

**Pirelli & C. S.p.A. - Milan**

**Six-Months Interim Report  
at June 30, 2006**

**PIRELLI & C. Società per Azioni**

**Registered office in Milan, Via G. Negri 10**

**Share Capital - Euros 2,791,311,344.64**

**Milan Companies Register No. 00860340157**

**Economic Administrative File (REA) No. 1055**

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**PIRELLI & C. S.p.A.****Board of Directors**<sup>1</sup>


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Honorary Chairman	Leopoldo Pirelli
Chairman <sup>2</sup>	Marco Tronchetti Provera
Deputy Chairman <sup>2</sup>	Alberto Pirelli
Deputy Chairman <sup>2</sup>	Carlo Alessandro Puri Negri
Managing Director <sup>2</sup> and General Manager	Carlo Buora
Directors	Carlo Acutis *
	Carlo Angelici * <sup>o</sup>
	Gilberto Benetton
	Alberto Bombassei *
	Franco Bruni * <sup>o</sup>
	Gabriele Galateri di Genola
	Mario Garraffo *
	Dino Piero Giarda *
	Berardino Libonati * ^
	Giulia Maria Ligresti
	Massimo Moratti
	Giovanni Perissinotto
	Giampiero Pesenti * ^
	Aldo Roveri * ^
	Carlo Secchi * <sup>o</sup>
	Paolo Vagnone

\* Independent director

<sup>o</sup> Member of the Internal Control and Corporate Governance Committee<sup>^</sup> Member of the Remuneration Committee

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Secretary to the Board	Anna Chiara Svelto
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**Board of Statutory Auditors**<sup>3</sup>


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Chairman	Luigi Guatri
Standing members	Enrico Laghi
	Paolo Francesco Lazzati
Alternate members	Franco Ghiringhelli
	Luigi Guerra

**General Managers**


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Administration and Control	Claudio De Conto
Finance	Luciano Gobbi

**Independent Auditors**<sup>4</sup>

PricewaterhouseCoopers S.p.A.

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1 Appointment: April 28, 2005. Expiry: shareholders' meeting called to approve the financial statements at December 31, 2007.

Alberto Bombassei was co-opted by the board of directors on September 12, 2006.

2 Office conferred by the board of directors' meeting held on April 28, 2005.

3 Appointment: April 21, 2006. Expiry: shareholders' meeting called to approve the financial statements at December 31, 2008.

4 Appointment conferred by the shareholders' meeting held on April 28, 2005.

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## DIRECTORS' REPORT ON OPERATIONS

### Performance of the Group

In the first half of 2006, growth was recorded in all principal economic indicators compared to the same period of the prior year thanks to the Group's strategy of focusing on activities with higher margins.

In summary, net sales grew by 7.2 percent, operating profit by 6.7 percent and income, on a comparable consolidation basis, by about 9 percent. Equity attributable to the equity holders of the company is equal to Euros 5,342 million compared to Euros 5,205 million at December 31, 2005 and net financial debt is Euros 1,575 million.

With regard to industrial activities, **Pirelli Tyre** closed the first six months with higher results, reaching net sales of more than Euros 2 billion with increases in both the Consumer and Industrial business areas.

As for real estate activities, **Pirelli Real Estate** recorded a 15 percent gain in operating profit including earnings from investments.

In broadband activities, **Pirelli Broadband Solutions** increased net sales by 14 percent and basically reported a breakeven in the operating result.

**Pirelli Ambiente**, working in the sector of technologies for sustainable development, continues to increase its net sales.

Consolidated **net sales** of the Group for the six months ending June 30, 2006 amount to Euros 2,445.9 million. This is an increase of 7.2 percent compared to Euros 2,281.4 million in the same period of 2005. Excluding the foreign exchange effect, net sales grew by 3.4 percent.

Consolidated **gross operating profit** is Euros 324.2 million (13.3 percent of net sales), up 5.8 percent compared to Euros 306.3 million in the first half of 2005. Excluding the nonrecurring expenses incurred for the project to list Pirelli Tyre S.p.A. (Euros 12.5 million), the consolidated gross operating profit is Euros 336.7 million (13.8 percent of net sales), with an increase of approximately 10 percent compared to the same period of 2005.

Consolidated **operating profit** amounts to Euros 216.1 million, an increase of 6.7 percent compared to Euros 202.5 million for the six months ending June 30, 2005 with growth across all business segments. The profit margin (ROS - Return on Sales) at the consolidated level is equal to 8.8 percent. Excluding the nonrecurring expenses incurred for the project to list Pirelli Tyre S.p.A., the consolidated operating profit is Euros 228.6 million (+12.9 percent compared to the first half of 2005), with a ROS of 9.3 percent (8.9 percent for the first six months to June 30, 2005).

**Earnings (losses) from investments**, which includes the effect of the result of the companies accounted for using the equity method and dividends from other unconsolidated holdings, is an earnings figure of Euros 165.2 million compared to Euros 133.4 million in the first half of 2005.

In particular, Olimpia contributed earnings of Euros 71.2 million compared to Euros 85.8 million in the first half of 2005. The difference compared to last year is due to the change in the net result of Telecom Italia S.p.A.. It should be pointed out that the interim financial statements of Olimpia S.p.A., included in the interim consolidated financial statements of the Group, have been drawn up in accordance with IFRS and comprise the valuation of the investment in Telecom Italia S.p.A. by the equity method.

This item also includes the results of the companies of the Pirelli Real Estate Group, which show earnings of Euros 54.6 million (Euros 44.6 million for the six months to June 30, 2005) and dividends received for Euros 43.3 million (Euros 20 million for the six months to June 30, 2005).

**Operating profit including earnings from investments** is equal to Euros 381.3 million. This is an increase of 13.5 percent compared to Euros 335.9 million for the first six months of 2005.

**Income** for the six months to June 30, 2006 is Euros 193.1 million, up 8.7 percent compared to the first half ending June 30, 2005 (Euros 177.6 million), on a comparable consolidation basis, before income (loss) from discontinued operations. In the first half of 2005, consolidated income including income from discontinued operations (Euros 32.8 million) was Euros 210.4 million.

**Income attributable to the equity holders of Pirelli & C. S.p.A.** for the first half ended June 30, 2006 is Euros 153 million (Euros 0.029 per share), compared to Euros 146.8 million in the first half of 2005, on a comparable consolidation basis, before income from discontinued operations. In the first half of 2005, income attributable to the equity holders of the company was Euros 179.6 million.

**Consolidated equity** at June 30, 2006 is Euros 5,714.6 million, compared to Euros 5,613.8 million at the end of 2005.

**Equity attributable to the equity holders of Pirelli & C. S.p.A.** at June 30, 2006 is Euros 5,342 million (Euros 0.995 per share) compared to Euros 5,204.9 million at the end of 2005 (Euros 0.979 per share).

The **net financial position** of the Group at June 30, 2006 is a net financial debt position of Euros 1,574.9 million, compared to Euros 1,494.7 million at March 31, 2006. The change during the quarter is primarily due to the effects of the payment of dividends of approximately Euros 160 million, offset in part by the proceeds of Euros 27 million on the exercise of Pirelli & C. warrants 2003-2006 and the net cash generated by operating activities. Net financial debt at June 30, 2005 was equal to Euros 2,338.2 million (of which Euros 714.9 million relates to the cables and systems activities sold), and at December 31, 2005 it was Euros 1,177.4 million.

At June 30, 2006, there are 28,455 **employees** of the Group compared to 26,827 at December 31, 2005. The increase of 1,628 in the number of the work force refers particularly to employees with temporary contracts (+1,015) and is mainly associated with the growth of operations in the tyre sector.

**The parent, Pirelli & C. S.p.A.**

The interim financial statements of the parent, Pirelli & C. S.p.A., prepared in accordance with IFRS, show income of Euros 132 million for the six months ended June 30, 2006 compared to Euros 131 million for the first half of 2005.

## **Significant events in the first six months**

The principal events which took place during the first six months of 2006 are as follows:

### **Corporate**

- On February 6, 2006, Olimpia S.p.A. and the shareholders Pirelli & C. S.p.A., Edizione Finance International S.A., Edizione Holding S.p.A., Banca Intesa S.p.A. and Unicredito Italiano S.p.A. sent Hopa S.p.A. the statement rescinding from the agreement signed among the parties in 2003. Therefore, at the expiration date (May 8, 2006), this agreement was not renewed.
- On February 14, 2006, the Pirelli & C. S.p.A. board of directors voted to undertake a course of action that would lead to the best way of appreciating the value of the tyres division (“Pirelli Tyres”), including its listing on the Electronic Trading Market of Borsa Italiana, with the understanding that Pirelli & C. S.p.A. would still hold the majority of the shares of Pirelli Tyres.  
In addition to the project to appreciate the value of Pirelli Tyres, the board of directors also approved a plan for the further concentration of resources in the strategic businesses of the Group through the disposal of financial investments for an equivalent amount of approximately Euros 400 million at current values, equal to about a half of that portfolio.
- During the first half of 2006, Pirelli Finance (Luxembourg) S.A., a wholly-owned subsidiary of Pirelli & C. S.p.A., exercised two call options on Telecom Italia S.p.A. shares for a total of 75,000,000 ordinary shares (equal to 0.56 percent of ordinary share capital) at the average price of Euros 2.35 per share for a total investment of Euros 176 million.

Furthermore, during the period, 10,400,000 Telecom Italia S.p.A. ordinary shares were purchased on the market (equal to 0.08 percent of ordinary share capital) at an average price per share of Euros 2.40 for a total investment of Euros 25 million.

After these transactions, Pirelli & C. S.p.A. holds, directly and indirectly, through Pirelli Finance (Luxembourg) S.A., 182,113,185 Telecom Italia S.p.A. ordinary shares (equal to 1.36 percent of ordinary share capital).

A forward share transaction signed on April 20, 2006 was put into place with Banca Caboto on the shares held by Pirelli Finance (Luxembourg) S.A. (134,957,885).

The shares were sold at the spot price per share of Euros 2.42 for a total of Euros 326.3 million and were subsequently repurchased on August 14, 2006 at a per share unit price of Euros 2.31 for a total of Euros 312 million.

- On March 27, and 28, 2006, Banca Intesa S.p.A. and UniCredito Italiano S.p.A. communicated their intention to withdraw from the shareholders' agreement, regarding the investment in Olimpia S.p.A. concluded in September 2001 with Pirelli & C. S.p.A., and consequently to exercise the right to sell their investments (equal to about 4.77 percent for each bank) to Pirelli & C. S.p.A.. The transfer of the investment will take place in October after expiration of the agreement (October 4, 2006) and will require Pirelli & C. S.p.A. to make a payment of about Euros 1.17 billion (of which Euros 130 million is already considered in the net financial position at December 31, 2005).
- On April 10, 2006, Pirelli Pneumatici S.p.A. (which later took the name of Pirelli Tyre S.p.A.), the company which heads all the tyre design, development, manufacturing and marketing activities of the Pirelli & C. S.p.A. Group, filed a request to list its ordinary shares with Borsa Italiana, with the shares put up for a public offering of sale by the 100 percent parent, Pirelli Tyre Holding N.V., a company which, in turn, is a wholly-owned subsidiary of Pirelli & C. S.p.A..

Subsequently, on June 30, 2006, the board of directors of Pirelli & C. S.p.A., – after the same resolution was passed by Pirelli Tyre Holding N.V. – decided not to go through with the IPO at the end of the offering period of the Pirelli Tyre S.p.A. shares.

Pirelli & C. S.p.A. deemed that the financial market conditions and, in particular, the stock market performance of the principal world tyre operators, would not make it possible to accurately and adequately value Pirelli Tyre S.p.A. so that it would reflect the intrinsic value of the company which is recognized as one of the most important tyre companies in the world in terms of profitability, positioning and capacity for innovation.

- On April 27, 2006, Pirelli Labs S.p.A., the Pirelli Group's center of technological excellence, and ENEA, Ente per le Nuove Tecnologie, l'Energia e l'Ambiente, launched three hi-tech research projects in the field of renewable energy sources and sustainable development within the sphere of a special five-year framework agreement.

The first research projects launched involve concentrated photovoltaic cell technology, a new generation of sensors for monitoring the environment and, finally, groundwork studies in the field of cold fusion.

The agreement between ENEA and Pirelli Labs also calls for the definition of other research projects in sectors of mutual interest.

The beginning of this partnership is further proof of Pirelli's commitment to the field of technologies for sustainable development.

- On June 16, 2006, Pirelli & C. S.p.A. sold a 15.26 percent stake in F.C. Internazionale Milano S.p.A. to the current majority stockholder of that company for Euros 13.5 million.

This transaction falls under the program approved by the board of directors of Pirelli & C. S.p.A. February 14, 2006 to further concentrate on its core business partly by disposing of non-strategic financial investments.

Pirelli & C. S.p.A., however, remains a shareholder of F.C. Internazionale Milano S.p.A. with a 4.2 percent stake. It is the company's intention to continue its current sponsorship relationship with F.C. Internazionale Milano S.p.A. and evaluate any new future possibilities of collaboration, especially in light of the considerable benefits this partnership has brought to the Pirelli brand over the years.

## Tyres Sector

- On March 22, 2006, Pirelli Pneus S.A. opened a new plant for manufacturing radial tyres for trucks and buses at Gravataí, in the Brazilian state of Rio Grande do Sul. The production unit is located in an area which already constitutes the Group's main center for the development and production of conventional motorcycle tyres. With a surface area of 573,000 m<sup>2</sup>, the new plant adds about 500 employees (direct and allied) to the current approximate 1,500 work force, and, when fully operational, will have a production capacity of 12,000 tons a year in addition to the current 64,000-ton production capacity.

80 percent of the Gravataí production is destined for the domestic market and 20 percent for export, mainly to countries in Latin America. The new plant calls for an overall investment of approximately Brazilian reais 116 million (more than US\$ 50 million) and, when fully operational, will contribute 8 percent to the sales of Pirelli Tyre in Brazil.

The opening of the new Gravataí plant has given another boost to Pirelli's presence in the radial truck tyre segment after the launch, in the second half of 2005, of production activities in China. These factories complete Pirelli Tyre's investment program in the Industrial segment, which can now count on new and more competitive production capacity to meet the growth in demand over the three-year period 2006-2008.

The investment in Gravataí is part of Pirelli Tyre's growth strategy on a global scale, which involves expanding into emerging markets in the Industrial sector and focusing on the Car and Motorcycle Premium segments. The new plant joins other Pirelli plants in the radial truck segment which are already operating in Italy, Turkey, Egypt, China and the Brazilian plant of Santo André.

- On May 8, 2006, Pirelli and Schrader Electronics signed an agreement with the aim of developing and marketing an innovative system, located, for the first time, directly inside the tyre and capable of detecting all kinds of identifying data in addition to temperature and pressure. The heart of the system consists of a miniature sensor which can function without batteries thanks to its capacity to generate its own energy.

Thanks to the new sensor, the tyre is able to interact with the vehicle, optimizing the on-board electronic systems, whose parameters adapt according to the information received from the device, leading to improved safety and performance.

The system, which was specially developed for original equipment, is particularly suitable for Run Flat tyres, since it allows for optimum management of the parameters when traveling with a flat tyre caused by a puncture.

On May 11, 2006, Francesco Gori, managing director of Pirelli Tyre, was elected president of the European Tyre and Rubber Manufacturers Association – ETRMA. The new non-profit organization replaces the previous representative body of rubber manufacturing companies founded in 1959 and has the aim of representing the tyre and rubber product industry within European Union institutions and other international organizations.

## Real estate activities

- On January 12, 2006, after winning the bid, which was concluded on October 14, 2005, for the purchase of a residential property portfolio in Berlin at the price of Euros 72.5 million, ownership was formally transferred to Tizian Wohnen 1 and Tizian Wohnen 2 – in which investments are held by the subsidiary P&K Real Estate. The properties purchased were part of the Corpus Immobiliengruppe property portfolio.
  
- On January 30, 2006, the board of directors of Pirelli RE SGR approved the management accounts at December 31, 2005 of Tecla Fondo Uffici, Berenice Fondo Uffici and Olinda Fondo Shops and passed resolutions on the following:
  - for Tecla Fondo Uffici, for the second half of 2005, the payment of dividends of Euros 21.92 per share (equal to 80 percent of distributable income) with a semiannual yield of 4.6 percent. Considering the full-year 2005, the dividend yield is equal to 9.3 percent, above the annual target dividend yield of 5.5 percent indicated at the time of placement. Also taking into account the previous years, the Fund has had an average annual yield of 8.6 percent on dividends alone paid since its placement;
  - for Olinda Fondo Shops, for the second half of 2005, the payment of dividends of Euros 19.54 per share (equal to 80 percent of distributable income) with a semiannual yield of 3.9 percent. Considering the full-year 2005, the dividend yield is equal to 7.3 percent, above the annual target dividend yield of 5.5 percent indicated at the time of placement. Also taking into account the previous years, the Fund has had an average annual yield of 6.7 percent on dividends alone paid since its placement;
  - for Berenice Fondo Uffici, with a mid-July 2005 placement, for the second half of 2005, the payment of dividends of Euros 15.05 per share (equal to 86 percent of distributable income) with a yield of 3 percent which corresponds to an annualized yield of 6.3 percent, above the annual target annual dividend yield of 4.75 percent indicated at the time of placement.

With regard to the closed-end unlisted reserved property investment funds, the annual dividend yield for Cloe Fondo Uffici was 15.3 percent, above the target dividend yield of 9.7 percent indicated at placement. For Teodora, operating only since mid-October 2005, the annualized dividend yield is 10.3 percent, above the target dividend yield of 7.5 percent indicated at the time of placement. For the subscribers of Clarice Light Industrial, the annual dividend yield is in line with the target yield of 9 percent indicated at the time of placement.

- On February 20, 2006, Pirelli RE and Merrill Lynch signed a binding agreement to set up a joint venture (with a 35 percent stake by Pirelli RE and a 65 percent stake by Merrill Lynch) for the investment of Euros 1.5 billion in the hotel tourism sector in Italy over the next five years.
- On March 29, 2006, the second investment in the Raissa Fund was finalized when 201 properties worth approximately Euros 158.1 million were contributed by Olivetti Multiservices (Telecom Italia Group) to this seeded fund intended for qualified investors. The contribution of the properties, which are commercial properties, are in addition to the properties conferred on December 28, 2005 worth about Euros 486 million. On June 29, 2006, the third investment was made in the Raissa Fondo Uffici when 57 properties worth approximately Euros 47 million were contributed by Olivetti Multiservices (Telecom Italia Group). The Fund is expected to be seeded by a total of 900 properties of which about Euros 790 million come from the Telecom Italia Group.
- On March 29, 2006, the Pirelli RE Group won the bid to build the new S. Anna di Como hospital. The work calls for a total investment of Euros 150 million. As a result of winning this bid, which is in addition to the project to build the Valpolcevera (Genoa) hospital which was won in 2005, Pirelli RE is achieving its objective of increasing its business in this sector.

- On March 30, 2006, Olivetti Multiservices (Telecom Italia Group) made a second contribution of 120 properties worth approximately Euros 70.8 million to the Spazio Industriale Fund. The contribution of the buildings is in addition to the conferral of properties finalized on December 29, 2005 worth approximately Euros 177 million. On June 26, 2006, the third contribution was made to the Spazio Industriale Fund by Olivetti Multiservices (Telecom Italia Group) for 54 buildings worth approximately Euros 42 million. The Telecom Italia Group is expected to contribute a total of more than 400 properties for a total of approximately Euros 300 million.
- On May 31, 2006, Resident Berlin 1 P&K GmbH undertook a commitment for the purchase of 16 buildings located in Berlin mainly for residential use at a price of Euros 61.1 million.
- On June 28, 2006, Pirelli RE Group, together with Conwert Immobilien and Eco Business-Immobilien, won the bid for the purchase from Allianz of a property portfolio in Austria worth approximately Euros 209 million. This property portfolio is principally located in the cities of Vienna, Innsbruck and Salzburg and it is composed of 31 mainly residential buildings and 47 buildings for office and commercial use. This transaction, which is in addition to the preceding acquisitions in Berlin and Warsaw, gives concrete form to Pirelli RE's expansion into Central and East Europe.

## **THE GROUP**

In this report on operations, in addition to the financial performance measures established by IFRS, certain non-IFRS measures originated from the latter are presented although they are not required by IFRS (“Non-GAAP Measures”).

These performance measures are presented for purposes of a better understanding of the trend of operations of the Group and should not be construed as a substitute for the information required by IFRS.

Specifically, the “Non-GAAP Measures” used are described as follows:

- **Gross operating profit:** this financial measure is used by the Group as the financial target in internal business plans and in external presentations (to analysts and investors). It represents a useful unit of measurement for the evaluation of the operating performance of the Group as a whole and for each single segment, in addition to the Operating Profit. The Gross Operating Profit is an intermediate performance measure represented by the Operating Profit from which depreciation and amortization are subtracted.
- **Earnings (losses) from investments:** earnings (losses) from investments consist of all the effects recorded in the income statement referring to investments. These include dividends, the share of the earnings (losses) of companies accounted for using the equity method, impairment losses of available-for sale financial assets and gains (losses) on the disposal of available-for-sale financial assets.

Movements in the fair value of assets available-for-sale that are recognized directly in equity are excluded.

- **Net financial (liquidity)/debt position:** this performance measure is represented by the gross financial debt less cash and cash equivalents as well as other interest-earning financial receivables. The Notes present a table that shows the balance sheet amounts used to calculate the net financial (liquidity)/debt position.

