Pirelli & C. Conference Call

Pirelli RE separation plan & 1Q'2010 Financial Results

Milan - May 5, 2010

Thank you and good morning ladies and gentlemen. Thank you for connecting to our conference call during which I shall introduce to you the Pirelli Real Estate's separation plan. Together with the top management of our Tire and Real Estate businesses I shall discuss with you the first quarter 2010 final results approved yesterday by both Boards of Directors.

Let's start from the Real Estate's separation plan, which will create value for both Pirelli & Co. and Pirelli Real Estate shareholders. In February 2009, when we presented the three-year plan, we stated that we wanted to focus on our core business and proceed with the reshaping of the assets in our portfolio, by dismissing those participations that we no longer regarded as strategic, while at the same time changing the perimeter of our broadband and real estate businesses. We have done a great deal of work in the last fifteen months, particularly in the real estate business. When the global economic crunch began, we had already rolled out a corporate reshaping program to put our company on the safe side. On the one hand, Pirelli & Co. granted to Pirelli Real Estate a 750 million euro credit line, allowing Pirelli Real Estate to deal with the downturn in the business without having to dismiss its key assets. On the other hand, we have turned the company upside down in order to allow it to express, once the crisis is over, its implicit value in which we believe. I wish to remind you that Pirelli Real Estate's overall value, given by the real estate business' net asset value, the NPL and SGR values, it is approximately 1.5 billion euros, as you can see on slide 21, or approximately 1 billion euros net of debt versus a current market capitalization of approximately 380 million euros. Therefore, we have changed and further streamlined our business model, switching from a trading to a mid-to-long term strategy with the purpose of maximizing current profits. We have reduced our headcounts from 3000 in 2007 to the current 1000. We have implemented a significant overhead cost reduction plan, which in 2010 will allow us to make further savings, worth approximately 100 million euros compared to 2008. Further to this and in terms of the current assets and financial profile, we reduced gearing to 0.7 after the successful 400 million euro capital increase finalized last summer and extended bank debt to medium term 24 months. Pirelli Real Estate is now starting to benefit from all the actions taken so far and this becomes evident from the gradual improvement of the operating results that will later be discussed by Mr. Malfatto. The real estate market is now showing the first signs of recovery. In the United States there are consistent signs of recovery, as recorded by the United States Census Bureau and the Department of Housing and Urban Development. Transactions increased by 26% in March compared with February this year and totaled +19% year-on-year. As it is customary under these circumstances, similar positive trends take a few more months to start in Europe, where we are exposed to more resilient markets. In Italy prices remain almost stable, with a slight increase in the number of transactions. The German residential market offers opportunities and in 2010 solidly continues along its stable track, with a slight improvement in the overall data related to rents and values. Rents are increasing between 2 and 3% in the major economic areas, while private investors with a good knowledge of the local market are the major buyers. It is also worth noting that foreign investors are back in the industrial real estate segment. In consideration of our corporate and market context, we thought that this was the right time to separate our real estate from our tire business, since we wanted them both to fully express their actual and potential values. Let's see the benefits expected for Pirelli & Co. shareholders. First, streamlining the shareholding structure and focusing on a single-business makes the equity story more visible and therefore more attractive to a greater number of institutions and investors. Second, the flexibility of our capital structure increases. Without Pirelli Real Estate, credit rating indexes improved, with a reduction of gross debt of over 400 million euros for Pirelli & Co., allowing for less expensive access to the capital market with potential benefits in terms of Parts expansion of our tire business.

Moving to slide number 4, before proceeding to assign Pirelli Real Estate shares, Pirelli & Co. will submit to the general shareholders' meeting, to be held by next July, the cancellation of the nominal value of the ordinary and saving shares, followed by a reverse stock split in the 1:11 ratio. Post reverse stock split par value will be 3.19 euros. Saving shares will be fully preserved and therefore no approval at the next shareholders meeting will be needed, nor any right of withdrawal will be triggered. This transaction is conceived to promote better stock trading by making the unit value of each share more transparent and an easier calculation of the dividend per share, earnings per share and multiples.

Moving to slide number 5: following the Pirelli & Co. reverse stock split, the total number of shares will be 487,991,493 of which 759,933.5 are Pirelli & Co.'s own portfolio shares. Pirelli & Co. and Pirelli Real Estate shares, amounting to approximately 58% of Pirelli Real Estate's capital, will be assigned to the 1:1 ratio. Pirelli & Co.'s own portfolio shares will not benefit from the assignment right which should be attributed proportionally to Pirelli & Co.'s ordinary and saving shareholders in the 1:1 ratio. To avoid having to assign fractions, Pirelli & Co. will maintain a stake in Pirelli Real Estate of 0.1% of the share capital. The assignment will take place through a reduction of Pirelli & Co.'s share capital, amounting to the portion assigned, based on the official price listing of Pirelli Real Estate's shares on the day before the general shareholders meeting.

Slide number 6: this slide shows that the general shareholders meeting is due to take place by the end of July and the actual assignment of Pirelli Real Estate's shares is due by next October.

