



Quarterly Report
First Quarter 2001

PIRELLI Società per azioni

Head office in Milan, Viale Sarca 222

Share Capital - Euros 1,042,408,785.08

Milan Companies Registry No. 00886890151

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

Chairman and Managing Director	Marco Tronchetti Provera
Deputy Chairman	Alberto Pirelli
Managing Director	Carlo Buora
Directors	Carlo Ciani Eugenio Coppola di Canzano Carlo De Benedetti Alberto Falck Giovanni Ferrario Giuseppe Gazzoni-Frascara Mario Greco Georg F. Kraymer Angelo Marchiò Luigi Orlando Riccardo Perissich Giampiero Pesenti Ennio Presutti Carlo Alessandro Puri Negri Vincenzo Sozzani Frank Vischer

Carlo Ciani and Mario Greco were appointed directors on May 8, 2001

Secretary to the Board	Sergio Lamacchia
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Board of Statutory Auditors

Chairman	Luigi Guatri
Standing members	Rosalba Casiraghi Giorgio Oggioni
Alternate members	Mario Brughera Alfredo Malguzzi

General Managers

Finance and Administration	Carlo Buora
Tyres Sector	Giovanni Ferrario
Cables and Systems Sector - Energy	Oscar Cristianci
Cables and Systems Sector - Telecom	Kevin Riddett

PIRELLI S.p.A. - MILAN
Quarterly Report – 1st Quarter 2001

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MANAGEMENT'S REPORT

Performance of the Group

Although characterized by an economic trend displaying signs of a slowdown, the first quarter 2001 shows an improvement in all operating components.

In particular, the operating profit totals Euros 134 million compared to Euros 97 million, with an increase of 38 percent.

Major events during the 1st quarter 2001

- In the first quarter 2001, Pirelli S.p.A. sold No. 32,023,550 treasury shares on the market for net proceeds of Euros 124 million, realizing a gain, before income taxes, of Euros 30 million.
- The already announced project to separate the Cables and Systems Sector into the Energy and Telecom sectors is proceeding according to plan with the target date set for the end of the year.

THE GROUP

The consolidated figures of the Group at March 31, 2001 can be summarized as follows:

	(in millions of euros)		
	1st quarter 2001	1st quarter 2000	Year 2000
. Sales revenues	1,933	1,762	7,477
. Gross operating profit	228	191	820
% of sales	11.8%	10.8%	11.0%
. Operating profit	134	97	437
% of sales	6.9%	5.5%	5.9%
. Financial income and expenses	20	(11)	(75)
. Income before extraordinary items and income taxes	154	86	362
% of sales	8.0%	4.9%	4.8%
. Extraordinary items	65	1,198	4,277
. Income before income taxes	219	1,284	4,639
% of sales	11.3%	n.s.	n.s.
. Income taxes	(71)	(338)	(1,013)
. Net income	148	946	3,626
% of sales	7.7%	n.s.	n.s.
. Net income attributable to Pirelli S.p.A.	149	942	5,756
. Earning per share (in Euros)	0.07	0.47	2.89
. Net financial position (liquidity)	(3,318)	(417)	(3,495)
. Employees (at period-end)	41,330	40,472	41,914
. Factories (number)	87	87	87

. Sales revenues

Sales revenues for the three months ended March 31, 2001 total Euros 1,933 million, with an increase of 9.7 percent compared to the corresponding period of the prior year. This change is mainly due to higher volumes and mix (+8 percent) and price variations (+1.5 percent).

. **Gross operating profit**

Gross operating profit for the three months ended March 31, 2001 is Euros 228 million (11.8 percent of sales revenues), with an increase compared to Euros 191 million (10.8 percent of sales revenues) for the same period of the prior year.

Besides the operating factor of growth, the supply agreement with Cisco Systems also contributed to the improvement by Euros 26 million.

