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

Quarterly Report

at September 30, 2008

PIRELLI & C. Società per Azioni

Registered office in Milan, Via G. Negri 10

Share capital - Euros 1,556,692,865.28

Milan Companies Register No. 00860340157

Economic Administrative File (REA) No. 1055

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Board of Directors [1]

Chairman [2]	Marco Tronchetti Provera
Deputy Chairman [2]	Alberto Pirelli
Deputy Chairman [2]	Carlo Alessandro Puri Negri
Directors:	Carlo Acutis *
	Carlo Angelici * o
	Cristiano Antonelli *
	Gilberto Benetton
	Alberto Bombassei * ^
	Franco Bruni * o
	Luigi Campiglio *
	Enrico Tommaso Cucchiani
	Berardino Libonati * ^
	Giulia Maria Ligresti
	Massimo Moratti
	Renato Pagliaro
	Umberto Paolucci *
	Giovanni Perissinotto
	Giampiero Pesenti * ^
	Luigi Roth *
	Carlo Secchi * o

* Independent director
o Member of the Internal Control and Corporate Governance Committee
^ Member of the Remuneration Committee

Secretary to the Board	Anna Chiara Svelto

Board of Statutory Auditors [3]

Chairman	Luigi Guatri
Standing members	Enrico Laghi
	Paolo Domenico Sfameni
Alternate members	Franco Ghiringhelli
	Luigi Guerra

General Manager

Operations	Claudio De Conto

Independent Auditors [4]

Reconta Ernst & Young S.p.A.

Manager responsible for the preparation of the financial reports of the company [5]

Claudio De Conto

1 Appointment: April 29, 2008. Expiry: shareholders' meeting called to approve the financial statements at December 31, 2010.
2 Post: conferred by the board of directors' meeting held on April 29, 2008.
3 Appointment: April 21, 2006. Expiry: shareholders' meeting called to approve the financial statements at December 31, 2008. Paolo Domenico Sfameni was appointed by the shareholders' meeting held on April 29, 2008 to replace Paolo Francesco Lazzati who resigned.
4 Post: conferred by the shareholders' meeting held on April 29, 2008.
5 Appointment: conferred by the board of directors' meeting held on April 29, 2008. Expiry: shareholders' meeting called to approve the financial statements at December 31, 2010.

INTERIM MANAGEMENT REPORT

During the first nine months of 2008, the **results of the Pirelli & C. S.p.A. Group** were influenced by the impact of the international financial crisis on the two main reference sectors (automotive and real estate) and on the levels of consumption, especially in Europe and North America.

The **tyre market** reported a growing weakness during the first nine months due to a combination of factors. In terms of volumes, the replacements channel, which generates most of the sales in the business, was penalized by a reduction in demand, especially in Western markets (both in the consumer and industrial markets), whereas, in the original equipment market, the marked fall in car registrations in Western Europe had a major impact (-10% in the third quarter, -5% in the first nine months compared to 2007) and in North America (-15% in the third quarter, -11% in the first nine months compared to 2007). The scenario also deteriorated in some of the emerging countries like China. In terms of margins, the sector suffered from the sharp rise in the prices of raw materials, which reached their highest peaks of the year in the third quarter, before beginning to fall rapidly. Pirelli will benefit from this especially from the first quarter of 2009 onwards. The rise in raw material costs meant a corresponding increase in the group’s costs in the first nine months of Euros 121 million (Euros 76 million in the third quarter alone).

The difficult economic situation continues in the **real estate market**, which was penalized by the fall in prices, the slowdown in transactions and difficulties in accessing credit, as well as a general climate of mistrust and uncertainty in the sector.

In this scenario, the **group** ended the first nine months with revenues that were substantially stable and a reduction in margins compared to 2007. These results were impacted above all by third-quarter performance which, in view of the current economic situation, ended with a decline in the most important indicators compared to both the same period of 2007 and the two previous quarters.

The result is a loss, especially due to the writedown of the investment in Telecom Italia recognized in the first half.
Thanks to its multinational industrial organization, Pirelli nevertheless benefited from a good business trend in emerging nations (especially in the countries of Latin America and in China) and an increase in the operating profit of the Industrial tyre division. It should also be noted that broadband activities reported a profit, with higher operating sales and margins.

In order to effectively confront the current economic situation, especially the weak reference markets in Europe, so that the group can count on future growth, Pirelli began a series of restructuring actions in the last few months and is placing greater emphasis on the development and competitiveness of its two main businesses.

