

Ladies and gentlemen, welcome to Pirelli's conference call, in which our Chairman, Mister Marco Tronchetti Provera, will release third quarter 2006 group results. I remind you that a Q&A session will follow after the presentation, and that you can find the presentation slides in the investor relation section of the Pirelli web site. Now, I would like to introduce you to Mister Marco Tronchetti Provera. Thank you.

**Good evening, ladies and gentlemen, thank you for joining us in our conference call. Today we're disclosing nine months 06 group results. I'll give you an overview on Pirelli's recent key events' results, then Mr. Gori will go through Pirelli's tire results, and Mr. Puri will highlight Pirelli Ambiente and Pirelli Real Estate results. A Q&A session will follow.**

**So, let's start pointing out the key events occurred during the last months: first, the private placement of the 38.9 of Pirelli tires stake, for an equity value of around 1.9 billion, and with a positive cash impact of 716 million, and a capital gain of 416 million, at consolidated level. Then the restatement of Olimpia's book value with a negative impact on equity of approximately 2.1 billion at consolidated level. On October 4, Pirelli increased its stake in Olimpia, reaching 80% of the share capital, related to the banks put option for a negative cash impact of approximately 1 billion. Pirelli real Estate signed a binding agreement of 29628 of Deutsche Gruntal. Gruntal Morgan agreed on Burk Giovanni and the estimated enterprise value at closing is 1.5 billion. Olimpia, Pirelli Edizione Holding, Edizione Finance signed a consultation pact with Generali and Mediobanca tying up 23.2% stake of TI ordinary shares. On October 25<sup>th</sup>, Pirelli Tire started the production of high-performance tires in Slatina, Romania; 2 million tires are expected to be produced during 07 and 4.5 million at a full capacity. Last but not least Pirelli sold, on October 27, its stake, the 1.92% in Capitalia, for a sum of 233 million, with a capital gain of 215 million, at consolidated level.**

**Now going in detail: next slide shows the effect of the Olimpia book value on Pirelli &Co. on the accounts; roughly 1.8 billion on the equity side, the effect on the group consolidated equity being roughly 2.1 billion. Net result at company level is negative for approximately 1.7 billion, while at group level, net result is negative for approximately 1.4 billion. Now, the cashing impact for the restatement of Olimpia at book value will affect net financial position, which was 1.4 billion at the end September 06.**

**Going to slide 4: it shows Pirelli Group results. At the end of September, sales grew 9.1% year-on-year, and stood at 3.6 billion; EBIT was close to 300 million: 299.7, increased by 7.8% year-on-year; and the return on sales being 8.3%; it was 8.4% in the same period of 05. Attributable net result was negative for 1.4 billion, affected by the governance in Olimpia book value restatement and the positive effect of 4 billion euro from the capital gain of the TI private placement.**

**Going more in detail: slide 5 shows the group EBIT variations. Year-on-year tire posted an EBIT increase of 300 million, net of IPO costs as well approximately 7.4 million. PBS improved the EBIT for 5 million, and Pirelli Real Estate for 10.4 million. EBIT, including results from equity participation, is up 11.1 million. Pirelli Ambiente gave its first positive contribution to EBIT, mainly due to the license fee paid by Real Estate Energy, a UK based company involved in the waste-for-energy business. Looking at group net financial position variation, net operating cash-flow was negative: 410 million 700,000 mainly due to the increase in tire business working capital related to the growth of the winter tire business, which is seasonal, and that will recover by year end; and raw materials' cost, anyhow, most of it is linked to seasonality. Net financial position: we stood at 1.4 billion at the end of September, growing for approximately 253 million from the beginning of the year, mainly due to the abovementioned items which are shown in detail in these slides.**

**Slide 7 gives an insight on the market asset value of Pirelli Group. On September 30, the Pirelli Group market asset value was around 5.1 billion, versus 1.3 billion of corporate net debt we will see for the year end 06. So, now I leave the floor to Francesco Gori, CEO of Pirelli Tire who will illustrate you the results of the tire business.**