Slide number 7: the equity structure changes I already commented at the beginning of my speech, so I won't go deeper into this matter; let's now talk about the first quarter results.

Moving to slide number 9 Pirelli & Co. closes the first quarter of 2010 with a marked improvement in all its businesses. Tire experienced a double digit growth and is among the best performers in the industry. Pirelli Real Estate is well on track, with an improvement of all major indicators. Breakeven was reached both at the EBIT and net income level. Pirelli Eco Technology posted a significant top-line improvement, a profitability increase and a debt reduction. We ended the quarter with a net attributable income positive for 39.2 million euros, a marked increase compared to the 9.5 million euros of the same period of last year. Finally, a careful management of the working capital, especially in the tire business, limited cash absorption despite business seasonality.

Let's skip the following two slides and move to slide number 12: a few more words on the net financial position. We ended the first quarter of 2010 with a net debt of 678 million euros and a cash absorption definitely lower than in the first quarter of 2009, the major drivers being: a more efficient level of stocks in tire and the group's stringent policy on commercial credit. The quarter was characterized by a 50 million euro investment, mainly tires, fully offset by depreciations. Finally, the 2009 restructuring program cash-out is worth 38 million euros, the total cash-out is 60 to 70 million euros, this is the figure expected for 2010.

Slide number 13: Pirelli's gross debt amounts to 1.8 billion, with 74% maturing starting from 2011… 2012, sorry. Pirelli can count on 925 million euros of committed credit lines, which increased by 100 million euros compared to the end of December 2009. Such variation is due to a partial refund of Pirelli Tire's credit lines.

Slide number 14: following the strong performance of Pirelli Tire in the first quarter 2010, we are raising our target for 2010 full-year. We forcast revenues between 4.9 and 5 billion euros versus 4.7-4.8 billion, and EBIT margin after restructuring costs of at least 6.5%. We confirm our guidance both on capital expenditure, that was 300 million euros, and on net debt of approximately 700 million euros. This slide also shows our guidance excluding Pirelli Real Estate from the consolidation perimeter, a revenue range of 4.6-4.7 billion and an EBIT margin in excess of at least 6.5%.
Now I thank you for your attention and I'll leave the floor to my colleagues who will discuss in greater detail the results reached in the first quarter of 2010 in each business. During the Q&A session, I will be available to answer your questions. And now I'll leave the floor to Mr. Malfatto. Please.

Thank you, Mr. Tronchetti. And good morning to everybody.
Before discussing the results in detail I wish to give you a few general indications on the real estate market trends. In the first quarter of the year, the real estate market, particularly in Italy, showed signs of stability, which confirmed our view that the worst is behind us. In some European real estate markets, and I'm referring specifically to the UK and to some extent Germany, particularly in the residential sector, mention has already been made of recovery, albeit a slow one. In Italy there was a slight increase in real estate transactions. But the size remains quite limited. Those involving properties of less than 1,000 square meters represent 70% of the total. And larger transactions are still suffering from the credit crunch.

In the next slide I would like to compare the quarterly results with some indications as to the sale at the end of April with 2009 results and the full-year 2010 targets. In general, and I'm pleased to point it out, in first quarter 2010 all the key performance indicators showed a strong improvement, compared to the same period of 2009, confirming the soundness of this business model and of the actions taken in the last 12-18 months. For the first time in 7 consecutive quarters, the company's closing the first quarter of the year with both a positive EBIT and a positive, albeit to a smaller extent, net profit. We are therefore confirming the targets for full-year 2010 already announced. In terms of real estate sales, I would like to give you the latest update on the total sales at the end of April, which come to approximately 400 million compared with the approximately 240 million in the same period of last year. This points to an overall market improvement and to the strength of our sales network. We will look at the sales trends more in detail in the slide that follows. I'm therefore very confident that we will be able to reach the full-year sales target of between 1.3 and 1.5 billion already disclosed to you. With regard to EBIT for the services platform including G&A, the result for the first quarter is positive and comes to approximately 5 million, marking a major improvement compared to the same period of last year. On the basis of this result, we are confirming the full-year target range of between +20 and +30 million. With regard to cost savings, we continue to benefit from the restructuring plan implemented in 2009. In the first quarter we achieved approximately 50% of the savings planned for the year, in line with our forecast. We are confident that we will reach the announced full-year target range of between 25 and 30 million. Coming to the net financial position, this is basically in line with the 2009 announcement, which confirms the strengthening of our financial structure. The 0.69 gearing remains basically unchanged with respect to December 2009 and greatly improved with respect to the 2.81 recorded in March 2009.