. **Operating profit**

Operating profit for the three months ended March 31, 2001 is Euros 134 million, equal to 6.9 percent of sales revenues, compared to Euros 97 million (5.5 percent of sales revenues) in the first quarter 2000.

Amortization and depreciation remain stable at Euros 94 million.

. **Financial income and expenses**

The net financial income balance is Euros 20 million compared to a net financial expense balance of Euros 11 million in the corresponding period of the prior year.

The increase is mainly due to a better average net financial position.

. **Income before extraordinary items and income taxes**

The **income before extraordinary items and income taxes** is equal to Euros 154 million compared to Euros 86 million in the first quarter 2000, with an increase of 79 percent.

. **Extraordinary items**

Extraordinary items include the gain, before income taxes, on the sale of Pirelli S.p.A. treasury shares on the market (Euros 30 million) and Euros 36 million recognized by Cisco Systems as part of the sale of the Terrestrial Optical Systems last year.

In the first quarter 2000, extraordinary items mainly included the gain, before income taxes, on the sale of the Terrestrial Optical Systems and production restructuring and rationalization expenses.

. **Net financial position**

The **net financial position** shows a liquidity position at March 31, 2001 of Euros 3,318 million compared to Euros 3,495 million at March 31, 2000. The change is principally due to seasonal factors which led to an increase in working capital.

. **Employees**

Employees number 41,330 at March 31, 2001 compared to 41,914 at December 31, 2000. The reduction of 584 units represents the difference between 1,778 units added and 2,362 units leaving.

CABLES AND SYSTEMS SECTOR

	(in millions of euros)		
	1 st quarter 2001	1 st quarter 2000	Year 2000
. Sales revenues	1,209	1,054	4,591
. Gross operating profit	136	95	466
% of sales	11.2%	9.0%	10.2%
. Operating profit	90	52	289
% of sales	7.4%	4.9%	6.3%
. Financial income and expenses	14	(6)	(14)
. Income before extraordinary items and income taxes	104	46	275
% of sales	8.7%	4.4%	6.0%
. Extraordinary items	36	1,365	2,173
. Income before income taxes	140	1,411	2,448
% of sales	11.6%	n.s.	n.s.
. Income taxes	(47)	(317)	(668)
. Net income	93	1,094	1,780
% of sales	7.7%	n.s.	n.s.
. Net financial position (liquidity)	(1,508)	(775)	(1,644)
. Employees (at period-end)	19,874	19,473	20,496
. Factories (number)	65	65	65

Sales revenues for the three months ended March 31, 2001 amount to Euros 1,209 million and show an increase of 14.7 percent compared to the same period of the prior year. This is attributable to the contribution made by the power cables operations purchased during 2000, which were not present in the first quarter of 2000 (former BICC and NKF businesses), as well as higher optical telephone cable volumes.

The change is due to:

• Volumes	+ 6.8%
• Prices	+ 3.0%
• Change in the scope of consolidation	+ 0.9%
• Mix and other	+ 4.0%

	+ 14.7%
	=====

Operating profit for the first quarter 2001, to which the supply agreement with Cisco Systems contributed Euros 26 million, is equal to Euros 90 million, compared to Euros 52 million in the first quarter 2000; the operating profit represents 7.4 percent of sales revenues (5.3 percent excluding the effect of the Cisco Systems agreement), compared to 4.9 percent of sales revenues in the corresponding period of the prior year.

An analysis of the change is presented as follows:

	Millions of euros
• Currency exchange effect	+ 1
• Prices (excluding metals)	+ 21
• Volumes and mix	+ 23
• Change in per unit costs	- 10
• Cisco Systems supply agreement	+ 26
• Change in the scope of consolidation	+ 1
• Other	- 24

	+ 38
	=====

Income before extraordinary items and income taxes is Euros 104 million compared to Euros 46 million in the first quarter 2000.

Extraordinary items show a net balance of extraordinary income of Euros 36 million due mainly to income recognized by Cisco Systems on the sale of the Terrestrial Optical Systems last year.