**Good afternoon everybody. Pirelli Tire net sales grew to 3 billion from 2.7 billion in nine months 2006, in particular during the first nine months of the year. Pirelli Tire recorded a 2-digit sales growth, +10.5%, notwithstanding negative market trends in North America; volumes were up 3.9%, including new Chinese operations, and price mix was up 3.4%, not fully compensating raw materials and energy costs increase. EBIT development was positive, showing a 9.3% return on sales before IPO costs, and 9.1 after IPO costs. Net income was 153.6 million euro.**

**Now let us see more in detail the results of the Pirelli Tire business units: next slide, as you are probably aware of, consumer segment includes both car and motorcycle tires, while for industrial we mean truck tires plus steelcord. As you can see, consumer segment results were positive, with sales at slightly above 2 billion euro, +9.4% year-on-year, and pre-IPO costs EBIT at 193.9 million, +13.7% year-on-year. Return on sales increased to 9.4% pre-IPO costs from 9% in 2005. Coming to the**

industrial segment: sales reached 919.6 million euro, +13% year-on-year, while pre-IPO costs EBIT decreased at 84.9 million, from 100.6 million, with 9.2% return on sales pre-IPO costs, versus 12.4% in 2005. This erosion's mainly due to record natural rubber prices not completely compensated by price increases in the marketplace.

I would like to give you some highlights in the next slide, number 10; first of all this success on the most important winter tire tests by automobile clubs and by Austrian, German, and Swiss magazines. Piorelli's Winter, Sottozero, No Sports, No Control, and Scorpion tires have been appointed best-in-class. In United States, JD Power awarded Piorelli again in 2006 in its yearly customer satisfaction study; then, as Mr. Tronchetti mentioned before, Piorelli Tire has started the production of high-performance tires in Slatina, Romania: next year approximately 2 million tires will be produced there, while, at full capacity, the facility's expected to produce over 4.5 million pieces. Finally, our list prices are expected to increase some 5% in Europe and in export markets, and 4% in the US. Thank you. The floor is back to the Chairman.

Thank you, Mr. Gori. Coming to PBS: sales grew 26% year-on-year, in line with our expectations, sales in photonics were 10 million, the EBITDA was in breakeven, while it was negative for 5.6 million in September 05; EBIT was positive for broadband access, 1 million, thanks to a growth in terms of volumes that compensated price pressure, but still negative in photonics products due to start-up costs. Net result was negative for 2.5 million including -6.9 million euro of third quarter 05; operational breakeven target for 06 is confirmed.

Now I would like to highlight the main achievements of Piorelli broadband solution by segments. First of all, let me point out the launch of the new dual mode phone, working with SIM cards and IP for ideal ADSL connection; the first supply agreement has been signed for Arcor, part of Vodafone group, and this will have to enlarge PBS customer bases. We announced cutting business with two of the most important players in Europe. For what concerns the photonics business, the dynamic tunable laser is now ready for pre-sale operations having passed all qualification trials.

So, let's now move to the Piorelli Ambiente and Piorelli Real Estate results, and I leave the floor to Mr. Carlo Puri. Carlo...