The highlights of the consolidated financial data of the Group for the first half of 2006 can be summarized as follows:

	(in millions of euros)		
	1 <sup>st</sup> Half 2006	1 <sup>st</sup> Half 2005	Year 2005
. Net sales	<b>2,445.9</b>	2,281.4	4,545.7
. Gross operating profit	<b>324.2</b>	306.3	567.6
% of net sales	<b>13.3%</b>	13.4%	12.5%
. Operating profit	<b>216.1</b>	202.5	354.9
% of net sales	<b>8.8%</b>	8.9%	7.8%
. Earnings (losses) from investments	<b>165.2</b>	133.4	267.1
. Operating profit incl. earnings (losses) from investments	<b>381.3</b>	335.9	622.0
. Financial income (expenses)	<b>(110.7)</b>	(87.2)	(144.4)
. Income taxes	<b>(77.5)</b>	(71.1)	(128.5)
<b>. Income from continuing operations</b>	<b>193.1</b>	177.6	349.1
% of net sales	<b>7.9%</b>	7.8%	7.7%
<b>. Income from discontinued operations</b>	<b>-</b>	32.8	49.8
<b>. Total income</b>	<b>193.1</b>	210.4	398.9
. Income attributable to the equity holders of Pirelli & C. S.p.A.	<b>153.0</b>	179.6	327.4
. Earnings per share (in euros)	<b>0.029</b>	0.038	0.066
. Equity	<b>5,714.6</b>	5,458.5	5,613.8
. Equity attributable to the equity holders of Pirelli & C. S.p.A.	<b>5,342.0</b>	5,098.0	5,204.9
. Equity per share (in euros)	<b>0.995</b>	0.959	0.979
. Net financial (liquidity)/debt position	<b>1,574.9</b>	2,338.2	1,177.4
<i>of which discontinued operations</i>		714.9	
. Capital expenditures	<b>126</b>	118	234
. R&D expenditures	<b>87</b>	82	174
. Employees (number at period-end)	<b>28,455</b>	26,050	26,827
. Factories (number)	<b>24</b>	23	24
<i>Pirelli &amp; C. shares outstanding at end of period/year</i>			
. ordinary shares (number in millions)	5,233.1	5,180.6	5,180.7
. savings shares (number in millions)	134.8	134.8	134.8
. Total shares outstanding at end of period/year	5,367.9	5,315.4	5,315.5

For a more meaningful understanding of the performance of the Group in its various segments of business, the following economic data and the net financial position are provided divided by business segment.

(in millions of euros)	1 <sup>st</sup> Half 2006					TOTAL
	Tyres	Broadband	Environment	Real Estate	Other	
. Net sales	2,018.4	72.7	39.3	308.4	7.1	<b>2,445.9</b>
. Gross operating profit (loss)	292.6	(0.1)	1.9	42.0	(12.2)	<b>324.2</b>
. Operating profit (loss)	194.6	(0.6)	1.5	37.7	(17.1)	<b>216.1</b>
. Earnings (losses) from investments	0.4	0.0	0.0	54.6	110.2 (1)	<b>165.2</b>
. Operating profit (loss) incl. earnings (losses) from investments	195.0	(0.6)	1.5	92.3	93.1	<b>381.3</b>
. Financial income (expenses)	(24.6)	(2.3)	0.0	(0.6)	(83.2)	<b>(110.7)</b>
. Income taxes	(52.1)	(0.4)	(0.4)	(21.1)	(3.5)	<b>(77.5)</b>
. Income (Loss)	118.3	(3.3)	1.1	70.6	6.4	<b>193.1</b>
. Net financial (liquidity)/debt position	739.6	(1.0)	(1.6)	82.3	755.6	<b>1,574.9</b>

  

(in millions of euros)	1 <sup>st</sup> Half 2005					TOTAL
	Tyres	Broadband	Environment	Real Estate	Other	
. Net sales	1,795.8	63.9	28.8	363.0	29.9	<b>2,281.4</b>
. Gross operating profit (loss)	279.6	(2.3)	(1.0)	39.9	(9.9)	<b>306.3</b>
. Operating profit (loss)	187.0	(2.6)	(1.8)	35.7	(15.8)	<b>202.5</b>
. Earnings (losses) from investments	0.2	-	-	44.6	88.6 (1)	<b>133.4</b>
. Operating profit (loss) incl. earnings (losses) from investments	187.2	(2.6)	(1.8)	80.3	72.8	<b>335.9</b>
. Financial income (expenses)	(15.9)	(0.7)	0.0	0.1	(70.7)	<b>(87.2)</b>
. Income taxes	(55.1)	(0.3)	0.0	(20.0)	4.3	<b>(71.1)</b>
. Income (Loss)	116.2	(3.6)	(1.8)	60.4	6.4	<b>177.6</b>
. Net financial (liquidity)/debt position	349.6	2.6	(5.7)	42.6	1,234.2	<b>1,623.3</b>
. Net financial (liquidity)/debt position of discontinued operations						<b>714.9</b>
. Total net financial (liquidity)/debt position						<b>2,338.2</b>

(1) The valuation of Olimpia S.p.A. by the equity method shows earnings of Euros 71 million (Euros 86 million in 2005)

## Net sales

Net sales amount to Euros 2,445.9 million for the six months ending June 30, 2006, with an increase, on a comparable consolidation basis, of 3.4 percent compared to the corresponding period of the prior year. Considering also the foreign exchange effect, the increase is 7.2 percent.

The breakdown of the percentage distribution of sales by business segment is as follows:

	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
Tyres Sector	82.5%	78.7%
Pirelli Broadband Solutions	3.0%	2.8%
Environment Sector	1.6%	1.3%
Pirelli Real Estate	12.6%	15.9%
Other	0.3%	1.3%

A breakdown of the change on a comparable consolidation basis by business segment of the Group is as follows:

Tyres Sector	+	7.4%
Pirelli Broadband Solutions	+	13.8%
Environment Sector	+	36.5%
Pirelli Real Estate	-	15.0%
<b>Total group</b>		<u><u>+ 3.4%</u></u>
Foreign exchange effect		<u>+ 3.8%</u>
<b>Total change</b>		<u><u>+ 7.2%</u></u>

### **Operating profit**

Operating profit for the first six months of 2006 is Euros 216.1 million, representing 8.8 percent of net sales compared to Euros 202.5 million for the corresponding period of 2005 (8.9 percent of net sales). Excluding nonrecurring expenses incurred for the project to list Pirelli Tyre S.p.A., the consolidated operating profit from ordinary operations is Euros 228.6 million (+12.9 percent compared to the first half of 2005) with a ROS of 9.3 percent compared to 8.9 percent in the first half of 2005.

A breakdown of the change by business segment of the Group can be summarized as follows (in millions of euros):

<b>Operating profit 1<sup>st</sup> Half 2005</b>		<b>202.5</b>
<hr/>		
. Tyres Sector	7.6	
. Pirelli Broadband Solutions	2.0	
. Environment Sector	3.3	
. Pirelli Real Estate	2.0	
. Other	(1.3)	
		<b>13.6</b>
<b>Operating profit 1<sup>st</sup> Half 2006</b>		<b>216.1</b>
<hr/>		

#### **Earnings (losses) from investments**

Earnings (losses) from investments amounts to earnings of Euros 165.2 million compared to earnings of Euros 133.4 million in the first half of 2005.

It includes the earnings of Olimpia S.p.A., valued by the equity method, for Euros 71.2 million (Euros 85.8 million in the first half of 2005). The difference compared to the first half of last year is due to the change in Telecom Italia S.p.A.'s income for the first half of the year. Note should be taken of the fact that the interim financial statements of Olimpia, which are consolidated in the Group's interim financial statements, include, in accordance with IFRS, the valuation of the investment in Telecom Italia S.p.A. by the equity method.

The item includes the results of the companies in the real estate sector valued by the equity method, which show earnings for Euros 54.6 million (Euros 44.7 million in the first half of 2005), dividends received for Euros 43.3 million (Euros 19.6 million in the first half of 2005), impairments of investments for Euros 1.9 million and losses on the disposal of available-for-sale financial assets for Euros 3 million.

**Financial income (expenses)**

Financial income (expenses) is a net financial expense balance of Euros 110.7 million compared to Euros 87.2 million in the same period of 2005.

This item includes a negative amount of Euros 58.6 million for the measurement of the derivatives on Telecom Italia S.p.A. securities that were already in the financial statements at December 31, 2005 and held by Pirelli Finance (Luxembourg) S.A. (Euros 44.8 million in the first half of 2005).

**Income**

Income from continuing operations for the six months ending June 30, 2006 is Euros 193.1 million, an increase of approximately 9 percent compared to the first half of 2005 (Euros 177.6 million) on a comparable consolidation basis, before income from discontinued operations.

In the first half of 2005, consolidated income, including income from discontinued operations of Euros 32.8 million, was Euros 210.4 million.

The income attributable to the equity holders of Pirelli & C. S.p.A. for the six months to June 30, 2006 is Euros 153 million (Euros 0.029 per share).

## Equity

Consolidated equity went from Euros 5,613.8 million at December 31, 2005 to Euros 5,714.6 million at June 30, 2006.

The change in equity can be summarized as follows:

	(in millions of euros)
. Translation differences	(64)
. Income for the period	193
. Dividends to third parties paid by:	(163)
- Pirelli & C. S.p.A.	(114)
- Pirelli & C. Real Estate S.p.A.	(37)
- Other Group companies	(12)
. Exercise of Pirelli & C. Real Estate S.p.A. stock options	12
. Pirelli & C Real Estate S.p.A. treasury share purchases/sales	(25)
. Fair value adjustment of available-for-sale financial assets	54
. Net actuarial gains (losses) on employee benefits	48
. Exercise of warrants 2003/2006	27
. Change in Olimpia valuation	28
. Purchase of shares from minority shareholders	(8)
. Other changes	(1)
	<b>101</b>

The equity attributable to the equity holders of Pirelli & C. S.p.A. went from Euros 5,204.9 million (Euros 0.979 per share) at December 31, 2005 to Euros 5,342 million (Euros 0.995 per share) at June 30, 2006.

**Net financial position**

The net debt position is Euros 1,574.9 million compared to Euros 1,177.4 million at December 31, 2005, with a change of Euros 397.5 million.

The change is summarized in the following table:

	(in millions of euros)
. Cash flows used in ordinary activities	(36.7)
. Exercise of warrants 2003/2006	27.3
. Purchase of Telecom Italia shares	(201.0)
. Purchase of Capitalia shares	(38.2)
. Partial sale of F.C. Internazionale Milano	13.5
. Dividends paid	(162.4)
<b>Change in net financial position</b>	<b>(397.5)</b>

**R&D expenditures**

R&D expenditures went from Euros 82 million in the first six months of 2005 (3.6 percent of net sales) to Euros 87 million in the first half of 2006 (3.6 percent of net sales). Such expenditures are completely expensed to income.

## Employees

At June 30, 2006, there are 28,455 employees (including 4,117 temporary employees), compared to 26,827 at December 31, 2005. The increase in the work force principally refers to employees with temporary contracts.

The breakdown of employees by geographical area and by business segment is as follows:

	<b>June 30, 2006</b>		<b>December 31, 2005</b>	
<b>Geographical area</b>				
Europe:				
. Italy	7,094	24.93%	7,041	26.25%
. Other European countries	7,418	26.07%	7,066	26.33%
North America	247	0.87%	222	0.83%
Central and South America	9,604	33.75%	9,136	34.06%
Oceania, Africa and Asia	4,092	14.38%	3,362	12.53%
	<b>28,455</b>	<b>100.00%</b>	<b>26,827</b>	<b>100.00%</b>
<b>Business segment</b>				
Tyres Sector	25,214	88.61%	23,673	88.24%
Pirelli Real Estate	1,692	5.95%	1,614	6.02%
Pirelli Broadband Solutions	146	0.51%	122	0.45%
Environment Sector	48	0.17%	43	0.16%
Other	1,355	4.76%	1,375	5.13%
	<b>28,455</b>	<b>100.00%</b>	<b>26,827</b>	<b>100.00%</b>

**Significant events subsequent to the end of the first six months**

- On July 4, 2006, Pirelli & C. S.p.A., Edizione Finance International S.A. and Edizione Holding S.p.A. together with Hopa S.p.A. communicated that they had reached full agreement over all the aspects relating to the cash settlement of the investments held in Olimpia S.p.A. and in Holinvest S.p.A. following the dissolution of the shareholders' agreements that were already in existence among the above companies.

This agreement provided for:

- the purchase on the part of Pirelli & C. S.p.A., Edizione Finance International S.A. and Edizione Holding S.p.A. of all the shares held by Hopa S.p.A. in Olimpia S.p.A. (equal to 16 percent of capital) for a cash settlement of Euros 622 million (of which Euros 208 million relates to the premium to which Hopa had the right on the basis of previous agreements);
- the purchase on the part of Hopa S.p.A. of all the shares held by Olimpia S.p.A. in Holinvest S.p.A. (equal to 19.999 percent of capital) for a cash settlement of Euros 86 million.

Holinvest S.p.A., at that date, was the owner of 492,697,862 Telecom Italia S.p.A. shares, equal to about 3.68 percent of ordinary share capital.

On the basis of the terms of the agreement, 320,253,610 Telecom Italia S.p.A. shares held by Holinvest S.p.A. (equal to 65 percent of the total shares in its possession) are covered by a pre-emptive two-year agreement in favor of Olimpia S.p.A. which also establishes that Holinvest S.p.A. may not effect new purchases of Telecom Italia S.p.A. shares without the prior agreement of Olimpia S.p.A. during the same period.

The purchases of the investments and the signing of the pre-emptive agreement were finalized on July 12, 2006.

Specifically, Pirelli & C. S.p.A. purchased 12.8 percent of Olimpia S.p.A. for an outlay of Euros 331 million. At the same time, it paid its share of the premium due to Hopa S.p.A. of Euros 166 million, which had already been set aside in the 2005 financial statements.

- On July 27, 2006, the board of directors of Pirelli & C. S.p.A. examined a transaction with some leading Italian and international financial institutions (Banca Intesa, Banca Leonardo Group, Capitalia, One Equity Partners – JP Morgan Group, Lehman Brothers and Mediobanca) for the sale of a minority interest in the capital of Pirelli Tyre S.p.A., for the purpose of a later IPO.

Subsequently, on July 29, 2006, the relevant agreements were reached for the sale of 38.9 percent of the capital of Pirelli Tyre S.p.A. for consideration equal to Euros 740 million, with an equity value for the entire company of about Euros 1.9 billion.

The purchase of the minority interest in Pirelli Tyre S.p.A., finalized on August 2, 2006, was carried out by Speed S.p.A., an Italian company in which about a 19 percent stake each is held by Banca Intesa, Capitalia, One Equity Partners – JP Morgan Group, Lehman Brothers and Mediobanca and about 4 percent stake by the Banca Leonardo Group.

The agreements provide that the purchasing companies may start and conduct, within a period of four years and six months from the closing date, an Initial Public Offering of the shares acquired.

Pirelli has the right to repurchase the shares that were sold in the event in which, after four years and six months, the shares have not been placed in an IPO.

The relationships between the seller and the buyer are regulated by shareholder agreements which provide, among other things, that the acquiring company may designate five out of the thirteen directors on the board of directors of Pirelli Tyre S.p.A. and appoint a member of the board of statutory auditors.

After a lock-up period of six months, and after receiving Pirelli's approval, the acquiring company or its shareholders will have the right to sell up to 49 percent of the shares originally purchased to qualified parties (leading financial institutions or mutual funds).

A commission of 3 percent of the equivalent amount of the transaction was paid to the financial institutions and an additional 1 percent will be paid on an annual basis until the IPO.

- On August 2, 2006, Pirelli RE Group and Calyon, the corporate investment bank of the Credit Agricole Group, signed a binding agreement to establish a joint venture to invest in Europe in the non-performing loans segment.

The joint venture, in which Pirelli RE will have a 33 percent interest and Calyon a 67 percent interest, is committed to acquiring 100 percent of five non-performing mortgage loan receivable portfolios held since November 2004 by the Pirelli RE/MSREF joint venture with a residual gross book value of approximately Euros 2.6 billion. After the new strategic partnership is established, Pirelli RE will take over 53 percent of Credit Servicing (in which it already has a 47 percent stake) and 25 percent of Asset Management NPL (in which it already has a 25 percent stake) from the Morgan Stanley real estate funds. The portfolio of loans purchased from Banco Popolare di Verona e Novara last June 7 will also be transferred to the non-performing loan portfolio of the joint venture.

At the same time, the joint venture established in August 2004 between Pirelli RE Group (25 percent) and Morgan Stanley Real Estate Funds (75 percent) for the purpose of investments on the Italian market has been dissolved; the American investment bank will remain a strategic partner of Pirelli RE in the offices sector.

The closing of the transaction is scheduled to take place by the end of 2006 on condition of approval by the Antitrust Authority and by the trustees of the outstanding securitization transactions.

### **Outlook for the current year**

The results achieved in the first half of the year confirm the forecasts of a further improvement in results for 2006 compared to the prior year, unless external extraordinary events occur which cannot be foreseen at the time.

## **TYRES SECTOR**

The consolidated results of Pirelli Tyre for the six months ended June 30, 2006 show a double-digit increase in sales and a significant improvement in ordinary operations compared to the first six months of 2005, even though an increase in raw material costs penalized the entire sector.

The highlights of the consolidated financial data of the Tyres Sector for the first half of 2006 can be summarized as follows:

	(in millions of euros)		
	1 <sup>st</sup> Half 2006	1 <sup>st</sup> Half 2005	Year 2005
. Net sales	<b>2,018.4</b>	1,795.8	3,632.9
. Gross operating profit	<b>292.6</b>	279.6	518.1
% of net sales	<b>14.5%</b>	15.6%	14.3%
. Operating profit	<b>194.6</b>	187.0	328.8
% of net sales	<b>9.6%</b> <sup>(1)</sup>	10.4%	9.1%
. Financial income (expenses)	<b>(24.2)</b>	(15.7)	(33.4)
. Income taxes	<b>(52.1)</b>	(55.1)	(97.0)
. Income	<b>118.3</b>	116.2	198.4
% of net sales	<b>5.9%</b>	6.5%	5.5%
. Net financial (liquidity)/debt position	<b>739.6</b>	349.6	237.4
. Capital expenditures	<b>115</b>	93	208
. R&D expenditures	<b>74</b>	73	146
. Employees (number at period-end)	<b>25,214</b>	22,824	23,673
. Factories (number)	<b>24</b>	23	24

**Net sales** amount to Euros 2,018.4 million, with an increase of 12.4 percent for the corresponding period of the prior year. Excluding the foreign exchange effect, net sales rose by 7.4 percent.

The change can be summarized as follows:

• Volumes	+	4.3%
• Prices/mix	+	3.1%
		<hr/>
<b>Change on a comparable basis</b>	+	<b>7.4%</b>
		<hr/>
• Foreign exchange effect	+	5.0%
		<hr/>
<b>Total change</b>	+	<b>12.4%</b>
		<hr/>

**Gross operating profit** went from Euros 279.6 million in the first half of 2005 to Euros 292.6 million in the first half of 2006 (14.5 percent of net sales). Excluding nonrecurring expenses incurred for the project to list Pirelli Tyre S.p.A. (Euros 6.5 million), the gross operating profit is Euros 299.1 million, with an increase of approximately 7 percent compared to the same period of 2005.

**Operating profit** is Euros 194.6 million, an increase of 4.1 percent over the corresponding period of the prior year. Operating profit as a percentage of sales is 9.6 percent compared to Euros 187 million or 10.4 percent of net sales in the first half of 2005.

Excluding nonrecurring expenses incurred for the project to list Pirelli Tyre S.p.A. (Euros 6.5 million), the operating profit from ordinary operations is Euros 201.1 million (+7.5 percent compared to 2005) with ROS at 10 percent.

The increase in operating profit is due to the positive impact associated with the growth of sales and efficiencies, which more than compensated the increase in the costs of production factors. The decline in the profit percentage can principally be ascribed to the increase in raw material costs and the effect of the start-up of the new factory in China.

The change in operating profit can be summarized as follows (in millions of euros):

<b>Operating profit 1<sup>st</sup> Half 2005</b>		<b>187.0</b>
<hr/>		
. Foreign exchange effect	15.6	
. Prices/mix	7.7	
. Volumes	29.3	
. Production factors per unit cost	(56.9)	
. Efficiencies	11.1	
. Depreciation	(1.4)	
. Other	2.2	
		<b>7.6</b>
<b>Operating profit 1<sup>st</sup> Half 2006</b>		<b>194.6</b>
<hr/>		

**Income** for the six months ending June 30, 2006 is Euros 118.3 million (after financial expenses of Euros 24.2 million and income tax expenses of Euros 52.1 million) compared to income in the first half of 2005 of Euros 116.2 million (after financial expenses of Euros 15.7 million and income tax expenses of Euros 55.1 million).

With regard to financial expenses, as a result of the reorganization of the company effected during the first quarter, the sector had an increase in net debt equal to Euros 406 million.

The **net financial position** is a net debt position of Euros 739.6 million compared to Euros 237.4 million at December 31, 2005.

At June 30, 2006, there are 25,214 **employees** (including 3,957 temporary employees) compared to 23,673 employees (including 2,958 temporary employees) at December 31, 2005. The increase is due to the development of activities in China and Romania.

There are 24 **factories**, unchanged compared to December 31, 2005.

## Consumer market

During the first six months of 2006, there was an overall increase in sales and profitability compared to the same period of 2005, thanks to higher volumes and a better price/mix. In particular, net sales totaled Euros 1,403 million (+11 percent compared to the first half of 2005) and the operating profit from ordinary operations amounted to Euros 140.7 million (+18 percent), with ROS at 10 percent.

In the **Cars** segment, demand was generally negative in North and South America, while demand grew in Europe, driven by the segments with higher added value, such as High-performance, Ultra high-performance and SUV tyres.

With regard to Pirelli products, during the first six months of 2006, Pirelli's position in the world ranking was strengthened, thanks especially to the P Zero, Eufori@ and Scorpion ranges. During the period under consideration, with the P Zero range, Pirelli confirmed its supremacy over more recent models manufactured by other leading tyre manufacturers.

During the six-month period, Pirelli launched the innovative K-Pressure Optic system for active tyre-pressure control and Scorpion ATR, the new high-performance product line for 4 x 4 vehicles.

In the **Motorcycle** segment, there was an improvement in demand in all the main market segments, especially in North and South America, where Pirelli and Metzeler increased their market share.

The first half of 2006 saw the successful launch of Sportec M3 under the Metzeler brand and Diablo Superbike, Supercorsa and Corsa III under the Pirelli brand.

### **Industrial market**

The first half of 2006 closed with sales totaling Euros 616 million, an increase of 16 percent compared to the same period of 2005. The operating profit from ordinary operations amounted to Euros 60.4 million, a contraction of 10 percent compared to the first half of 2005. The decline is due to an increase in costs that was higher than expected, especially in the case of natural rubber and energy. ROS was 9.8 percent. Market demand was positive overall in Europe and contracted in South America.

In the **Truck Tyre** segment, Pirelli consolidated the market share reported in the prior year (Europe, the Mediterranean Area and South America). During the first six months of the year, tyre production began under the Pirelli brand at the Yanzhou production facility in China.

**Steelcord** products closed the first half of 2006 with an increase in sales volumes of 10 percent, in the presence of an increase in world consumption of 7 percent. China, South America and Eastern Europe were again the areas with the highest growth rates.