As you can see on slide 17, the result for the first quarter 2010 confirms the company's improved performance with a net profit that comes to 0.4 million, compared to a loss of 15.8 million in the first quarter 2009. The result is entirely attributable to the company's ordinary operations, which include recurring profit from the service platform and profit from investments, as there were neither restructuring charges nor write-downs nor revaluations of the co-investments and the investments in funds and vehicle companies. With regard to appraisals, I wish to remind you that these are normally made every six months, in June and December of each year, but we do not expect to see any great changes, as we believe that the market and our book values have reached the bottom of the Italian real estate cycle. Let's now look at the EBIT including income from equity participation and interest income on shareholders loans to funds and vehicle companies. As we saw earlier, this shows a positive 10.3 million euros. As you can see on the total column on the right, the service platform shows a positive result of 5 million, net of G&A costs, versus a loss of 1.3 million in the previous financial year. Turning to the results in the different sectors, starting with Italy, we can see an overall 13.1 million improvement of both the service platform and the vehicle companies and funds compared to last year. The improvement of the service platform is attributable to an overall improvement in efficiency, while the investment activities reflect the lower impact of the hedging derivatives and the disposal of non-strategic equity investments, which had generated losses in the past, and I'm referring to the equity investments in UPIM and Italia Turismo; as for Germany, we exceeded breakeven, with both the service platform and investments in black. This was also due to the positive effects of a more efficient management and cost savings. More precisely, the investments benefited from a lower impact of hedging derivatives and better financial and operating management. Poland reached breakeven, whilst waiting for the completion of the urban authorization process of the Lucchini site. There was also an improvement in the NPLs in terms of both investments and credit servicing. Lastly, G&A dropped with respect to the first quarter 2009, which had already shown great improvement over 2008. Let's now see the way sales developed: as already mentioned, data for April greatly improved compared to the same period of 2009. Sales were approximately worth 400 million euros against approximately 243 million euros in April 2009, even if in March 2010 sales were 28 million euro lower than in March 2009. The April figure allows us to be confident in reaching the year-end targets, as announced to the market, within a range of between 1.3 and 1.5 billion euros. This shows how impactful our actions are and the effectiveness of our network also in a situation of market instability. Our future strategy will therefore be freeing our capital invested in no longer strategic investments and rebalancing our portfolio to an increasingly higher quality of assets, particularly in Italy. Incidentally, this result was achieved by keeping the best assets in our portfolio, the so-called "trophy assets", like the Rinascente building or Cloesan assets, just to mention a few and selling low-yield limited value potential and non-strategic assets. The overall April sales reduced gross margin of approximately 3.1%; our sales for this fiscal year in Italy is expected to reach approximately 1,050 billion euros… sorry, 1.50 billion euros, of which approximately 250

million euros from development projects, approximately 200 million euros from Soho and trading assets with very low yields and other non-core assets worth approximately 600 million euros. Our target in Germany is to make approximately 300 million euros worth of sales, whilst in Poland we aim to reach approximately 50 million euros.
Moving to the following slide, you can see the trend of our managed portfolio. In March this year our assets under management are worth 16.4 billion euros, of which 13.9 billion are basically co-invested, in line with our 2009 year-end targets. The decrease is due to the sale made over the period under scrutiny, while our managed portfolio increased by 600 million euros and reached 1 billion euros, in line with the current strategy aiming at increasing our enlisted portfolio mainly through management contracts.
Next slide, please. In the slide you can see the key data of our invested portfolio by geographical area. I wish to point out that the figures are assessed internally. As you perfectly know, our portfolio is submitted to an independent third party appraisal in June and December each year. The situation is practically stable if compared to year-end 2009. The net asset value stands at 1.2 billion euros and unrealized capital gains are approximately 180 million euros. Total net invested capital is of approximately 1.183 million, of which 865 million in real estate and with an exposure abroad of approximately 250 million.
Let’s have a look at the next slide: overall savings in the first quarter amount to 14.2 million euros, equal to approximately 50% of the full-year target. I’ll now hand over to Mr. Claudio De Conto who will comment on the financial position.

Thank you, Giulio, and good morning everyone.
If you could please move to slide 23, I would like to show some more details on the status of the separation. As you can see, both banks and partners have positively looked upon the transaction. Indeed banks, from which the waiver was necessary from the transaction, have all granted the waivers for the change of control. And you see the list. And almost all partners, partners in our real estate vehicles, have agreed; we are only waiting for the finalization of the ongoing negotiation with Merrill Lynch which, in any case, will not affect the feasibility of the overall transaction and does not have any material impact on the company. For the purpose of information, the net invested capital of the funds that we have with them… for Pirelli Real Estate the net invested capital, I repeat, is of approximately 12 million euros and the pro-quota NAV is of approximately 13 million euros. So, let’s say that all that was needed has been achieved.
If we go to the following slide, and we can comment on the evolution of the net financial position, not including shareholders loans, as of March 31st, you can see that it is negative for 458.6 million euros, and is substantially in line with the December 2009 446 million euros. The 12.8 million euro difference compared with December is attributable to the combined effect of a debt reduction of 8.8 million euros, thanks to sales and distribution from investment, and an increase mostly due to the payment of interest as well as restructuring cost capex and equity contribution to participated vehicles and funds.
If we move to slide 25, in this slide we’d like to show you the development of Pirelli Real Estate pre- and post-separation corporate lines. After the transaction the committed lines amount to 580 million euros, and that includes confirmation by Pirelli & Co. of 150 million euro lines, of which the terms and conditions will be in line with the Club Deal ones.
If we go to the slide which shows some details about the financial situation of participated vehicles and funds, we can see that as far as the financial situation on investment funds and vehicles is concerned, given assets for 15.4 billion, the overall net bank debt is 10.9 billion, of which 2.9 billion is the real estate pro-quota debt; I, as usual, wish to remind you that this is a non-recourse debt, with the exception of 29 million, and, as you can see on