Thank you Mr. Tronchetti. Good evening everybody. First of all, let me remind you that Piorelli Ambiente, 'ambiente' is the Italian word for environment, is the second startup of Piorelli Group, and is characterized by three main divisions: Piorelli Ambiente Eco-technology for the production of Y-diesel GECAM and of diesel particulate filters for the reduction of emission of diesel engines. Piorelli Ambiente Renewable Energy which develops solutions for the use of renewable energy, for instance on the recovery of municipal solid waste; and Piorelli Ambiente Site Re-Mediation dealing with environment acclamation and requalification of contaminated sites. In the third quarter 2006 Piorelli Ambiente sales reached 45.5 million euro from around 40.1 million euro in September 05. Net results stood at a little bit more than breakeven, at 0.5 million, improving from negative 2.5 of the third quarter of 2005. Now let's have a look at the Piorelli results: before giving you the details of the nine months' results, I would like to remind you that third quarter results have been affected by a temporary slowdown of the activity, resulting from the uncertainty created by the government decree on the taxation of real estate. The mandate decree has become effective for financial real estate institutions, funds and leasing companies, only from the 1<sup>st</sup> of October. In the first nine months, aggregated revenue per quarter, reached 915 million euro, substantially in line with last year. Operating profits, including income from equity participation, has increased by 11% to 115.16 million euro; net profit after minority stands at 84 million euro, up approximately 8% over the same period of last year. Adjusted net financial position, including the ongoing deconsolidation of the non-performing loans that we have acquired in the last three months, reached 429 million euro with a gearing of 0.78, in line with the business plan 2006-2008. We expect a double-digit growth in the last quarter of the current year, and therefore a growth for 2006 in line with our three-year plan, with a KAGER between 10 and 15%.

If we go now to slide 15: in giving you the details of our most significant achievements, I have to refer two figures, including also October 2006, since the month has been very busy for the company. We have completed very important transactions, the most relevant is the binding agreement signed for the acquisition of the German company DGAG, which has a portfolio of around 1.5 billion euro, and represents a strategic step in our international expansion in Germany. After such an acquisition, our asset under management exceeds 15 billion euro, with Piorelli Real Estate share being around 23%, around 3.4 billion euro; around 2 billion euro of asset under management... under management, are held outside Italy, we are therefore close to the 20% target of international asset under management set out for 2008. We have also increased the share of asset under management owned

through funds, which today amount to 6.7 million euro, and we have a total of 12 operating funds: 3 opportunistic and 9 core plus. At the beginning of October, we completed the listing of Spazio Investments at the AIM, the Alternative Investment Market in London, with an IPO of around 300 million euro, which was oversubscribed by the most important institutional investor. Spazio Investment represents the largest platform investing in Italy in the logistics and life industrial sector. We opened the first day with a value of the share of 12.5, and today it's around 14 euro per share. We have also completed a significant amount of acquisitions, in the year, around 3.4 million euro, including DGAG, therefore reaching in advance the targets set out for 2006. We have further developed the service provider in franchising (...) business, with good results, especially in technical services, that is projects, facility and property management, which have posted an EBIT of around 18 million euro, with a 40% increase, with respect to the nine months 2005. Thank you to everybody, I will now give the floor back to Mr. Tronchetti for the group outlook.

Thank you Carlo. So, to sum up, we expect a good fourth quarter in the tire business: EBITDA should reach an operating breakeven, net debt should reach 2 billion, excluding the Pirelli Real Estate journal acquisitions, with an impact on group net financial position that will be approximately 80 million and Pirelli Group confirms for 06 an increase on all operating results with a sound financial structure. Thank you very much for your attention, now let' start the Q&A session. Thank you.

### Q&A session:

1. Mr. Serge Escudè from UBM:

*Good evening, everybody. I have three questions; four, actually. Is it possible to expect in the near future a further write-off of TI stake in Olimpia? In particular if the market price of TI remains at the current level? That's the first question; and for the tire sector: what is the expected trend of EBIT for the next year? Now the third question's about raw materials: in the tire sector what are you expecting as a trend for... for also the trading price? And my last question's about the trend in price that you are expecting in 2007: are you planning further increases in prices? Thank you.*

Thank you. So, we don't have any plans to increase our participation in TI or in Olimpia, so we already have 18%, we have the agreement with Mediobanca and Generali, we go up to 22.5%, then we have another 1.30% in Pirelli balance sheet, so we feel comfortable...

*My question was about further write-off of TI share in Olimpia. Further write-off. If you think that this level now is appropriate, with respect to the current market price?*

No, as you know, the evaluation is based on international accounting, IAS; the evaluation is based on fair value that's cost to sale, and the... so the... all the evolution has been made and confirmed by analysts and professors, so this value is convenient and we do not expect any variation. I also have to remind you that this is a value that is based on 30<sup>th</sup> of September value of TI shares, which is different from the actual value. Going to tires, I leave the floor to Mr. Gori to answer the EBIT and raw material questions. Please, Mr. Gori.