### **Outlook for the current year**

Pirelli Tyre expects a continued improvement in the operating results compared to the prior year.

## **PIRELLI BROADBAND SOLUTIONS**

The highlights of the data of Pirelli Broadband Solutions for the first half of 2006 can be summarized as follows:

	(in millions of euros)		
	<b>1<sup>st</sup> Half 2006</b>	1 <sup>st</sup> Half 2005	Year 2005
. Net sales	<b>72.7</b>	63.9	112.2
. Gross operating loss	<b>(0.1)</b>	(2.3)	(6.3)
% of net sales	<b>n.s.</b>	n.s.	n.s.
. Operating loss	<b>(0.6)</b>	(2.6)	(7.0)
% of net sales	<b>n.s.</b>	n.s.	n.s.
. Financial income (expenses)	<b>(2.3)</b>	(0.7)	(0.7)
. Income taxes	<b>(0.4)</b>	(0.3)	(0.4)
. Loss	<b>(3.3)</b>	(3.6)	(8.1)
% of net sales	<b>n.s.</b>	n.s.	n.s.
. Net financial (liquidity)/debt position	<b>(1.0)</b>	2.6	7.2
. Employees (number at period-end)	<b>146</b>	112	122

**Net sales** for the six months ending June 30, 2006 amount to Euros 72.7 million, with an increase of 13.8 percent compared to Euros 63.9 million for the first half of 2005 due partly to the marketing of new second-generation photonics products for Euros 7.7 million.

The **gross operating result** reached a breakeven and represents an improvement over the gross operating loss of Euros 2.3 million in the first half of 2005.

The **operating result** shows a profit for broadband access activities but was nevertheless hurt by the result of second-generation photonics products so that the overall operating result is a loss of Euros 0.6 million. This is an improvement over the operating loss of Euros 2.6 million for the corresponding period of 2005.

The **loss** for the six months ending June 30, 2006 is Euros 3.3 million compared to Euros 3.6 million for the six months ending June 30, 2005.

The **net financial position** is a net liquidity position of Euros 1 million.

At June 30, 2006, there are 146 **employees**, an increase of 24 compared to December 2005.

### **Broadband Access**

Development activities in the first half of the year 2006 focused on four product lines: access gateways, Set-top Box, PMP and Extenders.

With regard to residential access gateways, development of the ADSL2+ platform was completed, resulting in the products Agv3 (Telecom Italia) and HAG v02 (Fastweb).

In addition, gateway development projects were started with the aim of completing the product portfolio: Discus Multiplay (ADSL2+, 4 Ethernet, Wi-Fi 11g, USB2.0h, 2FXS + FXO, 1 USB1.1d, smart card reader), Modem combo (ADSL2+, 1 Ethernet, 1 USB1.1d), Wireless router (ADSL2+, 4 Ethernet, 1 USB1.1d), Router (ADSL2+, 4 Ethernet, 1 USB1.1d), AG2+ and AGW2+ for Telecom Italia. The whole portfolio is based on Broadcom technology (the current market leader) and incorporates an embedded SW solution which can be used on all the products being developed, which will allow tele-management using the TR-069 protocol.

A strategic collaboration agreement has been signed with the French company OneAccess. Thanks to the agreement, Pirelli Broadband Solutions has the exclusive rights in Italy for a complete portfolio of routers and IAD for the small business market, which is in direct competition with the products of Cisco, the market leader.

The Set-top Box project continued with the development of a H.264 single chipset which integrates Alcatel OMP 2.1 middleware, requested by Telecom Italia.

The first version of the product developed implements the IP-TV function, with the decoding of Conditional Access by means of a smart card, and includes a DVB-T tuner for decoding digital Free To Air signals.

The second version being developed also includes the support of a hard disk for PVR functions.

Work also began on the integration phase of the Microsoft MS-TV2 middleware project.

The PMP project was re-organized in order to keep up with new developments in the market.

The product, still based on the JMS bus architecture, will incorporate core functions in the roadmap (back-up and restore smart card, group management), will manage the products of Pirelli or third-parties by means of plug-ins on the bus and will implement suitable customized features according to the requirements of individual customers.

With regard to the range of Extenders, the qualification of the Power Lines (PLC) adapter based on Home-Plug 85Mb/s and DS2 200Mb/s technology has been completed.

The testing phase of MIMO technology began for video-over-wireless distribution applications, although it is thought that current technologies are not as competitive as the 802.11n standard, which is expected to be finalized in the first half of 2007.

To complete the product portfolio, a dual-mode Wi-Fi and GSM/GPRS telephone has been introduced for fixed-mobile convergence applications.

The telephone is based on SIP technology, in which Pirelli gained considerable experience in 2004 when it used its own access gateways to support Telecom Italia's Alice mia service, implemented with Wi-Fi telephones.

The product has already been selected by the German operator Arcor and is in the process of being tested by the main European carriers, since it is one of the first on the market to be in a competitive price range suited to use by the consumer clientele.

### **New Photonics Products**

During the first half of 2006, development activities focused mainly on three areas: innovative optical components, optical modules and optical transport systems.

With regard to optical systems, the commercial success, which began in August 2005, of the optical Coarse WDM system known as City8™, continued. Overall, more than 1,200 devices were sold in Italy, France, Germany, Sweden and the United States. During 2006, this product, which is being continuously integrated with new functions, will evolve so that it can support signals at 10 Gbit/s, while maintaining its distinctive characteristics of versatility and low cost. The applications of the device, which, for the moment, mainly involve the support of new services (such as IP-TV) or the strengthening of already-existing metropolitan broadband networks, will be extended to higher levels of the network so that it also covers metro-regional access sectors.

In the field of optical components, the qualification of the Tunable Laser for application in transmission systems for metropolitan optical and transport networks is nearing completion. Samples of the product have already been supplied to a large number of customers, some of whom are completing the task of integrating it electronically within their systems.

In the field of optical modules, the supply of Radio over Fiber modules has begun, based on the existing supply agreement with Alcatel. Alcatel has completed the phase of integrating the module inside its third-generation mobile systems.

Finally, the in-house development of the line of innovative opto-electronics modules (MSA and XFP format) begun in December 2005 and based on optical devices using nanotechnology (such as the Tunable Laser and the Optical Dispersion Compensator) continues. The use of these modules in optical transmission equipment in metropolitan networks will make it possible to augment flexibility and reduce costs for the operator.

The first prototypes of the modules will be demonstrated at customers' premises before the end of 2006. These developments will make it possible to expand the product portfolio and to make a quantum leap forward in the chain of value.

### **Outlook for the current year**

For the rest of the year, both the access market and the market of photonics based on optical devices using nanotechnology are expected to show a continuous growth which would confirm the increase in sales and the improvement in the operating result that has already been recorded in the first half.

## **PIRELLI & C. REAL ESTATE**

As confirmation of the growth in results, income attributable to the equity holders of the company reached Euros 70 million in the first six months of 2006 compared to Euros 59.8 million for the first six months of 2005, with an increase of 17 percent.

### **Economic review**

In reading the income statement presented below, it should be noted that the aggregate revenues and the operating profit including earnings from investments, because of the type of business conducted by the Group, are the most important indicators and express, respectively, the business volumes managed and the trend in results.

(in millions of euros)

	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
<b>Aggregate revenues</b>	<b>1,706.2</b>	<b>1,741.7</b>
Consolidated revenues	308.4	363.0
<b>Operating profit including earnings from investments (*)</b>	<b>92.3</b>	<b>80.3</b>
<b>Income attributable to the equity holders of the company</b>	<b>70.0</b>	<b>59.8</b>

(\*) Operating profit including earnings (losses) from investments comprises the operating profit (Euros 37.7 million for the first half of 2006) in addition to the share of earnings (losses) of companies accounted for by the equity method (Euros 52.8 million for the first half of 2006) and income from real estate investment funds (Euros 1.8 million for the first half of 2006). That amount also includes Euros 32.8 million for the fair value adjustments of properties (IAS 40) in the first half of 2006.

**Aggregate revenues** amount to Euros 1,706.2 million and are basically in line with the figure in the first half of 2005 of Euros 1,741.7 million.

**Consolidated revenues** amount to Euros 308.4 million compared to Euros 363.0 million for the first six months ending June 30, 2005.

**Operating profit including earnings from investments** is Euros 92.3 million, with an increase of 15 percent compared to Euros 80.3 million in the first half of 2005.

**Income attributable** to the equity holders of the company is Euros 70.0 million, compared to Euros 59.8 million for the first half of June 2005, with a growth of 17 percent.

### **Balance sheet and financial review**

(in millions of euros)	6/30/2006	12/31/2005
<b>Fixed assets</b>	<b>572.7</b>	<b>410.7</b>
<i>. including investments in funds and investment companies (*)</i>	433.4	303.3
<b>Net working capital</b>	<b>96.2</b>	<b>215.9</b>
<b>Net invested capital</b>	<b>668.9</b>	<b>626.6</b>
<b>Equity</b>	<b>529.6</b>	<b>552.1</b>
<i>. of which attributable to the equity holders of the company</i>	518.6	535.4
<b>Provisions and contributions</b>	<b>57.0</b>	<b>44.0</b>
<b>Net financial (liquidity)/debt position</b>	<b>82.3</b>	<b>30.5</b>
<i>. of which loans by shareholders</i>	(382.9)	(262.0)
<b>Total net invested capital financed</b>	<b>668.9</b>	<b>626.6</b>
<b>Net financial (liquidity)/debt position before shareholder loans</b>	<b>465.2</b>	<b>292.5</b>
<b>Gearing ratio, financial position before shareholder loans (**)</b>	<b>0.88</b>	<b>0.53</b>

(\*) This item includes investments in associates and joint ventures, investments in real estate investment funds and junior notes.

(\*\*) The gearing ratio corresponds to the ratio of net financial (liquidity)/debt position before shareholder loans to equity.

**Equity attributable** to the equity holders of the company at June 30, 2006 is Euros 518.6 million compared to Euros 535.4 million at December 31, 2005, with a decrease of Euros 16.8 million.

The change is basically due to the combined effect of an increase in the income for the period (+Euros 70 million) and the increase in share capital with a share premium to service stock options (+Euros 12.3 million) and a decrease generated by the payment of dividends (-Euros 77.3 million) and the purchase of treasury stock (-Euros 25.1 million di euro).

The **net financial position** shows a net debt position of Euros 82.3 million compared to Euros 30.5 million at December 31, 2005.

The **adjusted net financial position** (expressed before shareholder loans made to minority-owned companies) is a net debt position of Euros 465.2 million, compared to Euros 292.5 million at December 31, 2005. The increase is not only due to the payment of dividends but also to the most recent acquisitions that have not yet been converted over to the normal business model which calls for their deconsolidation in the second half (specifically the real estate investments in Poland and the non-performing loans in Italy).

The **gearing** ratio is 0.88 compared to 0.53 at December 31, 2005.

**Fixed assets** total Euros 572.7 million at June 30, 2006 compared to Euros 410.7 million at the end of 2005, with an increase of Euros 162 million. The change is due to an increase in the value of the investments in associates and joint ventures for Euros 129.5 million and the purchase of securities from the securitization of the non-performing loans of the former Banco di Sicilia in addition to the investments made in Pirelli Pekao RE for a 75 percent stake and in Pirelli RE SGR for the remaining 12.7 percent interest.

**Net working capital** at June 30, 2006 is equal to Euros 96.2 million compared to Euros 215.9 million at the end of 2005. The reduction of Euros 119.7 million is due

to the combined effect of the increase in inventories, largely due to acquisitions made in Poland during the first six months, a significant reduction in trade receivables and an increase in other payables as a result of the purchase of the non-performing loans from Banco di Sicilia.

### **Outlook for the current year**

Considering the final approval of the law for the conversion of Legislative Decree No. 223/2006, published on August 11, 2006, and the recognition of the role of financial real estate agents starting from October 1, 2006, the company in the third quarter expects a slowdown in business and for the full-year confirms an increase in the operating profit including earnings from investments in the low range indicated in the three-year plan 2006-2008 (CAGR 10-15 percent).

**PIRELLI AMBIENTE**

The highlights of the consolidated data of Pirelli Ambiente for the first half of 2006 can be summarized as follows:

	(in millions of euros)		
	<b>1<sup>st</sup> Half 2006</b>	1 <sup>st</sup> Half 2005	Year 2005
. Net sales	<b>39.3</b>	28.8	61.5
. Gross operating profit (loss)	<b>1.9</b>	(1.0)	(2.0)
% of net sales	<b>n.s.</b>	n.s.	n.s.
. Operating profit (loss)	<b>1.5</b>	(1.8)	(3.6)
% of net sales	<b>n.s.</b>	n.s.	n.s.
. Financial income (expenses)	-	-	-
. Income taxes	<b>(0.4)</b>	0.0	0.2
. Income (Loss)	<b>1.1</b>	(1.8)	(3.4)
% of net sales	<b>n.s.</b>	n.s.	n.s.
. Net financial (liquidity)/debt position	<b>(1.6)</b>	(5.7)	0.8
. Employees (number at period-end)	<b>48</b>	40	43

**Pirelli & C. Ambiente Renewable Energy S.p.A.**

The result for the first half of 2006 benefited from the agreement signed at the end of the prior year, which provides for the granting of licenses, patents, know-how and assistance by the company to the UK start-up ReEnergy Group P.l.c..

Last January, the company received the sum established in the agreement for the granting of the licenses, patents and know-how of Pounds sterling 1.8 million, equal to Euros 2.7 million (net of the 8 percent withholding tax equal to Euros 0.2 million). Furthermore, since January, the company has supplied assistance to the start-up, based on a four-year service contract against payment of a “fixed amount”. The services supplied in the first six months of 2006 amount to Euros 0.2 million.

In addition, if the CDR-P (Refuse Derived Fuel-Pirelli) market in the U.K. becomes stronger, the agreement provides for the possibility of forming a joint venture with ReEnergy Group P.l.c. to build up the business.

During the first half of 2006, the company continued to promote negotiations with the aim of starting new projects in the field of renewable energy sources through the production of a quality fuel (CDR-P) derived from solid urban waste for the subsequent start of renewable energy development through the replacement of primary fossil fuels in existing systems.

During the first six months of the current year, the activities for producing the quality fuel (CDR-P) were profitably conducted through the associate I.D.E.A. Granda S.C.R.L., which recovered 8,605 tons of fuel compared to 7,350 tons in the same period of 2005.

#### **Pirelli & C. Ambiente Eco Technology S.p.A.**

During the first half of 2006, the emulsions division returned to a profit position which made it possible to absorb the costs sustained for the development of post-treatment filtering systems to reduce emissions from diesel-powered vehicles and the costs of maintaining the structure.

With regard to emulsions, the reduction of approximately 17 percent of the volumes of Gecam marketed in Italy compared to the same period of 2005 was offset by the positive trend of per unit margins and the reduction of costs. The remarkable increase of volumes marketed in France, which almost tripled compared to the same period of the prior year, enabled the subsidiary Gecam France to achieve a fundamental economic balance.

With regard to the diesel post-treatment filtering systems, deliveries of the contract for ATM Milano were completed for sales of approximately Euros 1.2 million and activities were further intensified to develop, perfect and market new models. This will continue until the uncertainty surrounding standards on the homologation of vehicles equipped with filtering systems is resolved, allowing the development of a promising market in this sector. Meanwhile, work continued on the building of a production site at Arese, scheduled to start production in the early months of 2007.

### **Pirelli & C. Ambiente Site Remediation S.p.A.**

The activities conducted involve the full-scale management of environmental problems, principally in the companies of the Pirelli & C. S.p.A. Group, and with particular reference to Environmental Due Diligence, evaluation, planning and management of activities such as demolition and land reclamation conducted by specialist companies which are authorized to conduct such work.

The most significant contracts completed or still in progress during the first six months of 2006 include: clean-up of the former Cartiere Burgo paper factory; start and completion of soil remediation at the former industrial site of Sesto S. Giovanni; completion of activities begun in 2004 to reclaim the former site of Pirelli Cables & Systems in the Milan Bicocca area, and investigations to assess the environmental situation of the former ENI site at Portogruaro.

### **Outlook for the current year**

Pirelli Ambiente expects to report an improvement compared to the prior year.

## PROFORMA DATA

### Proforma consolidated economic and financial data assuming the line-by-line consolidation of Olimpia S.p.A.

Proforma consolidated data at June 30, 2006 of Pirelli & C. S.p.A. is presented below, assuming the consolidation line-by-line of Olimpia S.p.A..

	Interim consolidated financial statements 6/30/2006 Pirelli & C. S.p.A. (1)	Proforma adjustments				Proforma interim consolidated financial statements 6/30/2006 Pirelli & C S.p.A. (2)
		Elimination of Olimpia S.p.A. result attributable to Pirelli & C S.p.A.	Olimpia S.p.A. line-by-line consolidation	Olimpia S.p.A. consolidation entries	Total proforma adjustments	
(in millions of euros)						
<b>Condensed income statement</b>						
Net sales	2,446	-	-	-	-	2,446
Operating profit	216	-	-	-	-	216
Financial income (expenses)/ valuation adjustments to financial assets	54	(71)	118	-	47	101
Income taxes	(77)	-	-	-	-	(77)
Income	193	(71)	118	-	47	240
Income - attributable to the equity holders of Pirelli & C. S.p.A.	153	(71)	71	-	-	153
<b>Reclassified balance sheet</b>						
Equity	5,715	(71)	7,589	(4,675)	2,843	8,558
- of which equity attributable to the equity holders of Pirelli & C. S.p.A.	5,342	(71)	4,588	(4,517)	-	5,342
Net financial (liquidity)/debt position	1,575	-	3,223	-	3,223	4,798

(1) Pirelli & C. S.p.A. interim consolidated financial statements (investment in Olimpia S.p.A. accounted for by the equity method with Olimpia accounting for Telecom Italia by the equity method).  
(2) Proforma data (line-by-line consolidation of Olimpia S.p.A.).

The proforma consolidated economic and financial data has been prepared using:

- the interim financial statements of Olimpia S.p.A. at June 30, 2006, adjusted to conform with IFRS, wherein the investment in Telecom Italia S.p.A. is accounted for by the equity method (using interim financial statements prepared in accordance with IFRS);
- the interim consolidated financial statements of Pirelli & C. S.p.A. at June 30, 2006 (prepared in accordance with IFRS) wherein Olimpia S.p.A. is accounted for, in turn, by the equity method.

The principal proforma adjustments included in the above table are as follows:

- in the column “Elimination of Olimpia S.p.A. result attributable to Pirelli & C. S.p.A.”: elimination of the income statement and balance sheet effects of valuing Olimpia S.p.A. by the equity method in the Pirelli & C. S.p.A. interim consolidated financial statements at June 30, 2006;
- in the column “Olimpia S.p.A. line-by-line consolidation”: inclusion of the assets, liabilities, costs and revenues resulting from the interim financial statements at June 30, 2006 of Olimpia S.p.A., prepared in accordance with IFRS consistent with the Pirelli Group, attributing the share of net equity and the results of operations to the minority interest. It should be pointed out that the forward purchase of 124,129,937 Telecom Italia S.p.A. ordinary shares, concluded by Olimpia S.p.A. in 2001, was accounted for at original cost as an increase in the investment in Telecom Italia S.p.A. with a contra-entry to the relative payable account;

- in the column “Olimpia S.p.A. consolidation entries”, the carrying amount of the Olimpia investment in the Pirelli interim financial statements was eliminated against the underlying share of the accounting net equity.

For purposes of this representation, the difference between the carrying amount of the Olimpia investment in the Pirelli interim consolidated financial statements and the underlying share of net equity (Euros 312 million for Pirelli’s share equal to 60.4 percent and Euros 516 million for the entire amount) was directly deducted from equity (with a contra-entry to the carrying amount of the Telecom Italia S.p.A. investment).

A comparison of equity and net debt between the consolidated financial statements of Pirelli & C. S.p.A. and the proforma consolidated financial data of Pirelli & C. S.p.A. at December 31, 2005 and at June 30, 2006 is presented below, assuming:

- the line-by-line consolidation of Olimpia S.p.A.;
- the line-by-line consolidation of both Olimpia S.p.A. and the Telecom Italia group.

<i>(in millions of euros)</i>	Equity		Net debt		Net debt/Equity		Equity attributable to the equity holders of Pirelli & C. S.p.A.	
	6/30/2006	12/31/2005	6/30/2006	12/31/2005	6/30/2006	12/31/2005	6/30/2006	12/31/2005
Pirelli & C. S.p.A. Group: interim consolidated data	5,715	5,614	1,575	1,177	0.28	0.21	5,342	5,205
Pirelli & C. S.p.A. Group: interim proforma consolidated data with Olimpia S.p.A. consolidated line-by-line	8,558	8,393	4,798	4,667	0.56	0.56	5,342	5,205
Pirelli & C. S.p.A. Group: interim proforma consolidated data with Olimpia S.p.A. and the Telecom Italia group consolidated line-by-line	30,927	32,029	46,113	44,525	1.49	1.39	5,342	5,205

## **CORPORATE GOVERNANCE**

A good system of Corporate Governance puts the board of directors at the center of the enterprise as the main body delegated to manage the company in the interests of the shareholders. On the basis of this system, a proper practice for disclosure of the choices and formative processes of corporate decisions must be established, along with an effective internal control system and rigorous monitoring of potential conflicts of interest. There must also be solid principles of conduct governing interactions with related parties.

As disclosed in the annual report - in a specific section and available on the corporate website, to which reference should be made - these benchmarks are firmly inscribed in the system of values Pirelli has established for the definition, preparation and adoption of codes, principles and procedures regulating corporate life. These codes, principles and procedures are periodically reviewed and, where necessary, updated to account for legislative and regulatory innovations, changes in the international best practices, and developments in the company's operations.

In this section of the interim report, disclosure is provided of the updates and the supplements made to the corporate governance system of the company in the first half of the year.

In particular, the ordinary shareholders' meeting held on April 21, 2006 elected the new board of statutory auditors.

The following were elected statutory auditors of the company for the three years 2006-2008:

- Luigi Guatri (Chairman of the Board of Statutory Auditors)
- Enrico Laghi (Standing Auditor)
- Paolo Francesco Lazzati (Standing Auditor)
- Franco Ghiringhelli (Alternate Auditor)
- Luigi Guerra (Alternate Auditor)

The members of the board of statutory auditors were elected using the slate system of voting.

In the manner established in the bylaws and in compliance with the recommendations contained in the new Self-Regulatory Code of listed companies, a single slate was presented (by the components of the Pirelli & C. Voting Trust). The list was made public by the company in the 15 days prior to the shareholders' meeting by publication of the list on the corporate website together with the curriculum vitae of the candidates running for the posts.