the right side of the slide, the refinancing needs for maturity amount to 200 million as far as 2010 is concerned, 400 2011 and 500 2012. Refinancing needs for all the vehicles in the short term also thanks to the recent agreement reached in Germany, with the banks financing the Highstreet deal is limited. In fact, in 2010 the refinancing need amounts to the approximately 200 million previously mentioned. It is worth underlining that in the three years after 2012 the refinancing needs in Germany are very limited, to only about 12% of the total, and if you focus on the main characteristics of the pro-quota debt, you can read that the overall real estate portfolio loan-to-value is 67%, with Italy, which has a slight improvement and is reduced to 57, Germany 79 and Poland 40, substantially stable vis-à-vis 2009. The average duration is 3.2 years, but I can provide you with the information that if you look at the duration for Germany that is in excess of 4 years and therefore the one with the shortest duration is Italy, which is the one with the lowest loan-to-value ratio, that in theory implies that the refinancing shouldn't pose any serious issue.
If we can now finally move to the last slide, slide 27, which does show you a view of the balance sheet, I'm not going through the lines because I don't think there's any major movement to comment, but I just want to highlight to you the solidity of the company, which is fortified by the gearing ratio, which remains below 0.7.
Thank you and I'll now leave the floor to Mr. Francesco Gori.

Thank you Mr. De Conto, and I would like to move to slide 29: Q1 2010 results confirm Pirelli Tire as one of the strong performers in the industry, a 20% top-line growth, 19% net of exchange rate impact, supported by both a positive volume growth trend and a price/mix increase of 1.4% versus an average of -2 of the peers; the price/mix main drivers being: our product/mix improvement, by continuous innovation and high quality, that's typically been among Pirelli's main brand features. The price increase impact will be visible starting from Q2 2010. High profitability with margin close to 9% and a 50 million euro net profit close to Q4 results. The keys of these good results are: a value-based strategy in mature markets, Europe and North America, with a strong top-of-the-range positioning, an effective presence in high-growth markets, and a careful cost control policy.

Moving to slide 30: let's take a closer look at performance by geographical areas. The weight of emerging markets accounting for 49% of total sales, with +3 percentage points compared to Q1 2009 is growing. LatAm leads the growth, due to our presence in Mercosur, where we strengthened our market leadership. In Europe, 42% of sales, a 10% year-on-year growth, will benefit from both the production recovery of the prestige and premium car segments, segments that did not enjoy State incentives last year and are not enjoying State incentives this year, as well as the positive trend of green performance tires in the Replacement business, above our earlier expectations and testifying our end-customers' appreciation, when it comes to green and high-performing products. North America, where Pirelli's the only present in the consumer segment, is one of our target countries. We focus our various strategies with a selective approach in both the management of the distribution network and the partnerships with major Premium and Prestige European OEMs, while we keep supplying our US OEMs only on their top-of-the-range vehicles.

Moving to the next slide, number 31: our savings program continues in line with our full-year target of 60 million euros. Our savings plan highlights includes production increase in low-cost countries, continuous actions to achieve efficiencies in raw material usage and weight and further actions on discretionary costs. I wish to remind you, however, that in Q1

2010, while starting to benefit savings from the Spanish plant shut-down, our results are impacted by the start-up costs of the new Italian factory in Settimo Torinese.

Next slide 32: looking at the profitability trend, the year-on-year improvement drivers are: a strong volume growth, a positive price/mix impact and efficiencies from restructuring programs and full use of car and production capacity. As to raw materials, the cost increase impact into our P&L in Q1 is substantially offset by a positive exchange rate, due to the appreciation of the Brazilian and Romanian currencies versus the US dollar. Other input cost variations, worth 7.4 million euros, are mainly linked to inflation, given our exposure in high-inflation countries. And, finally the variation of other costs reflects both allocations of the incentive plan to senior management, 3 million euros not included in Q1 2009, and higher R&D costs and marketing expenses.

Next slide, number 33: we close our Q1 2010 with a net debt of 1.1 billion and a cash absorption definitely lower than in Q1 2009, the major drivers being: a low level of stocks and a stringent policy on commercial credits. Q1 is characterized by 48 million euros of investments, +10 million euros on 2009, totally offset by depreciations. The 2010 investment plan is worth well above 300 million euros, to allow Pirelli to increase its production capacity by 20% by the end of 2011. Finally, the cash-out due to the 2009 restructuring program is worth 22 million euros, approximately 50% of the total cash-out for Tire in 2010.

Let's now briefly analyze each business segment and its market trends. Slide 34: consumer business. Q1 data confirms the overall market recovery, despite we are still far from pre-crisis levels in Europe and North America. In Original Equipment Q1 2010 acceleration is connected to the recovery of the car production and North America leads the way with a 70% year-on-year growth. In the less volatile Replacement segment, dealers restocking supported Q1 growth.