In particular, these actions refer to:

<u>Tyre business</u>

- new capital expenditures to strengthen the group's presence in areas with higher growth and increase the competitiveness of the industrial base (increases in the production capacity in Brazil, China and Romania and the imminent start of a joint venture in Russia);
- focus on technology and development of new products (*Car*: launch of the new Pirelli Cinturato, the eco-sustainable tyre for the European market, and the Winter Sottozero Serie II tyre, a new high-performance and high-safety winter tyre.

Motorcycle: introduction of the Scorpion Trail tyre for the enduro-street segment and the Metzeler Roadtec Z6 Interact tyre for the Sport Touring segment; *Industrial*: renewal of 70% of the tyre range in China and introduction of new sizes for the low-profile tyres in Europe);

- restructuring measures to strengthen the competitiveness of the industrial organization in Europe and reduce the costs of the central structures.

Real estate business

- restructuring plan with the aim initially of saving Euros 25/30 million in 2009. The plan, announced in the quarterly report at March 31, 2008, is proceeding according to the established timeframe and will bring a benefit in excess of Euros 30 million already starting in the year 2009;
- modification of the business model to reflect the changed scenario by reorganizing activities into three business units: residential, commercial and non-performing loans.

Restructuring expenses in the first nine months of 2008 total Euros 49.3 million (Euros 31.7 million in the tyre business and Euros 17.6 million in the real estate business).

Group results

Consolidated net sales in the first nine months of 2008 amount to Euros 3,898.6 million. Sales are basically stable (+0.3 percent), on a like-for-like basis, compared to the first nine months of 2007, excluding the exchange rate effect and sales relating to the deconsolidation of DGAG real estate assets. Taking into account the DGAG effect, sales in the first nine months of 2007 amounted to Euros 5,229.2 million.
Consolidated net sales in the third quarter amount to Euros 1,213.3 million ° (°-4.6°percent on a comparable basis).

EBIT (Operating profit) before restructuring expenses in the first nine months of 2008 amounts to Euros 241.6 million, a decrease of 18.7 percent compared to Euros 297.3 million in the first nine months of 2007. If restructuring expenses, equal to Euros 49.3 million, are also considered, the operating profit in the first nine months is Euros 192.3 million.
EBIT in the third quarter, before restructuring expenses (Euros 28.1 million in the period July to September), is Euros 30.1 million. This is a sharp reduction compared to the same period of 2007 (Euros 76 million in the third quarter of 2007) owing to the weakness of the two main activities.

EBIT including earnings (losses) from investments in the first nine months of 2008, which includes the effect of earnings or losses from companies accounted for by the equity method and dividends from unconsolidated holdings, is Euros 109.6 million (Euros 462.1 million at September 30, 2007). This result includes the impairment loss of Euros 155 million on the 1.36% stake in Telecom Italia S.p.A. held by the Group. **EBIT including earnings (losses) from investments in the third quarter of 2008** amounts to Euros 11.7 million (Euros 113.3 million in the third quarter of 2007). This result was influenced by a lower contribution from Pirelli RE's investment holdings due to the slowdown of the real estate market and the positive impact of the acquisitions of the minority stakes in the subsidiaries of the Tyre sector in Turkey (Euros 27.3 million).

The **total consolidated net result for the nine months to September 30, 2008** is a **loss** of Euros 36.3 million, compared to income of Euros 243.3 million in the same period of 2007.

The **loss attributable to the equity holders of Pirelli & C. S.p.A. for the nine months to September 30, 2008** is Euros 51.3 million, compared to income of Euros 129.8 million in the first nine months of 2007.

The **loss attributable to the equity holders of Pirelli & C. S.p.A. in the third quarter** is Euros 15.1 million (income of Euros 21.6 million in the third quarter of 2007), due to lower margins and restructuring expenses for the major businesses.

Total consolidated equity at September 30, 2008 is Euros 2,809.0 million, compared to Euros 3,804.1 million at the end of 2007 and Euros 3,002.4 million at June 30, 2008. **Equity attributable to the equity holders of Pirelli & C. S.p.A.** at September 30, 2008 amounts to Euros 2,499.6 million (Euros 0.466 per share), compared to Euros 2,980.2 million (Euros 0.555 per share) at the end of 2007 and Euros 2,608.1 million (Euros 0.486 per share) at June 30, 2008.

The **net financial position of the group at September 30, 2008** is a net debt position of Euros 1,055.7 million, compared to a net debt position of Euros 823.0 million at June 30, 2008. Contributing to the change during the third quarter is the buyback of the minority stakes in the Turkish tyre businesses (Euros 43.3 million), the acquisition of the stake in Highstreet by Pirelli RE (Euros 59.8 million), the investment in CyOptics (Euros 12.7 million) and the increase in working capital due partly to the economic weakness of the business. The net financial position at December 31, 2007 was a liquidity position of Euros 302.1 million.