The first quarter 2000 showed a net balance of extraordinary income of Euros 1,365 million which included gains, before income taxes, on the sale of the Terrestrial Optical Systems to Cisco Systems, as well as restructuring expenses.

Net income for the first quarter of 2001 is Euros 93 million, after income taxes of Euros 47 million.

The **net financial position** shows a liquidity position of Euros 1,508 million compared to Euros 1,644 million at December 31, 2000. The change is due operating requirements during the period.

Employees of the sector at March 31, 2001 number 19,874, a reduction of 622 compared to 20,496 at December 31, 2000.

The integration of the businesses acquired from BICCGeneral in the third quarter 2000 was completed within the established time frame, according to plan.

As previously announced, the separation into the Energy and Telecom sectors commenced during the quarter and is expected to be concluded by the end of the year.

For purposes of information, certain key data is presented below together with a brief commentary on the two sectors of Energy and Telecom.

(in millions of euros)	Energy Sector			Telecom Sector		
	1 st quarter	1 st quarter	Year	1 st quarter	1 st quarter	Year
	2001	2000	2000	2001	2000	2000
Sales revenues	815	722	3,162	399	320	1,376
Operating profit	12	22	58	55	30	154
<i>% of sales</i>	1.5%	3.0%	1.8%	13.8%	9.4%	11.2%

Energy

Sales in the Energy sector show an increase compared to the first quarter of the prior year (+13 percent) due to the effect of the increase in volumes owing to the acquisition of the former BICC and NKF businesses.

The positive performance of the cables businesses for the general market, high voltage cables, special cables and accessories was partly offset by the negative trend in the utilities and submarine systems businesses.

Geographically, Europe and South America show sales on the rise while North America displays a falloff in volumes owing to the unfavorable economic situation.

The total operating profit is lower on account of a deterioration in the mix and the continuation of some production inefficiencies due to the restructuring process currently underway.

Restructuring continues, in particular, in the United Kingdom, in Italy (former BICC units) and in Germany.

Telecom

During the course of the first quarter 2001, sales revenues of the Cables and Systems Sector – Telecom rose significantly (+24 percent), compared to the same period of the prior year, in a market still characterized by strong pressure over fiber optic cables on account of a supply that is growing but still insufficient overall.

The satisfactory trend in sales has been recorded in all the geographical areas (Europe, North and South America, Southeast Asia) in which Pirelli has an important industrial presence.

In following the development plan decided the previous year, investments have continued in order to increase productive capacity, both for optical fiber production (in Italy and South America) and cables production (in particular, in the United States and in the United Kingdom). As a consequence of the above, the overall profitability of the Telecom business has improved significantly.

Compared to the prior year, however, the submarine cables and systems business shows a decline, owing to a stagnant market and a halt called for many projects.

The structure dedicated to the research of optical fibers has been increased during the quarter, as has the development of new businesses (Access Network).

TYRES SECTOR

Results of the Tyres Sector

The key figures for the Sector are presented below:

	(in millions of euros)		
	1st quarter 2001	1st quarter 2000	Year 2000
. Sales revenues	729	707	2,880
. Gross operating profit	101	102	370
% of sales	13.9%	14.4%	12.8%
. Operating profit	57	54	180
% of sales	7.8%	7.6%	6.3%
. Financial income and expenses	(17)	(14)	(79)
. Income before extraordinary items and income taxes	40	40	101
% of sales	5.5%	5.7%	3.5%
. Extraordinary items	0	(183)	(224)
. Income before income taxes	40	(143)	(123)
% of sales	5.5%	n.s.	n.s.
. Income taxes	(12)	(18)	(49)
. Net income (loss)	28	(161)	(172)
% of sales	3.8%	n.s.	n.s.
. Net financial position (liquidity)/debt	851	597	748
. Personnel (at period-end)	20,655	20,265	20,637
. Factories (number)	22	22	22

Sales revenues for the three months ended March 31, 2001 show an increase of 3.0 percent compared to the same period of the prior year, thanks mainly to the favorable trend in volumes (+3.7 percent), mix (+1.2 percent), a slight reduction in the price list (−0.6 percent) and the currency exchange effect (−1.3 percent).