Slide 35: the performance of Pirelli Tire in the consumer segment is characterized by a top-line double-digit growth driven by the positive sales trend in the major markets and by the price/mix improvement, despite the Original Equipment channel's higher weight, some 4 points more than in Q1 2009. As already mentioned, the price/mix main driver in the consumer segment is the product/mix improvement for both the Replacement and OE businesses. Profitability definitely improving at +66% year-on-year.
In the following slide I wish to highlight the outcome of the Pirelli Tire continuous innovation, slide 36. We recently introduced a new product in the green performance platform: Scorpion Verde, the new tire for the SUV and crossover segments. Pirelli's superior quality standards were also highlighted by the recognition offered by the intensive tests made by the German ADAC and Swiss automobile clubs, highlighting both Cinturato P7 and Cinturato P6 as the best tested tires; these tests are made available to over 20 million drivers in those key markets.

Next slide, 37: Pirelli's top quality has also recently been acknowledged with the 2010 JD Power award in the US in the performance segment of their OE Tire Customer Satisfaction Study.

And next slide, 38: in the motorbike segment, where Pirelli's the leader, we introduced the first tire that can be customized by the end-user, Diablo Rosso Corsa, adding a multi-zone compound technology derived from our World Superbike recent experience.

Let's now move to the industrial business, on slide 39: the overall recovery of the economy, although different in the various geographical areas, is having a positive impact on our industrial business, with a significant year-on-year improvement in tire sales. Also in Q1 Mercosur leads the growth in the Original Equipment business and consolidates the recovery trend in the Replacement business.

The next slide, 40: some positioning in the emerging markets allow Pirelli Tire to close this quarter with a record 28% revenue growth and a profitability further increasing to 8.7%, +1.2 percentage points versus the previous year. Revenues performance drivers being: volume supported growth, +24%, and price/mix improvement by 1.8%.
Moving to slide 41: Pirelli has developed a green performance truck tire too, Series 01 both low rolling resistance, fuel saving, less CO2 emission, retreadability, improved mileage and a remarkable low noise level.

Next slide, 42: one of the main issues is the ability by the industry to overturn the current raw material cost increase. The progressive increase in the price of natural rubber wasn't expected. A number of factors did play a role: from the bad weather conditions in Asia to a strong recovery in tire production, especially in China, as well as speculative actions on natural rubber prices and, finally the political crisis in Thailand. Knowing what were the major causes is not going to take us far, yet the conclusion is that it is unlikely that the average price in 2010 will go much below 3000 dollars per ton if tire demand remains positive till year end. In this scenario, Pirelli was among the first few players to pioneer price increases. Prices are being increased in all markets worldwide and we just announced a second rubber price increase in North America valid from July 1st. Further increases might be enforced in the second half of 2010, where market demand keeps growing strongly.

Next slide, 43: our strong Q1 performance within a framework of better awareness in terms of price increase by the industry led us to review our targets for the current year. We are forecasting a 10% or more top-line growth if compared to an initial 6-8% target, an EBIT floor of between 320 and 330 million euros, assuming the raw material cost headwind higher than 250 million euros, while the guidance on capex is, of course, confirmed.
Moving to Pirelli Eco Technology on slide 44, the trends improved in Q1 in terms of revenue/mix, filters accounting for 46% of the sales; operating results: losses halved if compared to Q4 09, despite the negative impact of the Chinese start-up program to build our filters factory. Reduction of debts achieved through a careful working capital management policy. 2010 targets are confirmed, with a double-digit revenue growth, and operating results at breakeven, together with a positive cash-flow generation.

We have come to the end of my presentation, and I hand over to Mr. Tronchetti.

Thank you, Mr. Gori. We are now ready for the Q&A session.

Q&A session:

1. Mr. Francesco Previtera from Banca Akros:

Yes. Good morning everybody. Just one question regarding the Pirelli Real Estate capital increase. You said that it will be a 10% of the shareholders capital; if you can explain the amount and the condition how it will be set and if the two banks will get the whole capital increase or if they are going to cover part of it? The second detail was about the financing between Pirelli & Co. and Pirelli Real Estate if this capital increase will be devoted to completely reimburse this line. Thank you.

Thank you. So, first of all, the capital increase is up to 10%. What we have in mind and we have agreed with Mediobanca and Unicredito is that they will be covering a reserved capital increase of 20 million, 10 each. This capital increase will be finalized when we will split the company and we will deliver the shares in October next to shareholders. The price will be the market price when the transaction will be finalized. So, this is a capital increase that we mentioned is “up to” but in fact is 20 million.
Second, it has nothing to do with the financing of Pirelli & Co. or Pirelli Real Estate. Pirelli & Co. has a “pari passo” with the other lenders to Pirelli Real Estate and so the repayment of the financing will be made “pari passo” to each of the lenders, including Pirelli & Co.

2. Ms. Monica Bosio from Banca IMI:

Yes, good morning. My question is on raw materials on Pirelli Tire. The new assumption for the headwind is 250 million, I assume that this 250 million still accounts to the recent price increase in North America, but does not account likely future price increases. Maybe in Europe. My question is: are you keen to further increase prices in Europe? Maybe starting from, let’s say, July? And if so, could you please quantify the further 4% increase the potential offset from raw materials… for the gain that you could have gained given the current raw material conditions? And the second question is more general: how do you see the current raw material situation for the next year? Do you believe that these levels are sustainable also for the next year? Thank you.