The **number of employees of the group at September 30, 2008** is 31,682 (including 3,649 with temporary contracts) compared to 30,813 at December 31, 2007 (including 3,632 with temporary contracts).

<u>The Parent, Pirelli & C. S.p.A.</u>

The **net result** of Pirelli & C. S.p.A. in the first nine months ended September 30, 2008 is a **loss** of Euros 22.2 million compared to income of Euros 124.9 million in the same period of 2007. The result for the first nine months of 2008 was affected by the impairment loss of Euros 155.3 million recognized on the investment held directly and indirectly in Telecom Italia S.p.A..

Equity at September 30, 2008 is Euros 1,806.7 million (of which Euros 1,554.6 million relates to share capital) compared to Euros 2,076 million at the end of 2007.

SIGNIFICANT EVENTS IN THE THIRD QUARTER

On July 10, 2008, the Italian Ministry for the Environment signed an agreement with the City of Beijing to begin an experiment in the Chinese capital on the antiparticulate filter technology developed by Pirelli Eco Technology. Such filters are capable of reducing fine particle diesel engine emissions by more than 95 percent.
The agreement calls for the installation of Pirelli filtering systems on heavy vehicles (mainly buses, but also trucks and later snow ploughs and tractors) that will be supplied to the local public transport company. The first filtering systems were installed before the start of the Olympics.

On July 15, 2008, Pirelli announced a restructuring plan for the Manresa factory in order to protect its presence in Spain. In fact, for some time now, a large part of the production at the Catalan plant occurs at conditions that are not competitive. The situation is further complicated by a difficult economic and market scenario which is increasingly deteriorating. The pivotal element of the plan will consist of focusing the Manresa plant on products with a better margin and reducing articles that are manufactured at a loss. The restructuring plan calls for a reduction in production capacity and in the factory's workforce by about 30 percent by the end of 2008 and will affect approximately 280 workers.

On July 28, 2008, the Consortium formed by RREEF Alternative Investment, Pirelli RE, the Generali Group and the Borletti Group completed the acquisition of a 49 percent stake in Highstreet, an investment company that owns the properties leased to the German Karstadt department store chain. Highstreet has a portfolio consisting of 164 properties located throughout the German territory. The total gross area is 3.2 million square meters (the gross sales area is 2.1 million square meters). The enterprise value is equal to approximately Euros 4.56 billion, with about Euros 3.5 billion of loans secured by the properties.

On August 21, 2008, Pirelli Tyre purchased the minority stakes in the two subsidiaries through which it operates in Turkey from Isbank. The group acquired 25.75 percent of Pirelli Turk Lastikleri (which manufactures and markets car and industrial vehicle tyres) and 48 percent of Celikord (which manufactures and markets steelcord). As part of the transaction, Pirelli also acquired another 1 percent stake in Celikord from other shareholders. The total amount of the transaction is about Euros 43 million, with a positive impact on the result of Euros 27.3 million. Following the agreement, Pirelli holds 95.35 percent of Pirelli Turk Lastikleri and 100 percent of Celikord. The operation strengthens the group's position in a country that is strategic in terms of manufacturing, marketing and logistics.

During the third quarter of 2008, Pirelli & C. S.p.A. purchased on the market 290,468 Pirelli & C. Real Estate S.p.A. shares for a total outlay of Euros 3.9 million. As of September 30, 2008, the investment held directly by Pirelli & C. S.p.A. was equal 56.08 percent.

Subsequent to September 30, 2008, Pirelli & C. S.p.A. purchased on the market another 156,000 Pirelli & C. Real Estate S.p.A. shares for a total amount of Euros 1.2 million, bringing its direct investment to 56.45%.

THE GROUP

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

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

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

- **Gross operating profit**: this financial measure is used by the group as the financial target in internal business plans and in external presentations (to analysts and investors). It represents a useful unit of measurement for the evaluation of the operating performance of the group as a whole and for each single segment, in addition to the Operating Profit. The Gross Operating Profit is an intermediate performance measure represented by the Operating Profit from which depreciation and amortization are excluded.
- **Earnings (losses) from investments:** earnings (losses) from investments consist of all the effects recorded in the income statement referring to investments that are not consolidated line-by-line. These include dividends, the share of the earnings (losses) of companies accounted for using the equity method, impairment losses on available-for-sale financial assets and gains (losses) on the disposal of available-for-sale financial assets.