Car/Light truck tyre volumes for the first quarter are basically in line with that of the first quarter of 2000: the reduction in the replacements channel in Turkey and North America is compensated by the favorable performance in other geographical areas. The volumes of the “high range” of Pirelli trademark car tyres have been especially positive; they show an increase of 9 percent over the prior year (in particular, in Europe and South America), thanks mainly to the good performance of the replacements channel.

Truck volumes show an improvement of 1 percent compared to 2000, where the slowdown in Turkey is more than compensated by the positive performance of the other geographical areas. The higher replacements volumes offset the falloff in the original equipment market.

Motorcycle tyres are positive and total volumes increased by 18 percent; volumes rose for replacements, thanks to the good performance displayed in South America and Europe, and also for original equipment.

Operating profit for the three months ended March 31, 2001 is Euros 57 million compared to Euros 54 million in the first quarter of 2000, with the return on sales equal to 7.8 percent against 7.6 percent in 2000: the positive contribution made by volumes and mix, accompanied by steps to improve efficiency on both variable components and staff structures more than compensated the negative change in sales prices, the increase in raw materials prices, the increase in costs and the negative contribution by the exchange effect.

Specifically, the increase of Euros 3 million compared to the prior year is due to:

	Millions of euros
• Sales prices	- 4
• Raw material per unit costs	- 18
• Change in per unit costs	- 6
• Currency exchange effect	- 3
• Volumes and mix	+ 30
• Efficiency and other	+ 4

	+ 3
	=====

Financial income and expenses show a higher net financial expense balance of Euros 3 million due mainly to a higher debt level.

Income before extraordinary items and income taxes is stable compared to the first quarter of 2000 at Euros 40 million.

Extraordinary items, which shows a nil balance in 2001, mainly included production restructuring and rationalization expenses in the first quarter of 2000 (Euros 188 million).

Income taxes are Euros 12 million, with a decrease compared to 2000 of Euros 6 million, especially on account of tax credits due to the collection of dividends from Italian units in advance.

Net income is Euros 28 million compared to a loss of Euros 161 million in the first quarter of 2000.

The **net financial position** registers an increase of Euros 103 million compared to December 31, 2000 which can be ascribed to seasonal factors and to the capital expenditure program.

At March 31, 2001, **employees** number 20,655, a figure substantially unchanged compared to December 31, 2000 (20,637 units).

SIGNIFICANT EVENTS SUBSEQUENT TO THE QUARTER AND OUTLOOK FOR THE CURRENT YEAR

On April 18, Pirelli Cavi e Sistemi S.p.A. and e.Biscom S.p.A. signed a cooperation agreement for the development of new Internet access solutions using fiber optics.

The agreement calls for Pirelli Cavi e Sistemi to purchase a 1 percent stake in e.Biscom from the partners of the company for about Euros 48.7 million.

For the current year, on the basis of the results achieved to date, despite a deteriorating economic-financial scenario, we expect to reach a result, at both the level of operating and net result (without taking into account the extraordinary items of the past year), that is at least in line with the year 2000.

RELATED PARTY DISCLOSURES

According to Consob Communications No. 97001574 of February 20, 1997 and No. 98015375 of February 27, 1998 which deal with related party transactions among Group companies, the effects of such transactions on the balance sheet and statement of income of the consolidated financial statements at March 31, 2001 are presented in the following table.

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

The following table presents the major transactions at March 31, 2001 that Pirelli S.p.A. Group has entered into with the parent companies (Pirelli & C. A.p.A. and Pirelli & C. Luxembourg S.A.) and the subsidiaries of the latter companies, which are included in the scope of consolidation of Pirelli & C. A.p.A..