In accordance with the provisions of art. 148 of Legislative Decree No. 58/1998, the election of the chairman of the board of statutory auditors was passed by resolution of the shareholders' meeting of the company, since the bylaws no longer provide for the chairman of the board of the statutory auditors to be chosen from the top of the list presented by the majority shareholders. The immediate application of this new law was rendered public when the notice of the shareholders' meeting was published. The same shareholders' meeting also voted to set the gross annual compensation for each standing auditor at Euros 41,500 and the gross annual compensation for the chairman of the board of statutory auditors at Euro 62,000. It also established that the statutory auditor who is called to sit on the Oversight Committee, as set forth by Legislative Decree No. 231/01 (Paolo Francesco Lazzati), will receive additional gross annual compensation of Euros 10,000.

The shareholders were able to vote on each single point separately (election of the standing and alternate auditors, election of the chairman of the board of statutory auditors and determination of the compensation for the standing auditors).

During the first half, Carlo De Benedetti, an independent director of the company, resigned his post, indicating that he wished to relinquish all posts held as director in companies other than those of the Group he heads.

To replace him, on September 12, 2006, the board of directors appointed Alberto Bombassei, also an independent director.

The subject of transparency with regard to transactions involving the company's shares or financial instruments related thereto carried out directly or through persons by relevant parties or by persons closely connected thereto (insider dealing) is, at this time, fully regulated by Legislative Decree No. 58/1998 (art. 114) and by Consob (articles 152-sexies and subsequent articles the Regulation of Issuers). As a result, beginning from the date of April 1, 2006, the Code of Conduct relative to insider dealing adopted by the company in November 2002 is superseded.

Following the recent introduction into national law (Community Law 2004) of the so-called Market Abuse Directive, enactment of the so-called law on savings and the "new" Self-Regulatory Code of Borsa Italiana (March 2006) to which the company adheres, in light of the whole of the new law, Pirelli has set up a working group to examine and review certain governance documents, including the bylaws, the Rules of Proceeding for Shareholders' Meetings and the continuous and periodical disclosure of information to the company's governing boards. The results of these actions taken by the company with regard to the whole of the law, besides recommendations and indications formulated in the Self-Regulatory Code, will be specifically disclosed to the public inside the Annual Report on the corporate governance system which will, as usual, be included in the next annual financial statements.

### **Composition of the share capital**

At September 12, 2006, the share capital of Pirelli & C. S.p.A. is Euros 2,791,311,344.64, divided into 5,367,906,432 shares of par value Euros 0.52 each, of which 5,233,142,003 are ordinary shares and 134,764,429 are non-convertible savings shares.

The share capital may be increased up to a maximum nominal amount of Euros 2,819,508,786.64 for:

- the issuance of a maximum of 54,225,850 ordinary shares of par value Euros 0.52 each, at the price of Euros 1.15 each, of which Euros 0.63 is for the share premium, for the possible exercise of the options granted to senior and junior executives of the companies and its subsidiaries and their subsidiaries as part of the “Pirelli to People” and “Group Senior Executives” stock option plans set up by the merged company, Pirelli S.p.A., in 2001.

During the course of the first half, the Pirelli & C. ordinary share warrants 2003-2006 lapsed and are therefore without value. The warrants had been issued in execution of the resolution passed by the shareholders’ meeting held on May 7, 2003. At the end of the period to exercise the warrants (June 20, 2006), 99.84 percent of the total warrants issued had been exercised.

To the best of the company’s knowledge, no legal or natural person can exercise control pursuant to art. 93 of Legislative Decree 58/1998.

Participants in the Pirelli & C. S.p.A. Voting Trust - the purpose of which is to ensure Pirelli & C. share structure stability and uniformity in corporate management policy - along with an extract from the agreement’s text, and are available on the corporate website: [www.pirelli.com](http://www.pirelli.com).

### **Relations with investors and other shareholders**

In line with its tradition of transparency and fairness, the company actively promotes relations with shareholders, institutional investors and with financial analysts within the proper limits of their respective roles and periodically organizes meetings with representatives from the Italian and international financial communities.

Furthermore, since March 1999, the company established an Investor Relations Department to foster continuous dialogue with the financial market. The Investor Relations Department, which reports directly to Managing Director Carlo Buora, is headed by Alberto Borgia and has its own section in the corporate website at [www.pirelli.com](http://www.pirelli.com).

In this section of the website, investors can find every document of interest, in English as well as Italian, related to financial reporting (for example, the annual financial statements and the half-yearly and quarterly reports) and the company's corporate governance system (for example, the Rules of conduct for transactions with related parties, the Procedure for satisfying the requirements of Article 150.1 of Legislative Decree 58/1998, the procedure for the management and communication to the public of privileged information and the minutes of shareholders' meetings). The section also gives access to press releases issued by the company and the documentation that the company makes available to the financial community in presentations and/or meetings and information on the company's share capital and shareholders (including the publication of any shareholders' agreements).

Pirelli & C. was one of the first companies in Italy and Europe to publish specific inserts in the mass media as well as one of the first to set up a kit on its website for small investors.

Investor queries may be sent to: e-mail: [ir@pirelli.com](mailto:ir@pirelli.com); tel.: +39.0264422949; fax: +39.0264424686.

## PIRELLI & C. S.p.A. – SUMMARY DATA

### Balance sheet and financial position

	(in millions of euros)	
	6/30/2006	12/31/2005
Property, plant and equipment	105	52
Intangible assets	2	2
Financial assets	6,531	6,433
Net working capital	(442)	(391)
	<b>6,196</b>	<b>6,096</b>
Equity	4,756	4,661
Provisions	192	193
Net financial (liquidity)/debt position	1,248	1,242
	<b>6,196</b>	<b>6,096</b>

The above data presents the balance sheet and financial position of the company. The most significant changes during the first half of 2006 refer to the following:

- **property, plant and equipment** increased by Euros 53 million mainly as a result of a finance lease contract relating to a building taken over by Pirelli Tyre S.p.A. (Euros 55 million).
- **financial assets** increased by Euros 98 million partly as a result of the measurement at fair value of the available-for-sale assets (Euros 49 million) and partly due to the investments made in Capitalia S.p.A. (Euros 38 million), Mediobanca S.p.A. (Euros 14 million), Assicurazioni Generali S.p.A. (Euros 5 million) and Banca Leonardo S.p.A. (Euros 4 million). The above investments were in part offset by the sale of a 15.3 percent stake in F.C. Internazionale Milano S.p.A. (Euros 11 million) and the writedown of G.I.M. Generale Industrie Metallurgiche S.p.A. (Euros 1 million).

- **equity** increased by Euros 95 million compared to the prior year. The changes in equity are presented in the following table:

(in millions of euros)	
<b>Equity at 12/31/2005</b>	<b>4,661</b>
Dividends paid	(114)
Share capital increase for exercise of warrants	27
Income (expenses) recognized directly in equity:	
- Fair value adjustment of available-for-sale financial assets	49
- Other	1
Total income (expenses) recognized directly in equity	<b>50</b>
Income for the period	132
<b>Equity at 6/30/2006</b>	<b>4,756</b>

- the **net debt position** went from Euros 1,242 million at December 31, 2005 to Euros 1,248 million at June 30, 2006, with a net increase of Euros 6 million. A summary of the changes is detailed in the following table:

(in millions of euros)	
<b>Net debt position at 12/31/2005</b>	<b>1,242</b>
Financial investments	(61)
Investments in property, plant and equipment	(55)
Dividends collected	165
Dividends paid	(114)
Share capital increase	27
Change in net working capital	60
Other changes	(16)
<b>Net debt position at 6/30/2006</b>	<b>1,248</b>

**Income statement**

	(in millions of euros)	
	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
Financial income (expenses)	(24)	(33)
Investment income	173	175
Valuation adjustments to financial assets	(2)	(18)
Other operating income (expenses)	(16)	(2)
<b>Income before income taxes</b>	<b>131</b>	<b>122</b>
Income taxes	1	9
<b>Income for the period</b>	<b>132</b>	<b>131</b>

The income for the first half of 2006 amounts to Euros 132 million compared to Euros 131 million in the first half of 2005.

- **financial income (expenses)** compared to the first half of 2005 show an improvement of Euros 9 million. This improvement is due principally to the effect of the sale of the Energy and Telecom cables businesses to Goldman Sachs Capital Partners, concluded on July 28, 2005, and the gain realized on the sale of F.C. Internazionale Milano S.p.A. (Euros 2 million) and lower banking charges (Euros 2 million).
- The decrease in **valuation adjustments to financial assets** is basically the result of the writedown of the investment in F.C. Internazionale Milano S.p.A. effected in the first half of 2005 (Euros 15 million).
- The net expense balance of **other operating income (expenses)** is higher due to the IPO costs and the change/reduction in the services rendered following the sale of the cables activities on July 28, 2005.

The Board of Directors

Milan, September 12, 2006

**THE GROUP**  
**INTERIM CONSOLIDATED FINANCIAL STATEMENTS**  
**AND NOTES**

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<b>CONSOLIDATED BALANCE SHEET</b>		<b>6/30/2006</b>	<b>12/31/2005</b>
(in thousands of euros)			
<b>ASSETS</b>			
3	Property, plant and equipment	1,544,502	1,571,972
5	Intangible assets	505,840	476,801
6	Investments in associates and joint ventures	4,687,321	4,542,902
7	Available-for-sale financial assets	1,321,860	1,032,317
8	Deferred tax assets	66,484	77,046
10	Other receivables	721,321	529,393
	Tax receivables	20,121	18,619
4	Investment properties	-	5,140
<b>NON-CURRENT ASSETS</b>		<b>8,867,449</b>	<b>8,254,190</b>
11	Inventories	766,236	681,056
9	Trade receivables	1,059,261	943,434
10	Other receivables	202,667	272,252
12	Financial assets held for trading	127,649	179,636
13	Cash and cash equivalents	886,869	300,331
	Tax receivables	73,460	110,961
22	Financial instruments	37,641	67,061
<b>CURRENT ASSETS</b>		<b>3,153,783</b>	<b>2,554,731</b>
<b>TOTAL ASSETS</b>		<b>12,021,232</b>	<b>10,808,921</b>
<b>EQUITY</b>			
14.1	Attributable to the equity holders of the company	5,342,002	5,204,859
	Share capital	2,789,950	2,762,696
	Other reserves	2,112,950	2,010,712
	Retained earnings	286,057	104,035
	Net income for the period	153,045	327,416
14.2	Attributable to the minority interest:	372,593	408,947
	Reserves	332,495	337,413
	Net income for the period	40,098	71,534
<b>TOTAL EQUITY</b>		<b>5,714,595</b>	<b>5,613,806</b>
<b>LIABILITIES</b>			
19	Borrowings from banks and other financial institutions	1,150,093	1,550,512
21	Other payables	118,930	53,196
17	Provisions for other liabilities and charges	200,441	181,532
16	Deferred tax liabilities	46,726	49,352
18	Employee benefit obligations	423,819	510,802
	Tax payables	9,764	8,706
22	Financial instruments	4,578	2,048
<b>NON-CURRENT LIABILITIES</b>		<b>1,954,351</b>	<b>2,356,148</b>
19	Borrowings from banks and other financial institutions	2,072,255	600,362
20	Trade payables	1,072,687	1,018,264
21	Other payables	712,353	771,538
17	Provisions for other liabilities and charges	36,875	43,028
	Tax payables	131,953	111,501
22	Financial instruments	326,163	294,274
<b>CURRENT LIABILITIES</b>		<b>4,352,286</b>	<b>2,838,967</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>12,021,232</b>	<b>10,808,921</b>

## CONSOLIDATED INCOME STATEMENT

1<sup>st</sup> Half 20061<sup>st</sup> Half 2005

(in thousands of euros)

24	Revenues from sales and services	<b>2,445,883</b>	2,281,419
25	Other income	<b>137,166</b>	137,876
	Change in inventories of work in process, semifinished and finished products	<b>64,017</b>	4,118
	Raw materials and consumables used	<b>(946,768)</b>	(868,869)
26	Personnel costs	<b>(540,999)</b>	(506,962)
27	Amortization, depreciation and impairments	<b>(109,052)</b>	(106,048)
28	Other expenses	<b>(837,153)</b>	(741,951)
	Increase in property, plant and equipment from internal work	<b>3,044</b>	3,007
<b>OPERATING PROFIT</b>		<b>216,138</b>	202,590
29	Financial income	<b>210,235</b>	119,474
30	Financial expenses	<b>(247,203)</b>	(164,289)
31	Dividends	<b>43,259</b>	19,636
32	Valuation of financial assets	<b>(76,932)</b>	(57,873)
33	Share of earnings (losses) of associates and joint ventures	<b>125,114</b>	129,243
<b>INCOME BEFORE INCOME TAXES</b>		<b>270,611</b>	248,781
34	Income taxes	<b>(77,468)</b>	(71,129)
<b>INCOME FROM CONTINUING OPERATIONS</b>		<b>193,143</b>	177,652
	Income from discontinued operations	-	32,773
<b>INCOME FOR THE PERIOD</b>		<b>193,143</b>	210,425
<b>Attributable to:</b>			
	equity holders of the company	<b>153,045</b>	179,611
	minority interest	<b>40,098</b>	30,814

### 35 EARNINGS PER SHARE (euros per thousand of shares)

#### *basic earnings per share*

continuing operations	28.77	31.49
discontinued operations	-	7.05
	28.77	38.54

#### *diluted earnings per share*

continuing operations	28.77	31.33
discontinued operations	-	7.01
	28.77	38.34

## CONSOLIDATED STATEMENT OF RECOGNIZED INCOME AND EXPENSE

	(in millions of euros)	
	6/30/2006	6/30/2005
Differences on translation of foreign currency financial statements	(64)	158
Fair value adjustment of available-for-sale financial assets	49	143
Net actuarial gains (losses) on employee benefits (net of tax effects) (*)	48	
Fair value adjustment of derivatives designated as cash flow hedges (Olimpia)	28	
Gains (Losses) taken to income upon disposal of available-for-sale financial assets, or impairments	5	
<b>Income (Expenses) recognized directly in equity</b>	<b>66</b>	<b>301</b>
Income for the period	193	210
<b>Total income (expenses) recognized directly in equity</b>	<b>259</b>	<b>511</b>
<b>Attributable to:</b>		
- equity holders of the company	238	468
- minority interest	21	43

(\*) The Group has elected to adopt the option that allows it to recognize directly in equity actuarial gains (losses) on employee benefit obligations starting from September 2005 retrospectively. The effect at January 1, 2005 is included in opening equity at January 1, 2005. Therefore, at June 30, 2005, no actuarial calculations were made.

<b>CONSOLIDATED STATEMENT OF CASH FLOWS</b>		
	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
	(in thousands of euros)	
Income	193,143	177,652
Amortization, depreciation / impairment losses & reversals of intangible assets and property, plant and equipment	109,052	103,716
Financial expenses	247,203	164,289
Financial income	(210,235)	(119,474)
Dividends	(43,259)	(19,636)
Valuation of financial assets	76,932	57,873
Share of earnings (losses) of associates and joint ventures	(125,114)	(129,243)
Change in inventories	(85,180)	(2,673)
Change in trade receivables / payables	(61,404)	(41,419)
Change in other receivables / payables	50,720	(61,453)
Change in employee benefit obligations / other provisions	28,853	102,864
Other changes	7,769	13,745
<b>A Net cash flows provided by (used for) operating activities</b>	<b>188,480</b>	<b>246,241</b>
Investments in property, plant and equipment	(125,651)	(105,999)
Disposals of property, plant and equipment	10,547	11,245
Investments in intangible assets	(35,335)	(2,370)
Disposals of intangible assets	105	-
Acquisitions of investments in associates and joint ventures	(38,455)	(1,344,000)
Disposals of investments in associates and joint ventures	4	-
Acquisitions of available-for-sale financial assets	(263,470)	(145,276)
Disposals of available-for-sale financial assets	13,500	-
Dividends received	43,259	19,890
<b>B Net cash flows provided by (used for) investing activities</b>	<b>(395,496)</b>	<b>(1,566,510)</b>
Change in share capital and share premium reserve	27,254	1,059,600
Other changes in equity	(12,727)	-
Change in financial payables	1,088,629	326,266
Change in financial receivables	(109,976)	66,832
Financial income/Financial expenses	(36,968)	(44,815)
Dividends paid	(162,372)	(149,542)
<b>C Net cash flows provided by (used for) financing activities</b>	<b>793,840</b>	<b>1,258,341</b>
<b>D Total cash flows from discontinued operations</b>	<b>-</b>	<b>(269,172)</b>
<b>E Total cash flows provided by (used) during the period (A+B+C+D)</b>	<b>586,824</b>	<b>(331,100)</b>
<b>F Cash and cash equivalents, at beginning of the period</b>	<b>146,310</b>	<b>509,055</b>
<b>G Exchange differences on translation of cash and cash equivalents</b>	<b>(17,476)</b>	
<b>H Cash and cash equivalents, at end of the period (E+F+G) <sup>(°)</sup></b>	<b>715,658</b>	<b>177,955</b>
<sup>(°)</sup> of which:		
cash	886,869	217,068
bank overdrafts	(171,211)	(39,113)

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

### **1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

#### **Basis of presentation**

As set forth in article 81 of Consob Regulation No. 11971 dated May 14, 1999 and subsequent amendments introduced by Consob resolution No. 14990 dated April 14, 2005, the Pirelli & C. Group has prepared the six-months interim report at June 30, 2006 on a condensed basis in compliance with IAS 34.

The valuation and measurement of the data for the first half of 2006 are based upon IAS/IFRS in force as of today's date and on their current "interpretation" indicated in the documents issued thus far by the "International Financial Reporting Interpretations Committee - IFRIC". The IAS/IFRS in force at December 31, 2006 could be different from those used in the preparation of these interim financial statements due to the future endorsement by the European Commission of new standards, new interpretations and guidelines issued by the "International Financial Reporting Interpretations Committee". The consolidated financial statements as at December 31, 2006 could be affected by such changes.

The accounting policies adopted in the preparation of the six-months interim report on the consolidated financial statements as at June 30, 2006 are the same as those disclosed in the notes to the financial statements at December 31, 2005 except for the change in the accounting policy for investment properties described below.

For purposes of a better accounting representation and a more appropriate presentation of the transactions for a more meaningful understanding of the financial statements and comparability with the major domestic and, in particular, international operators, starting from these interim financial statements for the six months ending June 30, 2006, as permitted by IAS 40, the Group has decided to measure investment properties at fair value instead of cost, net of the relative depreciation and impairment losses.

This treatment has not resulted in any change to the prior year's retained earnings since the value of investment properties in the financial statements at December 31, 2005 approximated fair value.

The accounting policy for investment properties, as changed, is as follows:

**Investments properties**

Investment properties are defined as property held to earn rentals or for capital appreciation or both.

Investment properties are initially recognized at cost, including transaction costs, and subsequently remeasured at fair value. The changes in the fair values of investment properties are recorded in the income statement.

The fair value of an investment property reflects the market value at the balance sheet date and represents the amount at which the investment property could be exchanged between knowledgeable and willing parties in an arm's length transaction and after the outcome of adequate sales negotiations in which the parties acted knowledgeably, prudently and without obligations.

Each single property is measured and takes into consideration the future rental income and, where significant, the relative costs, discounted by applying a discount rate that reflects the risks specific to the cash flows generated by the asset.

The income or expense representing changes in the fair values of investment properties is recorded in the income statement in the year in which the change occurs.

The gain or loss on disposals of investment properties is calculated as the difference between the net proceeds and the accounting amount of the asset and is recorded in the income statement in the year of disposal.

When there is a change in use of an investment property from inventories to investment property to be recognized at fair value, the difference between the fair value at the balance sheet date and the previous accounting amount is recorded in the income statement.

When there is a change in use from investment property recognized at fair value to owner-occupied property or inventories, the fair value at the date of the change of use is considered the cost of the property under its new classification.

**Seasonal factors affecting revenues**

Revenues are not significantly affected by seasonal factors.





### **3. PROPERTY, PLANT AND EQUIPMENT**

The composition and movements in property, plant and equipment are as follows:

	(in thousands of euros)					
	6/30/2006			12/31/2005		
	Gross book amount	Accumulated Depreciation	Net carrying amount	Gross book amount	Accumulated Depreciation	Net carrying amount
Land and improvements	81,835	-	81,835	67,272	-	67,272
Buildings	621,074	(268,682)	352,392	616,589	(274,890)	341,699
Plant and machinery	2,387,973	(1,443,880)	944,093	2,421,571	(1,449,690)	971,881
Industrial and commercial equipment	499,142	(386,549)	112,593	509,673	(387,135)	122,538
Other property, plant and equipment	233,074	(179,485)	53,589	249,667	(181,085)	68,582
	<b>3,823,098</b>	<b>(2,278,596)</b>	<b>1,544,502</b>	<b>3,864,772</b>	<b>(2,292,800)</b>	<b>1,571,972</b>

	(in thousands of euros)						
	Movements in the gross book amount						
	12/31/2005	Exchange differences	Increase	Decrease	Reclassifica- tions	Other	6/30/2006
Land and improvements	67,272	(3,389)	3,698	(1,025)	4,076	11,203	81,835
Buildings	616,589	(16,193)	33,037	(2,178)	(5,045)	(5,136)	621,074
Plant and machinery	2,421,571	(94,996)	67,658	(6,579)	744	(425)	2,387,973
Industrial and commercial equipment	509,673	(20,860)	14,130	(5,921)	2,239	(119)	499,142
Other property, plant and equipment	249,667	(6,374)	7,129	(15,882)	(2,014)	548	233,074
<b>Total</b>	<b>3,864,772</b>	<b>(141,812)</b>	<b>125,652</b>	<b>(31,585)</b>	<b>-</b>	<b>6,071</b>	<b>3,823,098</b>

	(in thousands of euros)						
	Movements in accumulated depreciation						
	12/31/2005	Exchange difference	Reclassifica- tions	Decrease	Depreciation	Other	6/30/2006
Buildings	(274,890)	6,471	-	1,073	(11,252)	9,916	(268,682)
Plant and machinery	(1,449,690)	63,444	(23)	4,812	(62,244)	(179)	(1,443,880)
Industrial and commercial equipment	(387,135)	17,030	28	4,470	(21,040)	98	(386,549)
Other property, plant and equipment	(181,085)	5,086	(5)	15,641	(8,134)	(10,988)	(179,485)
	<b>(2,292,800)</b>	<b>92,031</b>	<b>-</b>	<b>25,996</b>	<b>(102,670)</b>	<b>(1,153)</b>	<b>(2,278,596)</b>

	(in thousands of euros)							
	Movements in the net carrying amount							
	12/31/2005	Exchange difference	Increase	Decrease	Reclassifica- tions	Depreciation	Other	6/30/2006
Land and improvements	67,272	(3,389)	3,698	(1,025)	4,076	-	11,203	81,835
Buildings	341,699	(9,722)	33,037	(1,105)	(5,045)	(11,252)	4,780	352,392
Plant and machinery	971,881	(31,552)	67,658	(1,767)	721	(62,244)	(604)	944,093
Industrial and commercial equipment	122,538	(3,830)	14,130	(1,451)	2,267	(21,040)	(21)	112,593
Other property, plant and equipment	68,582	(1,288)	7,129	(241)	(2,019)	(8,134)	(10,440)	53,589
	<b>1,571,972</b>	<b>(49,781)</b>	<b>125,652</b>	<b>(5,589)</b>	<b>-</b>	<b>(102,670)</b>	<b>4,918</b>	<b>1,544,502</b>

### **4. INVESTMENT PROPERTIES**

At December 31, 2005, investment properties included a former industrial structure called the “Bicocca Hangar” which was owned by Lambda S.r.l.. Following its sale in 2006 to Pirelli & C. Real Estate S.p.A. and the change in use, the hangar has been reclassified to property, plant and equipment under land and buildings.