Yes. The 250 million euro headwind is concerning the raw materials extra costs. To compensate these extra costs we believe we will be able to partially offset with the 3% overall price/mix improvement full year and clearly with the extra volumes. Of course Europe is included in the price increase action. On chart 42 you will see the major markets where we have increased or we are increasing prices. And in the case of the US we are going to have a second round in summertime, which might happen also in Europe, even though at this time the industry is executing the first round only.
As far as raw material prices next year, I’m sorry, I don’t know, but I think that with the speed of entry of the industry that is capitalizing price increases in the second half, the industry should be well-positioned, let me say, to any changes… any non-dramatic changes in the raw material structure costs.

Okay. Thank you very much. So, if we assume that maybe you’re going to do a second round in the price increase in Europe, could I assume that the 330 million euros of EBIT for *tires is really a floor and that there could be really some upside potential thanks to the price increase, a second round of the price increase in Europe?*

It does not depend on us only, it is also depending on the reaction of the competitors, but the price increase in America, the second round is showing that the industry does want to compensate for these extra costs.

Okay.

Of course the demand is the real driver. So, we have to look at what the demand level in the second half will be. We feel positive on the third quarter because of the winter season in Europe, the restocking of dealers and so on, and there's always a question mark on the fourth quarter.

Okay.

More specifically, when you put a floor you do all the best to improve it.

Okay.

So I think that that is the answer.

Okay. Thank you very much.

3. Mr. Edoardo Spina from Morgan Stanley:

Yes. Good morning. Thank you. I would have four questions, actually, if possible. The first one is on raw materials, a follow-up on a previous question. If I assume all the commodity prices where they are, is it reasonable to forecast headwind for next year of around 1 million? Is that, like, a reasonable number or just too much or too little? The second question is on price increases in Latin America… in South America: if you could give us some color on the magnitude of these increases? Are they closer to the ones, let's say, 10% that you do in Africa or the 4% in North America? And if you could give us some color as well on how they're… you know, developing? Is it easier to implement them there than it is in Europe? Or, I don't know, any color on that would be great. The other question is on the Formula 1 costs: I saw you are participating in the… are bidding for the supply. Bridgestone disclosed 70 million US dollars last year for costs, and I was wondering whether this could be a good comparable… comparison for your costs? Or what you expect on that side. And very lastly on Africa and the Middle East: any guidance for a volume increase in the region? Is it reasonable to assume high-teens growth in volumes? Thank you very much.

I will answer to some questions and then I'll hand over to Mr. Tronchetti concerning the Formula 1 issue. Raw materials 2011 is an average on average. If prices remain the same, as Q1 was better than… was lower in terms of costs, you may have this, let's say, 100 million euro increase over the period. Yes. Something like that. Latin America price management is a much different one than in Europe for many reasons: number 1) the exchange rate is part of the price game and the… it keeps changing, and you have, I mean, a strong real, a weak Argentinean pesos, an improbable bolivar in Venezuela, so, I mean, you can imagine that there is no percentage and every month, if not every week, our people manages prices looking at the exchange rate. This helps a lot and makes life easier, because dealers… everybody, consumers, are educated to changing price environments. So, because of this, historically and still today the price management is much more flexible in that region of the world than in mature markets. But I cannot give you a percentage, because it goes from double-digit in certain countries to a zero level in Brazil which is, however, compensating with a strong exchange rate. Middle East Africa: yes, we target volume growth. Unfortunately this year you saw it in Q1, we were not able to support it because factory saturation did not allow us to have extra tires available for this area and we privileged Pacific Asia, Europe, North and South America.

Okay. Thank you.

So, going to the Formula 1. So, we entered into discussion to supply Formula 1 next year, because we have the technology, the people, the brand to do it and the target is to supply Formula 1 to make some money, not to lose some money. So, this is why we entered into discussion. So, nothing to do with what has happened in the past and I think that the discussions that are going on are based on the fact that no one can afford to do any business losing money. So that's the reason why we believe that there is an opportunity, both for the teams and for Pirelli to leverage on brand and technology, and to make a good deal for both Formula 1 and Pirelli.

Okay. Thank you very much.

4. Mr. Martino De Ambroggi from Equita SIM:

Thank you. Good morning everybody. Three questions on tires: the first is if you can elaborate a bit more on the +10% growth of sales for the tire business split between the different effects that you have in your mind. The second question concerns the natural rubber average cost: what is your current assumption included in the 250 million headwind for the current year? It was 3000 dollars per ton in your previous indication. And the third one is not directly concerning Pirelli Tire, but you gave a guidance for net debt for the entire group flat, so always in the region of 700 million, while I thought the net working capital would have absorbed something, because of the growth in raw material costs. So I was wondering how much of the Pirelli Real Estate rights issue is included? If it's only 20 million well, the question doesn't make any sense… but just a clarification on it. And why the net working capital is not affecting such a figure. Plus I have two follow-up questions on other issues. Thanks.