  Changes in the fair value of available-for-sale financial assets which are recognized directly in equity are excluded.
- **Net financial (liquidity)/debt position:** this performance measure is represented by the gross financial debt less cash and cash equivalents as well as other interest-earning financial receivables. The section “Interim consolidated financial statements and comments” presents a table that shows the balance sheet amounts used to calculate the net financial (liquidity)/debt position.

The highlights of the interim consolidated financial statements for the third quarter and nine months ending September 30, 2008 can be summarized as follows:

(in millions of euros)

	3rd Quarter 2008	3rd Quarter 2007	**9 months to 9/30/2008**	9 months to 9/30/2007	Year 2007
. Net sales	**1,213.3**	2,036.6	**3,898.6**	5,229.2	6,499.9
. Net sales (excluding DGAG deconsolidation)	**1,213.3**	1,283.3	**3,898.6**	3,946.0	5,204.3
. Gross operating profit before restructuring expenses	**85.2**	129.6	**402.0**	456.1	593.9
% of net sales (excluding DGAG deconsolidation)	**7.0%**	10.1%	**10.3%**	11.6%	11.4%
. **Operating profit before restructuring expenses**	**30.1**	76.0	**241.6**	297.3	381.3
% of net sales (excluding DGAG deconsolidation)	**2.5%**	5.9%	**6.2%**	7.5%	7.3%
. Restructuring expenses	**(28.1)**	-	**(49.3)**	-	-
. **Operating profit**	**2.0**	76.0	**192.3**	297.3	381.3
% of net sales (excluding DGAG deconsolidation)	**0.2%**	5.9%	**4.9%**	7.5%	7.3%
. Earnings (losses) from investments	**9.7**	37.3	**(82.7)**	164.8	195.3
. **Operating profit incl. earnings (losses) from investments and before restructuring expenses**	**39.8**	113.3	**158.9**	462.1	576.6
. Operating profit incl. earnings (losses) from investments	**11.7**	113.3	**109.6**	462.1	576.6
. Financial income (expenses)	**(12.4)**	(52.1)	**(39.0)**	(133.3)	(137.8)
. Income taxes	**(26.1)**	(30.4)	**(94.8)**	(109.6)	(133.5)
. **Income (loss) from continuing operations**	**(26.8)**	30.8	**(24.2)**	219.2	305.3
% of net sales (excluding DGAG deconsolidation)	**(2.2%)**	2.4%	**(0.6%)**	5.6%	5.9%
. **Income/(loss) from discontinued operations**	**-**	14.2	**(12.1)**	24.1	18.3
. **Total income/(loss)**	**(26.8)**	45.0	**(36.3)**	243.3	323.6
. Income/(loss) attributable to the equity holders of Pirelli & C. S.p.A.	**(15.1)**	21.6	**(51.3)**	129.8	164.5
. Earnings per share (in euros)			**(0.010)**	0.024	0.031
. Total equity			**2,809.0**	4,665.1	3,804.1
. Equity attributable to the equity holders of Pirelli & C. S.p.A.			**2,499.6**	3,858.3	2,980.2
. Equity per share (in euros)			**0.466**	0.719	0.555
. Net financial (liquidity)/debt position			**1,055.7**	2,328.8	(302.1)
. R&D expenditures			**123**	130	173
. Employees (number at period-end)			**31,682**	31,502	30,813
. Factories			**24**	24	24
Pirelli & C. shares					
. ordinary shares (number in millions)			5,233.1	5,233.1	5,233.1
of which treasury shares			*2.6*	*2.6*	*2.6*
. savings shares (number in millions)			134.8	134.8	134.8
of which treasury shares			*4.5*	-	-
. Total shares			5,367.9	5,367.9	5,367.9

For a more meaningful understanding of the group's performance, the following economic data and the net financial position are presented by business segment.

