



CONSOLIDATED REPORT
FIRST QUARTER 2000

PIRELLI Società per azioni

Head office in Milan, Viale Sarca 222

Share capital – Euro 1,034,124,774.28

Milan Courts, Companies Register No. 15901

PIRELLI S.p.A.**Board of Directors**

Chairman and CEO

Marco Tronchetti Provera

Deputy Chairman

Alberto Pirelli

Directors

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 Eugenio Coppola di Canzano
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 Angelo Marchiò
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 Luigi Orlando
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 Giampiero Pesenti
 Ennio Presutti
 Carlo Alessandro Puri Negri
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Sergio Lamacchia

Board of Statutory Auditors

Chairman

Luigi Guatri

Standing members

Rosalba Casiraghi
 Giorgio Oggioni

Alternate members

Mario Brughera
 Alfredo Malguzzi

General Managers

Finance and Administration

Carlo Buora

Tyre Sector

Giovanni Ferrario

Cables and Systems Sector

Giuseppe Morchio

PIRELLI S.p.A. - MILAN**Consolidated Report
First Quarter 2000**
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MANAGEMENT'S DISCUSSION AND ANALYSIS

Performance of the Group

The start of 2000 was characterized by a competitive scenario that was substantially unchanged compared to the prior year and by strong pressure over raw material prices.

In this first quarter, the Group increased volumes which, together with the steps taken to reduce costs and improve productive operations, made it possible to increase results compared to the corresponding period of the prior year. The operating margin rose from Euros 77 to Euros 97 million.

Major events during the first quarter of 2000

- In February 2000, the sale was concluded for the Terrestrial Optical Systems business to Cisco Systems. The deal, taking into account the related expenses, led to an improvement at the level of net result of Euros 1,131 million.
- On January 14, 2000, the acquisition of the majority interest in Pirelli Telecom Cables Co. Ltd Wuxi (China) was concluded and the stake is now equal to 66.47 percent.
- Also finalized in the first quarter was the acquisition by Pirelli Cavi e Sistemi of the Draka business activities in Finland and Holland.
- In February 2000, Pirelli Group reached an understanding with BICCGeneral for the purchase of the power cables business which had belonged to the BICC plc British group and was bought last year by the US group General Cable. As announced, the deal is still being examined by the European Commission and we expect to arrive at a positive solution in a reasonably short period of time.
- In order to raise competitiveness, actions were undertaken to restructure and rationalize productive operations - over the next 15 months - which will involve extraordinary expenses quantifiable in about Euro 248 million, of which one-quarter of the amount is for the Cables and Systems Sector and three-quarters for the Tyres Sector.

The Group

The consolidated figures of the Group for the first quarter ending March 31, 2000 can be summarized as follows:

€	Millions of euros		
	First quarter 2000	First quarter 1999	1999
. Sales revenues	1,762	1,496	6,482
. Gross operating profit	191	159	678
% of sales	10.8%	10.6%	10.5%
. Operating profit	97	77	331
% of sales	5.5%	5.2%	5.1%
Net financial (liquidity) debt	(417)	588	1,017
No. of employees (at period end)	40,472	41,102	40,103
No. of factories	87	85	87

Sales revenues

Sales revenues for the first quarter ended March 31, 2000 total Euros 1,762 million, an increase of 17.8% compared to the corresponding period of the prior year. This change is due mainly to higher volumes (+11.3%), a positive exchange effect (+6.9%), the consolidation of the units acquired in the previous year (+2.0%), less the effect of the exclusion of the Photonics business from consolidation (-4.8%).

- **Gross operating profit**

Gross operating profit for the first quarter ended March 31, 2000 is Euros 191 million (10.8% of sales revenues), an increase compared to Euros 159 million (10.6% of sales revenues) for the same period of the prior year.

- **Operating profit**

Operating profit for the first quarter ended March 31, 2000 is Euros 97 million and is equal to 5.5% of sales revenues compared to Euros 77 million (5.2% of sales revenues) in the corresponding period of the prior year. The improvement in the result, in both Sectors, can chiefly be attributable to higher volumes.

- **Net financial position**

Net financial position shows a liquidity balance of Euros 417 million compared to a net debt balance of Euros 1,017 million at December 31, 1999. The variation can be ascribed principally to the net effect of the extraordinary transactions (sale of the our Terrestrial Optical Systems business to Cisco Systems and acquisition of the cable operations in Finland and Holland).

- **Personnel**

Personnel number 40,472 at March 31, 2000 compared to 40,103 at December 31, 1999.