I'll start with the financial position. So, the guidance we confirm is the 700 million at year-end, the working capital increase we consider within this figure is an increase of 15 million, which can be absorbed thanks to a better handling of all areas, including stocks, and there is nothing linked to the capital increase of Pirelli Real Estate because we consider it with the company already split.

Concerning the 10% growth, it's basically split in: at least 7% comes from volumes and 3% or more coming from price/mix. Concerning the natural rubber price, I think we already told you we plan our results on an average 3000 dollars and, I mean, every week the scenario is fluctuating, now it's going a bit down, of course the 3000 dollars per ton is referring to the most popular grade of natural rubber, the so-called TSR trading, not the more expensive RSS3. Now, again, the price today is a bit lower than 3000 dollars per ton but at least experts say that by August or September with the winter season in Indonesia prices may go up again, so the average will be around 3000 dollars and we think we can manage our results around this average.

Okay. It is basically unchanged. And could you remind us the split between the RSS3 and the TSR 20? It's 10-90 if I'm not wrong?

No, in our case, given the high price of RSS3, we are of course moving down to 10%.

Okay.

I mean, it's clear, we are… we are reducing to this level.

Okay. And the two follow-up questions are: one regarding the (…) losses in the parent company; if there is any update for the possible utilization becoming just one company after Pirelli RE's spin-off? And the last one: I understand that the Pirelli RE rights issue is a one-off event, it seems to be only 20 million, but if it's not so I understand that the qualitative impact of such news but what are the reasons for this rights issue? Obviously, if there is some more rights issue to be done. If it's only 20 million euros, the message is clear.

So, the losses in the balance sheet that can be valued reducing taxation are only linked to Olympia, but mainly linked to Olympia and will remain in the balance sheet of Pirelli & Co. What we are doing, also with the support of an important consultant, is to maximize the efficiency in our fiscal planning and so we don't need, we mentioned in the past, the merger between Pirelli Tyre and Pirelli & Co., we have seen that there is no fiscal advantage because on a consolidated basis we have the same result, we… the best we had out of it was the reduction of costs we already implemented last year, but what we are focused on today is mainly reducing the impact of taxation thanks to a better planning and I think we can have some results out of it within the next twelve months.

Is it too early to talk about a potential target?

Now it's too early, because we are doing some actions, we are studying some other actions, so we don't have yet a picture that can be delivered to the market. Anyhow, there will be an improvement.

Okay.

For the capital increase it's a one-shot event, it's a sign of commitment on the one hand and of confidence that we consider very positively. That's why we agreed with Mediobanca and Unicredito to do it. But it's a one-off and no one else is expected to enter into this capital increase. So, the capital increase will be 20 million.

Okay. Perfect. Thank you.

Thank you.

5. Mr. Alberto Villa from Intermonte:

Hi to everybody. I have a few questions on the real estate business. The first one is on some press rumors we've been reading recently about the syndicated part and the commitment to lock up the shares of Pirelli Real Estate coming from the split. Can you comment on that? Or giving us… give us some anticipation? There were also rumors about new, let's say, industrial or non-financial shareholders being new potential partners or new future shareholders being interested and looking at Pirelli Real Estate. Is there anything going on at this stage? And my second question is on disposals target for the real estate: I understand you had an acceleration in April. Can you give us an idea of how it is developing in terms of the selling price compared to the open market value of the assets you're selling? And most of the targets of the disposals come from Italy; are you having negotiations ongoing that make you confident about reaching those targets? My final question is on Karstadt and Baubecon, which are the two, let's say, more critical portfolios in Germany. Is there any news on those two names? Especially because we have seen there has been a postponement in the selling of the operating activities of Karstadt. Are there any new thoughts on the resolution of this portfolio or the future exit of this portfolio? Thank you.

Thank you. So, starting with the lock up: the lock up in Pirelli Real Estate after the splitting will be the… within the shareholders that are part of the syndicate of Pirelli & Co. Most of them have already indicated their interest in being part of it. No one else… the only one… new entry will be Unicredito, and Fonsai and Allianz and Lucchini probably will not be part of it, but anyhow will be lower than 30% and the shareholders have already mentioned their intent to be part of it.

Unicredito and Mediobanca will be part as well?

Yes, they will.

Okay.

Yes, they have declared their interest to be part of it.

Okay.

So, no one else is in touch with us, there are no negotiations going on. Anything you read here and there is without any ground, it's meaningless, or it's only rumors without contacts with us. And we don't want to have any contact with… what we are looking for now is to increase our portfolio, to have a larger, let's say, portfolio under management, it's increasing and we have… we hope to have some good news in the next months on that. And so, nothing on that side. About Germany, now Mr. Malfatto will provide you with an answer. The first answer I want to provide you with is that the portfolio we sold until now in April is more than 400 million euros, there are no losses, there is a plus 3.5% average, even if the portfolio we sold is largely linked to low-yield assets and to no-yield assets. So that means that the market, as Mr. Malfatto mentioned at the beginning, is providing some positive signs, also in Germany. But now I'll leave the floor to Mr. Malfatto to say more about Germany.

