	**1,617**	**9**	**(69)**	**1,808**	**57**	**1,865**
	Dividends	-	-	-	(91)	(91)	(5)	(96)
230 100	Treasury stock	-	-	-	8	8	-	8
(6 250 000)	Capital reduction [4]	(19)	(233)	-	-	(252)	-	(252)
51 333	Share-based payments	1	1	-	7	9	-	9
	Income and expenses recognized directly through equity	-	-	131	(33)	98	4	102
	Net income	-	-	-	142	142	6	148
	Other movements [3]	-	-	-	(48)	(48)	(19)	(67)
76 702 653	**Stockholders' equity at December 31, 2005 (Restated)** [1]	**233**	**1,385**	**140**	**(84)**	**1,674**	**43**	**1,717**
	Dividends	-	-	-	(84)	(84)	(4)	(88)
121 000	Treasury stock	-	-	-	4	4	-	4
	Capital increase	-	-	-	-	-	1	1
70 260	Share-based payments	-	2	-	11	13	-	13
	Income and expenses recognized directly through equity	-	-	(66)	14	(52)	(3)	(55)
	Net income	-	-	-	161	161	5	166
	Other movements	-	-	-	(2)	(2)	(4)	(6)
76 893 913	**Stockholders' equity at December 31, 2006**	**233**	**1,387**	**74**	**20**	**1,714**	**38**	**1,752**

(1) Stockholders' equity at January 1, 2004, December 31, 2004 and December 31, 2005 has been restated from the amounts published on February 9, 2006, as described in note 6.

(2) This item includes:

- 18 million euros in equalization tax relating to dividends paid in 2004;
- 83 million euros in equalization tax which became due (on dividends paid in 2001 and 2002) further to the corporate income tax rebate obtained in 2004.

(3) This item includes the impact of minority interest buyouts relating to Valeo Climatisation in 2004, as well as to Valeo Zexel China Climate Control and Valeo Thermal Systems Japan Corp. in 2005.

(4) Capital reduction carried out following the purchase by Valeo of around 7.5% of its own shares, in connection with a public share buyback offer and a simplified public tender offer.

The notes are an integral part of the consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. ACCOUNTING POLICIES

The consolidated financial statements of the Valeo Group for the year ended December 31, 2006 include the accounts of Valeo, its subsidiaries and the Group's share of associates and jointly controlled entities.

Valeo is an independent Group fully focused on the design, production and sale of components, systems and modules for the automobile sector. It is one of the world's top automotive suppliers.

Valeo is a French legal entity, listed on the Paris Stock Exchange, whose head office is located at 43, rue Bayen, 75017 Paris.

Valeo's consolidated accounts were authorized for issue by the Board of Directors on February 12, 2007.

They will be submitted for approval to the Annual General Meeting of shareholders which will be convened on May 21, 2007.

1.1. Accounting standards applied

Under European Union regulation 1606/2002 of July 19, 2002, the consolidated financial statements have been prepared in conformity with International Financial Reporting Standards (IFRS) approved by the European Union.

The Group has elected for early application, respectively as of January 1, 2004 and 2005, of the two following amendments to IFRS that are obligatorily applicable as from January 1, 2006:

- the amendment to IAS 19 introducing the option to recognize actuarial gains and losses on defined benefit pension plans in reserves;
- the amendment to IAS 39 relating to hedge accounting of forecast inter-company transactions.

New accounting standards that are not yet obligatorily applicable, that have not been adopted early and that may have an impact on the Group's financial statements are as follows:

- IFRS 7 "Financial Instruments: Disclosures"', applicable as from January 1, 2007;
- IFRS 8 "Operating Segments"; this standard, which has not yet been approved by the European Union, is obligatorily applicable as from 2009.

The potential impacts of these two standards on the Group's financial statements are currently being analyzed.

1.2. Basis of preparation

The financial statements are presented in euros and are rounded to the closest million.

In addition they have been prepared in accordance with the principal assumptions of IFRS:

- true and fair view,
- going concern,
- accrual basis of accounting,
- consistency of preparation,
- materiality and aggregation.

Preparation of the financial statements requires Valeo to make estimates and assumptions which could have an impact on the amounts at which assets, liabilities, income and expenses are stated. These estimates, and the assumptions underlying them, have been made on the basis of past experience and of other factors considered to be reasonable in the circumstances. They thus serve as the basis for the judgment made in determining the carrying amounts of assets and liabilities which could not be determined directly from other sources. The definitive amounts that will be stated in Valeo's future financial statements may be different from the amounts currently estimated. These estimates and assumptions are reviewed on a continuous basis.

1.3. Consolidation methods

The consolidated financial statements include the accounts of Valeo and companies under its direct and indirect control.

The proportionate consolidation method is used when the contractual arrangements for control of a company specify that it is under the joint control of the two venturers. Companies of this type are called joint ventures. In this case, the Group's share of each asset and liability and each item of income and expense is aggregated, line-by-line, with similar items in its consolidated financial statements.

All significant inter-company transactions are eliminated (for joint ventures the elimination is performed to the extent of the Group's ownership interest in the company), as are gains on inter-company disposals of assets, inter-company profits included in inventories and inter-company dividends.

Companies over which Valeo has the power to exercise significant influence are accounted for by the equity method. Valeo is considered to exercise significant influence over companies in which the Group owns more than 20% of the voting rights. This method consists of replacing the book value of the investments by the Group's equity in the associate's underlying net assets, including goodwill.

Companies acquired during the year are consolidated as from the date at which the Group exercises (sole or joint) control or significant influence.

1.4. Foreign currency translation

Each Group company maintains its accounting records in its functional currency. A company's functional currency is the currency of the principal economic environment in which it operates, generally being the local currency.

Transactions carried out in a currency other than the company's functional currency are translated using the rate prevailing at the transaction date. Monetary assets and liabilities denominated in foreign currency are translated at the year-end exchange rate. Non-monetary assets and liabilities denominated in foreign currency are recognized at the historical exchange rate prevailing at the transaction date. Differences arising from the translation of foreign currency transactions are recognized in income, with the exception of differences relating to loans and borrowings which are in substance an integral part of the net investment in a foreign subsidiary. These are recorded, for their amount net of tax, in consolidated stockholders' equity under translation reserves until such time as the net investment is disposed of, at which time they are recognized in income.

The financial statements of foreign subsidiaries whose functional currency is not the euro are translated into euros as follows:

- assets and liabilities are translated at the year-end exchange rate;
- income statement accounts are translated into euros at the exchange rates applicable at the transaction dates or, in practice, at the average exchange rate for the period, as long as this is not rendered inappropriate as a basis for translation by major fluctuations in exchange rates during the period;
- unrealized gains or losses arising from the translation of the financial statements of foreign subsidiaries are recorded through stockholders' equity.

1.5. Operating revenues

Operating revenues are comprised of net sales and other operating revenues.

Net sales primarily include sales of finished goods and also include all tooling revenues. Sales of finished goods and tooling revenues are recognized at the date on which the Group transfers substantially all the risks and rewards related to ownership to the buyer and is no longer involved in the management or in the effective control of the goods sold. In cases where the Group retains control of the future risks and rewards related to tooling, any customer contributions are recognized over the duration of the project, over a maximum of 4 years.

Other operating revenues consist of all revenues for which the associated costs are recorded below the gross margin line. They mainly comprise sales of prototypes and contributions received from customers to development costs. Such contributions are deferred as appropriate and are taken to income over the period of sale of the corresponding products, over a maximum of 4 years.

1.6. Gross margin and operating income

Gross margin is defined as the difference between net sales and cost of sales. Cost of sales primarily corresponds to the cost of goods sold.

Operating income includes all income and expenses other than:

- cost of net debt,
- other financial income and expenses,
- income taxes,
- equity in net earnings of associates,
- income from non-strategic activities.

In order to facilitate interpretation of the statement of income and of Group performance, unusual items that are material to the consolidated financial statements are separately presented within operating income under "Other income and expenses".

1.7. Financial income and expenses

Financial income and expenses are comprised, firstly, of the cost of net debt and, secondly, of other financial income and expenses.

The cost of net debt corresponds to interest paid on debt less interest earned on cash and cash equivalents.

Other financial income and expenses notably include:

- foreign exchange gains and losses, including the impact of derivative instruments used as hedges,
- charges to provisions for credit risk as well as the cost of credit insurance,
- the effect of unwinding discount on provisions, including discount on provisions for pensions and other employee benefits,
- and the expected return on pension and other post-employment benefit plan assets.

1.8. Earnings per share

Basic earnings per share are calculated by dividing consolidated net income by the weighted average number of shares outstanding during the year, excluding the average number of shares held in treasury stock.

Diluted earnings per share are calculated by including potentially dilutive instruments such as stock options or convertible bonds, when such instruments have a dilutive effect, which is particularly the case for stock subscription options when their exercise price is below the market price (average Valeo share price over the year). When funds are received on the exercise of these rights (such as on the subscription of shares), they are deemed to be allocated in priority to the purchase of shares at market price. This calculation method – known as the treasury stock method – serves to determine the "unpurchased" shares to be added to the shares of common stock outstanding for the purposes of computing the dilution. When funds are received at the date of issue of dilutive instruments (such as for convertible bonds), net income is adjusted for the net of tax interest savings which would result from the conversion of the bonds into shares.

1.9. Business combinations

All identifiable assets acquired and liabilities and contingent liabilities assumed, are recognized at their fair value at the date of transfer of control to the Group (acquisition date), independently of recognition of any minority interests.

The cost of a business combination is equal to the acquisition price, plus any costs directly attributable to the acquisition. Any excess of the acquisition cost over the fair value of the net assets acquired and liabilities and contingent liabilities recognized, is recorded in assets as goodwill. Goodwill is not amortized but is rather subject to an impairment test at least once a year.

1.10. Intangible assets

Innovation can be analyzed as either research or development. Research is planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding. Development is the application of research findings with a view to creating new products, before the start of commercial production.

Research costs are recognized in expenses in the year they are incurred.

Development expenditure is capitalized where the Group can demonstrate:

- that it has the intention, and the technical and financial resources to complete the development;
- that the intangible asset will generate future economic benefits;
- and that the cost of the intangible asset can be measured reliably.

Capitalized development costs are then amortized over a maximum period of 4 years from the start of volume production. Impairment losses may, as required, be recognized in respect of capitalized development costs.

Other intangible assets are carried at cost less any amortization and impairment losses recognized. They are amortized on a straight-line basis over their expected useful lives.

Intangible assets with indefinite useful lives are subject to an impairment test in accordance with the methodology set out in note 1.12. Intangible assets which are not yet in use at year-end are also subject to such impairment tests.

1.11. Property, plant and equipment

Property, plant and equipment are carried at cost, excluding interest expense, less accumulated depreciation and impairment losses. Material revaluations, recorded in accordance with laws and regulations applicable in countries in which the Group operates, have been eliminated in order to ensure the consistency of valuation method of all fixed assets in the Group.

Tooling which is specific to a given project is subjected to an economic analysis of contractual relations with the automaker in order to determine which party has control over the future risks and rewards relating to the specific tooling. When Valeo has such control, tooling is recorded in the balance sheet. In the event that Valeo does not have control, it is included in inventories until sold. Any resulting loss on the tooling contract (corresponding to the difference between the automaker's contribution and the cost of the tooling) is provided for as soon as the amount of the loss is known.

When the terms of a lease, entered into by the Group as lessee, transfer substantially all risks and rewards inherent in ownership to the Group, the corresponding asset is recognized in property, plant and equipment in the Group's balance sheet at a cost equal to the lesser of its fair value and the present value of future minimum lease payments. Such assets are subject to depreciation and, if necessary, provisions for impairment. The corresponding obligation is recorded as a liability.

Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets concerned:

- buildings 20 years
- fixtures and fittings 8 years
- machinery and equipment 4 to 8 years
- other fixed assets 3 to 8 years

Land is not depreciated.

Capital grants received are recognized in liabilities and are written back to income proportionately to the recognition of depreciation of the corresponding assets.

1.12. Impairment of assets

At each balance sheet date, the Group assesses whether there is an indication that an asset (other than a financial asset), a cash generating unit (CGU – as defined by IAS 36), or a group of CGUs may be impaired.

CGUs are autonomous management entities at the level of which the resource allocation process is performed and results are analyzed. They generally correspond to production sites or to groups of production sites.

Intangible assets with indefinite useful lives are systematically subjected to an impairment test at least once a year. If the asset's carrying amount is greater than its recoverable amount, it is written down to its recoverable amount.

The recoverable amount of an asset or a CGU is the higher of its fair value less costs to sell and its value in use. The method applied is the discounted present value of future cash flows expected to derive from an asset or a CGU. The discount rate used is the rate that reflects both the current assessment of the time value of money and risks specific to the asset (or group of assets) for which future cash flows estimates have not been adjusted.

Impairment losses are allocated to CGU assets in the following order: firstly to the goodwill allocated to the CGU and then to the other CGU assets in proportion to their carrying amounts.

Impairment losses recognized on goodwill balances are never reversed. For other assets, when an indicator shows that the asset may no longer be impaired, the impairment loss previously recognized is reversed in an amount so that the new carrying amount is the lesser of the recoverable amount and the carrying amount that the asset would have had if the impairment had not been recognized in the first place.

1.13. Financial assets and liabilities

Financial assets include non-consolidated investments, loans, accounts and notes receivable, derivatives and cash and cash equivalents. Financial liabilities include debt, accounts and notes payable, derivatives and short-term bank debt.

Recognition and measurement principles in respect of financial assets and liabilities are defined in IAS 32 and IAS 39. Valeo has elected to apply these standards with effect from January 1, 2005. The impact of the change in accounting policy was recorded in equity at that date.

1.13.1. Financial assets at fair value through income

Cash and cash equivalents are comprised of marketable securities such as money-market funds, deposits, and very short-term risk-free securities which can be easily sold or converted into cash as well as cash at bank. Such investments are generally held to be sold within a short timeframe.

1.13.2. Trading receivables and payables

Trading receivables and payables are initially recognized at fair value. The fair value of accounts receivable and accounts payable is deemed to be their nominal amount in view of the fact that periods to payment are generally less than 3 months. Such trading receivables and payables are subsequently valued at amortized cost.

Accounts receivable can be subject to provisions for impairment in value. If an event of loss is identified during the financial year subsequent to initial recognition of the receivable, the required provision will be calculated by comparing the estimated future cash flows to the carrying amount in the balance sheet. Provisions are recognized through other financial expenses if they are related to a risk of insolvency of the debtor.

1.13.3. Non-current financial assets

Non-current financial assets include investments and loans and other long-term financial assets:

- investments are available-for-sale financial assets. They are initially recognized on origination at fair value. Any subsequent change in fair value is recognized through stockholders' equity or through income in the event of a prolonged decline in value;
- long-term loans are held-to-maturity financial assets. They are initially recognized at fair value on origination and are subsequently valued on an amortized cost basis;
- other non-current financial assets are securities with maturities greater than 3 months. These securities are recognized in non-current financial assets at fair value, with changes in fair value being recognized through income. Such securities can be easily sold and are risk-free.

1.13.4. Debt

Bonds and other loans

Bonds and loans are valued at amortized cost. The amount of interest recognized in financial expenses is calculated by applying the loan's effective interest rate to its carrying amount. Any difference between the expense calculated using the effective interest rate and the actual interest payment impacts the value at which the loan is recognized.

Hedge accounting is generally applied to financial debt hedged by interest rate swaps. Such loans are revalued to their fair value, which is related to changes in interest rates.