Thank you Mr. Tronchetti. EBIT: we expect an increase in EBIT under the assumption that raw material costs will be on average at the same level of 2006. This is the basis on which we are building up our budget for next year. And, as far as trading price, if you mean a selling price...

Yes.

...including mix, we expect to improve overall our price mix variance next year.

**Sorry, just to give you another information about the criteria of evaluation: the evaluation... the devaluation to 3 euro was based on the two methodologies: the value news and the fair value that's close to sale. So, the sale price was confirmed by the two different kinds of evaluation, that came to the same result.**

*I'm sorry to insist, but you made a devaluation, but do you think that a further devaluation might be, or may be necessary if the price of TI remains at this level? Because it can't be anymore consistent in 3 or 4 or 6 months' time. So, my question is: these experts that you are mentioning may, in six months' time require... or the authority may require a further devaluation of the stake? This is the question I'm asking. Do you think it's fair now that you will not move anymore?*

**So, to give you an even more precise answer, I mentioned before that the evaluation based on value news and fair value that's close to sale was an evaluation based on 30<sup>th</sup> of September values, which was, if I remember well, around 224; the actual price is 240, so I think that, taking into account the evaluation we made, we do not expect any need of further devaluation for the next months.**

*Thank you.*

**Thank you.**

**2. Ms. Carola Bardelli from Deutsche Bank:**

*Good evening. I was wondering after the creation of the shareholders' agreement outside of Olimpia, should we exclude the entrance of new shareholders in Olimpia, or is this still a possibility? This is the first question. Then I would have another one, if I may: you said in the last conference call that you expected Telecom Italia's dividend to remain unchanged versus last year, so I'm wondering if you think that the new management could consider a cut in the dividend or if you are sticking to your expectation with regards to the dividend that Olimpia will be getting from Telecom Italia? Thank you.*

**So, the first question about the new shareholders: I already mentioned in the last conference call that we are open to new shareholders, in case they are to pay the right price, and they have a real interest in entering in Olimpia. On dividends: I am a shareholder, I'm not part of the management as up to date... to present to the general meeting a proposal about dividends, and I think that Mr. Rossi gave an answer yesterday during the conference call of TI.**

*Okay. Can I ask a follow-up question? Why hasn't there been a write-down in Olimpia; so why a write-down in Pirelli and not in Olimpia?*

**As you know, Olimpia's not a listed company, it doesn't make a quarterly balance sheet, it makes the balance sheet only at year-end, so it will be done at year-end.**

*Okay. Thank you.*

**Thank you.**

**3. Mr. Philip Beair from SG:**

*Good evening. Phil Belus from Société Générale. So, the first question's on the tire business: I would like to know if, we see there's some improvement expected in the industrial business in Latin America in the coming months? Second point concerning the winter season: it seemed that the season started very early, and you got good conditions, about your tires, but do you think that Q4 earnings from tires will be much better than last year? And the last question is about debt on the tire business: do you think that the working capital will be lower? And the debt of tire business will be lower at the end of the year, than at the end of nine months?*

Please, Mr. Gori.

**Yes. About the truck business, or industrial business: as you see, margins this year have been squeezed by the strong increase of natural rubber prices. As I told you before, we plan that next year natural rubber prices may stay around the average level of this year; under this assumption, there will be a recovery in terms of price mix, that will help recovering partially the profitability that we enjoyed until last year. Nevertheless, volumes will also help: we expect volumes to come back even in South America, Middle East and China, so overall an improvement in the EBIT and return on sale in the industrial business. As far as winter tire business is concerned, this is a very good year, an exceptional year, I would say, we have been selling very well till now, and better than the market, at least in Europe; we also expect a positive fourth quarter development, which will, overall, imply a record sales level for 2006. Working capital has been affected by the strong increase of sales; nevertheless, we plan to keep it under control by the end of the year, with a similar trend as last year.**