## **5. INTANGIBLE ASSETS**

The composition and movements in intangible assets are as follows:

	(in thousands of euros)						
	12/31/2005	Exchange differences	Increase	Decrease	Amortization	Other	6/30/2006
Patents and intellectual property rights	992	-	-	-	(135)	20	877
Concessions, licenses and trademarks	21,330	-	4,193	(64)	(992)	-	24,467
Goodwill	440,568	(84)	29,948	-	-	-	470,432
Software	12,437	(21)	1,172	(18)	(4,036)	(184)	9,350
Other intangible assets	1,474	(19)	22	(216)	(219)	(328)	714
	<b>476,801</b>	<b>(124)</b>	<b>35,335</b>	<b>(298)</b>	<b>(5,382)</b>	<b>(492)</b>	<b>505,840</b>

The increase in “Goodwill” mainly refers to the following transactions in the real estate segment:

- purchase from the minority shareholder of Pirelli & C. Real Estate Società di Gestione del Risparmio S.p.A. of the shares held as a result of the sale option exercised by the latter. The price was established on the basis of a global valuation of the company, equal to approximately Euros 315 million, made by Credit Suisse;
- purchase from Bank Pekao S.A. of 75 percent of Pekao Development Sp.zo.o., now Pirelli Pekao Real Estate Sp.zo.o., one of the major real estate operators on the Polish market employing about 40 staff and managing several residential development projects in the city of Warsaw.

## **6. INVESTMENTS IN ASSOCIATES AND JOINT VENTURES**

Investments in associates and joint ventures total Euros 4,687,321 thousand compared to Euros 4,542,902 thousand at December 31, 2005.

Movements during the period are as follows:

	(in thousands of euros)
	<b>6/30/2006</b>
Beginning amount	4,542,902
Acquisition/change in share capital and reserves	65,927
Distribution of dividends	(43,222)
Share of earnings (losses)	125,114
Reclassification	(1,206)
Other	(2,194)
	<b>4,687,321</b>

The following table details the movements in investments in associates:

	(in thousands of euros)						
	12/31/2005	Acquisitions/ changes in share capital and reserves	Distribution of dividends	Share of earnings (losses)	Reclassifications	Other	6/30/2006
Dixia S.r.l.	5.822	16	-	(16)	-	-	5.822
Orione Immobiliare Prima S.p.A.	12.946	-	(11.435)	(755)	-	-	756
Turismo e Immobiliare S.p.A.	4.061	121	-	(269)	-	-	3.913
Stip Tunisi	1.206	-	-	-	(1.206)	-	-
SMP Melfi S.r.l.	1.807	-	-	-	-	(1.807)	-
Eurostazioni S.p.A.	53.861	-	(1.570)	1.072	-	(924)	52.439
Other	3.232	73	(1.964)	434	-	172	1.947
<b>Total investments in associates</b>	<b>82.935</b>	<b>210</b>	<b>(14.969)</b>	<b>466</b>	<b>(1.206)</b>	<b>(2.559)</b>	<b>64.877</b>

The following table details the movements in investments in joint ventures:

	(in thousands of euros)						
	12/31/2005	Acquisitions/ share capital and reserves	Distribution of dividends	Share of earnings (losses)	Reclassifications	Other	6/30/2006
Afrodite S.à r.l.	923	(60)	-	357	-	-	1.220
Alceo B.V.	621	-	-	(929)	-	308	-
Alnitak S. à r.l.	-	1.693	-	17	-	-	1.710
Altair Zander Italia S.r.l.	61	-	-	14	-	-	75
Aree Urbane S.r.l.	8.167	17	-	(408)	-	-	7.776
Artemide S.à r.l.	714	(78)	-	193	-	-	829
Bernini Immobiliare S.r.l.	1.323	(570)	(472)	(281)	-	-	-
Capitol Immobiliare S.r.l.	3	-	-	(60)	-	57	-
Castello S.r.l.	43	-	-	130	-	-	173
Colombo S.a.r.l.	1.347	541	-	1.375	-	-	3.263
Consorzio G6 Advisor	22	-	-	-	-	-	22
Continuum S.r.l.	6.226	-	(2.702)	1.035	-	-	4.559
Credit Servicing S.p.A.	9.001	13	(1.895)	(675)	-	-	6.444
Domogest S.r.l.	908	-	-	121	-	-	1.029
Doria S.a.r.l.	1.357	546	-	1.350	-	-	3.253
Elle Dieci S.c.a.r.l.	40	-	-	-	-	-	40
Elle Tre S.c.a.r.l.	40	-	-	-	-	-	40
Erice S.r.l.	1.053	-	-	121	-	-	1.174
Espelha - Serviços de Consultadoria Lda.	-	35.081	-	1.261	-	-	36.342
Fattoria Medicea S.r.l.	-	541	-	(12)	-	-	529
Galatea S.r.l.	-	348	-	(1)	-	-	347
Geolidro S.r.l.	10.497	(10.350)	-	(167)	-	-	-
Immobiliare Prizia S.r.l.	4.178	(19)	-	164	-	-	4.323
IN Holdings I S.a.r.l.	2.184	-	-	64	-	-	2.248
Induxia S.r.l.	2.307	-	-	(58)	-	-	2.249
Inimm Due S.a.r.l.	2.192	-	-	125	-	-	2.317
Iniziative Immobiliari S.r.l.	14.188	-	(8.409)	(184)	-	-	5.595
Localto S.p.A.	615	536	-	149	-	-	1.300
Localto ReoCo S.r.l.	-	4	-	-	-	-	4
LSF Italian Finance Company S.r.l.	5	-	-	-	-	-	5
Masaccio S.r.l.	-	196	-	(1)	-	-	195
Masseto I B.V.	23.163	-	-	5.731	-	-	28.894
Max B.V.	692	(1)	-	(165)	-	-	526
M.S.M.C. Italy Holding B.V.	17.533	52	(8.175)	5.215	-	-	14.625
Mirandia- Trading e Consultoria Lda	41.607	-	-	1.006	-	-	42.613
MP Facility S.r.l.	2.062	-	(890)	(486)	-	-	686
MSPRE Luxembourg S.à r.l.	898	(979)	-	81	-	-	-
Nivola S.r.l.	-	-	-	-	-	-	-
Progetto Bicocca La Piazza S.r.l.	557	-	-	(201)	-	-	356
Popoy Holding B.V.	15.489	-	-	2.450	-	-	17.939
Progetto Gioberti S.r.l.	42	-	-	5	-	-	47
Quadrifoglio Milano S.p.A.	5.509	69	-	(180)	-	-	5.398
Resident Berlin P&K 1 GmbH	-	758	-	-	-	-	758
Rinascente/Upim S.r.l.	9.819	-	-	(5.234)	-	-	4.585
Riva dei Ronchi S.r.l.	766	26	-	(30)	-	-	762
Solaris S.r.l.	9.463	-	(5.391)	434	-	-	4.506
Spazio Industriale B.V.	1.936	-	(113)	92	-	-	1.915
Spazio Industriale II B.V.	3.674	6.060	(206)	33.312	-	-	42.840
Tamerice Immobiliare S.r.l.	3.475	(64)	-	7.060	-	-	10.471
Tizian Wohnen 1 GmbH	12	1.948	-	5	-	-	1.965
Tizian Wohnen 2 GmbH	12	568	-	67	-	-	647
Trinoro S.à r.l.	-	11	-	(1)	-	-	10
Trixia S.r.l.	2.359	-	-	(563)	-	-	1.796
Tronador - Consultoria Economica Lda	3.593	-	-	(244)	-	-	3.349
Vespucci S.a.r.l.	1.347	540	-	1.375	-	-	3.262
Olimpia S.p.A.	4.247.944	28.270	-	71.219	-	-	4.347.433
<b>Total investments in joint ventures</b>	<b>4.459.967</b>	<b>65.717</b>	<b>(28.253)</b>	<b>124.648</b>	<b>-</b>	<b>365</b>	<b>4.622.444</b>
<b>TOTAL INVESTMENTS IN ASSOCIATES AND JOINT VENTURES</b>	<b>4.542.902</b>	<b>65.927</b>	<b>(43.222)</b>	<b>125.114</b>	<b>(1.206)</b>	<b>(2.194)</b>	<b>4.687.321</b>

“Acquisitions/changes in share capital and reserves”, equal to Euros 65,927 thousand, principally includes:

- Euros 35,081 thousand relating to the purchase of a 49 percent interest in the company Espelha - Serviços de Consultadoria Lda., for Euros 3 thousand, and the subsequent payment against a capital increase for Euros 35,069 thousand;
- Euros 28,270 thousand, relating almost entirely to the income on the changes in the fair value of the outstanding interest rate swaps in the Olimpia S.p.A. joint venture, which met the criteria for hedge accounting, and which transited directly from equity.

As for the share of earnings (losses), reference should be made to the comments in the note “share of earnings (losses) of associates and joint ventures” in the income statement.

## **7. AVAILABLE-FOR-SALE FINANCIAL ASSETS**

Available-for-sale financial assets amount to Euros 1,321,860 thousand compared to Euros 1,032,317 thousand at December 31, 2005.

Movements during the period are as follows:

	(in thousands of euros)
	<b>6/30/2006</b>
Beginning amount	1,032,317
Increase	263,470
Decrease	(28,031)
Impairments	(1,880)
Gains (Losses) taken to income upon disposal of available-for-sale financial assets, or impairments, previously recorded in equity	5,058
Fair value adjustment gains (losses) recognized in equity	48,979
Reclassifications	1,206
Other	741
	<b>1,321,860</b>

The increase is principally due to the purchase of Telecom Italia S.p.A. shares (Euros 201,233 thousand), Assicurazioni Generali S.p.A. shares (Euros 4,567 thousand), Capitalia S.p.A. shares (Euros 38,219 thousand), Mediobanca S.p.A. shares (Euros 13,545 thousand) and Banca Leonardo S.p.A. shares (Euros 4,598 thousand).

The decrease refers mainly to the sale of F.C. Internazionale Milano S.p.A. shares (Euros 10,997 thousand) and Equinox shares (Euros 7,944 thousand).

## **8. DEFERRED TAX ASSETS**

Deferred tax assets amount to Euros 66,484 thousand compared to Euros 77,046 thousand at December 31, 2005.

## **9. TRADE RECEIVABLES**

Trade receivables are analyzed as follows:

	(in thousands of euros)					
	<b>June 30, 2006</b>			<b>December 31, 2005</b>		
	<b>Total</b>	<b>Non-current</b>	<b>Current</b>	<b>Total</b>	<b>Non-current</b>	<b>Current</b>
Associates and joint ventures	88,666	-	88,666	133,608	-	133,608
Third parties	964,429	-	964,429	804,492	-	804,492
Receivables on construction contracts	6,166	-	6,166	5,334	-	5,334
	<b>1,059,261</b>	<b>-</b>	<b>1,059,261</b>	<b>943,434</b>	<b>-</b>	<b>943,434</b>

## **10. OTHER RECEIVABLES**

Other receivables can be analyzed as follows:

(in thousands of euros)

	June 30, 2006			December 31, 2005		
	Total	Non-current	Current	Total	Non-current	Current
Associates and Joint Ventures						
- financial receivables	323,411	322,498	913	262,497	262,187	310
- other receivables	18,522	15	18,507	1,015	-	1,015
financial receivables from others	315,549	249,801	65,748	232,860	206,254	26,606
prepaid expenses	19,233	434	18,799	17,069	250	16,819
expenses	16,867	12,491	4,376	14,845	6,176	8,669
rights not called up	32	-	32	-	-	-
receivables from employees	7,110	2,522	4,588	5,241	2,308	2,933
agencies	3,673	-	3,673	2,554	-	2,554
receivables for junior notes	97,252	97,252	-	16,669	16,669	-
other receivables	122,339	36,308	86,031	248,895	35,549	213,346
	<b>923,988</b>	<b>721,321</b>	<b>202,667</b>	<b>801,645</b>	<b>529,393</b>	<b>272,252</b>

Non-current financial receivables from associates and joint ventures, equal to Euros 322,498 thousand, are almost entirely held by the Pirelli & C. Real Estate group, and are classified as non-current since the collection times, connected to the plans for the disposal of properties held directly and indirectly by the companies, will be concluded over a period of between two and five years.

Non-current financial receivables from others principally include a fixed-rate vendor loan for an amount of Euros 135,000 thousand maturing on January 28, 2016 granted to Prysmian (Lux) S.à.r.l. under the agreement reached on July 28, 2005 between Pirelli and Goldman Sachs Capital Partners regarding the sale of the Pirelli Energy and Telecom Cables and Systems businesses.

The increase in “receivables for junior notes” is due to the purchase of Class E and DPP junior notes by Pirelli & C. Real Estate S.p.A. in June 2006 for Euros 80,000 thousand. The junior notes refer to a non-performing loan portfolio of the former Banco di Sicilia which is mainly composed of receivables for loans guaranteed by properties with the remaining part by unsecured receivables.

## **11. INVENTORIES**

Inventories may be analyzed as follows:

	(in thousands of euros)	
	<b>6/30/2006</b>	<b>12/31/2005</b>
Tyres Sector	553,678	546,287
Real Estate	202,373	128,768
Other	10,185	6,001
	<b>766,236</b>	<b>681,056</b>

	(in thousands of euros)	
	<b>6/30/2006</b>	<b>12/31/2005</b>
Raw materials, auxiliaries and consumables	192,846	161,812
Sundry materials	3,146	4,086
Work in process and semifinished products	154,310	94,686
Finished products	167,291	172,581
Merchandise purchased for resale	206,209	201,420
Land to be developed	29,765	22,102
Advances	12,669	24,369
	<b>766,236</b>	<b>681,056</b>

## **12. FINANCIAL ASSETS HELD FOR TRADING**

These refer to securities, mainly bonds issued and guaranteed by governments and banking institutions, classified as held for trading. The positions are held at leading banks.

## **13. CASH AND CASH EQUIVALENTS**

	(in thousands of euros)	
	<b>6/30/2006</b>	<b>12/31/2005</b>
Bank and postal deposits	884,091	297,916
Cash on hand	2,778	2,415
	<b>886,869</b>	<b>300,331</b>

## 14. EQUITY

The changes in equity are detailed below:

	attributable to the equity holders of the company						Total attributable to parent company shareholders	Minority interest	Total
	Share capital	Share premium reserve	Legal reserve	Reserve for translation differences	Reserve for fair value adjustment of AFS assets	Other reserves / Retained earnings			
(in millions of euros)									
<b>Balance at January 1, 2005</b>	<b>1,799</b>	<b>500</b>	<b>75</b>	<b>24</b>	<b>0</b>	<b>1,241</b>	<b>3,639</b>	<b>339</b>	<b>3,978</b>
Total recognized income and expenses in equity				146	143		289	12	301
Income for the first half						179	179	31	210
Appropriation of income as per resolution of 4/28/2005:									
- Legal reserve			7			(7)	-		-
- dividend payment						(113)	(113)		(113)
Other dividends paid to third parties								(35)	(35)
Exercise of warrants 2003-2006	175					(174)	1		1
Pirelli & C. share capital increase	789	259					1,048		1,048
PRE stock options exercised in the period							-	11	11
Other						2	2	2	4
<b>Balance at June 30, 2005</b>	<b>2,763</b>	<b>759</b>	<b>82</b>	<b>170</b>	<b>143</b>	<b>1,128</b>	<b>5,045</b>	<b>360</b>	<b>5,405</b>
Total recognized income and expenses in equity				28	(37)	19	10	(6)	4
Income for the second half						148	148	41	189
Other dividends paid to third parties								(1)	(1)
PRE stock options exercised in the period							-	(3)	(3)
Yanzhou Evolution Tyre CO Ltd Consolidation							-	21	21
Other						2	2	(3)	(1)
							-	-	-
<b>Balance at December 31, 2005</b>	<b>2,763</b>	<b>759</b>	<b>82</b>	<b>198</b>	<b>106</b>	<b>1,297</b>	<b>5,205</b>	<b>409</b>	<b>5,614</b>
Total recognized income and expenses in equity				(45)	54	76	85	(19)	66
Income for the first half						153	153	40	193
Appropriation of income as per resolution of 4/21/2006:									
- Legal reserve			7			(7)	-		-
- dividend payment						(114)	(114)		(114)
Other dividends paid to third parties								(49)	(49)
Exercise of warrants 2003-2006	27						27		27
Movements in Pirelli & C. Real Estate S.p.A. treasury shares						(14)	(14)	(11)	(25)
PRE stock options exercised in the period							-	12	12
Acquisition of interests from third parties							-	(8)	(8)
Other							-	(1)	(1)
							-	-	-
<b>Balance at June 30, 2006</b>	<b>2,790</b>	<b>759</b>	<b>89</b>	<b>153</b>	<b>160</b>	<b>1,391</b>	<b>5,342</b>	<b>373</b>	<b>5,715</b>

## **14.1 ATTRIBUTABLE TO THE EQUITY HOLDERS OF THE COMPANY**

**Share capital** amounts to Euros 2,789,950 thousand at June 30, 2006 and consists of 5,230,524,503 ordinary shares and 134,764,429 savings shares, all with a par value of Euros 0.52 per share and normal dividend rights.

The changes in share capital are detailed below:

	Number of ordinary shares (thousands)(*)	Number of savings shares (thousands)	Ordinary shares (€ thousands)	Savings shares (€ thousands)	Total (€ thousands)
<b>Balance at December 31, 2005</b>	<b>5,178,112</b>	<b>134,764</b>	<b>2,692,619</b>	<b>70,077</b>	<b>2,762,696</b>
Exercise of warrants	52,412		27,254		27,254
<b>Balance at June 30, 2006</b>	<b>5,230,524</b>	<b>134,764</b>	<b>2,719,873</b>	<b>70,077</b>	<b>2,789,950</b>

(\*) Net of 2,617,500 treasury shares in portfolio

The date to exercise the warrants expired on June 20, 2006. The number of unexercised warrants was 2,452,150.

## **14.2 ATTRIBUTABLE TO THE MINORITY INTEREST**

The minority interest in equity went from Euros 408,947 thousand at December 31, 2005 to Euros 372,593 thousand at June 30, 2006. The change is mainly due to the combined effect of the income for the first half of 2006, the payment of last year's dividends and the impact of the translation of foreign currency financial statements to euros.

The major percentages of investments held by minority interests are as follows:

	6/30/2006	12/31/2005
Shared Service Center s.c.a r.l. (Italy)	50.00%	50.00%
Celikord A.S. (Turkey)	49.00%	49.00%
Pirelli & C. Ambiente S.p.A. (ex-Pirelli & C. Ambiente Holding S.p.A.)	49.00%	49.00%
Pirelli & C. Real Estate S.p.A. (Italy)	46.86%	46.74%
Pirelli Tyre Co. Ltd (ex-Yanzhou Evolution Tyre CO. Ltd)	40.00%	40.00%
Turk Pirelli Lastikleri A.S. (Turkey)	34.41%	36.94%
S.C. Cord Romania S.R.L (Romania)	20.00%	20.00%
Alexandria Tire Co. S.A.E. (Egypt)	10.90%	13.19%
Pirelli de Venezuela C.A. (Venezuela)	3.78%	3.78%

## **15. STOCK OPTION PLANS**

During the period ended June 30, 2006, the company did not introduce any stock option plans.

Pirelli & C. S.p.A. has two existing stock option plans for the senior executives and staff of Pirelli & C. S.p.A. and other companies in the Group which were granted option rights, not transferable to third parties, for the subscription/purchase of Pirelli & C. S.p.A. ordinary shares.

IFRS 2 “Share-based Payment” has not been applied to these plans since the options were granted before November 7, 2002.

The following disclosure is provided on the above plans called *Pirelli to People* and *Group Senior Executives*.