- OCEANE

Bonds convertible into new shares or exchangeable for new or existing shares (OCEANE) grant bearers an option for conversion into common shares of Valeo. They constitute a compound financial instrument which, under IAS 32, must be split into its two components:

- the value of the debt component is calculated by discounting the future contractual cash flows at the market rate applicable at the date of issue of the bond (taking account of credit risk at the date of issue) for a similar instrument with the same characteristics but without a conversion option;
- the value of the equity component is calculated as the difference between the proceeds of the bond issue and the amount of the debt component.

- Short-term bank debt

This caption mainly includes credit balances with banks and commercial paper issued by Valeo for its short-term financing needs. Commercial paper has a maximum maturity of 3 months and is valued at amortized cost.

1.13.5. Recognition and measurement of derivatives

Derivatives are recognized in the balance sheet at fair value under the other current financial assets and other current financial liabilities captions. The accounting impact of changes in fair value of derivatives differs depending on whether hedge accounting is applied or not.

When hedge accounting is applied:

- for fair value hedges of recognized assets and liabilities, the hedged portion of these items is stated at fair value. Changes in this fair value are recognized through income and offset, for the effective portion, the symmetrical changes in the fair value of the derivatives;
- for cash flow hedges, the effective portion of the change in the fair value of the derivative is recognized directly through equity and the ineffective portion is taken to other financial income and expenses;
- for hedges of net investments in foreign subsidiaries, the change in fair value of the hedging instruments is taken to equity (for the effective portion) until the disposal of the net investment.

In cases where hedge accounting is not applied, changes in the fair value of derivatives are recognized in other financial income and expenses.

- Foreign currency derivatives

Changes in the value of derivatives are generally recognized in financial income and offset, as applicable, by changes in the fair value of the underlying receivables and payables. In certain cases, the Group applies hedge accounting for highly probable future flows as from the inception of the hedging relationship: changes in the fair value of the derivatives are then recognized through equity for the effective component of the hedge. Amounts that flowed through equity are subsequently taken to operating income when the underlying hedged item affects operating income. The ineffective portion is recognized in other financial income and expenses.

- Metals derivatives

The Group applies cash flow hedge accounting. The effective portion of the hedge is reclassified from equity to operating income when the hedged position affects income. The ineffective portion is recognized in other financial income and expenses.

- Interest rate derivatives

The Group generally applies fair value hedge accounting. Changes in the fair value of debt, related to changes in interest rates, and symmetrical changes in the fair value of the interest rate derivatives are recognized in other financial income and expenses for the period.

In certain cases, interest rate derivatives are not designated as hedging instruments in the meaning ascribed to that term by IAS 39. In such cases changes in fair value are recognized in other financial income and expenses for the period.

1.14. Inventories

Inventories are stated at the lower of cost or net realizable value. Cost includes the cost of raw materials, labor and other direct manufacturing costs on the basis of normal activity levels. These costs are determined by the "First in-First out" (FIFO) method which, due to the rapid inventory turnover rate, approximates the latest purchase cost at the balance sheet date.

A provision for impairment in value is recorded by comparison to net realizable value.

1.15. Income taxes

Income tax expense includes current income taxes and deferred taxes of consolidated companies. Deferred taxes are accounted for using the liability method on all temporary differences between the tax base and the carrying amount of assets and liabilities in the consolidated financial statements and on all tax loss carry forwards. The main temporary differences relate to provisions for pensions and other employee benefits and other temporarily non-deductible provisions. Deferred tax assets and liabilities are calculated using enacted, or virtually enacted, tax rates that will be in force at the time of reversal of the temporary differences.

Deferred tax assets are only recognized to the extent that it appears probable that the Valeo Group will generate future taxable profits against which these tax assets will be able to be recovered.

The Group reviews the probability of future recovery of deferred tax assets on a periodic basis. This review can, if necessary, lead the Group to no longer recognize deferred tax assets that it had recognized in prior years.

Taxes payable and tax credits receivable on planned dividend distributions by subsidiaries are recorded in the statement of income.

1.16. Share-based payments

Employee stock option plans and plans for granting free shares and Stock Appreciation Rights (SARs) to employees lead to recognition of a personnel expense. This expense corresponds to the fair value of the instrument issued. It is recognized over the rights' vesting period. Fair value is estimated on the basis of valuation models adapted to the characteristics of the instruments (Black-Scholes-Merton model for options, Monte Carlo method for SARs, etc.).

1.17. Pensions and other employee benefits

Pensions and other employee benefits cover two categories of employee benefits:

- post-employment benefits which include statutory retirement bonuses, supplementary pension benefits and coverage of certain medical costs for retirees and early retirees;
- other long-term benefits payable (during employment), corresponding primarily to long-service bonuses.

These benefits are broken down into:

- defined contribution plans, under which the employer pays fixed contributions on a regular basis and has no legal or constructive obligation to pay further contributions;
- defined benefit plans, under which the employer guarantees a future level of benefits.

The provision for pensions and other employee benefits (including long-term benefits) is equal to the present value of Valeo's future benefit obligation less, where appropriate, the fair value of plan assets in funds allocated to finance such benefits. The calculation of this provision is based on valuations performed by independent actuaries using the projected unit credit method and final salaries. These valuations incorporate both financial assumptions (discount rate, expected rate of return on plan assets, salary increases, rise in medical costs) and demographic assumptions, including rate of employee turnover, retirement age and life expectancy.

The effects of differences between previous actuarial assumptions and what has actually occurred (experience adjustments) and the effect of changes in actuarial assumptions (assumption adjustments) give rise to actuarial gains and losses. Such actuarial gains and losses arising on long-term benefits during employment are fully recognized in the income statement at each balance sheet date. However as regards post-employment benefits, actuarial gains and losses are recognized directly through equity in the financial year in which they arise, in application of the option provided by IAS 19 as amended in December 2004.

1.18. Provisions

A provision is recognized when the Group has a legal or constructive obligation resulting from a past event, where it is probable that future outflows of resources embodying economic benefits will be necessary to extinguish the obligation and where the obligation can be estimated reliably. Commitments resulting from restructuring plans are recognized when the detailed plans have been prepared and when commencement of implementation, or an announcement, has created a reasonable expectation among the individuals concerned.

Provision is made for estimated product warranty costs at the time of sale of the products. The corresponding expense is recognized in cost of sales.

When the effect of the time value of money is material, the amount of the provision is discounted using the risk free rate applicable to the corresponding country and maturity. The increase in the provision related to the passage of time (termed "unwinding") is recognized through income in other financial income and expenses.

1.19. Assets held for sale and non-strategic operations

When the Group expects to recover the value of an asset, or a group of assets, through sale rather than through use, such assets are presented separately under the "Assets held for sale" caption in the balance sheet. Any liabilities related to such assets are also presented under a separate caption in balance sheet liabilities. Assets classified as held for sale are valued at the lower of their carrying amount and their estimated sale price "less costs to sell". Such assets are thus no longer subject to depreciation and amortization. Any impairment losses and the result of sale of these assets are recognized through Group operating income.

In accordance with IFRS 5, non-strategic operations represent a major line of business of the Group, an operation that forms part of a single coordinated plan to dispose of a line of business or a company acquired solely with a view to resale. Classification as a non-strategic operation occurs at the date of sale or at a prior date if the business meets the criteria to be recognized as an asset held for sale. The results of these operations, as well as any capital gains or losses on disposal, are presented, net of tax, under a separate income statement caption.

1.20. Segment reporting

According to IAS 14, segment reporting should be provided at two levels – a primary and secondary level. The choice of segments and of levels of disclosure depends on the differences in terms of risk and return and on the organizational structure of the Group.

The Group's risks and returns are based on the nature of its products or services, of its production processes, the type of clients to whom the products or services are to be sold, the methods used to distribute the products or provide the services and the nature of the regulatory environment. They also depend on the countries in which the Group operates and markets its products, raw material costs used in the production cycle and the Group's capacity to innovate in order to offer its clients products that meet market expectations.

Analysis of these factors demonstrates that they are common to the Group's business as a whole and different business segments cannot be separately identified within the meaning of IAS 14.

The Group is organized in a multi-dimensional manner:

- the Group is decentralized into autonomous Divisions in which the allocation of resources and performance measurement are carried out. However, as there are approximately one hundred such divisions, none of them can be considered to be material within the meaning of IAS 14;
- the Divisions benefit from the support of Valeo's functional networks and Branches, which oversee the coherence of the Group's Product Families; they also exploit synergies with the Innovation Domains, and are coordinated by National Directorates.

In 2006, the Group's organization was unchanged from 2005, which saw the strengthening of the role of the three Innovation Domains and the grouping together of all the industrial branches under a single management team.

Analysis of this organizational structure does not allow any specific dimension of the Group's business to be favored over others from the perspective of IAS 14.

In consequence, the above matters lead:

- to the conclusion that the Group as a whole operates as a single business segment ("Automotive equipment");
- to the provision, for the secondary level of segment reporting, of disclosures by geographical area, supplemented by information in respect of the most appropriate criteria for understanding of the Group's business.

2. CHANGES IN THE SCOPE OF CONSOLIDATION

2.1. Sale of Electric Motors & Actuators business

In December 2006, Valeo sold its Electric Motors & Actuators business to the Japanese group Nidec. The sale price for this business was 142 million euros. This transaction generated a capital gain of 46 million euros before tax and 41 million euros after tax. This positive impact is recognized in the statement of income for 2006 under "Non-strategic activities".

The Electric Motors & Actuators business was already classified in "Non-strategic activities" in the interim financial statements published at June 30, 2006, in accordance with the criteria set out in IFRS 5. The profit after tax of the Electric Motors & Actuators business for the three financial years 2004, 2005 and 2006 is thus presented in aggregate under "Non-strategic activities" in the statement of income.

In accordance with IFRS 5, all assets and liabilities of this business are not aggregated under specific balance sheet captions at December 31, 2004 and 2005. In 2006, at the date of disposal of the Electric Motors & Actuators business, the assets and liabilities related to this business exited the Group's consolidated balance sheet.

- The components of the income statement caption "non-strategic activities" are as follows:

(In millions of euros)	2006	2005	2004
Income of non-strategic activities before income taxes	(4)	(12)	12
Pre-tax capital gain on disposal of non-strategic activities	46	-	-
Income taxes on income of non-strategic activities	(1)	-	(4)
Income taxes on capital gain on disposal of non-strategic activities	(5)	-	-
Net income of non-strategic activities	**36**	**(12)**	**8**

- Income from non-strategic activities attributable to equity holders of the company is analyzed as follows:

(In millions of euros)	2006	2005	2004
Income from non-strategic activities attributable to equity holders of the company			
• Basic earnings per share (in euros)	0.47	(0.15)	0.10
• Diluted earnings per share (in euros)	0.47	(0.14)	0.09

- Cash flows from non-strategic activities are analyzed as follows:

(In millions of euros)	2006	2005	2004
Cash flows from operating activities - non-strategic activities	4	12	15
Cash flows used in investing activities - non-strategic activities	(6)	(10)	(13)
Cash flows from financing activities - non-strategic activities	19	5	24
Change in net cash	**17**	**7**	**26**

The impacts of the disposal of the Electric Motors & Actuators business on consolidated net sales and on the Group consolidated balance sheet are analyzed respectively in paragraphs 3.1 and 2.6.

2.2. Sale of Parrot

In the context of Parrot's IPO, Valeo decided to sell its 14.8% interest in the company. The capital gain on the sale of this non-consolidated investment was recognized in "Other financial income and expenses" for an amount of 24 million euros.

2.3. Investment in Threestar, a Korean company

In February 2006, Valeo acquired 50% of Threestar, the leading Korean manufacturer of automobile radiators. Valeo Samsung Thermal Systems, created through this agreement, was proportionally consolidated from January 1, 2006, with the remaining 50% of the capital being owned by the Samsung Climate Control Group. This company contributed 9 million euros to Group sales in 2006.

2.4. Disposal of Zexel Logitec

Valeo sold Zexel Logitec on June 30, 2006, and the company was deconsolidated as of that date. Zexel Logitec contributed 30 million euros to Group sales in 2006 for the period from January 1 to June 30. It contributed 53 million euros to Group sales in 2005. The capital gain recognized by the Group in the year in "Other income and expenses" amounted to 14 million euros.

2.5. Other transactions carried out in 2006

2.5.1. Ichikoh

Valeo raised its interest in Ichikoh, one of the largest Japanese lighting systems suppliers, from 28.2% at December 31, 2005 to 29.4% at December 31, 2006. Ichikoh is accounted for by the equity method.

2.5.2. Valeo Raytheon Systems Inc.

Valeo continued to invest in Raytheon Systems Inc., increasing its stake from 73.1% at December 31, 2005 to 77.2% at December 31, 2006. Valeo owns Raytheon Systems Inc. jointly with the Raytheon Group, and accounts for its interest by the proportional consolidation method because of the characteristics of the partnership agreement.

2.5.3. Investments in China

In the first half of 2006, Valeo created a Chinese joint-venture with Ichikoh and increased its interest in the Chinese company Hubei Valeo Auto Lighting Systems Co. Ltd. from 75% to 100%. These two transactions did not have material impacts on Group sales in 2006.

2.6. Impact of changes in scope of consolidation on the consolidated balance sheet

The assets, liabilities and contingent liabilities that have been acquired or sold in 2006, 2005 and 2004, measured at their date of entry into the Group or exit from the Group, are analyzed below and reconciled with the corresponding cash flows:

	2006			2005	2004
(In millions of euros)	Disposal of Electric Motors & Actuators	Other	Total		
Goodwill related to businesses sold	(23)	(3)	(26)	-	-
Other intangible assets	(10)	(3)	(13)	198	1
Property, plant and equipment	(58)	2	(56)	150	5
Investments in associates	-	3	3	8	(1)
Deferred tax assets	(2)	-	(2)	1	-
Current assets	(56)	(5)	(61)	298	9
Stockholders' equity	(50)	(13)	(63)	48	24
Long-term debt	1	-	1	(54)	(2)
Other non-current liabilities	33	-	33	(218)	(3)
Current liabilities	43	5	48	(244)	(6)
Net assets acquired (sold)	**(122)**	**(14)**	**(136)**	**187**	**27**
Minority interests	-	4	4	19	38
Total net assets acquired (sold) after minority interests	**(122)**	**(10)**	**(132)**	**206**	**65**
Goodwill on entities acquired	-	8	8	260	8
Impact of changes in scope of consolidation	**(122)**	**(2)**	**(124)**	**466**	**73**

The impact of changes in scope of consolidation in 2006 amounts to 124 million euros, after deducting costs paid on the sale of the Electric Motors & Actuators business.

The impact of the changes in the scope of consolidation on Group cash in 2005 (466 million euros) is mainly due to the following two transactions:

- acquisition of the Engine Electronics business of Johnson Controls Inc. for a total cost of 321 million euros; and
- acquisition of the remainder of the shares of ZVCC (Zexel Valeo Climate Control) and VZCCC (Valeo Zexel China Climate Control) for a total cost of 104 million euros.

In 2004, Group cash was notably impacted by the following changes in the scope of consolidation:

- buyout of the remaining minority interests in Valeo Climatisation;
- the increase in Valeo's interest in Shanghai Valeo Automotive Electrical Systems Co. Ltd. from 30% to 50%.

3. NOTES TO THE STATEMENT OF INCOME

3.1. Net sales

Group net sales amounted to 9,970 million euros in 2006 versus 9,736 million euros in 2005, an increase of 2.4% on the comparable prior-year period.