CONTINUING OPERATIONS (in millions of euros)	**9 months to 9/30/2008** Tyre	Real Estate	Broadband	Other businesses	Other	TOTAL
. Net sales	3,229.2	527.1	92.3	54.1	(4.1)	**3,898.6**
. Gross operating profit (loss) before restructuring exp.	378.3	38.3	3.8	(10.2)	(8.2)	**402.0**
. **Operating profit (loss) before restructuring exp.**	**231.8**	**30.0**	**3.2**	**(11.0)**	**(12.4)**	**241.6**
. Restructuring expenses	(31.7)	(17.6)	-	-	-	**(49.3)**
. Operating profit (loss)	200.1	12.4	3.2	(11.0)	(12.4)	**192.3**
. Earnings (losses) from investments	27.6	3.0	-	(0.7)	(112.6)	**(82.7)**
. **Operating profit (loss) incl. earnings (losses) from investments before restructuring expenses**	**259.4**	**33.0**	**3.2**	**(11.7)**	**(125.0)**	**158.9**
. Operating profit (loss) incl. earnings (losses) from investments	227.7	15.4	3.2	(11.7)	(125.0)	**109.6**
. Financial income (expenses)	(43.0)	(13.8)	(1.3)	(1.3)	20.4	**(39.0)**
. Income taxes	(76.4)	(12.2)	0.4	(0.2)	(6.4)	**(94.8)**
. **Income (loss) from continuing operations**	**108.3**	**(10.6)**	**2.3**	**(13.2)**	**(111.0)**	**(24.2)**
. Loss from discontinued operations			(10.9)		(1.2)	**(12.1)**
. **Income (loss)**						**(36.3)**
. Net financial (liquidity)/debt position	892.4	323.8	32.0	17.2	(209.7)	**1,055.7**

CONTINUING OPERATIONS (in millions of euros)	**9 months to 9/30/2007** Tyre	Real Estate	Broadband	Other businesses	Other	TOTAL
. Net sales	3,191.8	1,895.7	86.7	50.7	4.3	**5,229.2**
. Net sales (excluding DGAG)		612.5				**3,946.0**
. Gross operating profit (loss)	430.6	33.3	2.7	(4.5)	(6.0)	**456.1**
. **Operating profit (loss) before restructuring exp.**	**286.2**	**26.1**	**2.0**	**(5.0)**	**(12.0)**	**297.3**
. Restructuring expenses	-	-	-	-	-	-
Operating profit (loss)	286.2	26.1	2.0	(5.0)	(12.0)	**297.3**
. Earnings (losses) from investments	0.4	137.9	-	-	26.5	**164.8**
. **Operating profit (loss) incl. earnings (losses) from investments before restructuring expenses**	**286.6**	**164.0**	**2.0**	**(5.0)**	**14.5**	**462.1**
. Operating profit (loss) incl. earnings (losses) from investments	286.6	164.0	2.0	(5.0)	14.5	**462.1**
. Financial income (expenses)	(43.2)	(40.5)	(2.5)	(0.3)	(46.8)	**(133.3)**
. Income taxes	(83.4)	(21.0)		-	(5.2)	**(109.6)**
. **Income (loss) from continuing operations**	**160.0**	**102.5**	**(0.5)**	**(5.3)**	**(37.5)**	**219.2**
. Loss from discontinued operations			(12.1)		36.2	**24.1**
. **Income (loss)**						**243.3**
. Net financial (liquidity)/debt position	687.0	337.4	37.6	12.8	1,254.0	**2,328.8**

Net sales

Net sales in the nine months ending September 30, 2008 amount to Euros 3,898.6 million compared to Euros 5,229.2 million in the first nine months of 2007.

A percentage breakdown of net sales by business segment on a like-for-like basis is as follows:

	9 months to 9/30/2008	**9 months to 9/30/2007**
Pirelli Tyre	82.8%	80.9%
Pirelli Real Estate	13.5%	15.5%
Broadband Access	1.4%	1.4%
Other Businesses	2.3%	2.2%
	100.0%	100.0%

A percentage breakdown of the change in net sales by business segment on a like-for-like basis is as follows:

Pirelli Tyre	+	3.1%		
Pirelli Real Estate	-	13.9%		
Broadband Access	+	6.5%		
Other Businesses	+	6.7%		
Total group			+	**0.3%**
Foreign exchange effect			-	0.8%
Net sales for DGAG deconsolidation			-	24.8%
Total change			**-**	**25.4%**

The breakdown of net sales by geographical area on a like-for-like basis is as follows:

(in millions of euro)

	9 months to 9/30/2008		9 months to 9/30/2007 (*)	
Europe:				
. Italy	861.3	22.10%	1,097.5	20.99%
. Other European Countries (*)	1,271.8	32.62%	2,505.0	47.90%
North America	217.7	5.58%	253.8	4.85%
Central and South America	1,052.9	27.01%	877.6	16.78%
Oceania, Africa and Asia	494.9	12.69%	495.3	9.48%
	3,898.6	**100.00%**	**5,229.2**	**100.00%**

(*) In 2007, this line included the effect of the deconsolidation of DGAG assets for Euros 1,283.2 million

Net sales in the third quarter of 2008 amount to Euros 1,213.3 million compared to Euros 2,036.6 million in the same period of the prior year.