*Okay. Thank you. And two questions concerning... so that's a good debt level, can you just summarize what the situation is concerning the acquisition of DGAG and the impact on the debt at the end of the year? And all in all, here you state to be in your debt: what would be the impact of the acquisition of DGAG on the debt?*

**It's Carlo Puri speaking. For the DGAG... it's an already settled acquisition, with the same business model on which we are used to work; so, all the residential assets will be... are already sold to the JV between us and Deutsche Bank, 65:35; 35 is Pirelli Real Estate; the commercial assets are already sold with another binding contract between JV, Morgan Stanley, the fund of Morgan Stanley Misdres, Pirelli Real Estate 70:30; 30 is Pirelli Real Estate; and services and the platform of asset management will stay 100% to Pirelli Real Estate. So, at the end of the process, the impact will be something in the round of 80-85 million euro; at the beginning of the process, it will be 1.5.**

*But the process...*

**...and all the finance, with exception of this, is no-recourse finance to Pirelli Real Estate. So there is no guarantee from Pirelli Real Estate, no guarantee from Pirelli &Co.**

*Okay. Thank you. And just how long would be the process?*

**The process... you know, it depends on bureaucracy... it can be something between 4-7 months.**

*Okay. Thank you.*

**Thank you.**

**4. Mr. Damian Maltarp from Cazenove:**

*Yeah. Thank you very much. It's two questions. The first one: is it possible for you to tell us what the level of distributable reserves is, at the parent company level? Is that just a difference between the total shareholders equity and the share capital? And possibly, how should we expect that to change in the course of the rest of the year? And the second question is just on the Olimpia's shareholders' pact: could you just help me understand why you felt the need to enter into this pact? And what you expected to deliver? Thanks very much.*

**So, the Olimpia... I will start with the Olimpia pact: the Olimpia pact is basically a pact to keep stability in a time when there were a lot of rumors about weakness here and there; having planned to send off stake between us and Olimpia, I mean Pirelli and Benetton, we felt comfortable but there were a lot of rumors and the offer by Mediobanca and Generali, I think, to join us, to support the TI management, was a way to stabilize and to give more stability to an environment where there was a lot of misinformation going around about that, about many other stories. So, I think it was a good way to stabilize the situation, and to support the group or the company. Going to the second, that was the first, question: I give the floor to Mr. Riconte, who will provide you the details of the question about the reserves. Please, Mr. Riconte.**

**Thank you Mr. Tronchetti. The question, and the answer, quite simply: the net equity of the parent company before the devaluation was 4.7 billion euro, taking into account the devaluation, we will end up with a total capital of 2.936, out of which 2790 is the nominal share capital and the difference will be constituted by reserves for an amount of approximately 170 million euro. Thank you.**

*And that's fully distributable. It doesn't include any legal reserves, for example.*

**Yeah. Theoretically it's fully distributable, but of course it's not result because it's capital.**

*Sorry, just one final follow-up question: did you approach Mediobanca and Generali, or did they approach you?*

**Well, we got together by chance.**

*Okay, thanks very much.*

**Thank you.**

No more questions at the moment.

**5. Mr. Roman Zulauf from Merrill Lynch:**

*Okay. I have two questions at the moment. The first one: what are your net debt targets for the next two years? And what is the general outlook for your tire segment? Thank you.*

**Well, we think that the debt will stay around the existing level, we don't have any... we feel comfortable as we are. The tires... the tire business is growing fast thanks to the new plants we have built, thanks to the capacity; so we have built a new plant in China, a new plant in Romania, the new capacity in Brazil; so, I think we have a future of growth, mainly in the 'I' segment that is our core business, so we see that... we see growth.**

*Okay, thank you.*

**Thank you.**

No more questions at the moment.

**So, thank you very much to everybody. Thank you for being with us in this conference call. Good evening.**

Ladies and Gentlemen, the conference call is over. Thank you for calling Pirelli.