Changes in Group structure and changes in exchange rates had positive impacts of 1.5% and 0.5%, respectively. Consolidated net sales remained stable between 2005 and 2006 on a comparable Group structure and exchange rate basis.

As indicated in note 2.1, these amounts do not include net sales of the Electric Motors & Actuators business, which is included under the "Non-strategic activities" income statement caption for the three financial years presented.

Net sales of the Electric Motors & Actuators business amounted respectively to 224, 253 and 267 million euros for the 2006, 2005 and 2004 financial years.

The increase in net sales in 2005 compared to 2004 is principally due to the following two transactions:

- the acquisition of the Engine Electronics business of Johnson Controls Inc. on March 1, 2005, which had a favorable impact of 365 million euros on net sales; and
- the increase of Valeo's interest in a Japanese company, Valeo Thermal Systems Japan Corp., from 50% to 100% on April 1, 2005. This additional investment contributed 255 million euros to Group net sales.

3.2. Personnel expenses

	2006	2005	2004
Total employees (excluding non-strategic activities) (1)	69,700	68,600	64,500

(1) Including temporary staff.

The increase in the number of employees between 2004 and 2005 is due to the two main acquisitions carried out in 2005, as described in note 3.1.

The statement of income presents operating expenses by function. Operating expenses include the following personnel-related expenses:

(In millions of euros)	2006	2005	2004
Wages and salaries (1)	1,794	1,739	1,634
Social charges	421	392	391
Share-based payments	11	7	5
Pension expenses in respect of defined contribution schemes	115	126	136

(1) Including temporary staff.

Pension costs under defined benefit plans are set out in note 4.10.2.

3.3. Research and development expenditure

In 2006, research and development expenditure amounted to 661 million euros after deduction of 15 million euros corresponding to research tax credits granted in connection with these research and development costs.

In the previously published 2005 and 2004 statements of income, research and development tax credits were recognized under "income taxes". Research and development expenditure relating to these years has been restated in a manner comparable to 2006. Such expenditure amounted to 640 and 580 million euros for 2005 and 2004, respectively, after deduction of research tax credits of 6 and 5 million euros.

This reclassification of research tax credits did not modify either stockholders' equity or income from core activities for 2005 and 2004.

3.4. Other income and expenses

(In millions of euros)	2006	2005	2004
Claims and litigation	(13)	(16)	(9)
Restructuring and asset impairment	(61)	(34)	(74)
Goodwill impairment	-	-	(15)
Other	4	-	-
Other income and expenses	**(70)**	**(50)**	**(98)**

3.4.1. Claims and litigation

In 2006, this account mainly includes costs relating to commercial and labor disputes in progress.

The Group recognized income of 23 million euros in 2005 following the favorable completion of an industrial property dispute. The balance on this account notably includes costs related to the resolution in the year of customer claims.

3.4.2. Restructuring and asset impairment losses

- **Asset impairment losses**

Asset impairment losses of 15 million euros were recognized in other income and expenses in 2006, compared with 27 million euros in 2005.

These impairment losses mainly result from impairment tests carried out in accordance with the following methodology:

The recoverable amounts of groups of CGUs is calculated using five-year cash flow projections prepared on the basis of the budgets and medium-term plans of the Group's divisions. The forecasts are based on past experience, macroeconomic data in respect of the automobile market, order backlogs and products under development. After five years, cash flows are extrapolated using a growth rate of 1%. This growth rate does not exceed the average long-term growth rate of the Group's business sector. A post-tax discount rate of 7.5% is applied to the cash flows in 2006 (7% in 2005, 8% in 2004), on the basis of the Group's weighted average cost of capital. The use of after tax rates leads to the calculation of recoverable amounts identical to those that would be obtained from applying pre-tax rates to non-taxed cash flows.

These tests led the Group to recognize an exceptional impairment loss of 14 million euros in 2006 and 11 million euros in 2005 on a CGU in the lighting systems product group.

- **Restructuring**

Restructuring expenses of 46 million euros were recognized in 2006, comprising costs relating to the rationalization and closure of industrial sites, mainly in Western Europe.

3.4.3. Goodwill impairment

Goodwill is allocated to cash generating units (CGUs) on the basis of the product groups to which the goodwill is related. Such goodwill is subject to impairment tests at least once a year, following the same method as that used for the CGUs (see note 3.4.2).

These tests did not give rise to recognition of any goodwill impairment in 2006 and 2005; however they led to recognition of an impairment loss of 15 million euros at December 31, 2004.

3.4.4. Other

In 2006, this caption notably includes the capital gain on the disposal of Zexel Logitec Company for an amount of 14 million euros.

The balance on this account notably includes costs relating to strategic transactions.

3.5. Cost of net debt

(In millions of euros)	2006	2005	2004
Interest expense (1)	(78)	(72)	(49)
Interest income	21	20	17
Cost of net debt	**(57)**	**(52)**	**(32)**

(1) The application of IAS 39 on financial instruments at January 1, 2005 led to a year-on-year increase in interest expense of 7 million euros compared to 2004, mainly on OCEANE bonds.

3.6. Other financial income and expenses

(In millions of euros)	2006	2005	2004
Interest expense on unwinding of discount on pension obligations [1]	(49)	(56)	(52)
Expected returns on pension plan assets [1]	19	17	14
Currency gains and losses - net	1	(8)	(1)
Charges to provisions for credit risk	(4)	(6)	-
Gain (loss) on disposal of financial assets	27	-	-
Miscellaneous	(3)	1	2
Other financial income and expenses	**(9)**	**(52)**	**(37)**

(1) See note 4.10.2.

"Charges to provisions for credit risk" notably include an impairment provision of 2 million euros relating to a second tier customer, as well as the costs of credit insurance.

The "Gain (loss) on disposal of financial assets" caption mainly includes the income related to the sale of Parrot, for an amount of 24 million euros (see note 2.2).

3.7. Income taxes

3.7.1. Income tax expense

(In millions of euros)	2006	2005	2004
Current taxes	(84)	(71)	6
Deferred taxes	9	5	(24)
Income tax expense	**(75)**	**(66)**	**(18)**

3.7.2. Effective tax rate

The Group's average weighted tax rate for 2006 was 37% as against 30% in 2005 and 7% in 2004. The net tax charge for 2004 included an 83 million euro tax rebate received from the French tax authorities in respect of tax paid in 2001 on the gain from the disposal of the Group's 50% interest in LuK (an initial rebate of 88 million euros was received in 2003).

(% of income before tax)	2006	2005	2004
Standard tax rate in France	(34.4)	(34.9)	(35.4)
Impact of:			
• income taxed at other rates	8.5	6.8	1.7
• unused tax losses (current year) and unrecognized deferred tax assets	(27.6)	(24.4)	(16.1)
• use of prior-year tax losses	5.7	5.4	3.8
• permanent differences between book income and taxable income	7.4	6.3	3.0
• tax credits	3.8	10.8	35.9
Effective Group tax rate	**(36.6)**	**(30.0)**	**(7.1)**

3.8. Earnings per share

3.8.1. Basic earnings per share

	2006	2005	2004
Net income attributable to equity holders of the company (in millions of euros)	161	142	240
Average number of shares outstanding (in thousands)	76,795	79,320	82,202
Basic earnings per share (in euros)	**2.10**	**1.80**	**2.92**

3.8.2. Diluted earnings per share

	2006	2005	2004
Net income attributable to equity holders of the company (in millions of euros)	161	142	240
Interest expense on convertible bonds (1)	-	-	11
Average number of shares outstanding (in thousands)	76,795	79,320	82,202
Stock options (in thousands)	199	330	200
OCEANE convertible bonds (1)	-	-	10,105
Average number of shares used for the calculation of diluted earnings per share (in thousands)	76,994	79,650	92,507
Diluted earnings per share (in euros)	**2.09**	**1.79**	**2.71**

(1) Not taken into account in 2005 and 2006, in view of the potentially anti-dilutive impact of this adjustment (see note 1.8).

4. NOTES TO THE BALANCE SHEET

4.1. Goodwill

(In millions of euros)	2006	2005	2004
Net goodwill, January 1	**1,484**	**1,158**	**1,185**
Acquisitions during the year	8	260	5
Purchase price payments in respect of acquisitions made in previous years	-	-	3
Disposals	(26)	-	-
Translation adjustments	(51)	66	(20)
Impairment [1]	-	-	(15)
Net goodwill, December 31	**1,415**	**1,484**	**1,158**
Accumulated impairment losses at December 31	(32)	(33)	(33)

(1) See note 3.4.3.

In 2006, the change in goodwill excluding the effect of foreign currency movements is mainly due to the sale of the Electric Motors & Actuators business (see note 2.1).

In 2005, Valeo notably carried out the following transactions:

- acquisition of the Engine Electronics business of Johnson Controls Inc.;
- purchase of the entire share capital of Japanese company Valeo Thermal Systems Japan Corp.;
- increase of its interest in two Thai companies, Valeo Siam Thermal Systems Co. Ltd. and Valeo Thermal Systems Sales Thailand Co. Ltd.

Following identification and measurement of the assets acquired and liabilities assumed, goodwill relating to these 2005 acquisitions amounted to 260 million euros at December 31, 2005.

The main goodwill balances are broken down by group of CGUs as follows:

At December 31

(In millions of euros)	2006	2005	2004
Wiper Systems	221	236	216
Electronics and Connective Systems	213	217	214
Climate Control	209	223	175
Switches and Detection Systems	170	175	167
Engine Management Systems	181	181	-
Other	421	452	386
TOTAL	**1,415**	**1,484**	**1,158**

4.2. Other intangible assets

At December 31	2006			2005	2004
(In millions of euros)	Gross value	Amortization and impairment losses	Net value	Net value	Net value
Software	132	(97)	35	32	29
Patents and licenses	85	(54)	31	56	11
Capitalized development expenditure	550	(258)	292	279	222
Other	187	(17)	170	155	19
Intangible assets	**954**	**(426)**	**528**	**522**	**281**

Other intangible assets include customer relationship intangibles, mainly purchased in the context of 2005 acquisitions. In addition, patents and licenses include assets relating to technology intangibles acquired.

Changes in other intangible assets over 2004, 2005 and 2006 are analyzed below:

- 2004

(In millions of euros)	Software	Patents and licenses	Capitalized development expenditure	Other intangible assets	Total
Gross at January 1, 2004	**75**	**39**	**233**	**28**	**375**
Accumulated amortization and impairment	(52)	(25)	(50)	(14)	**(141)**
Net at January 1, 2004	**23**	**14**	**183**	**14**	**234**
Acquisitions	9	3	97	13	**122**
Disposals	2	(1)	(3)	(1)	**(3)**
Changes in scope of consolidation	-	-	-	1	**1**
Impairment losses	-	-	(6)	-	**(6)**
Amortization	(14)	(6)	(47)	(2)	**(69)**
Translation adjustments	-	-	(1)	-	**(1)**
Reclassifications	9	1	(1)	(6)	**3**
Net at December 31, 2004	**29**	**11**	**222**	**19**	**281**

- 2005

(In millions of euros)	Software	Patents and licenses	Capitalized development expenditure	Other intangible assets	Total
Gross at January 1, 2005	**94**	**41**	**325**	**27**	**487**
Accumulated amortization and impairment	(65)	(30)	(103)	(8)	**(206)**
Net at January 1, 2005	**29**	**11**	**222**	**19**	**281**
Acquisitions	12	2	118	13	**145**
Disposals	2	(1)	-	(3)	**(2)**
Changes in scope of consolidation	1	53	3	141	**198**
Impairment losses	-	-	(7)	(1)	**(8)**
Amortization	(19)	(10)	(65)	(7)	**(101)**
Translation adjustments	1	(1)	8	(1)	**7**
Reclassifications	6	2	-	(6)	**2**
Net at December 31, 2005	**32**	**56**	**279**	**155**	**522**

▪ 2006

(In millions of euros)	Software	Patents and licenses	Capitalized development expenditure	Other intangible assets	Total
Gross at January 1, 2006	**119**	**96**	**458**	**171**	**844**
Accumulated amortization and impairment	(87)	(40)	(179)	(16)	**(322)**
Net at January 1, 2006	**32**	**56**	**279**	**155**	**522**
Acquisitions	13	4	128	19	**164**
Disposals	-	-	(2)	-	**(2)**
Changes in scope of consolidation	(2)	(2)	(8)	(1)	**(13)**
Impairment losses	-	-	(10)	-	**(10)**
Amortization	(19)	(9)	(85)	(8)	**(121)**
Translation adjustments	(1)	(1)	(4)	(1)	**(7)**
Reclassifications	12	(17)	(6)	6	**(5)**
Net at December 31, 2006	**35**	**31**	**292**	**170**	**528**

4.3. Property, plant and equipment

At December 31	2006				2005		2004	
(In millions of euros)	Gross carrying amount	Depreciation and impairment losses	Net carrying amount	of which finance leases	Net carrying amount	of which finance leases	Net carrying amount	of which finance leases
Land	156	(10)	146	-	167	-	145	1
Buildings	971	(552)	419	6	458	15	456	12
Plant and equipment	3,322	(2,452)	870	4	933	5	880	4
Specific tooling	1,169	(1,023)	146	3	155	9	152	7
Other	468	(370)	98	5	123	6	120	8
Non-current assets in progress	239	-	239	-	205	-	192	-
Property, plant and equipment	**6,325**	**4,407**	**1,918**	**18**	**2,041**	**35**	**1,945**	**32**

Property, plant and equipment pledged as security amounted to 24 million euros at December 31, 2006.

Changes in property, plant and equipment over 2004, 2005 and 2006 are analyzed below:

▪ 2004

(In millions of euros)	Land	Buildings	Plant and equipment	Specific tooling	Other	Fixed assets in progress	Total
Gross at January 1, 2004	**156**	**895**	**2,927**	**1,000**	**475**	**197**	**5,650**
Accumulated depreciation and impairment	(8)	(449)	(1,972)	(812)	(353)	-	**(3,594)**
Net at January 1, 2004	**148**	**446**	**955**	**188**	**122**	**197**	**2,056**
Capital expenditure	2	37	110	42	40	200	**431**
Disposals	-	(6)	(2)	(4)	(2)	(11)	**(25)**
Changes in scope of consolidation	-	2	3	-	-	-	**5**
Impairment losses	(1)	-	(8)	(3)	-	-	**(12)**
Depreciation	-	(48)	(274)	(112)	(57)	-	**(491)**
Translation adjustments	(2)	1	(3)	-	-	1	**(3)**
Reclassifications	(2)	24	99	41	17	(195)	**(16)**
Net at December 31, 2004	**145**	**456**	**880**	**152**	**120**	**192**	**1,945**

▪ 2005

(In millions of euros)	Land	Buildings	Plant and equipment	Specific tooling	Other	Fixed assets in progress	Total
Gross at January 1, 2005	**155**	**934**	**2,977**	**1,021**	**489**	**192**	**5,768**
Accumulated depreciation and impairment	(10)	(478)	(2,097)	(869)	(369)	-	**(3,823)**
Net at January 1, 2005	**145**	**456**	**880**	**152**	**120**	**192**	**1,945**
Capital expenditure	1	19	154	65	43	165	**447**
Disposals	(10)	(13)	(8)	(2)	-	(12)	**(45)**
Available-for-sale assets (1)	(2)	(9)	-	-	-	-	**(11)**
Changes in scope of consolidation	30	20	71	4	7	18	**150**
Impairment losses	(1)	(2)	(12)	(2)	(9)	-	**(26)**
Depreciation	-	(50)	(286)	(113)	(55)	-	**(504)**
Translation adjustments	6	20	40	9	6	7	**88**
Reclassifications	(2)	17	94	42	11	(165)	**(3)**
Net at December 31, 2005	**167**	**458**	**933**	**155**	**123**	**205**	**2,041**

▪ 2006

(In millions of euros)	Land	Buildings	Plant and equipment	Specific tooling	Other	Fixed assets in progress	Total
Gross at January 1, 2006	**178**	**1,012**	**3,346**	**1,155**	**538**	**205**	**6,434**
Accumulated depreciation and impairment	(11)	(554)	(2,413)	(1,000)	(415)	-	**(4,393)**
Net at January 1, 2006	**167**	**458**	**933**	**155**	**123**	**205**	**2,041**
Capital expenditure	2	24	179	63	33	191	**492**
Disposals	-	(1)	(1)	(2)	(3)	(8)	**(15)**
Available-for-sale assets (1)	-	(9)	-	-	-	-	**(9)**
Changes in scope of consolidation	(8)	(17)	(20)	(4)	(3)	(4)	**(56)**
Impairment losses	(1)	-	(5)	(1)	(1)	-	**(8)**
Depreciation	(1)	(50)	(284)	(103)	(46)	-	**(484)**
Translation adjustments	(8)	(6)	(13)	(3)	(3)	(6)	**(39)**
Reclassifications	(5)	20	81	41	(2)	(139)	**(4)**
Net at December 31, 2006	**146**	**419**	**870**	**146**	**98**	**239**	**1,918**

(1) In the context of application of IFRS 5, buildings for which the Group is actively seeking buyers are classified in Assets held for sale.