Yes, coming back to the disposal process, and to what has been told by Mr. Tronchetti, that we have in pipeline some discussions for the sale of some land and development activities, because our strategy is to focus on building assets and selling both: part of the development and part of the SOHO asset. So we are quite confident to reach our target by the end of the year. As far as Germany is concerned, for Baubecon we are continuing to reduce the vacancy rate… now we are continuing to reduce the vacancy… the vacancy rate. We started last year with over 6.5% of vacancy rate and we reached right now less than 5%. We are discussing even with the Blender for discussing the issue of the covenant for the cure of the covenants and we are quite confident of reaching an agreement in a short time. As far as concerned Karstadt, as you may know, the credit committee has delayed the date for the approval of the cash-in plan by the end of May. We have in due diligence two bidders for the Karstadt group: one is Kritten and the second one has not been disclosed by the liquidator and even some of the shareholders could be interested in looking at the company with the aim of keeping great concern of the company that will create value for the property company thanks to the agreement we reached in February for the restructuring of the financing with banks.

Thank you very much.

6. Mr. Giuseppe Puglisi from Intermonte:

Good morning, Puglisi, Intermonte. I have two questions on Pirelli Tire. The first one regards the utilization rate: I would like to know what is the actual factory utilization rate in the different geographic areas. The second regards the price management: I would like to understand… better understand what is your capability to increase prices in the different geographic areas without increasing distressed counts? And so if there is some difference between, for instance, Mercosur and Europe or the US? And the third one regards the delivery time: I would like to know what is actually your average delivery time to dealers and if it's increasing or reducing? Thank you.

So, as far as the first question is concerned, Q1 has been running at very high capacity utilization levels, differently, of course, from Q1 2009, which has been the lowest overall. So, I mean, the percentage depends on what you put under the fraction. In our company we put 360 days, which is the theoretical maximum, and so to be well above 90% implies a very high utilization rate. As far as the price increase by area, with the exception of Latin America for the reasons I said in answering another question before, which makes price increase a function of the exchange rate and definitely an easier game than in other countries, Europe, North America basically have no major difference in pricing to the end-user. It depends a bit on the taxes, of course taxes are higher in Europe, with VAT, but that's it, there's no major difference, at least as far as Pirelli is concerned. Prices are a bit weaker, lower in Middle East Africa and then, again, in Asia Pacific relatively lower than Europe and North America but higher than Middle East Africa. That's it. As far as the delivery timing to our dealers, it depends on the agreement we have with these dealers. The dealers that are loyal to Pirelli have the shortest available time; we can also deliver twice in a day in certain areas, and then, of course, as far as winter season is concerned, we need to have dealers planning well in advance what they want to buy and they normally tell us what they want to buy starting already in July and so we are able to deliver to them in September-October, according to their order. So it is a planning approach similar to the car industry.

Yes, but given the high utilization rate, do you have some difficulties in some countries to maintain the delivery time assigned with the dealers?

Frankly speaking, it depends on the level of demand. If the planning has been well done. Of course Q1, if you look at the performance in volumes in the truck and in the industrial business, it's been very high and we've been suffering deliveries here and there, as I believe most of our competitors. but I would say this is the exception. Normally we are able to comply with the requirements.

And so you don't see any problem coming in the next few quarters? With the actual level of utilization.

No, well, of course still a tense situation between supply and demand, because I told you that our saturation is as high as more than 90%, but that's okay.

7. Mr. Gabriele Parini from Unicredit:

Yes, good morning, gentlemen. Just a question on the price environment in the… again… in the tire sector: I mean, obviously, we have seen all the announcements of price increases made by you and by your competitors, but my question is: what's your perception on the real or effective price increase currently in the market? I mean, do you see any risk of some of your competitors trying to gain market share keeping however prices low? Or do you believe that there is still a strict and close price listing within the sector? Thanks.

There is no discipline. If there was a good discipline, the industry would have raised prices on January 1st, because it was clear that the demand was coming strong, compared with Q1 09 and also Q4 09 had been a strong quarter in terms of sales, stocks were low, nevertheless, the industry was not so intelligent to increase prices at that time. So, as you see, there are still competitors who try and buy market share with no results, because if they do not increase prices, we do not increase prices. Now, after a quarter that has been one of the strongest in terms of demand, at least on the Replacement side, everybody's increasing prices. And we are too, of course. That's why we say we are pioneers in increasing prices. On the side of the impact on sales, if there is any consequence of a higher price versus the end-use of demand, given that the tire is a distressed purchase, which means you purchase a tire maybe every couple of years, if any, there is really no link between a one-digit percentage increase in the price of the tire and the end-use of demand. So, I think it's more linked to the raw materials, to the balance sheets of the tire manufacturers and I don't see anybody today able to be aggressive with the current level of price of raw materials.

If there are no other questions, I wish to express my most utmost thanks for your patience and endurance during the conference call and we’re looking forward to meeting you in Milan during our road show, and our investor relations team is available for any questions you may have. So, thanks a lot and see you soon during our road show.

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