Cables and Systems Sector

Millions of euros			
€	First quarter 2000	First quarter 1999	1999
. Sales revenues	1,054	863	3,921
. Gross operating profit	95	85	355
% of sales	9.0%	9.9%	9.1%
. Operating profit	52	44	183
% of sales	4.9%	5.1%	4.7%
Net financial (liquidity) debt	(775)	616	700
No. of employees (at period end)	19,473	20,598	19,046
No. of factories	65	63	65

Sales revenues for the first quarter ended March 31, 2000 amount to Euros 1,054 million.

The change compared to the first quarter of 1999 (+ 22.1%) is due to:

• Currency exchange effect	+ 7.6%
• Volumes	+ 15.5%
• Sale of photonics business	- 8.2%
• Acquisitions	+ 1.8%
• Prices	+ 4.6%
• Mix and other	+ 0.8%

	+ 22.1%
	=====

In Europe, sales revenues are increasing, except for Germany, owing to the positive effect of volumes and mix and also because of the higher value of copper and in the presence of a further fall in prices but to a lesser extent than in the prior year.

In North America, the performance of telecom activities was especially positive with significant increases in volumes for optic cables; power cable activities are also up.

In South America, operations remain at levels similar to the prior year for Brazil, while problems in the economy are not helping the results of the unit in Argentina.

Australia, downstream of the integration of the Metal Manufacturers power cables business, continues its development in a market which is expected to slow down.

Operating profit for the first quarter of 2000 amounts to Euros 52 million, an increase of Euros 8 million compared to the same period of the prior year, which can be summarized as follows:

	Millions of euros
• Currency exchange effect	+ 5
• Volume and mix	+ 26
• Prices	+ 45
• Materials	- 62
• Effect of sale of photonics business	- 10
• Change in per unit costs and other	+ 4

	+ 8
	=====

The **net financial position** shows a liquidity balance of Euros 775 million, having been particularly affected by extraordinary transactions (sale of the Terrestrial Optical Systems business to Cisco Systems and acquisition of the cables operations in Finland and Holland).

The total **workforce** of the sector at March 31, 2000 numbers 19,473, an increase compared to December 31, 1999 (+ 427 employees).

Tyres Sector

A summary of the consolidated figures for the Tyres Sector is presented below:

	Millions of euros		
€	First quarter 2000	First quarter 1999	1999
. Sales revenues	707	632	2,559
. Gross operating profit	102	84	349
% of sales	14.4%	13.3%	13.6%
. Operating profit	54	45	185
% of sales	7.6%	7.1%	7.2%
Net financial debt	597	429	535
No. of employees (at period end)	20,265	19,796	20,332
No. of factories	22	22	22

Sales revenues for the first quarter ended March 31, 2000 amount to Euros 707 million, compared to Euros 632 million for the corresponding period of 1999 (+11.9%).

The change can be analyzed as follows:

• Currency exchange effect	+ 5.8%
• Volumes	+ 5.6%
• Acquisitions	+ 2.3%
• Prices	- 2.2%
• Mix and other	+ 0.4%

	+ 11.9%
	=====

Car tyre volumes for the first quarter of 2000 show an increase of 5% compared to the first quarter of 1999: Original Equipment is positive thanks to the favorable trend in

Europe, South America and Turkey. The premium tyre range is also up. Replacements for the quarter are line with the prior year, while the premium range displays an increase over the same period of 1999.

Light Truck tyre volumes closed with a gain of 31% over 1999, showing an improvement in both Original Equipment (all geographic areas performed well) and Replacements (with the exception of Turkey, all the areas registered important increases). Volumes of Recreational tyres for both Original Equipment and Replacements are also positive.

Truck tyre volumes show an improvement of 19%: Replacements are positive, thanks to the good performance of Turkey, South America, Africa/Middle East and the consolidation of PTA Co.. Original Equipment is also positive.

Good performance in **Motorcycle tyres** show total volumes up 15%: Replacements are positive thanks to the good gains in both South America and Europe. Original Equipment is also doing well.

Operating profit for the first quarter ended March 31, 2000 shows a gain in absolute terms of 20% with a Return on Sales (ROS) at 7.6% compared to 7.1% in 1999: the positive contribution of volumes and mix, plus the measures taken to reduce costs, in addition to the favorable exchange effect, more than compensated the negative change in sales prices and the increase in the raw materials prices.