4.4. Investments in associates

Changes in the “Investments in associates” caption can be analyzed as follows:

(In millions of euros)	2006	2005	2004
Investments in associates at January 1	**116**	**96**	**99**
Share of profit in associates	-	6	5
Dividend payments	(4)	(4)	(3)
Impacts of changes in the scope of consolidation	3	8	(1)
Translation adjustments	(13)	7	(4)
Other	1	3	-
Investments in associates at December 31	**103**	**116**	**96**

At December 31	Ownership interest (%)			Equity in net assets (In millions of euros)		
	2006	2005	2004	2006	2005	2004
Ichikoh	29.4	28.2	22.7	72	80	64
Faw Valeo Climate Control	36.5	36.5	36.5	23	25	21
Other	-	-	-	8	11	11
Investments in associates	**-**	**-**	**-**	**103**	**116**	**96**

Ichikoh is a company listed on the Tokyo Stock Exchange. At December 31, 2006, the market capitalization of the shares held by the Valeo Group was 58 million euros. The carrying amount of the investment is supported by its value in use.

Summarized financial data in respect of associates are set out below:

(In millions of euros)	2006	2005	2 004
Total assets	703	754	776
Total liabilities	483	509	490
Total operating revenues	950	1,011	1,228
Net income for the period	(3)	20	20

4.5. Non-current financial assets

Non-current financial assets are broken down as follows:

At December 31 (In millions of euros)	2006	2005	2004
Non-consolidated investments	2	9	8
Long-term loans	16	12	2
Security deposits	3	3	2
Other	3	4	2
Non-current financial assets	**24**	**28**	**14**

4.6. Deferred taxes

Deferred tax assets and liabilities are offset when a legal right of offset of current tax assets and liabilities exists and the deferred tax assets and liabilities concern income taxes levied by the same tax authority. In France, Valeo elected for tax consolidation for the years 2003 to 2007. The tax group includes the parent company and its principal French subsidiaries that are eligible for tax consolidation.

Valeo also elected for tax consolidation for its subsidiaries in other countries whose legislation permits it (Germany, Spain, Italy, the United Kingdom and the United States).

At December 31

(In millions of euros)	2004	2005	Recognized through income	Other [1] movements	2006
Loss carry forwards [2]	17	12	9	12	33
Capitalized development expenditure	(69)	(82)	(14)	4	(92)
Pensions and other employee benefits	53	63	4	-	67
Other provisions	42	62	(10)	13	65
Inventories	13	15	-	-	15
Provisions for reorganization expenses	14	11	7	2	20
Tooling	9	8	(1)	-	7
Non-current assets	(5)	(4)	9	(6)	(1)
Other	(4)	6	5	(30)	(19)
Total deferred taxes	**70**	**91**	**9**	**(5)**	**95**
Of which: Deferred tax assets	83	100			96
Deferred tax liabilities	(13)	(9)			(1)

(1) Other movements comprise (1) million euros of deferred taxes relating to actuarial gains and losses recognized through stockholders' equity, (2) million euros related to the impact of changes in the scope of consolidation and (2) million euros related to translation adjustments. In addition, reclassifications have been made between the different types of deferred taxes.

(2) Deferred tax assets are recognized in respect of tax loss carry forwards to the extent that it is probable that future profits will be available against which they may be offset.

At December 31, 2006, deferred tax assets not recognized by the Group are broken down as follows:

At December 31

(In millions of euros)	Base	Potential tax saving
Tax loss carry forwards - expiration date 2007 to 2010	137	47
Tax loss carry forwards - expiration date 2010 and beyond	632	212
Tax loss carry forwards - available indefinitely	839	287
Current tax loss carry forwards	**1,608**	**546**
Unrecognized deferred tax assets on temporary differences	-	232
Total unrecognized deferred tax assets	**1,608**	**778**

4.7. Inventories

At December 31, 2006, inventories are broken down as follows:

At December 31	2006			2005	2004
(In millions of euros)	Gross	Provisions	Net	Net	Net
Raw materials	275	(44)	231	221	189
Work-in-progress	80	(6)	74	81	71
Finished goods, supplies and specific tooling	401	(59)	342	352	305
Inventories - net	**756**	**(109)**	**647**	**654**	**565**

Provisions for impairment in the value of inventories amounted to 109 million euros at December 31, 2006 (130 millions euros at December 31, 2005), including an allowance of 26 million euros in the year.

In 2005, allowances to provisions for impairment amounted to 35 million euros.

The cost of inventories recognized in cost of sales (excluding the Electric Motors & Actuators business) was 8,166 million euros in 2006 as against 7,923 million euros in 2005 and 7,230 million euros in 2004.

4.8. Accounts and notes receivable

At December 31

(In millions of euros)	2006	2005	2004
Accounts and notes receivable	**1,864**	**1,938**	1,748
Less provisions	(30)	(32)	(22)
Accounts and notes receivable - net	**1,834**	**1,906**	**1,726**

Allowances to provisions against accounts and notes receivable are recognized in "Other financial income and expenses" where such a provision results from a risk of client default (see note 3.6) and in administrative expenses in other cases.

4.9. Stockholders' equity

4.9.1. Share capital

At December 31, 2006, Valeo's share capital totaled 233 million euros, represented by 77,580,617 shares of common stock with a par value of 3 euros each, all fully paid-up. Shares that have been registered in the name of the same holder for at least four years carry double voting rights (2,215,541 at December 31, 2006).

Valeo's potential share capital would amount to 274 million euros, representing 91,430,106 shares, in the event of:

- the exercise of stock subscription options granted to Valeo Group employees;
- the conversion of bonds issued as part of the OCEANE program into new shares (see note 4.11.2).

The following employee stock option plans and free share plans approved by the Annual General Meeting were in progress at December 31, 2006:

- Terms and conditions of stock subscription plans

Year in which the plan was set up	Number of shares subject to options	Exercise price [(1)] of options (in euros)	Number of options [(2)] outstanding at December 31, 2006	Expiry date
2000	1,300,000	48.00	419,673	2008
2001	80,000	55.82	80,800	2009
2001	600,000	42.48	303,000	2009
2001	442,875	42.69	301,808	2009
2002	420,000	43.84	241,188	2010
2002	600,000	28.30	353,248	2010
2003	700,000	23.51	506,817	2011
2003	780,000	32.91	580,273	2011
2004	1,123,200	28.46	957,243	2012
Total	**6,046,075**		**3,744,050**	

(1) Exercise price equal to 100% of the average Valeo share price over the 20 trading days preceding the meeting of the Board of Directors or Management Board granting the stock subscription options.

(2) The number of shares includes the impact of the public share buyback offer and simplified public tender offer, which increased the share allocation ratio to 1.01 Valeo share from 1 Valeo share.

- Terms and conditions of stock option plans

Year in which the plan was set up	Number of shares subject to options	Exercise price [1] of options (in euros)	Number of options [2] outstanding at December 31, 2006	Expiry date
2003	500,000	32.91	371,457	2011
2004	280,800	32.74	240,370	2012
2005	650,000	32.32	596,380	2013
2006	187,000	33.75	187,000	2014
2006	1,309,250	32.63	1,309,250	2014
Total	**2,927,050**		**2,704,457**	

(1) Exercise price equal to 100% of the average Valeo share price over the 20 trading days preceding the meeting of the Board of Directors or Management Board or 100% of the average purchase price of treasury stock held if this is greater than the Valeo quoted share price.

(2) The number of shares includes the impact of the public share buyback offer and simplified public tender offer, applicable to grants prior to 2005, which increased the share allocation ratio to 1.01 Valeo share from 1 Valeo share.

- Terms and conditions of free share awards

Year in which plan was set up	Number of free shares granted	Number of shares not yet issued at Dec. 31, 2006	Year of vesting
2005	600,000 [1]	541,870	2008
2006	63,000 [2]	63,000	2008
2006	100,000	100,000	2009
Total	**763,000**	**704,870**	

(1) Including 300,000 shares granted subject to the Group achieving certain profitability criteria.

(2) Including 36,500 shares granted subject to the Group achieving certain profitability criteria.

Movements on the stock option plans can be analyzed as follows:

▪ 2004	2004	
	Number of options and free shares	Weighted average exercise price
Options not exercised at January 1, 2004	**5,524,925**	**40.92**
Options granted/free shares to be issued	1,404,000	29.32
Options cancelled	(393,700)	39.91
Options expired	(58,250)	67.40
Options exercised	-	-
Options not exercised/free shares not issued on December 31	**6,476,975**	**38.23**
Options which can be exercised on December 31, 2004	**3,288,725**	**46.75**

▪ 2005

	2005	
	Number of options and free shares	Weighted average exercise price
Options not exercised at January 1, 2005	**6,476,975**	**38.23**
Options granted/free shares to be issued	1,250,000	16.81
Options cancelled	(748,200)	37.67
Options expired	(485,250)	70.32
Options exercised	(51,120)	25.69
Options not exercised/free shares not issued on December 31	**6,442,405**	**31.82**
Options which can be exercised on December 31, 2005	**3,099,668**	**39.50**

▪ 2006

	2006	
	Number of options and free shares	Weighted average exercise price
Options not exercised at January 1, 2006	**6,442,405**	**31.82**
Options granted/free shares to be issued	1,659,250	29.55
Options cancelled	(490,575)	29.49
Options expired	(432,125)	50.01
Options exercised	(69,555)	25.88
Options not exercised/free shares not issued on December 31	**7,109,400**	**30.50**
Options which can be exercised on December 31, 2006	**3,759,575**	**35.21**

Taking account of the impact of the public share buyback offer and the simplified public tender offer, the 7,109,400 stock options and free shares in circulation at December 31, 2006 carry rights to 7,153,377 Valeo shares. The 69,555 options exercised in 2006 carried rights to 70,260 Valeo shares.

The principal data and assumptions underlying the valuation of equity instruments at fair value can be analyzed as follows:

Type	2006	
	March	November
	Free shares and purchase option	Free shares and purchase option
Share price at date of grant (euros)	31.79	30.16
Expected volatility (%)	- and 24.6	- and 29.0
Risk-free rate (%)	3.3 and 3.5	3.9
Dividend rate (%)	3.2	3.2
Duration of the option (years)	2.25 and 4	3 and 4
Fair value of the equity instrument (euros)	**29.28 and 4.92**	**26.32 and 5.54**

Type	2005 Free shares and purchase option	2004 Subscription option and purchase option	2003 Subscription option
Share price at date of grant (euros)	31.46	29.77	32.63 and 20.21
Expected volatility (%)	- and 26.4	25.8	31.7 and 36.6
Risk-free rate (%)	2.9 and 3.1	3.1	3.7 and 3.2
Dividend rate (%)	3.1	3.4	3.4
Duration of the option (years)	2.25 and 4	4	4

Expected volatility is determined as being the implicit volatility at the date of grant of the plan. The maturity of four years used for stock option plans corresponds to the period for which the availability of options is restricted by tax legislation, which is estimated to correspond to the duration of the option.

Given an employee turnover assumption of 5%, an expense of 11 million euros was recognized in respect of 2006, as against an expense of 7 million euros for 2005.

An expense of 2 million euros was recognized in 2004 reflecting recognition of a liability in respect of SARs (Share Appreciation Rights) granted in the context of an employee share plan. A derivative used to hedge the corresponding commitment was recognized on January 1, 2005 in an amount of 2 million euros on first time application of IAS 39.

At December 31, 2006, the liability and the derivative are both recognized in the Group's financial statements in an amount of 1 million euros. As rights related to the SARs ("Share Appreciation Rights") were not vested at the year-end their intrinsic value is nil.

4.9.2. Additional paid-in capital

Additional paid-in capital represents the net amount received, either in cash or in assets, in excess of the par value on issuance of Valeo shares.

4.9.3. Translation adjustment

The translation adjustment reserve at December 31, 2006 primarily includes gains and losses arising from the translation of the net assets of Valeo's Tunisian, Turkish, Mexican, US, Brazilian, Japanese, South Korean and Chinese subsidiaries.

4.9.4. Retained earnings

Consolidated retained earnings include net income for the year amounting to 161 million euros (before appropriation of the dividend to be proposed at the Annual General Meeting).

The balance of the parent company's distributable retained earnings amounts to 1,589 million euros, before appropriation of 2006 net income (respectively 1,593 and 1,596 million euros in 2005 and 2004).

4.9.5. Dividends per share

Dividends paid in 2006 amounted to 84,391 thousand euros, being 1.10 euro per share, as against 91,276 euros (1.10 euro per share) in 2005 and 85,307 thousand euros (1.05 euro per share) in 2004. A dividend of 1.10 euro per share for the year ended December 31, 2006 will be proposed to the Annual General Meeting. This distribution is not recognized in accrued liabilities in the financial statements at December 31, 2006.

4.9.6. Treasury stock

At December 31, 2006, Valeo owns 686,704 of its own shares, representing 0.89% of share capital, as against 807,704 shares (1.04%) at December 31, 2005 and 1,037,804 shares (1.24%) at December 31, 2004.