	<i>Pirelli to People</i>	<i>Group Senior Executives</i>
<b>Features of the plan</b>	Option rights granted, non-transferable to third parties, for the subscription of future new issues of Pirelli & C. ordinary shares or, as decided by the latter, for the purchase of treasury shares of Pirelli & C.	Option rights granted, non-transferable to third parties, for the subscription of future new issues of Pirelli & C. ordinary shares or, as decided by the latter, for the purchase of treasury shares of Pirelli & C.
<b>Recipients at June 30, 2006</b>	288 employees (senior executives, cadres, key employees) of the companies of the Group. Originally 725 persons at the date of approval of the plan.	29 senior executives of the companies of the Group. Originally 51 persons at the date of approval of the plan.
<b>Conditions for exercising options</b>	Continuance of employment.	(a) continuance of employment, and (b) the reaching, in the two-year period 2001-2002, of specific targets, assigned to each recipient.
<b>Subscription/purchase price per share</b>	Each option right granted gives the right to subscribe/purchase one Pirelli & C. ordinary share at the price of Euros 1.150 <sup>(1)</sup> .	Each option right granted gives the right to subscribe/purchase one Pirelli & C. ordinary share at the price of Euros 1.150 <sup>(1)</sup> .
<b>Vesting period of options</b>	Up to nine years from the date the options are granted (which took place on November 5, 2001), but not before one year has passed from that date for 50 percent of the options granted, two years for another 25 percent and three years for the remaining 25 percent.	As regards the options granted on November 5, 2001, up to nine years from the date the options are granted, but not before one year has passed from that date for 50 percent of the options, two years for another 25 percent and three years for the remaining 25 percent. For the options granted definitively on May 10, 2002, up to May 31, 2009 but not before June 1, 2002 for 50 percent of the options and not before January 1, 2003 for the remaining 50 percent.
<b>Maximum number of options for which the offer was open at December 31, 2005</b>	21,693,205 options equal to about 0.4 percent of outstanding ordinary shares destined for 309 recipients.	13,986,882 options equal to about 0.27 percent of outstanding ordinary shares destined for 31 recipients.
<b>Maximum number of options for which the offer was open at June 30, 2006</b>	20,712,670 options equal to about 0.38 percent of outstanding ordinary shares destined for 288 recipients.	13,730,882 options equal to about 0.26 percent of outstanding ordinary shares destined for 29 recipients.
<b>Options forfeit during the first half of 2006 as a result of persons leaving the Group</b>	980,535	256,000
<b>Shares issued during the period</b>	None	None

<sup>(1)</sup> This amount was changed (from Euros 1.284) on the basis of the adjustment factor established by AIAF on February 7, 2005 following the capital increase voted by the extraordinary shareholders' meeting held on January 21, 2005, in accordance with the Regulations of those Stock Option Plans in the event of transactions involving share capital.

With regard to the autonomous stock option plans put into place by Pirelli & C. Real Estate S.p.A., a listed subsidiary of Pirelli & C. S.p.A., and by its subsidiaries, reference should be made to the specific disclosure by that company.

## **16. DEFERRED TAX LIABILITIES**

Deferred tax liabilities amount to Euros 46,726 thousand compared to Euros 49,352 thousand at December 31, 2005.

## **17. PROVISIONS FOR OTHER LIABILITIES AND CHARGES**

The movements during the period in provisions for other liabilities and charges is presented in the following table:

<i>(in thousands of euros)</i>	
<b>Provisions for other liabilities and charges - non-current</b>	
<b>Beginning balance at December 31, 2005</b>	<b>181,532</b>
Exchange differences	289
Increase	16,066
Utilization	(1,808)
Excess amount released	-
Other	4,362
<b>Ending balance at June 30, 2006</b>	<b>200,441</b>

<i>(in thousands of euros)</i>	
<b>Provisions for other liabilities and charges - current</b>	
<b>Beginning balance at December 31, 2005</b>	<b>43,028</b>
Exchange differences	(579)
Increase	1,319
Utilization	(11,279)
Excess amount released	-
Other	4,386
<b>Ending balance at June 30, 2006</b>	<b>36,875</b>

These provisions mainly consist of accruals for litigation, industrial risks and claims, product warranties and other contingencies.

## **18. EMPLOYEE BENEFIT OBLIGATIONS**

These include:

	(in thousands of euros)	
	6/30/2006	12/31/2005
Pension funds:		
- funded	172,553	236,536
- unfunded	98,679	104,889
Employees' leaving indemnity	88,762	100,099
Medical care plans	29,493	33,386
Other benefits	34,332	35,892
	<b>423,819</b>	<b>510,802</b>

### **Pension funds**

The composition of pension funds, at June 30, 2006, is as follows:

	(in thousands of euros)				
					6/30/2006
	Germany	Total unfunded pension funds	USA	UK	Total funded pension funds
<b>Funded</b>					
Present value of funded obligations			147,869	878,554	1,026,423
Fair value of plan assets			(109,338)	(744,532)	(853,870)
<b>Unfunded</b>					
Present value of unfunded obligations	98,679	98,679			
<b>Net liability in the balance sheet</b>	<b>98,679</b>	<b>98,679</b>	<b>38,531</b>	<b>134,022</b>	<b>172,553</b>

The composition of pension funds, at December 31, 2005, was as follows:

(in thousands of euros)					
<b>6/30/2006</b>					
	Germany	Total unfunded pension funds	USA	UK	Total funded pension funds
<b>Funded</b>					
Present value of funded obligations			169,606	924,787	1,094,393
Fair value of plan assets			(117,610)	(740,247)	(857,857)
<b>Unfunded</b>					
Present value of unfunded obligations	104,889	104,889			
<b>Net liability in the balance sheet</b>	<b>104,889</b>	<b>104,889</b>	51,996	184,540	<b>236,536</b>

The amounts recognized in the income statement relating to pension funds are as follows:

(in thousands of euros)		
	<b>6/30/2006</b>	<b>6/30/2005</b>
Current service costs	2,336	5,600
Interest cost	28,090	27,593
Expected return on plan assets	(29,130)	(27,350)
	<b>1,296</b>	<b>5,843</b>

### Medical care plans

The composition of medical care plans is as follows:

(in thousands of euros)	
	<b>USA</b>
Liability in the balance sheet at June 30, 2006	29,493
Liability in the balance sheet at December 31, 2005	33,386

The amounts recognized in the income statement relating to medical care plans are as follows:

	(in thousands of euros)	
	6/30/2006	6/30/2005
Current service cost	4	19
Interest cost	810	424
	<b>814</b>	<b>443</b>

### **Other information**

The change in actuarial gains (losses) recognized in equity compared to December 31, 2005 is as follows:

	(in thousands of euros)
<b>Cumulative amount at 12/31/2005</b>	<b>(116,469)</b>
Exchange differences	1,978
1st half 2006	56,042
<b>Cumulative amount at 6/31/2006</b>	<b>(58,449)</b>

The breakdown by country is as follows:

	(in thousands of euros)				
					<b>cumulative at 6/30/2006</b>
	Italy	Germany	USA	UK	<b>Total</b>
Pension funds		(2,479)	(11,525)	(58,068)	<b>(72,073)</b>
Medical care plans			(2,116)		<b>(2,116)</b>
Employees' leaving indemnity	15,740				<b>15,740</b>
<b>Total actuarial gains/(losses) recognized in equity</b>	<b>15,740</b>	<b>(2,479)</b>	<b>(13,641)</b>	<b>(58,068)</b>	<b>(58,449)</b>

The main actuarial assumptions used to determine the net liabilities in the interim financial statements at June 30, 2006 are as follows:

	<b>Italy</b>	<b>Germany</b>	<b>UK</b>	<b>USA</b>
Discount rate	4.75%	4.75%	5.25%	6.25%
Inflation rate	2.0%	2.0%	2.75%	
Expected remuneration increase rate		2.50%	2.75%	

The main actuarial assumptions used at December 31, 2005 to determine the net liabilities in the financial statements and the estimated cost for the year 2006 are as follows:

	<b>Italy</b>	<b>Germany</b>	<b>UK</b>	<b>USA</b>
Discount rate	4.0%	4.25%	4.75%	5.50%
Inflation rate	2.0%	2.0%	2.50%	
Expected return on plan assets			6.85%	7.0%
Expected remuneration increase rate	3.2%	2.50%	2.50%	
Medical care cost trend rate - initial				9.5%
Medical care cost trend rate - final				4.5%

## **19. BORROWINGS FROM BANKS AND OTHER FINANCIAL INSTITUTIONS**

The analysis of borrowings from banks and other financial institutions is as follows:

	(in thousands of euros)					
	6/30/2006			12/31/2005		
	Total	Non-current	Current	Total	Non-current	Current
associates and joint ventures	27	-	27	-	-	-
bonds	1,150,000	650,000	500,000	1,150,000	1,150,000	-
borrowings from banks	1,936,701	430,935	1,505,766	836,109	311,999	524,110
borrowings from other financial institutions	55,548	32,885	22,663	78,553	50,468	28,085
finance lease payables	39,497	36,273	3,224	41,653	38,045	3,608
financial accrued liabilities and deferred income	40,575	-	40,575	44,559	-	44,559
	<b>3,222,348</b>	<b>1,150,093</b>	<b>2,072,255</b>	<b>2,150,874</b>	<b>1,550,512</b>	<b>600,362</b>

Borrowings from banks include a part of the put options on Olimpia S.p.A., held by shareholder banks. Such options imply that the economic benefits relating to ownership of the investment in Olimpia are, for the predominant part, transferred immediately to Pirelli. This has entailed an increase of the investment in Olimpia S.p.A. with a contra-entry to the liability inclusive of the derivative for an amount equal to Euros 130,000 thousand.

Bonds refer to Pirelli & C. S.p.A. 1998-2008 bonds of Euros 500,000 thousand, issued on October 21, 1998, paying interest at 4.875 percent and repayable in a one-off payment on October 21, 2008. The caption also includes bonds of Euros 500,000 thousand issued in 2002 by the subsidiary Pirelli Finance (Luxembourg) S.A., paying interest at a fixed rate of 6.5 percent, maturing on April 4, 2007, and bonds of Euros 150,000 thousand issued by Pirelli & C. S.p.A. in 1999, paying interest at 5.125 percent, maturing on April 7, 2009.

## **20. TRADE PAYABLES**

The analysis of trade payables is as follows:

	(in thousands of euros)					
	6/30/2006			12/31/2005		
	Total	Non-current	Current	Total	Non-current	Current
associates and joint ventures	10,263	-	10,263	11,390	-	11,390
others	941,804	-	941,804	902,476	-	902,476
notes payable	120,620	-	120,620	104,398	-	104,398
	<b>1,072,687</b>	<b>-</b>	<b>1,072,687</b>	<b>1,018,264</b>	<b>-</b>	<b>1,018,264</b>

## **21. OTHER PAYABLES**

The analysis of other payables is as follows:

	(in thousands of euros)					
	6/30/2006			12/31/2005		
	Total	Non-current	Current	Total	Non-current	Current
associates and joint ventures	632	-	632	315	-	315
trade and other accrued liabilities and deferred income	150,624	8,245	142,379	147,564	10,955	136,609
payables to employees	129,944	9	129,935	120,258	50	120,208
payables to social security agencies	28,313	1,774	26,539	38,977	1,481	37,496
payables for stock options	9,772	-	9,772	11,743	-	11,743
dividends payable	901	-	901	905	-	905
advances from customers	4,637	-	4,637	4,410	29	4,381
other payables	506,460	108,902	397,558	500,562	40,681	459,881
	<b>831,283</b>	<b>118,930</b>	<b>712,353</b>	<b>824,734</b>	<b>53,196</b>	<b>771,538</b>

“Other payables” mainly include the accrual for the risks associated with the right granted to Hopa under the shareholders’ agreements (Euros 165,925 thousand), the payables originating from the purchase, on the part of CFT Finanziaria S.p.A., of the non-performing loan portfolio of Banca Popolare di Intra (which will later become part of a securitization transaction) for an amount, net of advances paid, of Euros 23,310 thousand, and Euros 79,000 thousand relating to the purchase of Class E and DPP junior notes relating to a portfolio of non-performing loans of the former Banco di Sicilia purchased by Pirelli & C. Real Estate S.p.A..

## **22. FINANCIAL INSTRUMENTS**

Financial instruments can be analyzed as follows:

	(in thousands of euros)			
	6/30/2006		12/31/2005	
	<u>Assets</u>	<u>Liabilities</u>	<u>Assets</u>	<u>Liabilities</u>
Non-current financial instruments	-	4,578	-	2,048
Current financial instruments	37,641	326,163	67,061	294,274

Current financial instruments at June 30, 2006 mainly include:

**Assets:**

- measurement at fair value of forward currency purchases and sales in place at June 30, 2006 for Euros 34,666 thousand. These are derivative transactions which, although used for hedging purposes, are not designated as such under IAS/IFRS. The fair value is determined by using the forward exchange rate at the balance sheet date.

**Liabilities:**

- measurement at fair value of forward currency purchases and sales in place at June 30, 2006 (Euros 55,878 thousand current and Euros 4,578 thousand non-current). These are derivative transactions which, although used for hedging purposes, are not designated as such under IAS/IFRS. The fair value is determined by using the forward exchange rate at the balance sheet date;
- measurement at fair value of the put option granted to the shareholder banks of Olimpia under the shareholders' agreements (Euros 233,000 thousand);
- measurement at fair value of the options on asset swaps on Telecom Italia S.p.A. shares/convertible bonds held by the subsidiary Pirelli Finance (Luxembourg) S.A. (Euros 38,977 thousand).

## **23. COMMITMENTS AND CONTINGENCIES**

### **Personal guarantees**

#### *Sureties*

Pirelli & C. Real Estate S.p.A. provided sureties to guarantee loans made by credit institutions to associates and joint ventures for a total of Euros 55,390 thousand consisting of the shares of the associates and joint ventures pledged for an amount of Euros 49,232 thousand.

Banking institutions and insurance companies provided sundry sureties to fulfill contractual obligations of the Pirelli & C. Real Estate S.p.A. Group for a total of Euros 273,480 thousand.

#### *Other guarantees*

Other guarantees refer to the following guarantees provided by companies of the Pirelli & C. Real Estate S.p.A. Group:

- income guarantees provided to third parties on the sale of buildings for commercial use for Euros 3,584 thousand;
- guarantees connected with the successful outcome of the contribution of certain properties by the Telecom Italia Group to the closed-end funds of Pirelli RE – Raissa Fondo Comune di Investimento Immobiliare and to the closed-end speculative fund Spazio Industriale Fondo Comune di Investimento Immobiliare Speculativo for a maximum total of Euros 795 thousand;
- guarantees in connection with the purchase of a properties portfolio in Austria from the Allianz Group provided to ECO Business Immobilien AG and Conwert Immobilien Invest AG, both shareholders with a 33.33 percent stake each in the initiative, for a total estimated amount of Euros 20,875 thousand.

In addition, Pirelli & C. Real Estate S.p.A. has a commitment to cover its proportionate share of any negative difference between the flows from rental income and interest expense due to the lender banks by Tiglio I S.r.l. and Tiglio II S.r.l. on their credit lines expiring in 2009. At the moment, on the basis of available information, the projected revenue flows are higher than the estimated interest expense.

### **Commitments for purchases of properties**

Commitments for the purchase of properties refer to the commitment to purchase certain buildings that were not sold by Imser 60 S.r.l., for a maximum amount of Euros 320,000 thousand. The purchase price of these buildings is established by contract at about 20 percent of their market value. This option may be exercised by the counterpart up to May 31, 2022.

Furthermore, the Pirelli & C. Real Estate Group signed commitments for the purchase of certain buildings located in Berlin for an amount of Euros 68,100 thousand and an area located in Danzig (Poland) for a remaining amount of Euros 3,613 thousand.

### **Commitments for purchases of investments / shares of funds**

During the first half, the call option was exercised to repurchase the stake held by Simest S.p.A. in the subsidiary Alexandria Tire Co. (Egypt), for Euros 3,512 thousand.

*Sales options held by third parties*

These commitments principally refer to:

- Euros 5,693 thousand for the prorata purchase commitment undertaken by Pirelli & C. Real Estate S.p.A. in favor of Cordusio Immobiliare S.r.l. in respect of the option to sell the shares held by the latter in Lamaione S.r.l. to the companies Aida S.r.l. and M.S.M.C. Immobiliare 4 S.r.l.;
- Euros 22,500 thousand for the purchase commitment undertaken by Pirelli & C. Real Estate S.p.A. in respect of the option to sell, exercisable starting from January 1, 2008, in favor of Morgan Stanley Real Estate Funds, with reference to the purchase of 52.63 percent of the investment in Credit Servicing S.p.A.;
- the commitment undertaken by Pirelli & C. Real Estate Società di Gestione del Risparmio S.p.A. to subscribe to the shares of the closed-end real estate fund reserved for qualified investors named Fondo Abitare Sociale 1 – Fondo Comune Chiuso di Investimento Immobiliare Etico Riservato ad Investitori Qualificati, for an equivalent amount of Euros 2,422 thousand.

Furthermore, as part of the Cordusio transaction, Pirelli & C. Real Estate S.p.A. issued guarantees on behalf of the companies M.S.M.C. Immobiliare 4 S.r.l. for Euros 9,438 thousand and Aida S.r.l. for Euros 18,421 thousand.

*Put options given to third parties*

- The put options granted to the shareholders banks of Olimpia S.p.A., Banca Intesa S.p.A. and Unicredito Italiano S.p.A. (hereinafter, the “Banks”) under the shareholders’ agreement signed on September 14, 2001 and subsequently amended (“Banks’ Agreement”). These options can be exercised from September 2006, or before that date, in the case of irremediable dissent among the shareholders (so-called “Deadlock”) or in the case of withdrawal by Pirelli & C. S.p.A. from the Banks’ Agreement.

Under this Agreement, the put options can be exercised by the Banks at a price equal to the value of the economic capital of Olimpia plus a premium (the

“Price”). This Price shall be determined by the parties and shall not be less than the outlays made by the Banks (Floor) nor higher than such sum, less any dividends received, increased by an annual IRR, before income taxes, equal to 15 percent (Cap).

The valuation of the put options – at Euros 584,680 thousand for each Bank – was carried out, for Euros 520,000 thousand of that amount, by reference to the outlays effected by the Banks (Floor).

As for the remaining amount of Euros 64,680 thousand (outlays effected by each Bank for Olimpia’s capital increase in December 2003), the valuation was based – in accordance with what was agreed in one of the amendments to the Banks’ Agreement (specifically, the amendment dated December 16, 2003) – on the exercise price of the put on the shares that came to the Banks from the aforementioned capital increase, determined in an amount equal to the higher of Euros 3.53 and the weighted average price of reference recorded by the Telecom Italia shares in the 30 days of trading prior to the request of sale, multiplied by 18,322,946 shares.

The put option, relating to the shares coming from the above capital increase, was accounted for in the financial statements as an investment with a contra-entry to liabilities, in accordance with IAS/IFRS, since the economic benefits relating to ownership of the investment in Olimpia were for the major part transferred immediately to Pirelli (Euros 130 million). As a result, Pirelli’s investment in Olimpia is indicated at 60.5 percent (the effective investment is equal to 57.7 percent).

To cover the options granted to the banks, considered all together, liabilities are carried in the financial statements for Euros 233 million, recorded in financial instruments.

On March 27, and March 28, 2006, Banca Intesa S.p.A. and UniCredito Italiano S.p.A. communicated their intention to withdraw from the shareholders’ agreement and consequently to exercise the right to sell their investments (equal to about 4.77 percent for each bank) to Pirelli & C..

The transfer of the investment will take place in October after expiration of the agreement (October 4, 2006) and will require Pirelli & C. S.p.A. to make a payment of about Euros 1.17 billion (of which Euros 130 million is already considered in the net financial position at December 31, 2005).

- The put option granted to Edizione Finance International S.A./Edizione Holding S.p.A. (“Edizione”), under the shareholders’ agreement signed on August 7, 2001, and subsequently amended.

This put option can be exercised in the case of a (I) deadlock situation among the shareholders, (II) withdrawal on the part of Pirelli & C. S.p.A. from the shareholders’ agreements and (III) the occurrence of a substantial change in the controlling structure of Pirelli & C. S.p.A., by which is meant the exercise by parties other than those currently holding the determining power to nominate the majority of the members of the management board, with a consequent potential modification of the strategic guidelines.

The exercise price of the put option is equal, respectively, under the assumption (I) to the price equal to the value of the economic capital of Olimpia increased by a premium (the “Price”), in the case of (II) to the Price increased by an amount equal to 50 percent of the Price and in the case of (III) to the Price increased by an amount equal to 200 percent of the Price. In this case, however, there is no provision for a Floor or Cap as in the Banks’ Agreement.

- The irrevocable put option in favor of Marzotto S.p.A. for the transfer to Pirelli & C. Real Estate S.p.A. of the entire residual receivable for principal and interest due, at the date of December 31, 2006, by the same Marzotto S.p.A. from the joint venture Aree Urbane S.r.l. for amounts shown as shareholder loans. Subject to the exercise of that option, a call option in favor of Pirelli & C. Real Estate S.p.A. can be exercised for the purchase of the investment held by Marzotto S.p.A. in Aree Urbane S.r.l. (32.5 percent).

**Forward securities purchases**

These refer to the commitment undertaken by Pirelli Finance (Luxembourg) S.A. for the forward purchase (expiration date of November 23, 2006) of 200,000,000 Telecom Italia S.p.A. shares effected with Credit Agricole Lazard Financial Products Bank (Euros 200,000 thousand) and the commitment for the forward purchase of 47,155,300 Telecom Italia S.p.A. shares (expiration date of December 2006) signed with JP Morgan for an amount of Euros 142,100 thousand.

The measurement of these financial instruments at fair value, equal to Euros 38,977 thousand, is recorded in “financial instruments”.

## **24. REVENUES FROM SALES AND SERVICES**

Revenues from sales and services can be analyzed as follows:

	(in thousands of euros)	
	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
Revenues from sales of products	2,168,737	1,992,457
Revenues from services	273,781	280,600
Revenues on construction contracts	3,365	8,362
	<b>2,445,883</b>	<b>2,281,419</b>

## **25. OTHER INCOME**

“Other income” amounts to Euros 137,166 thousand compared to Euros 137,876 thousand at June 30, 2005 and includes rent income, commissions, royalties, compensation, insurance refunds and other minor items.

## **26. PERSONNEL COSTS**

Personnel costs consist of the following:

	(in thousands of euros)	
	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
Salaries and wages	405,248	374,561
Stock option costs	3,672	2,979
Social security costs	94,618	95,046
Leaving indemnity and similar costs	19,298	17,702
Defined contribution pension plan costs	4,538	1,122
Other costs	11,515	9,266
Defined benefit pension fund costs	1,296	5,843
Defined benefit medical care costs	814	443
	<b>540,999</b>	<b>506,962</b>

## **27. AMORTIZATION, DEPRECIATION AND IMPAIRMENTS**

Amortization, depreciation and impairments are as follows:

	(in thousands of euros)	
	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
amortization of intangible assets	5,382	7,651
depreciation of property, plant and equipment	102,670	96,065
impairment of property, plant and equipment	1,000	2,332
	<b>109,052</b>	<b>106,048</b>

## **28. OTHER EXPENSES**

“Other expenses” amount to Euros 837,153 thousand (Euros 741,951 thousand at June 30, 2005). Details are as follows:

	(in thousands of euros)	
	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
receivables writedown	6,554	6,466
other accruals	14,945	12,925
operating lease payments	3,564	5,767
rent and hires	29,751	24,149
EDP expenses	17,903	20,247
consulting fees	60,463	60,841
insurance	16,324	14,292
maintenance	43,192	39,693
selling expenses	142,591	115,098
cleaning expenses	21,427	13,531
contractual work expenses	14,423	19,258
traveling expenses	20,598	19,381
advertising expenses	70,561	73,716
fluids and power	75,383	62,055
other	299,474	254,532
	<b>837,153</b>	<b>741,951</b>

R&D expenses went from Euros 82 million in the first six months of 2005 (3.6 percent of sales) to Euros 87 million in the first half of 2006 (3.6 percent of sales). They are entirely expensed to income.