(in millions of euros)

Type of transaction	With parent companies	With subsidiaries of Pirelli & C. A.p.A.	Total
TRADE RECEIVABLES AND OTHER	0,3	21,1	21,4
TRADE PAYABLES AND OTHER	(1.3)	(171.3)	(172.6)
FINANCIAL RECEIVABLES	88,1	320,1	408,2
FINANCIAL PAYABLES	(56.3)	(26.7)	(83.0)
REVENUES FOR GOODS AND SERVICES	0,3	5,7	6,0
COSTS FOR GOODS AND SERVICES	(1.2)	(2.1)	(3.3)
FINANCIAL INCOME	0.8	3,1	39.9
FINANCIAL EXPENSES	(0.8)	(0.4)	(1.2)
EXTRAORDINARY EXPENSES	0.0	0.0	0.0

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

- **financial receivables**, relating to loans receivable by Pirelli International Ltd – UK – (subsidiary of Pirelli S.p.A.) from Pirelli & C. Luxembourg S.A.;
- **financial payables**, relating to transactions on the current account by Pirelli Servizi Finanziari S.p.A. with Pirelli & C. A.p.A.;
- **revenues for goods and services**, relating to the performance of various services rendered by Pirelli S.p.A. and Pirelli Informatica S.p.A. to Pirelli & C. A.p.A.;
- **costs for goods and services**, relating to costs for the corporate secretarial services and internal auditing rendered by Pirelli & C. A.p.A. on behalf of Pirelli S.p.A.;
- **financial income and expenses**, relating to interest income and expenses on the aforementioned current account transactions and loans, as well as costs and revenues for hedging transactions carried out by Pirelli International Ltd (subsidiary of Pirelli S.p.A.) on behalf of Pirelli & C. A.p.A.;

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

- **trade receivables and other**, relating to the sale of Pirelli Cavi e Sistemi S.p.A. buildings (subsidiary of Pirelli S.p.A.) to Lambda S.r.l. (indirect subsidiary of Pirelli & C. A.p.A.);
- **trade payables and other**, relating to services rendered by companies in the Pirelli & C. Real Estate S.p.A. Group (subsidiary of Pirelli & C. A.p.A.) to Pirelli S.p.A. and its subsidiaries, as well as the transfer of Pirelli & C. Real Estate S.p.A. tax credits to Pirelli Cavi e Sistemi S.p.A.;
- **financial receivables and payables**, relating to transactions on the current account by Pirelli Servizi Finanziari S.p.A. with companies in the Pirelli & C. Real Estate S.p.A. Group (subsidiary of Pirelli & C. A.p.A.);
- **revenues for goods and services**, relating to cost recoveries for various services rendered by Pirelli S.p.A. and Pirelli Informatica S.p.A. (subsidiary of Pirelli S.p.A.) on behalf of Pirelli & C. Real Estate S.p.A. and its subsidiaries;
- **costs for goods and services**, relating to costs for property management services incurred by Pirelli S.p.A. and its subsidiaries for the services rendered by companies in the Pirelli & C. Real Estate S.p.A. Group (subsidiary of Pirelli & C. A.p.A.);
- **financial income and expenses**, relating to interest income and expenses on the aforementioned current account and loan transactions.

**QUARTERLY DATA
AND
COMMENTS**

QUARTERLY DATA

	(in millions of euros)		
	1 st quarter 2001	1 st quarter 2000	Year 2000
. Sales revenues	1,933	1,762	7,477
. Other revenues	91	45	233
. Production value	2,024	1,807	7,710
. Cost of sales	(1,404)	(1,247)	(5,310)
. Labor costs	(392)	(369)	(1,580)
. Amortization and depreciation	(94)	(94)	(383)
. Operating profit	134	97	437
. Financial income and expenses	20	(11)	(75)
. Income before extraordinary items and income taxes	154	86	362
. Extraordinary items	65	1,198	4,277
. Income before income taxes	219	1,284	4,639
. Income taxes	(71)	(338)	(1,013)
. Net income	148	946	3,626