4.9.7. Minority interests

Changes in minority interests can be analyzed as follows:

(In millions of euros)	2006	2005	2004
Minority interests at January 1	**43**	**57**	**97**
Equity in net earnings	5	6	8
Dividends paid	(4)	(5)	(7)
Translation adjustment	(3)	4	(3)
Changes in the scope of consolidation	(3)	(19)	(38)
Minority interests at December 31	**38**	**43**	**57**

4.10. Provisions

Changes in provisions can be analyzed as follows:

(In millions of euros)	Provisions for reorganization expenses	Provisions for pensions and other employee benefits	Other provisions	Total
Provisions at January 1, 2004	**224**	**870**	**265**	**1,359**
Amounts used during the year	(102)	(112)	(57)	(271)
Impacts of changes in the scope of consolidation	-	1	2	3
Translation adjustments	(3)	(30)	(1)	(34)
Reclassification	(6)	6	(1)	(1)
Additions	57	39	100	196
Unwinding of discount	-	40	-	40
Reversals	(5)	-	(31)	(36)
Actuarial gains and losses recognized through equity	-	42	-	42
Provisions at December 31, 2004	**165**	**856**	**277**	**1,298**
Amounts used during the year	(103)	(89)	(91)	(283)
Impacts of changes in the scope of consolidation	10	15	192	217
Translation adjustments	10	62	13	85
Reclassification	(6)	13	(6)	1
Additions	108	89	154	351
Unwinding of discount	1	39	-	40
Reversals [(2)]	(4)	(152)	(49)	(205)
Actuarial gains and losses recognized through equity	-	50	-	50
Provisions at December 31, 2005	**181**	**883**	**490**	**1,554**
Amounts used during the year	(82)	(62)	(107)	(251)
Impacts of changes in the scope of consolidation	(3)	(27)	(3)	(33)
Translation adjustment	(10)	(34)	(6)	(50)
Reclassification [(1)]	42	(41)	3	4
Additions	55	28	105	188
Unwinding of discount	4	31	-	35
Reversals	(11)	(3)	(51)	(65)
Actuarial gains and losses recognized through equity	-	(27)	-	(27)
Provisions at December 31, 2006	**176**	**748**	**431**	**1,355**
Of which current portion (< 1 year)	89	73	256	418

(1) Including, in 2006, a reclassification of 41 million euros from provisions for pensions to provisions for reorganization expenses in connection with healthcare plans for early retirees in the United States.

(2) Releases of provisions for pension and other employee benefits include an amount of (127) million euros relating to amendments to the healthcare insurance plan in the United States and an amount of (20) million euros in connection with the reduction in benefit entitlement due to the closure of the Rochester site.

4.10.1. Provisions for reorganization expenses

Provisions for reorganization expenses correspond to a series of measures adopted by the Group as part of an industrial streamlining plan aimed at more closely tailoring Valeo's industrial base to customer requirements, in terms of cost competitiveness and geographical location. The provisions include costs relating primarily to:

- continued rightsizing and production streamlining measures;
- and specific severance payments (CATS) applicable at certain French sites, in accordance with the industry agreement signed in March 2001.

4.10.2. Provisions for pensions and other employee benefits

■ Description of the plans in force within the Group

The Group's commitments in relation to pensions and other employee benefits primarily concern the following defined benefit plans:

- termination benefits (France, Italy, Mexico, South Korea);
- supplementary pension benefits (United States, Germany, United Kingdom, Japan and France) which top up the statutory pension schemes in force in those countries. These plans are generally externally funded, with the exception being in Germany;
- the payment of certain medical and life insurance costs for retired employees (United States),
- certain of the above-mentioned benefits granted specifically under early retirement schemes (United States, Germany and France),
- other long-term benefits (long-service bonuses in France and Germany).

The costs relating to all of these benefits are accounted for in accordance with the accounting policy described in note 1.17.

■ Actuarial assumptions

The actuarial assumptions used by the Group to calculate its obligations relating to pensions and other employee benefits take into account the specific demographic and financial conditions of each country in which the Group operates and each Group company.

Discount rates are determined by reference to market yields at the valuation date on high quality corporate bonds with a term consistent with that of the employee benefits concerned.

In 2006, the average discount rates used in the countries representing the Group's most significant obligations were as follows:

At December 31	2006 (%)	2005 (%)	2004 (%)
France	4.5	4.3	4.5
Germany	4.4	4.1	4.8
United Kingdom	5.0	4.8	5.3
Italy	4.3	4.0	4.0
United States	5.9	5.6	5.7
Mexico	9.3	8.5	10.2
Japan	2.1	1.8	2.0
South Korea	5.3	5.8	4.5

The discount rates for early retirement plan obligations are lower than the rates set out above, as the obligations have shorter terms than for pensions.

The expected long-term return on plan assets has been calculated taking into account the structure of the investment portfolio in each country. The rates are as follows for the principal funds invested by the Group:

At December 31	2006 (%)	2005 (%)	2004 (%)
United States	8.5	8.5	8.5
United Kingdom	6.4	6.7	7.0
Japan	2.7	2.0	2.0
South Korea	4.5	4.5	5.0

The weighted average rate of long-term salary increases was 3.5% at December 31, 2006, unchanged compared to December 31, 2005. It was 3.6% at December 31, 2004.

The rate of increase for medical costs in the United States used to value the Group's obligations was 10% at December 31, 2006, 2005 and 2004, reducing by one percentage point a year from 2010 to reach 5% in 2014.

- Breakdown of obligations

At December 31, 2004

(In millions of euros)	France	Other European countries	North America	Other countries	Total
Present value of unfunded obligations	168	248	303	37	756
Present value of funded obligations	19	58	230	30	337
Market value of plan assets	(1)	(37)	(148)	(25)	(211)
Deficit	**186**	**269**	**385**	**42**	**882**
Unrecognized past service cost	(34)	-	8	-	(26)
Provisions recognized at December 31, 2004	**152**	**269**	**393**	**42**	**856**

At December 31, 2005

(In millions of euros)	France	Other European countries	North America	Other countries	Total
Present value of unfunded obligations	179	286	201	44	710
Present value of funded obligations	24	73	325	56	478
Market value of plan assets	(3)	(42)	(197)	(52)	(294)
Deficit	**200**	**317**	**329**	**48**	**894**
Unrecognized past service cost	(31)	-	20	-	(11)
Provisions recognized at December 31, 2005	**169**	**317**	**349**	**48**	**883**

At December 31, 2006

(In millions of euros)	France	Other European countries	North America	Other countries	Total
Present value of unfunded obligations	181	266	142	47	636
Present value of funded obligations	27	77	287	47	438
Market value of plan assets	(5)	(45)	(205)	(46)	(301)
Deficit	**203**	**298**	**224**	**48**	**773**
Unrecognized past service cost	(26)	-	1	-	(25)
Provisions recognized at December 31, 2006	**177**	**298**	**225**	**48**	**748**

■ Movements in provisions

(In millions of euros)	France	Other European countries	North America	Other countries	Total
Provisions at January 1, 2004	**148**	**254**	**436**	**32**	**870**
Actuarial gains and losses recognized through equity	5	14	18	5	42
Amounts used during the year (1)	(21)	(18)	(68)	(5)	(112)
Impacts of changes in the scope of consolidation	-	-	-	1	1
Reclassification pension/reorganization expenses	(3)	(1)	10	-	6
Translation adjustments	-	(1)	(30)	1	(30)
Provisions for the year (expense)					
• service cost	10	9	12	7	38
• interest expense	8	13	31	2	54
• past service cost	7	-	(6)	-	1
• expected return on plan assets	-	(2)	(11)	(1)	(14)
• other items	(2)	1	1	-	-
Provisions at December 31, 2004	**152**	**269**	**393**	**42**	**856**
Actuarial gains and losses recognized through equity	7	40	15	(12)	50
Amounts used during the year (1)	(19)	(14)	(49)	(7)	(89)
Impacts of changes in the scope of consolidation	5	1	2	7	15
Reclassification pension/reorganization expenses	-	-	13	-	13
Translation adjustments	-	1	54	7	62
Provisions for the year (expense)					
• service cost	10	10	10	9	39
• interest expense	8	14	31	3	56
• past service cost	6	-	(127) (2)	-	(121)
• expected return on plan assets	-	(2)	(14)	(1)	(17)
• other items	-	(2)	21 (3)	-	19
Provisions at December 31, 2005	**169**	**317**	**349**	**48**	**883**
Actuarial gains and losses recognized through equity	3	(4)	(28)	2	(27)
Amounts used during the year (1)	(22)	(14)	(18)	(8)	(62)
Impacts of changes in the scope of consolidation	-	(25)	(1)	(1)	(27)
Reclassification pension/reorganization expenses	-	1	(42)	-	(41)
Translation adjustments	-	1	(32)	(3)	(34)
Provisions for the year (expense)					
• service cost	17	10	7	8	42
• interest expense	8	14	25	3	50
• past service cost	5	-	(19)	-	(14)
• expected return on plan assets	-	(2)	(16)	(1)	(19)
• other items	(3)	-	-	-	(3)
Provisions at December 31, 2006	**177**	**298**	**225**	**48**	**748**
Of which current portion (< 1 year)	20	17	31	5	73

(1) Including benefits paid directly to beneficiaries or contributions paid to external funds, depending on the plan concerned.

(2) Corresponds to changes in retiree medical plans.

(3) Of which (20) million euros in connection with the reduction in benefit entitlement and the 41 million euro effect of acceleration of rights in the context of the closure of the Rochester site.

- Movements in obligations

(In millions of euros)	France	Other European countries	North America	Other countries	Total
Obligations at January 1, 2004	**165**	**281**	**550**	**59**	**1,055**
Service cost	10	9	11	8	38
Interest expense	8	13	31	2	54
Benefits paid	(21)	(18)	(42)	(7)	(88)
Actuarial gains and losses	2	12	25	4	43
Plan amendments	26	3	-	-	29
Impacts of changes in the scope of consolidation	-	-	-	1	1
Other	(3)	6	-	-	3
Translation adjustments	-	-	(42)	-	(42)
Obligations at December 31, 2004	**187**	**306**	**533**	**67**	**1,093**
Service cost	10	10	10	9	39
Interest expense	8	14	31	3	56
Benefits paid	(18)	(15)	(42)	(10)	(85)
Actuarial gains and losses	9	43	16	(7)	61
Plan amendments	2	(1)	(116)	-	(115)
Impacts of changes in the scope of consolidation	5	1	4	31	41
Other	-	-	13	-	13
Translation adjustments	-	1	77	7	85
Obligations at December 31, 2005	**203**	**359**	**526**	**100**	**1,188**
Service cost	17	10	7	8	42
Interest expense	8	14	25	3	50
Benefits paid	(21)	(15)	(10)	(10)	(56)
Actuarial gains and losses	3	(4)	(28)	2	(27)
Plan amendments	-	-	(19)	-	(19)
Impacts of changes in the scope of consolidation	-	(25)	(1)	(1)	(27)
Other	(2)	2	(18)	-	(18)
Translation adjustments	-	2	(53)	(8)	(59)
Obligations at December 31, 2006	**208**	**343**	**429**	**94**	**1,074**

Movements in plan assets

(In millions of euros)	France	Other European countries	North America	Other countries	Total
Plan assets at January 1, 2004	**2**	**33**	**116**	**28**	**179**
Expected return on plan assets	-	2	11	1	14
Contributions paid to external funds	1	2	31	2	36
Benefits paid	(1)	-	(5)	(4)	(10)
Actuarial gains and losses	(1)	-	7	(1)	5
Impacts of changes in the scope of consolidation	-	-	-	-	-
Other	-	-	-	-	-
Translation adjustments	-	-	(12)	(1)	(13)
Plan assets at December 31, 2004	**1**	**37**	**148**	**25**	**211**
Expected return on plan assets	-	2	14	1	17
Contributions paid to external funds	2	-	13	4	19
Benefits paid	(1)	(1)	(6)	(7)	(15)
Actuarial gains and losses	1	3	-	5	9
Impacts of changes in the scope of consolidation	-	-	3	23	26
Other	-	-	-	-	-
Translation adjustments	-	1	25	1	27
Plan assets at December 31, 2005	**3**	**42**	**197**	**52**	**294**
Expected return on plan assets	-	2	16	1	19
Contributions paid to external funds	2	1	9	3	15
Benefits paid	-	(1)	(1)	(5)	(7)
Actuarial gains and losses	-	-	1	-	1
Impacts of changes in the scope of consolidation	-	-	-	-	-
Other	-	-	5	-	5
Translation adjustments	-	1	(22)	(5)	(26)
Plan assets at December 31, 2006	**5**	**45**	**205**	**46**	**301**

Breakdown of plan assets

(In millions of euros)	France	Other European countries	North America	Other countries	Total
Cash at bank	-	-	3	22	25
Shares	1	28	125	-	154
Government bonds	-	5	13	-	18
Corporate bonds	-	4	7	3	14
Breakdown of plan assets at December 31, 2004	**1**	**37**	**148**	**25**	**211**
Cash at bank	-	-	5	4	9
Shares	2	29	163	19	213
Government bonds	-	7	22	25	54
Corporate bonds	1	6	7	4	18
Breakdown of plan assets at December 31, 2005	**3**	**42**	**197**	**52**	**294**
Cash at bank	-		6	8	14
Shares	3	44	167	15	229
Government bonds	-	1	22	23	46
Corporate bonds	2	-	10	-	12
Breakdown of plan assets at December 31, 2006	**5**	**45**	**205**	**46**	**301**

Contributions of 15 million euros were paid to external funds in 2006. Contributions in 2007 are estimated at 30 million euros.

The effective return on plan assets amounted to 31 million euros in 2006, as against 26 million euros in 2005 and 21 million euros in 2004.

The effects of a change of one point in the rate of increase in medical costs in the United States are as follows:

	2006		2005		2004	
(In millions of euros)	Increase	Decrease	Increase	Decrease	Increase	Decrease
Effect on service cost and interest expense	-	-	2	(2)	2	(2)
Effect on obligations	2	(2)	3	(3)	29	(23)

4.10.3. Other provisions

At December 31

(In millions of euros)	2006	2005	2004
Provisions for product warranties	180	226	108
Other [1]	251	264	169
Other provisions	**431**	**490**	**277**

(1) Other provisions mainly concern contractual, labor, environmental or tax risks and litigation.

At December 31, 2005, movements of 125 million euros in this account caption arise as a result of changes in the scope of consolidation in that year.

4.11. Debt

4.11.1. Gross debt

At December 31, 2006, the Group's gross debt can be analyzed as follows:

(In millions of euros)	2006	2005	2004
Long-term debt (note 4.11.2)	1,274	1,303	1,027
Current maturities of long-term debt (note 4.11.2)	54	581	188
Short-term debt (note 4.11.3)	274	157	175
Gross debt	**1,602**	**2,041**	**1,390**

4.11.2. Long-term debt

- Analysis of long-term debt

At December 31

(In millions of euros)	2006	2005	2004
Bond issues	595	1 094	500
OCEANE (1)	427	419	463
Syndicated loans	216	221	127
Lease obligations	15	25	28
Other borrowings	49	86	72
Accrued interest	26	39	25
Long-term debt	**1,328**	**1,884**	**1,215**

(1) The carrying amount of the OCEANE was reduced from 463 million euros to 419 million euros following application of IAS 32 at January 1, 2005.

Long-term debt includes:

- 600 million euros worth of eight-year fixed rate bonds issued by Valeo on June 24, 2005. The interest rate on these bonds is 3.75% of the nominal amount. These bonds were issued in the context of the Euro Medium Term Note program. The effective interest rate on these bonds is 3.89%;
- 463 million euros worth of bonds convertible for new shares or exchangeable for existing shares (OCEANE) issued on August 4, 2003, representing 9,975,754 bonds with a nominal value of 46.4 euros each. The interest on these bonds is 2.375% per annum payable in arrears on January 1 of each year. Bearers of the bonds can at any time request conversion and/or exchange into common stock on the basis of 1.013 Valeo shares for one bond.

  In addition, Valeo has a call option that may be exercised between January 31, 2007 and December 31, 2010 if the Valeo share is valued at an average price of 60 euros. The effective interest rate of the OCEANE amounts to 4.54% (4.46% excluding the call);
- two seven-year syndicated loans for a total amount of 225 million euros issued on July 29, 2005, hedged by two interest rate swaps which are perfectly matched in both amount and duration. These loans and the related hedges have the following characteristics:
  - the first loan is at a variable rate and incorporates a cap which limits the interest rate to a maximum of 4.735%. It is hedged by a derivative which offsets the option incorporated in the loan,
  - the second loan is at a fixed rate of 3.62% and incorporates a swap option that enables the Group to opt for a variable rate in 2009. It is hedged by a derivative which has identical characteristics to those of the option incorporated in the loan.