Specifically, the increase of Euros 9 million compared to the prior year is due to:

	Millions of euros
Sales prices	- 15
Raw material per unit costs	<u>- 16</u>
	<u>- 31</u>
Currency exchange effect	+ 4
Volumes and mix	+ 23
Effect of consolidating company in Egypt	+ 2
Change in per unit costs, efficiency and other	<u>+ 11</u>
	<u>+ 40</u>
Total change	<u>+ 9</u>

Net financial debt at March 31, 2000 amounts to Euros 597 million and shows an increase of Euros 62 million compared to December 31, 1999.

At March 31, 2000, the **workforce** numbers 20,265, a slight reduction compared to 20,332 at December 31, 1999.

Outlook for the current year

The prospects for the current year lead us to believe that the result from ordinary operations will show an improvement over than of 1999, to which positive extraordinary components should be added deriving from the Cisco Systems deal and the scheduled restructurings, as mentioned.

Related party disclosures

As to required disclosures according to article 2359 of the Italian Civil Code referring to Consob Communication No. 97001574 of February 20, 1997 and No. 98015375 of February 27, 1998, which deal with transactions by Group companies with related parties, the effects of such transactions on the balance sheet and statement of income of the consolidated financial statements at March 31, 2000 are presented below.

All the transactions, including those of the Group holding company and its subsidiaries, and those between subsidiaries, fall within the ordinary operations of the Group, are governed by market terms, and there are no transactions of an unusual and exceptional nature or in potential conflict of interest.

The following table presents the major transactions at March 31, 2000 that Pirelli S.p.A. Group has entered into with the parent companies (Pirelli & C. A.p.A. and Pirelli & C. Luxembourg S.A.) and the subsidiaries of the latter companies, which are included in the scope of consolidation of Pirelli & C. A.p.A..

(in millions of euros)

Type of transaction	With parent companies	With subsidiaries of Pirelli & C. A.p.A.	Total
TRADE RECEIVABLES AND OTHER	0.3	18.5	18.8
TRADE PAYABLES AND OTHER	(0.6)	(5.1)	(5.7)
FINANCIAL RECEIVABLES	1,446.5	200.6	1,647.1
FINANCIAL PAYABLES	(37.4)	(198.9)	(236.3)
REVENUES FOR GOODS AND SERVICES	0.2	0.3	0.5
COSTS FOR GOODS AND SERVICES	(0.7)	(2.7)	(3.4)
FINANCIAL INCOME	3.8	1.7	5.5
FINANCIAL EXPENSES	(2.0)	(0.7)	(2.7)

Transactions of Pirelli S.p.A. and its subsidiaries with the **parent companies** mainly refer to the following:

- **financial receivables**, relating to loans made by Pirelli Finance (Luxembourg) S.A. (subsidiary of Pirelli S.p.A.) to Pirelli & C. Luxembourg S.A. and by Pirelli Servizi Finanziari S.p.A. (subsidiary of Pirelli S.p.A.) to Pirelli & C. A.p.A.;
- **financial payables**, relating to current account transactions between Pirelli Servizi Finanziari S.p.A. and Pirelli & C. A.p.A.;
- **revenues for goods and services**, relating to the performance of various services rendered by Pirelli S.p.A. and its subsidiaries to Pirelli & C. A.p.A.;
- **costs for goods and services**, relating to costs for the corporate secretarial services rendered by Pirelli & C. A.p.A. on behalf of Pirelli S.p.A.;
- **financial income and expenses**, relating to interest income and expense on the aforementioned current account transactions and loans, as well as costs and revenues for hedging transactions carried out by Pirelli Finance (Luxembourg) S.A. (subsidiary of Pirelli S.p.A.) on behalf of Pirelli & C. A.p.A. and Pirelli & C. Luxembourg S.A..

Transactions of Pirelli S.p.A. and its subsidiaries with the **subsidiaries of Pirelli & C. A.p.A.** mainly refer to the following:

- **trade receivables and other**, relating to the remaining receivable by Pirelli Cavi e Sistemi S.p.A. (subsidiary of Pirelli S.p.A.) from Lambda S.r.l. (indirect subsidiary of Pirelli & C. A.p.A.), deriving from the sale of the property located at Viale Sarca 222 in Milan in December 1999;
- **trade payables and other**, relating to services rendered by companies in the Group of Milano Centrale S.p.A. (subsidiary of Pirelli & C. A.p.A.) to Pirelli S.p.A. and its subsidiaries and trading transactions by Pirelli Energie Deutschland GmbH and Turk Pirelli Enerji A.S. (subsidiary of Pirelli & C. A.p.A.) with companies in the Tyres Sector;
- **financial receivables and payables**, relating to transactions on the current account by Pirelli Servizi Finanziari S.p.A. with companies of the Group of Milano Centrale S.p.A. (subsidiary of Pirelli & C. A.p.A.);
- **revenues from goods and services**, relating to cost recoveries for various services rendered by Pirelli S.p.A. and Pirelli Informatica S.p.A. (subsidiary of Pirelli S.p.A.) on behalf of Milano Centrale e Servizi S.p.A. and its subsidiaries;
- **costs for goods and services**, relating to costs for property management services incurred by Pirelli S.p.A. and its subsidiaries for the services rendered by companies of the Group of Milano Centrale S.p.A. (subsidiary of Pirelli & C. A.p.A.);
- **financial income and expenses**, relating to interest income and expense on the aforementioned current account transactions.

**QUARTERLY DATA
AND
COMMENTS**

QUARTERLY DATA

				Millions of euros		
€	Statement of income	First quarter 2000	First quarter 1999	Dec. 31, 1999		
.	Sales revenues	1,762	1,496	6,482		
.	Other revenues	45	63	91		
.	Value of production	1,807	1,559	6,573		
		(1,247)	(1,043)	(4,475)		
.	Cost of sales					
.	Labor costs	(369)	(357)	(1,419)		
.	Amortization and depreciation	(94)	(82)	(348)		
		97	77	331		
.	Operating profit					

			Thousands of euros	
Net financial position	March 31, 2000	Dec. 31, 1999		
.	Short-term financial payables	840,498	643,503	
.	Cash and banks	(653,611)	(723,522)	
.	Short-term financial receivables	(1,745,363)	(271,682)	
	Short-term net financial position	(1,558,476)	(351,701)	
.	Medium/long-term financial payables	1,276,851	1,479,587	
.	Medium/long-term financial receivables	(135,524)	(110,797)	
	Medium/long-term net financial position	1,141,327	1,368,790	
	Net financial position, total	(417,149)	1,017,089	

COMMENTS ON QUARTERLY DATA

Form and content

The accounting principles, valuation criteria and principles of consolidation used in the preparing the quarterly data at March 31, 2000 are the same as those adopted for the financial statements at December 31, 1999 and disclosed in the previous annual report.

Economic review

Sales revenues

Sales revenues for the first quarter of 2000 amount to Euros 1,762 million compared to Euros 1,496 million for the first quarter of 1999.

The change of +17.8% compared to the corresponding period of 1999 can be analyzed as follows:

• Currency exchange effect	+ 6.9%
• Volume	+ 11.3%
• Effect of excluding the Photonics business from consolidation	- 4.8%
• Effect of consolidating units acquired	+ 2.0%
• Prices	+ 1.7%
• Mix and other	+ 0.7%

	+ 17.8%
	=====

A breakdown by sector and geographic area is as follows:

Sector	First quarter 2000	First quarter 1999	Geographic area	First quarter 2000	First quarter 1999
Cables and Systems	60%	59%	Europe	56.1%	57.0%
Tyres	40%	41%	North America	14.5%	15.8%
			Central and South America	16.3%	17.9%

Labor costs

Labor costs total Euros 369 million and represent 20.9% of sales revenues compared to 23.9% in the first quarter of 1999.

Amortization and depreciation

Amortization and depreciation and totals Euros 94 million, of which the amortization of intangible assets totals Euros 11 million and the depreciation of property, plant and equipment amounts to Euros 83 million compared to a total of Euros 82 million for the first quarter of 1999 (amortization of Euros 5 million and depreciation of Euros 77 million).

Operating profit

Operating profit is Euros 97 million (5.5% of sales revenues), an increase of Euros 20 million compared to the corresponding period of 1999. The change can be ascribed to:

	Millions of euros
• Currency exchange effect	+ 8
• Volumes and mix	+ 48
• Prices	+ 30
• Materials	- 78
• Effect of acquisitions	+ 2
• Effect of sale of photonics business	- 10
• Change in per unit costs	+ 20

	+ 20
	=====

Net financial position

The net financial position shows a net liquidity balance of Euros 417 million compared to a net debt balance of Euros 1,017 million at December 31, 1999.

The change during the quarter, equal to Euros 1,434 million, is due to the following:

	Millions of euros
• Exchange effect	- 6
• Effect of sale of Photonics business	- 1,465
• Other	+ 37

	- 1,434
	=====