	(in thousands of euros)	
Net financial position	3/31/2001	12/31/2000
. Short-term financial payables	412,372	581,256
. Accrued liabilities and deferred income for interest	23,215	22,682
. Cash and banks	(3,300,211)	(3,701,290)
. Other securities	(1,181,166)	(1,237,160)
. Short-term financial receivables	(482,507)	(369,116)
. Accrued income and prepaid expenses for interest	(29,257)	(13,946)
. Capital subscription rights	(30)	0
Net short-term financial position	(4,557,584)	(4,717,574)
. Medium/long-term financial payables	1,348,181	1,327,285
. Medium/long-term financial receivables	(99,640)	(96,565)
. Other securities	(8,739)	(8,370)
Net medium/long-term debt position	1,239,802	1,222,350
Net financial position	(3,317,782)	(3,495,224)

COMMENTS ON QUARTERLY DATA

Form and content

The accounting principles, valuation criteria and principles of consolidation used in preparing the quarterly data at March 31, 2001 are the same as those adopted for the financial statements at December 31, 2000 and disclosed in the previous annual report.

Economic review

Sales revenues

Sales revenues for the three months ended March 31, 2001 amount to Euros 1,933 million compared to Euros 1,762 million for the three months ended March 31, 2000.

The change of +9.7 percent compared to the corresponding period of 2000 can be analyzed as follows:

• Currency exchange effect	- 0.6%
• Volumes	+ 5.6%
• Change in the scope of consolidation	+ 0.5%
• Prices	+ 1.5%
• Mix	+ 2.4%
• Other	+ 0.3%

	+ 9.7%
	=====

A breakdown of sales revenues by sector and geographical area is as follows:

Sector	1 st Quarter 2001	1 st Quarter 2000	Geographical area	1 st Quarter 2001	1 st Quarter 2000
Cables and Systems	62%	60%	Italy	18.2%	12.3%
Tyres	38%	40%	Europe	42.0%	43.8%
			North America	16.2%	14.5%
			Central and South America	15.7%	16.3%
			Australia, Africa and Asia	7.9%	13.1%

Labor costs

Labor costs for the three months ended March 31, 2001 amount to Euros 392 million and represent 20.3 percent of sales revenues compared to 20.9 percent in the corresponding period of the prior year.

Amortization and depreciation

Amortization and depreciation for the first quarter 2001 amount to Euros 94 million, of which Euros 12 million refer to the amortization of intangible assets and Euros 82 million to the depreciation of property, plant and equipment, unchanged compared to the same period of the prior year.

Operating profit

Operating profit for the three months ended March 31, 2001 is Euros 134 million (6.9 percent of sales revenues). This is an increase of Euros 37 million over the same period of 2000. This change can be ascribed to:

	Millions of euros
• Currency exchange effect	- 2
• Volumes and mix	+ 54
• Prices (excluding metals)	+ 17
• Materials	- 20
• Change in the scope of consolidation	+ 1
• Cisco Systems supply agreement	+ 26
• Change in per unit costs	- 20
• Other	- 19

	+ 37
	=====

Financial income and expenses

Financial income and expenses show a net balance of financial income of Euros 20 million compared to a net balance of financial expense of Euros 11 million in the corresponding period of the prior year.

The increase is mainly due to a better average net financial position.

Extraordinary items

Extraordinary items include the gain on the sale of Pirelli S.p.A. treasury shares on the market (Euros 30 million) and Euros 36 million recognized by Cisco Systems as part of the sale of the Terrestrial Optical Systems last year.

In the first quarter 2000, extraordinary items mainly included the gain, before income taxes, on the sale of the Terrestrial Optical Systems, and production restructuring and rationalization expenses.

Net financial position

The net financial position shows a net liquidity position of Euros 3,318 million compared to Euros 3,495 million at December 31, 2000.

The change during the quarter, equal to Euros 177 million, is mainly due to the deterioration of working capital.