Operating profit

Operating profit in the nine months to September 30, 2008 amounts to Euros 192.3 million (4.9 percent of net sales) compared to Euros 297.3 million in the first nine months of 2007 (7.5 percent of net sales).

Operating profit in the third quarter of 2008 amounts to Euros 2.0 million compared to Euros 76.0 million in the third quarter of 2007.

Operating profit including earnings (losses) from investments

Operating profit including earnings (losses) from investments in the nine months to September 30, 2008 is Euros 109.6 million compared to Euros 462.1 million in the nine months to September 30, 2007.

The change is represented, according to the group's activities, as follows (in millions of euros):

Operating profit post-investments - 9 months to 9/30/2007		**462.1**
. Pirelli Tyre (exc.restructuring exp.)	(27.1)	
. Pirelli Real Estate (exc.restructuring exp.)	(131.0)	
. Broadband Access	1.2	
. Other Businesses	(6.7)	
. Impairment loss on Telecom Italia shares	(155.3)	
. Restructuring expenses	(49.3)	
. Other	15.7	
		(352.5)
Operating profit post-investments - 9 months to 9/30/2008		**109.6**

"Other" includes Euros 21.4 million relating to the release of charges for accruals set aside when the 38.9 percent stake in Pirelli Tyre S.p.A. was sold and which now, after reacquiring that stake, are no longer necessary.

In the third quarter, minority stakes in the subsidiaries in the Tyre sector in Turkey were also acquired for Euros 43.3 million, with a positive result on the earnings from investments for Euros 27.3 million as the purchase price was below the book value.

The first nine months of 2007 mainly included the earnings of the companies in the real estate sector accounted for by the equity method (Euros 79.7 million), the gain realized on the sale of 49 percent of the Facility business by Pirelli Real Estate (Euros 42.1 million), the gain realized by Pirelli Real Estate on the sale of 20 percent of the German-registered company Pirelli Real Estate Asset Management Deutschland GmbH (Euros 11.3 million) and dividends received (Euros 19.3°million).

Net result

The **loss from continuing operations in the nine months ended September 30, 2008** is Euros 24.2 million compared to income of Euros 219.2 million in the first nine months of 2007.

The **loss from discontinued operations in the first nine months ended September 30, 2008**, formed by the impact of the photonics business which is considered as a discontinued operation, is Euros 12.1 million. The **loss from discontinued operations in the first nine months of 2007,** included the negative effect of writing down the investment held by Pirelli & C. S.p.A. in Olimpia S.p.A. (Euros 54.8 million) to its sale price, the gain of Euros 91 million on the disposal of the warrants on Prysmian (Lux) S.à.r.l. to Goldman Sachs and the loss of Euros 12.1 million of the photonics business.

The **total net loss in the first nine months of 2008** is Euros 36.3 million compared to income of Euros 243.3 million in the first nine months of 2007.
The **loss attributable to the equity holders of Pirelli & C. S.p.A.** in the first nine months ended September 30, 2008 is Euros 51.3 million (a negative Euros 0.010 per share) compared to income of Euros 129.8 million in the first nine months ended September 30, 2007 (Euros 0.024 per share).

Equity

Equity decreased from Euros 3,804.1 million at December 31, 2007 to Euros 2,809.0 million at September 30, 2008.

The change during the period can be summarized as follows:

(in millions of euros)

	Group	Minority interest	Total
Equity at December 31, 2007	**2,980.2**	**823.9**	**3,804.1**
Translation differences	(26.9)	7.7	(19.2)
Income (loss) for the period	(51.3)	15.0	(36.3)
Dividends paid to minority interest by :			
- Pirelli & C. S.p.A	(93.2)		(93.2)
- Pirelli Tyre S.p.A.		(35.2)	(35.2)
- Pirelli & C. Real Estate S.p.A.		(36.5)	(36.5)
- Other group companies		(3.1)	(3.1)
Speed S.p.A. acquisition		(385.8)	(385.8)
Purchase of Pirelli & C. Real Estate S.p.A. shares		(17.4)	(17.4)
Change in fair value of available-for-sale financial assets/derivatives	(197.5)	(4.2)	(201.6)
Net actuarial gain (loss) on employee benefits	(110.4)	0.4	(110.0)
Purchases of minority stakes in Turkey tyre subsidiaries		(70.6)	(70.6)
Share capital increase in subsidiaries subscribed by minority interest		10.3	10.3
Other changes	(1.3)	4.8	3.5
Total changes	**(480.6)**	**(514.5)**	**(995.1)**
Equity at September 30, 2008	**2,499.6**	**309.4**	**2,809.0**

The equity attributable to the equity holders of Pirelli & C. S.p.A. at September 30, 2008 is equal to Euros 2,499.6 million (Euros 0.466 per share) compared to Euros 2,980.2 million at December 31, 2007 (Euros 0.555 per share).