## **29. FINANCIAL INCOME**

Financial income includes the following:

	(in thousands of euros)	
	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
Interest	36,231	37,655
Other financial income	22,828	8,500
Gains on exchange	141,235	72,444
Gains on disposal of available-for-sale financial assets	2,697	875
Gains on disposal of securities held for trading	7,244	-
	<b>210,235</b>	<b>119,474</b>

## **30. FINANCIAL EXPENSES**

Financial expenses includes the following:

	(in thousands of euros)	
	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
Bank interest	71,644	69,534
Other financial expenses	27,653	18,633
Losses on exchange	140,758	76,122
Losses on disposal of available-for-sale financial assets	5,734	-
Losses on the disposal of securities held for trading	1,414	-
	<b>247,203</b>	<b>164,289</b>

## **31. DIVIDENDS**

The amount of Euros 43,259 thousand in the first half of 2006 primarily refers to dividends received from Telecom Italia S.p.A. (Euros 26,344 thousand), from Capitalia S.p.A. (Euros 9,938 thousand) and from RCS MediaGroup S.p.A. (Euros 3,875 thousand).

In the first half of 2005, the amount of Euros 19,636 thousand mainly included dividends received from Telecom Italia S.p.A. (Euros 10,050 thousand), from Capitalia S.p.A. (Euros 3,355 thousand) and from RCS MediaGroup S.p.A. (Euros 853 thousand).

### **32. VALUATION OF FINANCIAL ASSETS**

The valuation of financial assets includes:

	(in thousands of euros)	
	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
Impairment loss of available-for-sale financial assets	(1,880)	(17,613)
Measurement at fair value of securities held for trading	790	11,536
Measurement at fair value of currency derivatives	(10,425)	(6,983)
Measurement at fair value of other derivatives	(65,417)	(44,813)
	<b>(76,932)</b>	<b>(57,873)</b>

The “impairment loss of available-for-sale financial assets” mainly includes the writedown of the investment in G.I.M. – Generale Industrie Metallurgiche S.p.A. (Euros 1,244 thousand).

The “measurement at fair value of securities held for trading” refers to the fair value adjustment at period-end of listed securities classified under IAS as financial assets at fair value through profit and loss.

The “measurement at fair value of other derivative instruments” relates to the measurement at fair value of options on Telecom Italia S.p.A. shares/convertible bonds, held by the subsidiary Pirelli Finance (Luxembourg) S.A..

### **33. SHARE OF EARNINGS (LOSSES) OF ASSOCIATES AND JOINT VENTURES**

The share of earnings (losses) of associates and joint ventures accounted for using the equity method amounts to earnings of Euros 125,114 thousand (Euros 129,243 thousand at June 30, 2005). The item particularly includes the earnings of Olimpia of Euros 71,219 thousand (Euros 85,779 thousand in the first six months of 2005) and the earnings of the investments in the real estate sector accounted for using the equity method of Euros 52,824 thousand (Euros 43,464 thousand in the first half of 2005).

The earnings (losses) of the real estate sector include Euros 33,312 thousand relating to the investment held in Spazio Industriale II BV, mainly as a result of the effect of the valuation at fair value of the properties (IAS 40) held by the closed-end speculative real estate fund named Spazio Industriale Fondo Comune di Investimento Immobiliare Speculativo, whose business plan calls for long-term appreciation. Such properties had previously been stated at the lower of cost and realizable value (IAS 2) by virtue of the different strategy and use of the properties.

### **34. INCOME TAXES**

Income taxes for the period are composed as follows:

	(in thousands of euros)	
	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
current income taxes	73,408	67,481
deferred income taxes	4,060	3,648
	<b>77,468</b>	<b>71,129</b>

### **35. EARNINGS PER SHARE**

**Basic earnings per share** is calculated by dividing the income attributable to the equity holders of the company (adjusted for the minimum dividends due to savings shares) by the weighted average number of outstanding ordinary shares during the period, excluding ordinary treasury shares.

	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
Income from <b>continuing operations</b> for the period attributable to the equity holders of the company	153	147
Income attributable to savings shares considering the extra 2%	(4)	(4)
<b>Adjusted income from continuing operations</b> for the period attributable to the equity holders of the company	<u>149</u>	<u>143</u>
Weighted average number of outstanding ordinary shares (in thousands)	<u>5,179,338</u>	<u>4,540,499</u>
<b>Basic earnings per ordinary share from continuing operations</b> (in euros per thousand of shares)	<u><b>28.77</b></u>	<u><b>31.49</b></u>
	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
Income from <b>discontinued operations</b> for the period attributable to the equity holders of the company	<u>0</u>	<u>32</u>
Income attributable to savings shares considering the extra 2%	<u>0</u>	<u>(1)</u>
<b>Adjusted income from discontinued operations</b> for the period attributable to the equity holders of the company	<u>0</u>	<u>31</u>
Weighted average number of outstanding ordinary shares (in thousands)	<u>5,179,338</u>	<u>4,540,499</u>
<b>Basic earnings per ordinary share from discontinued operations</b> (in euros per thousand of shares)	<u><b>0.00</b></u>	<u><b>7.05</b></u>

**Diluted earnings per share** is calculated by adjusting the weighted average number of outstanding ordinary shares to assume conversion of all dilutive potential ordinary shares.

The company has only one category of dilutive potential ordinary shares: stock options. Since the price to exercise the stock options is higher than market value, the stock options are assumed not to have been exercised.

At June 30, 2005, the dilutive potential shares deriving from the exercise of outstanding warrants had been considered. At June 30, 2006, there are no longer any warrants outstanding.

	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
Income from <b>continuing operations</b> for the period attributable to the equity holders of the company	153	147
Income attributable to savings shares considering the extra 2%	(4)	(4)
<b>Adjusted income from continuing operations</b> for the period attributable to the equity holders of the company	<u>149</u>	<u>143</u>
Weighted average number of outstanding ordinary shares (in thousands)	5,179,338	4,540,499
Adjustment for the issue of warrants		23,363
Adjusted weighted average number of outstanding ordinary shares (in thousands)	<u>5,179,338</u>	<u>4,563,862</u>
Diluted earnings per ordinary share from <b>continuing operations</b> (in euros per thousand of shares)	<u><b>28.77</b></u>	<u><b>31.33</b></u>
	<b>1<sup>st</sup> Half 2006</b>	<b>1<sup>st</sup> Half 2005</b>
Income from <b>discontinued operations</b> for the period attributable to the equity holders of the company	<u>0</u>	<u>32</u>
Weighted average number of outstanding ordinary shares (in thousands)	5,179,338	4,540,499
Adjustment for the issue of warrants	0	23,363
Adjusted weighted average number of outstanding ordinary shares (in thousands)	<u>5,179,338</u>	<u>4,563,862</u>
Diluted earnings per ordinary share from <b>discontinued operations</b> (in euros per thousand of shares)	<u><b>0.00</b></u>	<u><b>7.01</b></u>

### **36. DIVIDENDS PER SHARE**

The company paid dividends of Euros 108,767 thousand on the ordinary shares (Euros 0.0210 per share) and Euros 4,905 thousand on the savings shares (Euros 0.0364 per share).

### **37. RELATED PARTY DISCLOSURES**

Related party transactions, including intragroup transactions, are neither unusual nor exceptional but fall under the ordinary course of business of the companies of the Group. Such transactions, when not concluded at standard conditions or dictated by specific laws, are in any case conducted at arm's length.

The economic and balance sheet effect of transactions with related parties on the interim consolidated financial statements of the Pirelli Group at June 30, 2006 are as follows.

#### Transactions with associates and joint ventures:

(in millions of euros)		
Revenues for goods and services	85	These mainly refer to the supply of services to associates and joint ventures of Pirelli & C. Real Estate group
Costs for goods and services	4	
Financial income	8	
Trade receivables and other receivables	107	These mainly refer to receivables from associates and joint ventures of Pirelli & C. Real Estate group
Financial receivables	323	These refer to receivables from associates and joint ventures of Pirelli & C. Real Estate group
Trade payables and other payables	11	These mainly refer to payables to associates and joint ventures of Pirelli & C. Real Estate group

Transactions with parties related to Pirelli through directors (Telecom Italia group, Camfin group and F.C. Internazionale Milano S.p.A.):

(in millions of euros)

Revenues for goods and services	136	These refer to services rendered by Pirelli & C S.p.A., Shared Service Center s.c.r.l. and Pirelli & C. Real Estate S.p.A. to the Telecom Italia group (Euros 133 million), services rendered by Pirelli & C. Ambiente Eco Technology S.p.A. ( ex-Pirelli Ambiente Tecnologie S.p.A.) to the Camfin group (Euros 1 million) and services rendered to F.C. Internazionale Milano S.p.A. (Euros 2 million)
Costs for goods and services	45	These refer to telephone, computer and power services by the Telecom Italia group (Euros 15 million), the supply of natural gas by the Camfin Group (Euros 26 million) and costs for the sponsorship of F.C. Internazionale Milano S.p.A. (Euros 4 million)
Trade receivables and other receivables	66	These refer to receivables for the supply of the above services (to the Telecom Italia group for Euros 64 million, to the Camfin group Euros 1 million and to F.C. Internazionale Milano S.p.A. Euro 1 million)
Trade payables and other payables	15	These refer to payables for the supply of the above services (to the Telecom Italia group for Euros 5 million, the Camfin group for Euros 7 million and F.C. Internazionale Milano S.p.A. for Euros 3 million)

### **38. SIGNIFICANT SUBSEQUENT EVENTS**

- On July 4, 2006, Pirelli & C. S.p.A., Edizione Finance International S.A. and Edizione Holding S.p.A. together with Hopa S.p.A. communicated that they had reached full agreement over all the aspects relating to the cash settlement of the investments held in Olimpia S.p.A. and in Holinvest S.p.A. following the dissolution of the shareholders' agreements that were already in existence among the above companies.

This agreement provided for:

- the purchase on the part of Pirelli & C. S.p.A., Edizione Finance International S.A. and Edizione Holding S.p.A. of all the shares held by Hopa S.p.A. in Olimpia S.p.A. (equal to 16 percent of capital) for a cash settlement of Euros 622 million (of which Euros 208 million relates to the premium to which Hopa had the right on the basis of previous agreements);
- the purchase on the part of Hopa S.p.A. of all the shares held by Olimpia S.p.A. in Holinvest S.p.A. (equal to 19.999 percent of capital) for a cash settlement of Euros 86 million.

Holinvest S.p.A., at that date, was the owner of 492,697,862 Telecom Italia S.p.A. shares, equal to about 3.68 percent of ordinary share capital.

On the basis of the terms of the agreement, 320,253,610 Telecom Italia S.p.A. shares held by Holinvest S.p.A. (equal to 65 percent of the total shares in its possession) are covered by a pre-emptive two-year agreement in favor of Olimpia S.p.A. which also establishes that Holinvest may not effect new purchases of Telecom Italia S.p.A. shares without the prior agreement of Olimpia during the same period.

The purchases of the investments and the signing of the pre-emptive agreement were finalized on July 12, 2006.

Specifically, Pirelli & C. S.p.A. purchased 12.8 percent of Olimpia S.p.A. for an outlay of Euros 331 million. At the same time, it paid its share of the premium due to Hopa S.p.A. of Euros 166 million, which had already been set aside in the 2005 financial statements.

- On July 27, 2006, the board of directors of Pirelli & C. S.p.A. examined a transaction with some leading Italian and international financial institutions (Banca Intesa, Banca Leonardo Group, Capitalia, One Equity Partners – JP Morgan Group, Lehman Brothers and Mediobanca) for the sale of a minority interest in the capital of Pirelli Tyre S.p.A., for the purpose of a later IPO.

Subsequently, on July 29, 2006, the relevant agreements were reached for the sale of 38.9 percent of the capital of Pirelli Tyre S.p.A. for consideration equal to Euros 740 million, with an equity value for the entire company of about Euros 1.9 billion.

The purchase of the minority interest in Pirelli Tyre S.p.A., finalized on August 2, 2006, was carried out by Speed S.p.A., an Italian company in which about a 19 percent stake each is held by Banca Intesa, Capitalia, One Equity Partners – JP Morgan Group, Lehman Brothers and Mediobanca and about 4 percent stake by the Banca Leonardo Group.

The agreements provide that the purchasing companies may start and conduct, within a period of four years and six months from the closing date, an Initial Public Offering of the shares acquired.

Pirelli has the right to repurchase the shares that were sold in the event in which, after four years and six months, the shares have not been placed in an IPO.

The relationships between the seller and the buyer are regulated by shareholder agreements which provide, among other things, that the acquiring company may designate five out of the thirteen directors on the board of directors of Pirelli Tyre S.p.A. and appoint a member of the board of statutory auditors.

After a lock-up period of six months, and after receiving Pirelli's approval, the acquiring company or its shareholders will have the right to sell up to 49 percent of the shares originally purchased to qualified parties (leading financial institutions or mutual funds).

A commission of 3 percent of the equivalent amount of the transaction was paid to the financial institutions and an additional 1 percent will be paid on an annual basis until the IPO.

- On August 2, 2006, Pirelli RE and Calyon, the corporate investment bank of the Credit Agricole Group, signed a binding agreement to establish a joint venture to invest in Europe in the non-performing loans segment.

The joint venture, in which Pirelli RE will have a 33 percent interest and Calyon a 67 percent interest, is committed to acquiring 100 percent of five non-performing mortgage loan receivable portfolios held since November 2004 by the Pirelli RE/MSREF joint venture with a residual gross book value of approximately Euros 2.6 billion. After the new strategic partnership is established, Pirelli RE will take over 53 percent of Credit Servicing (in which it already has a 47 percent stake) and 25 percent of Asset Management NPL (in which it already has a 25 percent stake) from the Morgan Stanley real estate funds. The portfolio of loans purchased from Banco Popolare di Verona e Novara last June 7 will also be transferred to the non-performing loan portfolio of the joint venture.

At the same time, the joint venture established in August 2004 between Pirelli RE (25 percent) and Morgan Stanley Real Estate Funds (75 percent) for the purpose of investments on the Italian market will be dissolved; the American investment bank will remain a strategic partner of Pirelli RE in the offices sector.

The closing of the transaction is scheduled to take place by the end of 2006 on condition of approval by the Antitrust Authority and by the trustees of the outstanding securitization transactions.

### **39. OTHER INFORMATION**

#### **Exchange rates**

The main exchange rates used for consolidation purposes are as follows:

(local currency against euros)						
	Period-end		Change in	Average		Change in
	6/30/2006	12/31/2005	%	1 <sup>st</sup> Half 2006	1 <sup>st</sup> Half 2005	%
<b>Europe</b>						
British pound	0.6921	0.6853	0.99%	0.6871	0.6859	0.17%
Swiss franc	1.5672	1.5551	0.78%	1.5612	1.5462	0.97%
Slovakian koruna	38.3500	37.8800	1.24%	37.5667	30.0731	24.92%
<b>North America</b>						
American dollar	1.2713	1.1797	7.76%	1.2297	1.2848	(4.29%)
Canadian dollar	1.4132	1.3725	2.97%	1.3999	1.5875	(11.82%)
<b>South America</b>						
Brazilian real	2.7515	2.7613	(0.36%)	2.6963	3.3053	(18.43%)
Venezuela bolivar	2,733.2950	2,536.3550	7.76%	2,643.7690	2,662.9921	(0.72%)
Argentinean peso	3.9232	3.5769	9.68%	3.7705	3.7398	0.82%
<b>Oceania</b>						
Australian dollar	1.7117	1.6109	6.26%	1.6554	1.6627	(0.44%)
<b>Asia</b>						
Chinese renminbi	10.1648	9.5181	6.79%	9.8730	10.6337	(7.15%)
Singapore dollar	2.0137	1.9628	2.59%	1.9769	2.1163	(6.59%)
<b>Africa</b>						
Egyptian pound	7.3100	6.7567	8.19%	7.0577	7.4522	(5.29%)

**Net financial position**

Although it is a non-IFRS performance measure, the composition of the net financial (liquidity)/debt position is provided below for purposes of continuity of information with previous periods:

	(in millions of euros)	
<b>Net financial (liquidity)/debt position</b>	<b>6/30/2006</b>	<b>12/31/2005</b>
. Borrowings from banks and other financial institutions - current	2,030	556
. Financial accrued liabilities and deferred income - current	63	62
. Cash and cash equivalents	(887)	(300)
. Financial assets held for trading	(128)	(180)
. Financial receivables - current	(67)	(27)
. Financial accrued income and prepaid expenses - current	(7)	(12)
<b>Net short-term (liquidity)/debt</b>	<b>1,004</b>	<b>99</b>
. Borrowings from banks and other financial institutions - non-current	1,151	1,551
. Financial receivables - non-current	(572)	(468)
. Financial accrued income and prepaid expenses - non-current	(8)	(5)
<b>Net medium/long-term (liquidity)/debt</b>	<b>571</b>	<b>1,078</b>
<b>Total net financial (liquidity)/debt position</b>	<b>1,575</b>	<b>1,177</b>

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**Companies consolidated line-by-line**


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Company	Business	Headquarters	Share capital	Percentage ownership	Percentage of voting rights	Held by
<b>Europe</b>						
<b>Austria</b>						
ECOI-Immobilien Gmbh	Real Estate	Vienna	Euro	35.000	100,00%	P&K Real Estate Gmbh
Pirelli Gesellschaft mbH	Tyres	Vienna	Euro	726.728	100,00%	Pirelli Tyre (Europe) S.A.
<b>Belgium</b>						
Pirelli Tyres Belux S.A.	Tyres	Brussels	Euro	700.000	100,00%	Pirelli Tyre (Europe) S.A.
<b>France</b>						
Gecam France S.a.S	Environment	Paris	Euro	750.000	70,00%	Pirelli & C. Ambiente Eco Tecnology S.p.A. (ex-Pirelli & C. Ambiente Technologie S.p.A.)
Pirelli Broadband Solutions France S.a.r.l.	Environment	Paris	Euro	10.000	99,00%	Pirelli Broadband Solutions S.p.A.
					1,00%	Maristel S.p.A.
Pneus Pirelli S.a.S	Tyres	Roissy en France	Euro	1.515.858	100,00%	Pirelli Tyre (Europe) S.A.
<b>Germany</b>						
Deutsche Pirelli Reifen Holding Gmbh	Financial	Breuberg/Odenwald	Euro	7.694.943	100,00%	Pirelli Tyre Holland N.V.
Drahtcord Saar Geschaefsfuehrungs Gmbh	Tyres	Merzig	Deut. Mark	60.000	50,00%	Pirelli Deutschland Gmbh
Drahtcord Saar GmbH & Co. K.G.	Tyres	Merzig	Deut. Mark	30.000.000	50,00%	Pirelli Deutschland Gmbh
Driver Fleet Solution Gmbh	Tyres	Breuberg/Odenwald	Euro	26.000	100,00%	Deutsche Pirelli Reifen Holding Gmbh
P&K Real Estate Gmbh	Real Estate	Berlin	Euro	570.000	90,00%	Pirelli & C. Real Estate S.p.A.
Pirelli Deutschland Gmbh	Tyres	Breuberg/Odenwald	Euro	26.334.100	100,00%	Deutsche Pirelli Reifen Holding Gmbh
Pirelli Personal Service Gmbh	Tyres	Breuberg/Odenwald	Euro	25.000	100,00%	Deutsche Pirelli Reifen Holding Gmbh
PK Grundstueckverwaltung Gmbh	Tyres	Hoechst/Odenwald	Euro	26.000	100,00%	Deutsche Pirelli Reifen Holding Gmbh
Pneumobil Gmbh	Tyres	Breuberg/Odenwald	Euro	259.225	100,00%	Deutsche Pirelli Reifen Holding Gmbh
Resident Berlin Zwei P&K Gmbh	Real Estate	Berlin	Euro	100.000	100,00%	P&K Real Estate Gmbh
<b>Greece</b>						
Elastika Pirelli S.A.	Tyres	Athens	Euro	785.370	99,90%	Pirelli Tyre (Europe) S.A.
					0,10%	Pirelli Tyre S.p.A (ex-Pirelli Pneumatici S.p.A. )
Pirelli Hellas S.A. (in liquidation)	Tyres	Athens	US \$	22.050.000	79,86%	Pirelli Tyre Holding N.V.
<b>Hungary</b>						
Pirelli Hungary Tyre Trading and Services Ltd	Tyres	Budapest	Hun. Forint/000	3.000	100,00%	Pirelli Tyre (Europe) S.A.
<b>Ireland</b>						
Pirelli Reinsurance Company Ltd	Reinsurance	Dublin	US \$	7.150.000	100,00%	Pirelli Finance (Luxembourg) S.A.
<b>Italy</b>						
Acquario S.r.l. (in liquidation)	Real Estate	Genoa	Euro	255.000	100,00%	Pirelli & C. Real Estate S.p.A.
Alfa S.r.l.	Real Estate	Milan	Euro	2.600.000	100,00%	Pirelli & C. Real Estate S.p.A.
Altofim S.r.l.	Real Estate	Milan	Euro	78.000	100,00%	Beta S.r.l.
Asset Management NPL S.r.l.	Real Estate	Milan	Euro	10.000	75,00%	Pirelli & C. Real Estate S.p.A.
Bernini Immobiliare S.r.l.	Real Estate	Milan	Euro	500.000	14,00%	Pirelli & C. Real Estate S.p.A.
Beta S.r.l.	Real Estate	Milan	Euro	26.000	100,00%	Partecipazioni Real Estate S.p.A.
Botticino S.r.l.	Real Estate	Milan	Euro	10.000	100,00%	Pirelli & C. Real Estate S.p.A.
Casaclick S.p.A.	Real Estate	Milan	Euro	299.000	100,00%	Pirelli & C. Real Estate Agency S.p.A.
Centrale Immobiliare S.p.A.	Real Estate	Milan	Euro	5.200.000	100,00%	Pirelli & C. Real Estate S.p.A.
Centro Servizi Amministrativi Pirelli S.r.l.	Services	Milan	Euro	51.000	34,00%	Pirelli & C. S.p.A.
					33,00%	Pirelli Tyre S.p.A (ex-Pirelli Pneumatici S.p.A. )
					33,00%	Pirelli & C. Real Estate S.p.A.
CFT Finanziaria S.p.A.	Real Estate	Florence	Euro	10.010.000	100,00%	Partecipazioni Real Estate S.p.A.
Consorzio Stabile Pirelli RE Servizi	Real Estate	Milan	Euro	200.000	50,00%	Pirelli & C. Real Estate Project Management S.p.A.
					40,00%	Pirelli & C. Real Estate Facility Management S.p.A.
					10,00%	Somogi S.r.l.
Dolcetto 8 S.r.l.	Commercial	Milan	Euro	10.000	100,00%	Centrale Immobiliare S.p.A.
Driver Italia S.p.A.	Commercial	Milan	Euro	200.000	59,39%	Pirelli Tyre S.p.A (ex-Pirelli Pneumatici S.p.A. )