The 500 million euro bond issued by Valeo in 2001 was redeemed on maturity on July 13, 2006.

- Maturities of long-term debt

At December 31

(In millions of euros)	2008	2009	2010	2011	2012	2013 and beyond	Total
Bond issues	-	-	-	-	-	595	**595**
OCEANE	-	-	-	427	-	-	**427**
Syndicated loans	-	-	-	-	216	-	**216**
Lease obligations	3	2	1	-	-	2	**8**
Other borrowings	2	2	3	4	3	14	**28**
Total	**5**	**4**	**4**	**431**	**219**	**611**	**1,274**

4.11.3. Short-term debt

At December 31 (In millions of euros)	2006	2005	2004
Commercial paper	140	-	50
Short-term loans and overdrafts	134	157	125
Short-term debt	**274**	**157**	**175**

4.11.4. Cash and cash equivalents

At December 31 (In millions of euros)	2006	2005	2004
Marketable securities	97	454	488
Cash	521	495	380
Cash and cash equivalents	**618**	**949**	**868**

4.11.5. Net debt

Net debt is defined as all long-term debt (including current maturities thereof) and short-term debt, less loans, other non current financial assets and cash and cash equivalents.

- Net debt at January 1, 2005

Application of IAS 32 and IAS 39 at January 1, 2005 had the effect of reducing the Group's net debt by 23 million euros, mainly related to adjustments to the OCEANE and treasury stock.

- Breakdown of net debt

(In millions of euros)	2006	2005	January 1, 2005	2004
Long-term debt (note 4.11.2)	1,274	1,303	972	1,027
Current maturities of long-term debt (note 4.11.2)	54	581	188	188
Loans and other long-term financial assets	(16)	(12)	(2)	(2)
Total long-term debt	**1,312**	**1,872**	**1,158**	**1,213**
Short-term debt (note 4.11.3)	274	157	175	175
Cash and cash equivalents (note 4.11.4)	(618)	(949)	(836)	(868)
Net cash and cash equivalents	**(344)**	**(792)**	**(661)**	**(693)**
Net debt	**968**	**1,080**	**497**	**520**

4.11.6. Analysis of net debt by currency

Net debt can be analyzed as follows by currency:

At December 31

(In millions of euros)	2006	2005	2004
Euro	1,151	1,179	612
US dollar	(52)	(64)	(44)
Yen	34	110	66
Brazilian Real	(22)	(25)	(15)
Korean Won	(59)	(44)	(47)
Chinese Yuan	(24)	(21)	(23)
Other currencies	(60)	(55)	(29)
Total	**968**	**1,080**	**520**

4.12. Notes to the cash flow statement

4.12.1. Expenses (income) with no cash effect

(In millions of euros)	2006	2005	2004
Expenses (income) with no cash effect			
Depreciation, amortization and provisions for impairment	623	639	593
Net charges to/(reversals from) provisions	(96)	(99)	(84)
Customer contributions	(51)	(35)	(13)
Losses (gains) on sale of non-current assets	(74)	6	11
Expenses related to share-based payment	11	7	7
Other expenses (income) with no cash effect	(2)	-	2
Total	**411**	**518**	**516**

4.12.2. Changes in working capital

(In millions of euros)	2006	2005	2004
Changes in working capital			
Inventories	(17)	3	(5)
Accounts and notes receivable	5	53	21
Accounts and notes payable	88	30	51
Other receivables and payables	(28)	21	(22)
Total	**48**	**107**	**45**

5. ADDITIONAL DISCLOSURES

5.1. Segment reporting

The Valeo Group comprises a single business segment ("Automotive equipment"). The Group's secondary reporting level – geographical areas – corresponds to production areas. Additional information is included in order to provide a more relevant analysis of the Group's business.

Balance sheet and statement of income items relating to "Non-strategic activities" are restated as indicated in note 2.1.

5.1.1. Reporting by geographical area

(In millions of euros)	Net sales by market	Net sales by production area	Total assets	Capital [1] expenditure for the period	Number of employees
2006					
Europe	6,931	7,327	3,966	437	51,400
North America	1,325	1,263	539	86	7,200
South America	468	454	210	39	3,600
Asia	1,246	1,238	754	87	7,500
Eliminations	-	(312)	(147)	(2)	-
Total	**9,970**	**9,970**	**5,322**	**647**	**69,700**
2005					
Europe	6,785	7,163	4,048	436	51,400
North America	1,364	1,296	575	67	6,800
South America	429	402	195	35	3,400
Asia	1,158	1,134	759	59	7,000
Eliminations	-	(259)	(149)	(5)	-
Total	**9,736**	**9,736**	**5,428**	**592**	**68,600**
2004					
Europe	6,501	6,795	3,802	437	49,700
North America	1,356	1,284	498	59	6,900
South America	320	302	131	17	3,200
Asia	841	808	444	47	4,700
Eliminations	-	(171)	(70)	(7)	-
Total	**9,018**	**9,018**	**4,805**	**553**	**64,500**

[1] Capital expenditure in 2006 do not include those related to the Electric Motors & Actuators business which was sold in 2006.

Total segment assets reconcile to total Group assets as follows:

(In millions of euros)	2006	2005	2004
Total segment assets	5,322	5,428	4,805
Financial assets	755	1,117	976
Deferred tax assets	96	100	83
Goodwill	1,415	1,484	1,158
Total	**7,588**	**8,129**	**7,022**

Goodwill balances cannot be broken down by geographical area as they are allocated to groups of CGUs which belong to several such areas.

5.1.2. Research and development expenditure by Domain of Innovation and sales by product group

The objective of the Domains of Innovation is to enhance and support innovation by bringing together different technologies and product groups in order to propose overall solutions to the market based on the themes of comfort, safety and the environment.

(In millions of euros)	2006	2005 [1]	2004 [1]
Driving Assistance	178	175	164
Propulsion Efficiency	216	209	180
Comfort Enhancement	232	225	199
Other	35	37	42
Total	**661**	**646**	**585**

(1) Before taking into account the restatement related to research tax credits (see note 3.3).

The Domains of Innovation aim to assist development of sales of the product portfolio, production and sale of which is placed under the responsibility of the Group's divisions. The product portfolio is broken down into the following product groups:

(In millions of euros)	2006	2005	2004
Transmissions	761	742	693
Climate Control	1,546	1,510	1,397
Engine Cooling	1,550	1,475	1,435
Lighting Systems	1,189	1,151	1,071
Electrical Systems	1,084	1,041	985
Wiper Systems	1,027	1,056	1,163
Security Systems	719	676	661
Switches & Detection Systems	829	833	878
Electronics & Connective Systems	594	606	672
Compressors	430	398	190
Engine Management Systems	352	366	-
Other and eliminations	(111)	(118)	(127)
Total	**9,970**	**9,736**	**9,018**

5.2. Risk management policy

In the context of its industrial and sales activity, the Group operates in an international environment in which it is confronted with market risks, specifically foreign currency risk, price risk and interest rate risk. It uses derivatives to manage and reduce its exposure to changes in foreign exchange rates, raw materials prices and interest rates.

In general, foreign currency risks, price risks in respect of base metals and interest rate risks for all Group companies are managed centrally by Valeo.

In addition to market risks, the Group is also exposed to liquidity risk, financial instrument counterpart risk and to credit risk in respect of its accounts and notes receivable.

5.2.1. Market risks

- Foreign currency risk

Transaction risk

Group subsidiaries may bear transaction risk in respect of purchases or sales transacted in currencies other than their functional currency, whether such transactions are already recognized in the balance sheet or are simply forecast future transactions. Hedging of subsidiaries' current and future trading and investment transactions is generally performed for durations of less than six months.

Subsidiaries principally hedge their transactions with Valeo, which hedges net Group positions with external counterparts.

The principal hedging instruments that the Group uses are forward firm purchases and sales of foreign currencies, swaps and options.

Not all derivatives used by the Group to hedge its foreign currency risk qualify as hedging instruments in the meaning ascribed to that term by IAS 39.

In certain cases, however, the Group applies hedge accounting for highly probable future flows as from the date that the derivatives are put in place.

The unrealized loss of less than 1 million euros recognized in equity at December 31, 2005 was fully reclassified into operating income for the year.

No foreign currency derivative is recognized as a hedging instrument, in the meaning ascribed to that term by IAS 39, in the Group balance sheet at December 31, 2006.

At December 31, 2006, the Group's net position in its principal currencies is as follows:

At December 31 (In millions of euros)	USD	JPY	GBP	Euro
Total assets	228	82	4	2
Total liabilities	(31)	(94)	(11)	(3)
Net balance sheet position before risk management	**197**	**(12)**	**(7)**	**(1)**
Forward sales	(172)	(70)	(8)	(1)
Forward purchases	18	25	17	8
Risk management	(154)	(45)	9	7
Net position after risk management	**43**	**(57)**	**2**	**6**

The net position after risk management in dollars and yen corresponds to hedging of future flows.

Net investment risk

The Group is also exposed to foreign currency risk through its investments in its foreign subsidiaries, particularly to risks of a movement in the exchange rate of the currency of the country in which a subsidiary is located against the euro, which is the Group's functional currency. Such movements can impact Group stockholders' equity.

The Group can thus decide, on a case-by-case basis, to hedge the net investment. Any gain or loss resulting from such a hedge will be deferred by being recognized through stockholders' equity until such time as the foreign investment is wholly or partly sold.

No derivative instrument relating to hedging of a net investment is recognized in the Group balance sheet at December 31, 2006.

■ Metal risk

In order to reduce its exposure to changes in prices of non-ferrous metals, the Group hedges its future purchases of base metals over a period which is generally less than six months. The raw materials currently hedged (aluminum, processed aluminum, copper, zinc, and tin) are quoted on official markets.

The Group favors hedging instruments which do not involve physical delivery of the underlying commodity: swaps and options on the average monthly price.

Base metals derivatives used by the Group are designated as cash flow hedges under IAS 39. An unrealized gain of 6 million euros related to hedges in place at December 31, 2006 has been recognized through Group stockholders' equity.

The unrealized gain of 22 million euros recognized in stockholders' equity at December 31, 2005 was in respect of hedges on raw materials purchases in second-half 2005 and was thus fully taken to operating income in the first half of 2006.

The unrealized gain of 6 million euros at December 31, 2006 is broken down as follows by type of metal:

At December 31 (In millions of euros)	2006	2005
Aluminum	4	10
Processed aluminum	-	2
Copper	-	7
Tin	-	-
Zinc	2	3
Total	**6**	**22**

64% of the unrealized gain of 6 million euros relates to purchases of raw materials denominated in euros and 36% to purchases denominated in US dollars.

■ Interest rate risk

The Group uses interest rate swaps to convert exchange rates on its debt into either a variable or a fixed rate, either as from origination or during the term of the loan.

The interest rate derivatives used by the Group to hedge against changes in value of its fixed-rate debt are designated as fair value hedges under IAS 39. These derivatives are recorded at fair value in the balance sheet with changes in fair value being taken to income. The impact on income is offset, for the effective portion, by a symmetrical revaluation of the hedged component of the debt. The interest rate derivatives used by the Group to hedge its variable-rate debt are not designated as hedging instruments in the meaning ascribed to that term by IAS 39.

The Group's financing rate was 4.5% in 2006 (4.6% in 2005).

At December 31, 2006, 82% of long-term debt is at a fixed rate (83% at December 31, 2005)

Fixed-rate position

At December 31

(In millions of euros)	Less than 1 year	1 to 5 years	More than 5 years
Total assets at fixed rate	-	-	-
Total liabilities at fixed rate	53	440	830
Net fixed-rate position before risk management	**53**	**440**	**830**
Risk management	-	-	(225)
Net position after risk management	**53**	**440**	**605**

A decrease in interest rates of 1% would result in a change in the fair value of the net position of about 45 million euros.

Variable-rate position

At December 31

(In millions of euros)	Less than 1 year	1 to 5 years	More than 5 years
Total assets at variable rate	(618)	(16)	-
Total liabilities at variable rate	276	2	1
Net variable-rate position before risk management	**(342)**	**(14)**	**1**
Risk management	(2)	-	-
Net position after risk management	**(344)**	**(14)**	**1**

An increase of 1% in interest rates would lead to an increase in interest income of about 4 million euros.

5.2.2. Counterpart risk

In the context of financial markets transactions entered into for the purposes of risk management and treasury management, the Group is exposed to counterpart risk. Limits have been set by counterpart, taking account of the ratings of the counterparts with ratings agencies. This also has the effect of avoiding excessive concentration of market transactions with a limited number of banks.

5.2.3. Liquidity risk

The Group targets maximization of its operating cash flows in order to be in a position to finance both the investments required for its development and growth and the dividend paid to its stockholders.

In addition, the strategy followed aims to ensure that the Group has the cash resources necessary to meet all circumstances. For these reasons, the Group borrows long-term funds when market conditions are favorable, either from banks or by accessing public debt markets. Thus, in 2005, Valeo issued 600 million euros worth of Euro Medium Term Notes maturing in 2013. It also took out two syndicated loans for a total amount of 225 million euros maturing in 2012.

Valeo also has several confirmed bank credit lines available for an average period of three years in a total amount of 1.3 billion euros. None of these credit lines were used at December 31, 2006.

The Group also has a short-term commercial paper financing program in a maximum amount of 1.2 billion euros and a medium- and long-term Euro Medium Term Notes financing program in a maximum amount of 2 billion euros.

Covenants: existing credit lines have an early repayment clause related to the Group's debt/equity ratio. This requires that the Group's net debt should not exceed 120% of stockholders' equity. Non-compliance with this ratio causes the credit lines to be suspended and leads to early reimbursement of prior drawdowns. At December 31, 2006, the Group's ratio is well below this level.

The Euro Medium Term Notes include an option granted to the bondholders who can request early redemption of their bonds in the case of a change of control of Valeo which leads to a downgrade in the bond's rating to below investment grade. Such a change of control is deemed to occur if a stockholder, or several stockholders acting together, acquire(s) more than 50% of Valeo's share capital or come(s) to hold more than 50% of voting rights.

5.2.4. Credit risk

Through its sales, Valeo is exposed to credit risk, particularly to risk of default by its customers.

Valeo only operates in the automobile sector and is thus dependent on the sector's performance, principally in Europe and North America.

In 2006, a provision of 2 million euros, in respect of defaults by second tier customers, was recognized against accounts receivable.

Valeo works with all automakers in the sector. At December 31, 2006, 20% of the Group's accounts and notes receivable correspond to one of Valeo's four largest customers. Approximately 7% of this line relate to the two largest American automakers. The downturn in the automobile sector business environment in recent months has led the Group to strengthen control of customer risks and settlement periods which may, on a case-by-case basis, be subject to bilateral renegotiations with customers. The average settlement period at December 31, 2006 is 69 days.

Valeo also generates more than 7% of its net sales in the aftermarket. The Group's numerous, dispersed customer base in this market is constantly monitored and the risk of default is covered by a credit insurance policy. These customers represent slightly more than 7% of Group accounts and notes receivable at December 31, 2006.