Net financial position

The consolidated net financial position of the group went from a liquidity position of Euros 302.1 million at December 31, 2007 to a debt position of Euros 1,055.7 million at September 30, 2008. The change can be summarized as follows:

(in millions of euros)

Net financial position at December 31, 2007	**302.1**
Cash flows used in ordinary activities *	(80.4)
Financial and tax income (expenses)	(133.8)
Effect of Speed S.p.A. acquisition	(835.5)
Dividends paid to minority interest	(168.0)
Purchases of minority stakes in Turkey tyre subsidiaries	(43.3)
Investment in Cyoptics	(12.7)
PRE Investment in Highstreet	(59.8)
Purchase of Pirelli & C. Real Estate S.p.A. shares	(20.3)
Purchase of RCS shares	(4.0)
Total changes	**(1,357.8)**
Net financial position at September 30, 2008	**(1,055.7)**

* Includes the effect of the deconsolidation of the facility management business for Euros 102.4 million.

RELATED PARTY DISCLOSURES

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

The income statement, balance sheet and cash flow effects of transactions with related parties on the interim consolidated financial statements of the Pirelli Group for the nine months ended September 30, 2008 are as follows:

Transactions with associates and joint ventures:

(in millions of euros)

Revenues for goods and services	115.2	These mainly refer to mandates signed with companies of the Real Estate Group relating to services in respect of funds and asset management and technical and commercial services
Other expenses	27.5	These refer mainly to amounts recharged for various reasons of Pirelli & C. Real Estate, connected among other things with consortium expenses
Financial income	24.0	This includes mainly interest income relating to financial receivables from associates and joint ventures of Pirelli & C. Real Estate
Share of earnings (losses) of associates and joint ventures	(6.4)	This refers to the earnings or losses of the investments accounted for by the equity method
Financial expenses	0.1	
Current trade receivables	68.3	These mainly refer to receivables for services rendered to associates and joint ventures of Pirelli & C. Real Estate
Non-current other receivables	0.8	These refer to receivables of Pirelli & C. Real Estate
Non-current financial receivables	603.8	These mainly refer to loans made for real estate initiatives managed by individual companies of the Pirelli & C. Real Estate Group
Current other receivables	6.4	These refer to Pirelli & C. Real Estate and principally include a receivable for declared dividends to be collected
Current financial receivables	24.1	These mainly include transactions on the current account by the new companies which hold real estate assets in Germany
Current trade payables	34.5	These refer mainly to amounts recharged for various reasons of Pirelli & C. Real Estate
Current other payables	8.5	These refer mainly to amounts recharged for various reasons of Pirelli & C. Real Estate
Current borrowings from banks and other financial institutions	5.1	These mainly include intercompany current account payable balances by Pirelli & C. Real Estate companies
Current tax payables	1.0	These refer to payables by Pirelli & C. Real Estate S.p.A. to the company Trixia S.r.l. for expenses connected with that company's participation in the tax transparency regime pursuant to art. 115 of the TUIR, by virtue of which the positive or negative taxable amounts of the company will be allocated to the shareholders

Transactions with parties related to Pirelli through directors:

(in millions of euros)

Revenues from goods and services	0.8	These refer to services rendered by Pirelli & C. Real Estate S.p.A. and Pirelli & C. S.p.A. to the Camfin group
Other expenses	6.7	These refer to costs for the sponsorship of F.C. Internazionale Milano S.p.A.
Current trade receivables	0.4	These refer to receivables connected with the above services supplied to Camfin
Current trade payables	2.0	These refer to payables connected with the above services to F.C. Internazionale Milano S.p.A.
Dividends paid (cash flows)	22.7	Dividends to Camfin S.p.A. (Euros 21.9 million) and C.M.C. S.p.A. (Euros 0.8 million) from Pirelli & C. S.p.A.
Change in financial payables (cash flows)	218.9	Reimbursement of capital to Camfin S.p.A (Euros 211.1 million) and C.M.C. S.p.A. (Euros 7.8 million) by Pirelli & C. S.p.A.