Company	Business	Headquarters	Share capital	Percentage ownership	Percentage of voting rights	Held by
Edinord Gestioni S.p.A.	Real Estate	Milan	Euro 517.000	100,00%		Pirelli & C. Real Estate S.p.A.
Elle Uno Società Consortile a.r.l.	Real Estate	Milan	Euro 100.000	60,00%		Edinord Gestioni S.p.A.
Erato Finance S.r.l.	Real Estate	Milan	Euro 600.000	53,85%		Pirelli & C. Real Estate S.p.A.
Esedra S.r.l.	Real Estate	Milan	Euro 2.376.234	100,00%		Pirelli & C. Real Estate S.p.A.
FIM - Fabbrica Italiana di Mediazione S.r.l.	Real Estate	Milan	Euro 100.000	100,00%		Pirelli & C. Real Estate Agency S.p.A.
Geolidro S.p.A.	Real Estate	Naples	Euro 3.099.096	100,00%		Centrale Immobiliare S.p.A.
Golfo Aranci S.p.A. - Società di trasformazione Urbana	Real Estate	Milan	Euro 1.000.000	50,09%		Pirelli & C. Real Estate S.p.A.
				1,20%		Pirelli & C. Real Estate Project Management S.p.A.
				5,00%		Centrale Immobiliare S.p.A.
Iniziative Immobiliari 3 S.r.l.	Real Estate	Milan	Euro 10.000	100,00%		Iniziative Immobiliari 3 B.V.
Lambda S.r.l.	Real Estate	Milan	Euro 578.760	100,00%		Pirelli & C. Real Estate S.p.A.
Maristel S.p.A.	Telecommunications	Milan	Euro 1.020.000	100,00%		Pirelli Broadband Solutions S.p.A.
NewCo RE 1 S.r.l.	Real Estate	Milan	Euro 30.000	100,00%		Pirelli & C. Real Estate S.p.A.
NewCo RE 2 S.r.l.	Real Estate	Milan	Euro 10.000	100,00%		Pirelli & C. Real Estate S.p.A.
NewCo RE 4 S.r.l.	Real Estate	Milan	Euro 10.000	100,00%		Pirelli & C. Real Estate S.p.A.
NewCo RE 5 S.r.l.	Real Estate	Milan	Euro 40.000	100,00%		Pirelli & C. Real Estate S.p.A.
NewCo RE 6 S.r.l.	Real Estate	Milan	Euro 40.000	100,00%		Pirelli & C. Real Estate S.p.A.
NewCo RE 7 S.r.l.	Real Estate	Milan	Euro 40.000	100,00%		Pirelli & C. Real Estate S.p.A.
NewCo RE 8 S.r.l.	Real Estate	Milan	Euro 40.000	100,00%		Pirelli & C. Real Estate S.p.A.
NewCo RE 9 S.r.l.	Real Estate	Milan	Euro 40.000	100,00%		Pirelli & C. Real Estate S.p.A.
P.I.T. - Promozione Imprese e Territorio S.c.r.l.	Real Estate	Pozzuoli (Na)	Euro 25.823	100,00%		Pirelli & C. Real Estate Facility Management S.p.A.
Parcheggi Bicocca S.r.l.	Real Estate	Milan	Euro 1.500.000	75,00%		Pirelli & C. Real Estate S.p.A.
Partecipazioni Real Estate S.p.A.	Real Estate	Milan	Euro 1.360.280	100,00%		Pirelli & C. Real Estate S.p.A.
PBS S.C.a.r.l.	Real Estate	Milan	Euro 100.000	60,00%		Edinord Gestioni S.p.A.
Pirelli & C. Ambiente Eco Technology S.p.A. (ex-Pirelli & C. Ambiente Tecnologie S.p.A.)	Environment	Milan	Euro 2.080.000	100,00%		Pirelli & C. Ambiente S.p.A. (ex-Pirelli & C. Ambiente Holding S.p.A.)
Pirelli & C. Ambiente Renewable Energy S.p.A. (ex-Pirelli & C. Ambiente S.p.A.)	Environment	Milan	Euro 3.060.000	100,00%		Pirelli & C. Ambiente S.p.A. (ex-Pirelli & C. Ambiente Holding S.p.A.)
Pirelli & C. Ambiente S.p.A. (ex-Pirelli & C. Ambiente Holding S.p.A.)	Environment	Milan	Euro 23.120.000	51,00%		Pirelli & C. S.p.A.
Pirelli & C. Ambiente Site Remediation S.p.A. (ex-Pirelli & C. Ambiente Bonifiche S.r.l.)	Environment	Milan	Euro 155.700	100,00%		Pirelli & C. Ambiente S.p.A. (ex-Pirelli & C. Ambiente Holding S.p.A.)
Pirelli & C. Opere Generali S.p.A.	Real Estate	Milan	Euro 104.000	100,00%		Pirelli & C. Real Estate S.p.A.
Pirelli & C. Real Estate Agency S.p.A.	Real Estate	Milan	Euro 832.000	100,00%		Pirelli & C. Real Estate S.p.A.
Pirelli & C. Real Estate Energy S.p.A.	Real Estate	Milan	Euro 120.000	100,00%		Pirelli & C. Real Estate Facility Management S.p.A.
Pirelli & C. Real Estate Facility Management S.p.A.	Real Estate	Milan	Euro 5.561.000	100,00%		Pirelli & C. Real Estate S.p.A.
Pirelli & C. Real Estate Franchising Holding S.r.l.	Real Estate	Milan	Euro 120.000	70,00%		Pirelli & C. Real Estate S.p.A.
Pirelli & C. Real Estate Franchising S.p.A.	Real Estate	Milan	Euro 500.000	100,00%		Pirelli & C. Real Estate Franchising Holding S.r.l.
Pirelli & C. Real Estate Franchising Servizi Finanziari S.r.l.	Real Estate	Milan	Euro 10.000	100,00%		Pirelli & C. Real Estate Franchising Holding S.r.l.
Pirelli & C. Real Estate Opportunità Società di Gestione del Risparmio S.p.A.	Real Estate	Milan	Euro 1.000.000	100,00%		Pirelli & C. Real Estate S.p.A.
Pirelli & C. Real Estate Project Management S.p.A.	Real Estate	Milan	Euro 520.000	100,00%		Pirelli & C. Real Estate S.p.A.
Pirelli & C. Real Estate Property Management S.p.A.	Real Estate	Milan	Euro 114.400	100,00%		Pirelli & C. Real Estate S.p.A.
Pirelli & C. Real Estate S.p.A.	Real Estate	Milan	Euro 21.274.678	50,36%		Pirelli & C. S.p.A.
				5,24%	0,00%	Pirelli & C. Real Estate S.p.A.
Pirelli & C. Real Estate Società di Gestione del Risparmio S.p.A.	Real Estate	Milan	Euro 24.458.763	100,00%		Pirelli & C. Real Estate S.p.A.
Pirelli Broadband Solutions S.p.A.	Telecommunications	Milan	Euro 10.120.000	100,00%		Pirelli & C. S.p.A.
Pirelli Cultura S.p.A.	Sundry	Milan	Euro 1.000.000	100,00%		Pirelli & C. S.p.A.
Pirelli Labs S.p.A.	Research and Development	Milan	Euro 10.000.000	100,00%		Pirelli & C. S.p.A.
Pirelli Nastri Tecnici S.p.A. (in liquidation)	Sundry	Milan	Euro 384.642	100,00%		Pirelli & C. S.p.A.
Pirelli Servizi Finanziari S.p.A.	Financial	Milan	Euro 1.976.000	100,00%		Pirelli & C. S.p.A.
Pirelli Tyre S.p.A. (ex-Pirelli Pneumatici S.p.A.)	Tyres	Milan	Euro 256.820.000	100,00%		Pirelli Tyre Holding N.V.
Polo Viaggi S.r.l.	Travel Agency	Milan	Euro 46.800	100,00%		Pirelli & C. S.p.A.
Progetto Bicocca Università S.r.l.	Real Estate	Milan	Euro 50.360	50,50%		Pirelli & C. Real Estate S.p.A.
Progetto Salute Bollate S.r.l.	Real Estate	Milan	Euro 100.000	100,00%		Pirelli & C. Real Estate S.p.A.
Repeg Italian Finance S.r.l.	Real Estate	Milan	Euro 600.000	100,00%		Partecipazioni Real Estate S.p.A.
Rofau S.r.l.	Real Estate	Milan	Euro 10.000	100,00%		Altofim S.r.l.
Servizi Amministrativi Real Estate S.p.A.	Real Estate	Milan	Euro 520.000	100,00%		Pirelli & C. Real Estate S.p.A.
Servizi Aziendali Pirelli S.C.p.A.	Services	Milan	Euro 104.000	95,00%		Pirelli & C. S.p.A.
				2,00%		Pirelli Tyre S.p.A. (ex-Pirelli Pneumatici S.p.A.)
				1,00%		Polo Viaggi S.r.l.
				2,00%		Pirelli & C. Real Estate S.p.A.
Shared Service Center s.c.r.l.	Information Systems	Milan	Euro 1.756.612	50,00%		Pirelli & C. S.p.A.
Somogi S.r.l.	Real Estate	Milan	Euro 90.000	100,00%		Pirelli & C. Real Estate Facility Management S.p.A.
Progetto Vallata S.r.l.	Real Estate	Milan	Euro 1.500.000	80,00%		Pirelli & C. Real Estate S.p.A.
				5,00%		Pirelli & C. Real Estate Facility Management S.p.A.
				4,00%		Pirelli & C. Real Estate Project Management S.p.A.
Vindex S.r.l.	Real Estate	Brescia	Euro 12.000	37,00%		CFT Finanziaria S.p.A.
				32,00%		Partecipazioni Real Estate S.p.A.

Company	Business	Headquarters	Share capital	Percentage ownership	Percentage of voting rights	Held by
<b>Luxembourg</b>						
MSPRE Luxembourg NPL S.à r.l.	Real Estate	Luxembourg	Euro	12.500	100,00%	Partecipazioni Real Estate S.p.A.
Pirelli Finance (Luxembourg) S.A.	Financial	Luxembourg	Euro	270.228.168	100,00%	Pirelli & C. S.p.A.
<b>Poland</b>						
Driver Polska Sp.ZO.O.	Tyres	Warsaw	Pol. Zloty/mil.	100.000	72,50%	Pirelli Polska Sp.ZO.O.
Pirelli Pekao Real Estate Sp.ZO.O.	Tyres	Warsaw	Pol. Zloty/mil.	35.430	75,00%	Pirelli & C. Real Estate S.p.A.
Pirelli Polska Sp.ZO.O.	Tyres	Warsaw	Pol. Zloty/mil.	625.771	100,00%	Pirelli Tyre (Europe) S.A.
<b>Romania</b>						
S.C. Cord Romania S.R.L.	Tyres	Slatina	Rom. Leu/000	24.990.100	80,00%	Pirelli Tyre Holland N.V.
S.C. Pirelli Tyres Romania S.R.L.	Tyres	Slatina	Rom. Leu/000	77.169.800	95,00%	Pirelli Tyre Holland N.V.
					5,00%	Pirelli Tyre S.p.A (ex-Pirelli Pneumatici S.p.A. )
<b>Russia</b>						
OOO Pirelli Tyre Russia	Commercial	Moscow	Russian Rouble	950.000	95,00%	Pirelli Tyre (Europe) S.A.
					5,00%	Pirelli Tyre Holland N.V.
<b>Slovakia</b>						
Pirelli Slovakia S.R.O.	Tyres	Bratislava	Slov. Koruna	200.000	100,00%	Pirelli Tyre (Europe) S.A.
<b>Spain</b>						
Euro Driver Car S.L.	Tyres	Barcelona	Euro	690.000	25,00%	Pirelli Neumaticos S.A.
					26,00%	Proneus S.L.
Omnia Motor S.A.	Tyres	Barcelona	Euro	1.502.530	100,00%	Pirelli Neumaticos S.A.
Pirelli Neumaticos S.A.	Tyres	Barcelona	Euro	45.075.908	100,00%	Pirelli Tyre Holland N.V.
Proneus S.L.	Tyres	Barcelona	Euro	3.005	51,00%	Pirelli Neumaticos S.A.
<b>Sweden</b>						
Pirelli Tyre Nordic A.B.	Tyres	Bromma	Swed. Krona	950.000	100,00%	Pirelli Tyre (Europe) S.A.
<b>Switzerland</b>						
Agom S.A.	Tyres	Conthey	Swiss Franc	50.000	80,00%	Pirelli Tyre (Europe) S.A.
Agom S.A. Bioggio	Tyres	Bioggio	Swiss Franc	590.000	100,00%	Pirelli Tyre (Europe) S.A.
Pirelli Société de Services S.a.r.l.	Financial	Basel	Swiss Franc	50.000	100,00%	Pirelli Tyre (Europe) S.A.
Pirelli Société Générale S.A.	Financial	Basel	Swiss Franc	28.000.000	100,00%	Pirelli & C. S.p.A.
Pirelli Tyre (Europe) S.A.	Tyres	Basel	Swiss Franc	1.000.000	100,00%	Pirelli Tyre Holland N.V.
<b>The Netherlands</b>						
Iniziativa immobilization 3 B.V.	Real Estate	Amsterdam	Euro	4.500.000	100,00%	Pirelli & C. Real Estate S.p.A.
Pirelli China Tyre N.V.	Tyres	Heineenoord	Euro	8.045.000	100,00%	Pirelli Tyre Holland N.V.
Pirelli Tyre Holding N.V.	Tyres Holding Company	Heineenoord	Euro	250.000.000	100,00%	Pirelli & C. S.p.A.
Pirelli Tyre Holland N.V.	Commercial	Milan	Euro	3.045.000	100,00%	Pirelli Tyre S.p.A (ex-Pirelli Pneumatici S.p.A. )
Pirelli Tyres Nederland B.V.	Tyres	Heineenoord	Euro	18.152	100,00%	Pirelli Tyre (Europe) S.A.
Sipir Finance N.V.	Financial	Heineenoord	Euro	13.021.222	100,00%	Pirelli & C. S.p.A.
<b>Turkey</b>						
Celikord A.S.	Tyres	Istanbul	Turk. Lira/mil.	29.000.000	50,733%	Pirelli Tyre Holland N.V.
					0,27%	Pirelli Tyre S.p.A (ex-Pirelli Pneumatici S.p.A. )
Turk-Pirelli Lastikleri A.S.	Tyres	Istanbul	Turk. Lira/mil.	140.000.000	65,44%	Pirelli Tyre Holland N.V.
					0,15%	Pirelli Tyre S.p.A (ex-Pirelli Pneumatici S.p.A. )

Company	Business	Headquarters	Share capital	Percentage ownership	Percentage of voting rights	Held by
<b>United Kingdom</b>						
Central Tyre Ltd	Tyres	London	British Pound	100.000	100,00%	Pirelli UK Tyres Ltd
Courier Tyre Company (ex-Courier Tyre Company Ltd)	Tyres	London	British Pound	10.000	100,00%	Pirelli UK Tyres Ltd
CPK Auto Products Ltd	Tyres	London	British Pound	10.000	100,00%	Pirelli UK Tyres Ltd
CTC 1994 Ltd	Tyres	London	British Pound	984	100,00%	Central Tyre Ltd
Pirelli International Ltd	Financial	London	Euro	250.000.000	75,00%	Pirelli UK Tyre Holding Ltd
					25,00%	Pirelli Tyre S.p.A (ex-Pirelli Pneumatici S.p.A. )
Pirelli Tyres Ltd	Tyres	London	British Pound	16.000.000	100,00%	Pirelli UK Tyres Ltd
Pirelli UK Finance Ltd	Financial	London	British Pound	6.969.280	100,00%	Pirelli UK Ltd "C"
Pirelli UK Ltd "A"	Tyres Holding Company	London	British Pound	85.535.300	100,00%	Pirelli Tyre Holding N.V.
Pirelli UK Ltd "C"	Finance Holding Company	London	British Pound	11.625.978	100,00%	Pirelli & C. S.p.A.
Pirelli UK Tyre Holding Ltd	Finance Holding Company	London	British Pound	96.331.000	100,00%	Pirelli Tyre Holland N.V.
Pirelli UK Tyres Ltd	Tyres	London	British Pound	85.000.000	75,00%	Pirelli UK Tyre Holding Ltd
					25,00%	Pirelli Tyre S.p.A (ex-Pirelli Pneumatici S.p.A. )
<b>North America</b>						
<b>Canada</b>						
Pirelli Tire Inc.	Tyres	Frederic Town (New Brunswick)	Can. \$	6.000.000	100,00%	Pirelli Tyre (Europe) S.A.
<b>U.S.A.</b>						
Pirelli Broadband Solutions North America Inc	Telecommunications	Wilmington (Del.)	US \$	1,00	100,00%	Pirelli Broadband Solutions S.p.A.
Pirelli North America Inc.	Tyres	Wilmington (Del.)	US \$	10,00	100,00%	Pirelli Tyre Holland N.V.
Pirelli Tire LLC	Tyres	Wilmington (Del.)	US \$	1	100,00%	Pirelli North America Inc. "A"
<b>Central/South America</b>						
<b>Argentina</b>						
Pirelli Argentina de Mandatos S.A.	Services	Buenos Aires	Arg. Peso	500.000	100,00%	Pirelli Société Générale S.A.
Pirelli Neumaticos S.A.I.C.	Tyres	Buenos Aires	Arg. Peso	101.325.176	95,00%	Pirelli Tyre Holland N.V.
					5,00%	Pirelli Tyre S.p.A (ex-Pirelli Pneumatici S.p.A. )
<b>Brazil</b>						
Muriaé Ltda	Financial	Santo André	Bra. Real	80.000.000	100,00%	Pirelli Pneus S.A.
Novacorp Consultora e Serviços Corporativos Ltda	Holding	Santo André	Bra. Real	6.000	99,98%	Pirelli S.A.
Pirelli & C. Real Estate Ltda	Real Estate	Santo André	Bra. Real	2.000.000	100,00%	Pirelli S.A.
Pirelli Pneus Nordeste Ltda	Tyres	Feira de Santana	Bra. Real	29.991.402	100,00%	Pirelli Pneus S.A.
Pirelli Pneus S.A.	Tyres	Feira de Santana	Bra. Real	342.085.095	99,73%	99,57% Pirelli Tyre S.p.A (ex-Pirelli Pneumatici S.p.A. )
Pirelli S.A.	Financial	Sao Paulo	Bra. Real	49.189.271	100,00%	Pirelli & C. S.p.A.
Pneuc Comercial e Importadora Ltda	Tyres	Sao Paulo	Bra. Real	12.913.526	100,00%	Pirelli Pneus S.A.
<b>Chile</b>						
Pirelli Neumaticos Chile Limitada	Tyres	Santiago	US \$	1.918.451	99,98%	Pirelli Pneus S.A.
					0,02%	Pneuc Comercial e Importadora Ltda
<b>Colombia</b>						
Pirelli de Colombia S.A.	Tyres	Santa Fe De Bogota	Col. Peso/000	3.315.069	92,91%	Pirelli Pneus S.A.
					2,28%	Pirelli de Venezuela C.A.
					1,60%	Muriaé Ltda
					1,60%	Pirelli Pneus Nordeste Ltda
					1,60%	Pneuc Comercial e Importadora Ltda
<b>Mexico</b>						
Pirelli Neumaticos de Mexico S.A. de C.V.	Tyres	Mexico City	Mex. Peso	35.098.400	99,98%	Pirelli Pneus S.A.
					0,02%	Pneuc Comercial e Importadora Ltda
Servicios Pirelli Mexico S.A. de C.V.	Tyres	Mexico City	Mex. Peso	50.000	99,00%	Pirelli Pneus S.A.
					1,00%	Pneuc Comercial e Importadora Ltda
<b>Venezuela</b>						
Pirelli de Venezuela C.A.	Tyres	Valencia	Ven. Bolivar/000	20.062.679	96,22%	Pirelli Tyre Holland N.V.

Company	Business	Headquarters	Share capital	Percentage ownership	Percentage of voting rights	Held by
<b>Africa</b>						
<b>Egypt</b>						
Alexandria Tire Company S.A.E. (*)	Tyres	Alexandria	Egy. Pound	393.000.000	86,79%	Pirelli Tyre S.p.A (ex-Pirelli Pneumatici S.p.A. )
International Tire Company Ltd	Tyres	Alexandria	Egy. Pound	50.000	99,80%	Pirelli Tyre (Europe) S.A. Alexandria Tire Company S.A.E.
<b>South Africa</b>						
Pirelli Tyre (Pty) Ltd	Tyres	Sandton	S.A. Rand	1	100,00%	Pirelli Tyre (Europe) S.A.
<b>Oceania</b>						
<b>Australia</b>						
Pirelli Tyres Australia Pty Ltd	Tyres	Pymble - N.S.W.	Aus. \$	150.000	100,00%	Pirelli Tyre (Europe) S.A.
<b>New Zealand</b>						
Pirelli Tyres (NZ) Ltd	Tyres	Wellington	N.Z. \$	100	100,00%	Pirelli Tyres Australia Pty Ltd
<b>Asia</b>						
<b>China</b>						
Pirelli Tyre Co. Ltd (ex-Yanzhou Evolution Tyre CO. Ltd)	Tyres	Yanzhou	China Renmimbi	800.000.000	60,00%	Pirelli China Tyre N.V.
<b>Japan</b>						
Pirelli Japan Kabushiki Kaisha	Tyres	Tokyo	Jap. Yen	2.700.000.000	100,00%	Pirelli Tyre Holland N.V.
<b>Singapore</b>						
Pirelli Asia Pte Ltd	Tyres	Singapore	Sing. \$	2	100,00%	Pirelli Tyre (Europe) S.A.

(\*) For IAS purposes, the percentage ownership is 89.1%