5.2.5. Financial instruments

- Fair value of financial instruments

At December 31	2006	
(In millions of euros)	Carrying amount	Fair value
Non-current financial assets	24	24
Accounts and notes receivable	1,834	1,834
Cash and cash equivalents	618	618
ASSETS		
Bonds	595	564
OCEANE (debt component)	427	422
Syndicated loans	216	218
Other long-term debt	90	90
Accounts and notes payable	1,955	1,955
Short-term debt	274	274
LIABILITIES		

The fair values of bonds presented above are calculated on the basis of listed prices on active markets. For the debt component of the OCEANE and for the syndicated loans, fair value is estimated by discounting future cash flows at the market rate applicable at year-end, taking account of an issuer spread for the Group estimated at 0.549% for the OCEANE and at 0.60% for the syndicated loans.

- Fair value of derivatives

Foreign currency derivatives

The fair value of foreign currency derivatives is calculated using the following valuation method: future cash flows are calculated using forward exchange rates at year-end and are discounted using the interest rate of the valuation currency.

At December 31	2006	
(In millions of euros)	Nominal	Fair value
Forward foreign currency purchases	24	-
Forward foreign currency sales	(48)	1
Currency swaps	(120)	1
Total assets	**(144)**	**2**
Forward foreign currency purchases	33	(1)
Forward foreign currency sales	(30)	-
Currency swaps	(22)	-
Total liabilities	**(19)**	**(1)**
Net impact	**-**	**1**

Metals derivatives

At December 31	2006	
(In millions of euros)	Nominal	Fair value
Swaps – Purchases	81	7
Swaps – Sales	(2)	-
Total assets	**79**	**7**
Swaps – Purchases	36	(1)
Swaps – Sales	(3)	-
Total liabilities	**33**	**(1)**
Net impact	**-**	**6**

The fair value of metal derivatives is calculated using the following valuation method: future cash flows are calculated using forward raw materials prices and forward exchange rates at year-end and are then discounted using the interest rate of the valuation currency.

Interest rate derivatives

At December 31	2006	
(In millions of euros)	Nominal	Fair value
Interest rate swaps	227	(9)
Total liabilities	**227**	**(9)**

The fair value of interest rate swaps is calculated by discounting future cash flows at market interest rates at year-end.

5.3. Commitments given

To the best of Valeo's knowledge, no other significant commitments exist or exceptional events have occurred, other than those disclosed in the notes to the financial statements, that are likely to have a material impact on the business, financial position, results or assets and liabilities of the Group.

5.3.1. Lease commitments

Future minimum lease commitments existing at December 31, 2006 (excluding capital leases) are as follows:

At December 31

(In millions of euros)	2006	2005	2004
Less than 1 year	34	38	36
1 to 5 years	33	31	29
More than 5 years	9	10	9
Total	**76**	**79**	**74**

Lease rentals recognized in expenses in the year were as follows:

(In millions of euros)	2006	2005	2004
Rent	53	56	52

Lease commitments in respect of capital leases are as follows:

At December 31 (In millions of euros)	2006	2005	2004
Future minimum lease payments			
Less than 1 year	8	15	14
1 to 5 years	7	10	15
More than 5 years	2	3	2
Total future minimum lease payments	**17**	**28**	**31**
Of which interest charges	(2)	(3)	(3)
Present value of future lease payments			
Less than 1 year	8	14	13
1 to 5 years	6	9	13
More than 5 years	2	2	2
Total present value of future lease payments	**16**	**25**	**28**

5.3.2. Other commitments given

Valeo has also given the following commitments:

At December 31 (In millions of euros)	2006	2005	2004
Guarantees given	29	30	33
Non-cancellable purchase commitments for fixed assets	72	57	58
Other commitments given	101	66	49
Total	**202**	**153**	**140**

Other commitments correspond to warranties granted by Valeo in the context of sale transactions.

The following items, recognized in assets in the Group's balance sheet, have been pledged as security:

At December 31 (In millions of euros)	2006	2005	2004
Property, plant and equipment	24	84	49
Financial assets	12	12	13
Total	**36**	**96**	**62**

5.3.3. Claims and litigation

Known claims and litigation involving Valeo or its subsidiaries have been reviewed as of the date of these financial statements. Based on the advice of counsel, all necessary provisions have been made to cover the estimated contingencies and potential losses.

5.4. Commitments received

When Valeo purchased the Engine Electronics business of Johnson Controls Inc. on March 1, 2005, the latter company granted a warranty concerning the division's liabilities, including in particular a four-year warranty in respect of quality and product liability claims related to the activities of this division.

5.5. Contingent liabilities

The Group has contingent liabilities relating to legal proceedings arising in the normal course of its business.

The Group does not expect these items to give rise to material liabilities other than those that have already been recognized in its financial statements.

5.6. French statutory training entitlement

Under the French law of May 4, 2004 relating to professional training, each French employee of the Group, irrespective of qualifications, obtained a statutory training entitlement which can be accumulated and used at the employee's initiative, subject to agreement of the employer. Thus, since 2005, each employee has a new entitlement to at least 20 hours' training per year.

The cumulative volume of training hours corresponding to Group employees' vested rights under the statutory training entitlement is 875,000 hours for 2004, 2005 and 2006.

5.7. Related party transactions

5.7.1. Management and Directors' remuneration

Management and Directors are comprised of the members of the Group's Management Committee and its Board of Directors. Remuneration paid during the year is broken down as follows:

(In millions of euros)	2006	2005	2004
Salaries and other short-term benefits	12	12	13
Contract termination payments	-	-	2
Total	**12**	**12**	**15**

In addition, the Group recorded expenses related to pension obligations in an amount of 2 million euros in 2006 (2 million euros in 2005). It also recorded expenses in relation to stock option and free share plans in an amount of 3 million euros in 2006 (2 million euros in 2005).

At December 31, 2006, provisions included in the Group balance sheet in respect of these pension obligations amounted to 14 million euros (13 million euros at December 31, 2005).

5.7.2. Associates

The consolidated financial statements include transactions carried out in the normal course of business between the Group and its associates. These transactions are carried out at market prices.

(In millions of euros)	2006	2005	2004
Sales of goods and services	17	13	3
Purchases of goods and services	(7)	(18)	(17)
Interest and dividends received	3	4	3

At December 31

(In millions of euros)	2006	2005	2004
Operating receivables	4	4	4
Operating payables	1	1	3

5.7.3. Joint ventures

The consolidated financial statements include transactions carried out in the normal course of business between the Group and its joint ventures. These transactions are carried out at market prices.

(In millions of euros)	2006	2005	2004
Sales of goods and services	28	25	20
Purchases of goods and services	(11)	(9)	(12)
Interest and dividends received	2	4	9

At December 31

(In millions of euros)	2006	2005	2004
Operating receivables	13	10	10
Operating payables	5	4	5

5.8. Joint ventures

The following amounts are recorded in the Group's consolidated financial statements in respect of joint ventures consolidated under the proportionate method of consolidation:

At December 31

(In millions of euros)	2006	2 005	2 004
Non-current assets	70	51	163
Current assets	101	86	207
Non-current liabilities	12	15	67
Current liabilities	88	75	242
Total operating revenues	251	334	681
Total operating expenses	244	321	642

5.9. Subsequent events

On December 4, 2006, Valeo signed a Memorandum of Understanding with Ford Motor Company for the acquisition of the Sheldon Road site (Plymouth, Michigan) specialized in the production of heating systems. This acquisition is subject to the signature of a new competitive agreement with the United Auto Workers Union.

This site, which employs approximately 1,250 employees, supplies climate control systems and radiators to Ford's North American factories. Its forecast net sales for 2006 are 350 million euros.

6. RESTATEMENT OF 2004 AND 2005 FINANCIAL INFORMATION

IFRS requires that previously published comparative periods be restated in the following situations:

- activities meeting IFRS 5 criteria;
- business combinations (recognition of the definitive fair value of assets acquired and liabilities and contingent liabilities incurred or assumed when this fair value was estimated on a provisional basis at the previous balance sheet date);
- changes in accounting policies (subject to the transitional provisions for first-time application of new standards); and
- corrections of prior period errors.

Consequently, certain previously published financial data have been modified. Such restatements are described below.

The corresponding impacts (after tax) on stockholders' equity including minority interests as published on December 31, 2005 and December 31, 2004 are as follows:

(In millions of euros)	As originally reported	Business combinations	Other	As restated
Stockholders' equity at January 1, 2004	**1,850**	**-**	**(8)**	**1,842**
Income and expenses recognized directly through equity	(35)	-	-	(35)
Net income for the period	249	-	(1)	248
Other movements	(217)	-		(217)
Stockholders' equity at December 31, 2004	**1,847**	**-**	**(9)**	**1,838**
Impact of financial instruments (IAS32, IAS39)	27	-	-	27
Stockholders' equity at January 1, 2005	**1,874**	**-**	**(9)**	**1,865**
Income and expenses recognized directly through equity	102	-	-	102
Net income for the period	147	1	-	148
Other movements	(374)	(24)	-	(398)
Stockholders' equity at December 31, 2005	**1,749**	**(23)**	**(9)**	**1,717**

6.1. Business combinations

The impact on stockholders' equity at December 31, 2005 of restatements related to business combinations corresponds to remeasurements, in a total amount of 24 million euros, of provisions relating to:

- the interest previously held in Valeo Thermal Systems Japan Corp. (previously Zexel Valeo Climate Control);
- the interest previously held in Siam Zexel Co. and Valeo Thermal Systems Sales Thailand Co. Ltd. (previously Zexel Sales Thailand Co).

On the other hand, remeasurements of the interests acquired in these companies in 2005 have no impact on stockholders' equity as they gave rise to a simultaneous adjustment to goodwill (cf. note 4.1).

6.2. Other

Other restatements to stockholders' equity at December 31, 2004 and December 31, 2005 correspond notably to adjustments relating to pension obligations not previously identified, which have been recognized as corrections of errors in accordance with IAS 8.

7. LIST OF CONSOLIDATED COMPANIES

Companies	Countries	2006 % voting rights	2006 % interest	2005 % voting rights	2005 % interest	2004 % voting rights	2004 % interest
EUROPE							
Valeo	France			Parent company			
Cablea (merged with Valeo Câblage)	France	-	-	-	-	100	100
DAV	France	100	100	100	100	100	100
Equipement 11	France	100	100	100	100	100	100
Equipement 7	France	100	100	100	100	100	100
Valeo Cablâge (ex-Cablea and Financière Cablea)	France	100	100	100	100	100	100
SC2N	France	100	100	100	100	100	100
Société de Participations Valeo	France	100	100	100	100	100	100
Telma	France	100	100	100	100	100	100
Valeo Bayen	France	100	100	100	100	100	100
Valeo Electronique et Systèmes de Liaison	France	100	100	100	100	100	100
Valeo Embrayages	France	100	100	100	100	100	100
Valeo Equipements Electriques Moteur	France	100	100	100	100	100	100
Valeo Finance	France	100	100	100	100	100	100
Valeo Four Seasons (2)	France	50	50	50	50	50	50
Valeo Furukawa Wiring Systems (2)	France	50	50	50	50	50	50
Valeo Liaisons Electriques	France	100	100	100	100	100	100
Valeo Management Services	France	100	100	100	100	100	100
Valeo Matériaux de Friction	France	100	100	100	100	100	100
Valeo Plastic Omnium S.N.C. (2)	France	50	50	50	50	50	50
Valeo Sécurité Habitacle	France	100	100	100	100	100	100
Valeo Service	France	100	100	100	100	100	100
Valeo Switches and Detection Systems - VSDS	France	100	100	100	100	100	100
Valeo Systèmes de Contrôle Moteur	France	100	100	100	100	-	-
Valeo Systèmes d'Essuyage	France	100	100	100	100	100	100
Valeo Systèmes Thermiques	France	100	100	100	100	100	100
Valeo Thermique Habitacle	France	100	100	100	100	100	100
Valeo Venture	France	100	100	100	100	100	100
Valeo Vision	France	100	100	100	100	100	100
Valeo Zexel China Climate Control (merged with Valeo Syst. Thermiques)	France	-	-	-	-	60	60
Valeo Componentes Automoviles (7)	Spain	-	-	100	100	100	100
Valeo España, S.A.	Spain	100	100	100	100	100	100
Telma Retarder España, S.A.	Spain	100	100	100	100	100	100
Valeo Climatización, S.A.	Spain	100	100	100	100	100	100
Valeo Illuminación, S.A.	Spain	99.8	99.8	99.8	99.8	99.8	99.8
Valeo Materiales de Fricción, S.A.	Spain	100	100	100	100	100	100
Valeo Plastic OmniumS.L. (2)	Spain	50	50	50	50	50	50

(1) Company accounted for by the equity method.

(2) Company accounted for on a proportional basis.

(3) Company accounted for on a proportional basis on 2004 and fully consolidated since 2005.

(4) Company accounted for by the equity method in 2004 and fully consolidated since 2005.

(5) Company fully consolidated in 2004 and accounted on a proportional basis since 2005.

(6) Associated company sold in 2005.

Companies	Countries	2006		2005		2004	
		% voting rights	% interest	% voting rights	% interest	% voting rights	% interest
Valeo Service España, S.A.	Spain	100	100	100	100	100	100
Valeo Sistemas de Conexion Electrica, S.L.	Spain	100	100	100	100	100	100
Valeo Sistemas de Seguridad y de Cierre, S.A.	Spain	100	100	100	100	100	100
Valeo Sistemas Electricos, S.L.	Spain	100	100	100	100	100	100
Valeo Termico, S.A.	Spain	100	100	100	100	100	100
Cablagens do Ave	Portugal	100	100	100	100	100	100
Valeo Viana	Portugal	100	100	100	100	100	100
Cablauto, S.r.l.	Italy	100	100	100	100	100	100
Cavisud, S.r.l.	Italy	100	100	100	100	100	100
Valeo Service Italia, S.p.A.	Italy	99.9	99.9	99.9	99.9	99.9	99.9
Valeo, S.p.A.	Italy	99.9	99.9	99.9	99.9	99.9	99.9
Valeo Cablaggi e Commutazione, S.p.A.	Italy	100	100	100	100	100	100
Valeo Sicurezza Abitacolo, S.p.A.	Italy	100	99.9	100	99.9	100	99.9
Valeo Sistemi di Climatizzazione, S.p.A.	Italy	100	100	100	100	100	100
Valeo Auto Electric GmbH	Germany	100	100	100	100	100	100
Valeo Auto-Electric Beteiligungs GmbH	Germany	100	100	100	100	100	100
Valeo Germany Holding GmbH	Germany	100	100	100	100	100	100
Valeo Holding Deutschland GmbH	Germany	100	100	100	100	100	100
Valeo Grundvermogen Verwaltung GmbH	Germany	100	100	100	100	100	100
Telma Retarder Deutschland GmbH	Germany	100	100	100	100	100	100
Sylea GmbH	Germany	100	100	100	100	100	100
Valeo Beleuchtung Deutschland GmbH	Germany	100	100	100	100	100	100
Valeo Klimasysteme GmbH	Germany	100	100	100	100	100	100
Valeo Klimasysteme Verwaltung SAS & Co. KG	Germany	100	100	-	-	-	-
Valeo Motoren und Aktuatoren GmbH [7]	Germany	-	-	100	100	100	100
Valeo Schalter und Sensoren GmbH	Germany	100	100	100	100	100	100
Valeo Service Deutschland GmbH	Germany	100	100	100	100	100	100
Valeo Sicherheitssysteme GmbH	Germany	100	100	100	100	100	100
Valeo Verwaltungsbeteiligungs GmbH Co. KG	Germany	100	100	100	100	100	100
Valeo Wischersysteme GmbH	Germany	100	100	100	100	100	100
Valeo Compressor Europe GmbH (3) (ex-Zexel Valeo Compressor Europe GmbH)	Germany	100	100	100	100	50	50
Valeo UK Ltd.	United Kingdom	100	100	100	100	100	100
Labauto Ltd.	United Kingdom	100	100	100	100	100	100
Telma Retarder Ltd.	United Kingdom	100	100	100	100	100	100
Valeo Climate Control Ltd.	United Kingdom	100	100	100	100	100	100
Valeo Engine Cooling UK Ltd. (ex-Valeo Security Systems Ltd.)	United Kingdom	100	100	100	100	100	100
Valeo Service (UK) Ltd.	United Kingdom	100	100	100	100	100	100

(1) Company accounted for by the equity method.

(2) Company accounted for on a proportional basis.

(3) Company accounted for on a proportional basis on 2004 and fully consolidated since 2005.

(4) Company accounted for by the equity method in 2004 and fully consolidated since 2005.

(5) Company fully consolidated in 2004 and accounted on a proportional basis since 2005.

(6) Company sold in 2005.

(7) Company sold in 2006

Companies	Countries	2006 % voting rights	2006 % interest	2005 % voting rights	2005 % interest	2004 % voting rights	2004 % interest
Valeo Vision Belgique	Belgium	100	100	100	100	100	100
Valeo Service Belgique	Belgium	100	100	100	100	100	100
Coreval	Luxembourg	100	100	100	100	100	100
Valeo Holding Netherlands B.V.	Netherlands	100	100	100	100	100	100
Valeo International Holding B.V.	Netherlands	100	100	100	100	100	100
Valeo Service Benelux B.V.	Netherlands	100	100	100	100	100	100
Valeo Vymeniky Tepla S.r.o.	Czech Republic	100	100	100	100	100	100
Sylea Tchequia S.r.o.	Czech Republic	100	100	100	100	100	100
Valeo Autoklimatizace S.r.o.	Czech Republic	100	100	100	100	100	100
Valeo Compressor Czech S.r.o.(3)	Czech Republic	100	100	100	100	50	50
Valeo Slovakia S.r.o.	Slovakia	100	100	100	100	100	100
Valeo Autosystemy Sp.zo.o.	Poland	100	100	100	100	100	100
Valeo Service Eastern Europe Sp.zo.o.	Poland	100	100	100	100	100	100
Valeo Electric and Electronic Systems Sp.zo.o.	Poland	100	100	100	100	100	100
Valeo Auto Electric Hungary Spare Parts Production LLC	Hungary	100	100	100	100	100	100
Valeo Kabli, d.o.o.	Slovenia	100	100	100	100	100	100
Valeo Cablaje s.r.l. (ex-Valeo Electronice si Sisteme de Conectare Romania)	Romania	100	100	100	100	100	100
Valeo Electrical Connective Systems Srl	Romania	100	100	100	100	-	-
Cablea Tunisie, S.A.	Tunisia	100	100	100	100	100	100
DAV Tunisie, S.A.	Tunisia	100	100	100	100	100	100
Société Tunisienne de Câblages S.T.C.	Tunisia	100	100	100	100	100	100
Valeo Mateur (ex-Sylea Tunisie)	Tunisia	100	100	100	100	100	100
Valeo Embrayages Tunisie	Tunisia	100	100	100	100	100	100
Valeo Bouskoura (ex-Cabelec)	Morocco	100	100	100	100	100	100
Valeo Aim Sebaa (ex-Cablea Maroc)	Morocco	100	100	100	100	100	100
Cablinal Maroc, S.A.	Morocco	100	100	100	100	100	100
Valeo Bouznika, S.A.	Morocco	100	100	100	100	100	100
Nursan ED (1)	Turkey	40	40	40	40	40	40
Nursan OK (1)	Turkey	40	40	40	40	40	40
Valeo Otomotiv Dagitim A.S.	Turkey	100	100	100	100	100	100
Valeo Otomotiv Sistemleri Endustrisi A.S.	Turkey	100	100	100	100	100	100
Valeo Interbranch Aut Software Egypt	Egypt	100	100	-	-	-	-
Valeo Armco Engine Cooling Co. (2)	Iran	51	51	51	51	-	-
Valeo Systems South Africa (Proprietary) Ltd.	South Africa	51	51	51	51	51	51

(1) Company accounted for by the equity method.

(2) Company accounted for on a proportional basis.

(3) Company accounted for on a proportional basis on 2004 and fully consolidated since 2005.

(4) Company accounted for by the equity method in 2004 and fully consolidated since 2005.

(5) Company fully consolidated in 2004 and accounted on a proportional basis since 2005.

(6) Company sold in 2005.

(7) Company sold in 2006

Companies	Countries	2006 % voting rights	2006 % interest	2005 % voting rights	2005 % interest	2004 % voting rights	2004 % interest
NORTH AMERICA							
Valeo Aftermarket, Inc.	United States	100	100	100	100	100	100
Valeo Electrical Systems, Inc.	United States	100	100	100	100	100	100
Valeo Investment Holdings, Inc.	United States	100	100	100	100	100	100
Valeo Raytheon Systems, Inc. (5)	United States	77.2	77.2	73.1	73.1	66.6	66.6
Valeo Compressor North America, Inc. (3) (ex-Selective Technology, Inc.)	United States	100	100	100	100	50	50
Telma Retarder Inc.	United States	100	100	100	100	100	100
Valeo Acustar Thermal Systems, Inc.	United States	51	51	51	51	51	51
Valeo Climate Control Corp.	United States	100	100	100	100	100	100
Valeo Friction Materials, Inc.	United States	100	100	100	100	100	100
Valeo, Inc.	United States	100	100	100	100	100	100
Valeo Switches and Detection Systems, Inc.	United States	100	100	100	100	100	100
Valeo Sylvania, LLC (2)	United States	50	50	50	50	50	50
Valeo Sylvania Services S de RL de CV (2)	United States	50	50	50	50	50	50
Delmex de Juarez S de RL de CV	Mexico	100	100	100	100	100	100
Telma Retarder de Mexico, SA de CV	Mexico	100	100	100	100	100	100
Valeo Automotive Electrical Systems de Mexico, SA de CV	Mexico	100	100	100	100	100	100
Valeo Sistemas Electricos, SA de CV	Mexico	100	100	100	100	100	100
Valeo Sistemas Electricos Servicios S de RL de CV	Mexico	100	100	100	100	100	100
Valeo Sistemas Electronicos, SA de CV	Mexico	100	100	100	100	100	100
Valeo Sylvania Iluminacion, S de RL de CV (2)	Mexico	50	50	50	50	50	50
Valeo Termico, SA de CV	Mexico	100	100	100	100	100	100
Valeo Termico Servicios S de RL de CV	Mexico	100	100	100	100	100	100
Valeo Climate Control de Mexico, SA de CV	Mexico	100	100	100	100	100	100
Valeo Climate Control de Mexico Servicios S de RL de CV	Mexico	100	100	100	100	100	100
Valeo Materiales de Friccion de Mexico, SA de CV	Mexico	100	100	100	100	100	100
SOUTH AMERICA							
Valeo Climatizacao Brasil (merged with Valeo Sistemas Automotivos Ltda)	Brazil	-	-	-	-	100	100
Valeo Sistemas Automotivos Ltda	Brazil	100	100	100	100	100	100
Cibie Argentina, SA	Argentina	100	100	100	100	100	100
DAV Argentina, SA (merged with Cibie Agentina, SA)	Argentina	-	-	-	-	100	100
Emelar Sociedad Anonima	Argentina	100	100	100	100	100	68
Il Tevere (6)	Argentina	-	-	-	-	50	50
Interclima (6)	Argentina	-	-	-	-	50	26
Mirgor (6)	Argentina	-	-	-	-	50	26
Valeo Embragues Argentina, SA	Argentina	100	100	100	100	68	68
Valeo Termico Argentina, SA	Argentina	100	100	100	100	100	100
ASIA							
Valeo Compressor (Thailand) Co. Ltd. (3) (ex-Zexel Valeo Compressors)	Thailand	98.5	98.5	98.5	98.5	50	48.1
Valeo Compressor Clutch (Thailand) Co. Ltd. (3) (ex-Zexel Clutches Co. Ltd)	Thailand	97.3	97.3	97.3	97.3	50	48.1
Valeo Siam Thermal Systems Co. Ltd. (4) (ex-Siam Zexel Co. Ltd.)	Thailand	74.9	74.9	74.9	74.9	39	19.5
Valeo Thermal Systems Sales (Thaïland) (4) (ex-Zexel Sales Thailand)	Thailand	74.9	74.9	89.9	74.9	7.8	7.8

(1) Company accounted for by the equity method.

(2) Company accounted for on a proportional basis.

(3) Company accounted for on a proportional basis on 2004 and fully consolidated since 2005.

(4) Company accounted for by the equity method in 2004 and fully consolidated since 2005.

(5) Company fully consolidated in 2004 and accounted on a proportional basis since 2005.

(6) Company sold in 2005.

(7) Company sold in 2006

Companies	Countries	2006 % voting rights	2006 % interest	2005 % voting rights	2005 % interest	2004 % voting rights	2004 % interest
Valeo Electrical Systems Korea Ltd.	South Korea	100	100	100	100	100	100
Valeo Pyeong Hwa Co. Ltd. (2)	South Korea	50	50	50	50	50	50
Valeo Pyeong Hwa Distribution Co. Ltd. (2)	South Korea	50	50	50	50	50	50
Valeo Samsung Thermal Systems (2)	South Korea	50	50	-	-	-	-
Valeo Compressor Korea Co. Ltd. (3) (ex-Zexel Valeo Climate Control Korea Co. Ltd.)	South Korea	100	100	100	100	50	50
Dae Myong Corporation (3)	South Korea	100	100	100	100	50	50
Konno Sangyo Co. Ltd. (7)	Japan	-	-	100	100	50	50
Zexel Logistic Compagny (Butsuryu) (7)	Japan	-	-	100	100	50	50
Zexel Logitec Company (7)	Japan	-	-	100	100	50	50
Ichikoh Industries Ltd. (1)	Japan	29.4	29.4	28.2	28.2	22.7	22.7
Valeo Engine Cooling Japan Co. Ltd.	Japan	100	100	100	100	100	100
Valeo Unisia Transmissions	Japan	66	66	66	66	66	66
Valeo Thermal Systems Japan Corp. (3) (ex-Zexel Climate Control)	Japan	100	100	100	100	50	50
Valeo Automotives Transmissions Systems (Nanjing) Co. Ltd.	China	100	100	-	-	-	-
Hubei Valeo Autolighting Company Ltd.	China	100	100	75	75	75	75
Valeo Automotive Air Conditioning Hubei Co. Ltd.	China	55	55	55	55	55	33
FAW Valeo Climate Control System (1)	China	36.5	36.5	36.5	36.5	36.5	21.9
Huada Automotive Air Conditioner Co. Ltd. (1)	China	30	30	30	30	30	15
Valeo Lighting Hubei Technical center Co. Ltd.	China	100	100	100	100	100	100
Nanjing Valeo Clutch Co. Ltd. (2)	China	55	55	55	55	50	50
Shanghai Valeo Automotive Electrical Systems Co. Ltd. (2)	China	50	50	50	50	50	50
Valeo Shanghai Automotive Electric Motors Systems Co. Ltd.	China	55	55	55	55	55	55
Taizhou-Valeo Wenling Automotive Systems Co. Ltd.	China	100	100	55	55	55	55
Telma Vehicle Braking System (Shanghai) Co. Ltd.	China	70	70	70	70	-	-
Shenzhen Valeo Hangsheng Automotive Switches & Detection Syst. Co. Ltd.	China	75	75	75	75	-	-
Valeo Automotive Security Systems (Wuxi) Co. Ltd.	China	100	100	100	100	-	-
Valeo Fawer Compressor (Changchun) Co. Ltd. (2)	China	60	60	60	60	-	-
Valeo Management (Beijing) Co. Ltd.	China	100	100	-	-	-	-
Foshan Ichikoh Valeo Auto Lighting Systems Co. (2)	China	50	50	-	-	-	-
Engine Cooling Shashi Co. Ltd.	China	100	100	-	-	-	-
PT Zexel AC Indonesia (1)	Indonesia	49	49	49	49	49	24.5
Valeo Engineering Center (India) Private Limited	India	100	100	-	-	-	-
Amalgamations Valeo Clutch Private Ltd. (2)	India	50	50	50	50	50	50
Valeo Friction Materials India Limited	India	60	60	60	60	60	60

(1) Company accounted for by the equity method.

(2) Company accounted for on a proportional basis.

(3) Company accounted for on a proportional basis on 2004 and fully consolidated since 2005.

(4) Company accounted for by the equity method in 2004 and fully consolidated since 2005.

(5) Company fully consolidated in 2004 and accounted on a proportional basis since 2005.

(6) Company sold in 2005.

(7) Company sold in 2006

STATUTORY AUDITORS' REPORT ON THE 2006 IFRS CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2006

This is a free translation into English of the statutory auditors' report issued in French and is provided solely for the convenience of English speaking users. The statutory auditors' report includes information specifically required by French law in such reports, whether modified or not. This information is presented below the opinion on the consolidated financial statements and includes an explanatory paragraph discussing the auditors' assessments of certain significant accounting and auditing matters. These assessments were considered for the purpose of issuing an audit opinion on the consolidated financial statements taken as a whole and not to provide separate assurance on individual account captions or on information taken outside of the consolidated financial statements.

This report should be read in conjunction with, and construed in accordance with, French law and professional auditing standards applicable in France.

Following our appointment as statutory auditors by your Annual General Meeting, we have audited the accompanying consolidated financial statements of Valeo (the Company) for the year ended December 31, 2006, as presented on pages 1 to 53.

The consolidated financial statements have been approved by the Board of Directors. Our role is to express an opinion on these consolidated financial statements based on our audit.

1. Opinion on the consolidated financial statements

We conducted our audit in accordance with professional standards applicable in France. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated 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 presentation of the financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements give a true and fair view of the assets and liabilities and of the financial position of the consolidated group as at December 31, 2006 and of the results of its operations for the year then ended in accordance with IFRSs as adopted by the European Union.

2. Justification of our assessments

In accordance with the requirements of article L.823-9 of the French Commercial Code (*Code de commerce*) relating to the justification of our assessments, we bring to your attention the following matters:

The Company records provisions related to pensions and other post-employment benefits in accordance with the policy described in note 1.17 to the consolidated financial statements. Such obligations have generally been determined with the assistance of independent actuaries. We have reviewed the data and assumptions used and the calculations completed. We have not identified any item that could affect the amounts and methods used to account for pensions and other post-employment benefits.

The Company performs at the end of each year impairment tests of the amounts recorded as goodwill and also assesses whether indicators point to a lasting impairment of fixed assets in accordance with the policy described in note 1.12 to the consolidated financial statements. We have reviewed the methods and assumptions used by the Company in preparing the accounts and we have verified that such assumptions were reasonable.

These assessments were made in the context of our audit of the consolidated financial statements taken as a whole, and therefore contributed to the opinion which is expressed in the first part of this report.

3. Specific verification

In accordance with professional standards applicable in France, we have also verified the information given in the group's management report. We have no matters to report as to its fair presentation and its consistency with the consolidated financial statements.

Paris La Défense and Neuilly-sur-Seine, February 12, 2007

The Statutory Auditors

Salustro Reydel Member of KPMG International		PricewaterhouseCoopers Audit	
Jean-Pierre Crouzet	Emmanuel Paret	Serge Villepelet	Jean-Christophe Georghiou