SIGNIFICANT EVENTS SUBSEQUENT TO THE END OF THE THIRD QUARTER

On October 20, 2008, Pirelli Eco Technology, the company in the Pirelli Group which operates in the field of technologies for controlling emissions from diesel engines, announced that it was the first in Italy to obtain homologation from the Italian Ministry of Infrastructures and Transportation for five types of antiparticulate filters for existing light and heavy trucks. The antiparticulate filters, developed by Pirelli using silicon carbide technology, can reduce fine-particle diesel engine emissions by more than 95 percent, and will make a significant contribution to improving air quality. As a result of homologation, vehicles fitted with Pirelli's antiparticulate filters will have a better category of exhaust from the standpoint of the Euro standard (the range is Euro0 – Euro5). They will also be allowed to circulate freely in urban areas where vehicles that produce greater pollution are denied access.

On October 21, 2008, Pirelli & C. S.p.A. redeemed the 4.875% fixed interest bonds it issued for Euros 500 million in 1998.

On October 22, 2008, the City of Milan, the Lombardy Region and Bicocca University signed, with the agreement of Pirelli RE, representing the promoters of the "Grande Bicocca" Project (real estate investment funds held by foreign investors and a number of cooperatives), the new Development Plan. With the development of about 142,000 square meters of gross floor space, more than 810,000 square meters will have been completely redeveloped. The Plan calls for building residences with and without rent control, the University extension, commercial and entertainment facilities, public buildings (social housing for the lower income bracket and students, Bicocca Hangar) in addition to about 60,000 square meters of green areas.

On November 5, 2008, the board of directors of Pirelli RE approved the sale of its investment in Pirelli RE Integrated Facility Management BV (a 50-50 joint venture between Intesa Sanpaolo and Pirelli RE) to Manutencoop Facility Management. The closing of the transaction, once all the conditions precedent have been satisfied, is scheduled for the end of the year, subject to authorization by the Antitrust Authority. The Enterprise value is Euros 270 million.

On November 6, 2008, Pirelli & C. S.p.A. and Russian Technologies sealed an agreement on the basis of which the new industrial joint venture between the two companies, the details of which are being worked out, will start tyre production in Russia by the end of 2010. The agreements signed to date between the two companies call for the building of a new manufacturing site for car and truck tyres in the Samara region. The plant facilities will have an initial production capacity of about 4.2 million pieces, for a joint investment of approximately Euros 300 million.

OUTLOOK FOR THE CURRENT YEAR

For the full-year 2008, taking into account the statements made at the time of the publication of the June 30, 2008 results, the Pirelli & C. Group confirms the forecasts of overall consolidated EBIT before restructuring expenses at a figure below that of 2007. The entity of the reduction will be higher than that estimated at the end of the first half in view of a further deterioration of the markets of reference which occurred in the third quarter and which will likely continue into the last part of the year.

PIRELLI TYRE

The highlights can be summarized as follows:

(in millions of euros)

	3rd Quarter 2008	3rd Quarter 2007	**9 months to 9/30/2008**	9 months to 9/30/2007	Year 2007
. **Net sales**	**1,062.9**	1,040.4	**3,229.2**	3,191.8	4,161.7
. **Gross operating profit before restructuring expenses**	**91.8**	128.9	**378.3**	430.6	548.6
% on net sales	**8.6%**	12.4%	**11.7%**	13.5%	13.2%
. **Operating profit before restructuring expenses**	**40.8**	79.9	**231.8**	286.2	358.1
% on net sales	**3.8%**	7.7%	**7.2%**	9.0%	8.6%
. Restructuring expenses	**(26.7)**	-	**(31.7)**	-	-
. Operating profit	**14.1**	79.9	**200.1**	286.2	358.1
% on net sales	**1.3%**	7.7%	**6.2%**	9.0%	100.0%
. Earnings (losses) from investments	**27.3**	-	**27.6**	0.4	1.5
. **Operating profit (loss) incl. earnings (losses) from investments before restructuring expenses**	**68.1**	79.9	**259.4**	286.6	359.6
. Operating profit (loss) incl. earnings (losses) from investments	**41.4**	79.9	**227.7**	286.6	359.6
. Financial income (expenses)	**(13.3)**	(14.9)	**(43.0)**	(43.2)	(55.2)
. Income taxes	**(21.5)**	(22.4)	**(76.4)**	(83.4)	(93.9)
. **Income**	**6.6**	42.6	**108.3**	160.0	210.5
% on net sales	**0.6%**	4.1%	**3.4%**	5.0%	5.1%
. Net financial (liquidity)/debt position			**892.4**	687.0	559.6
. R&D expenses			**114**	113	148
. Employees (number at period-end)			**29,151**	27,138	27,224
. Factories (number)			**24**	24	24

In the third quarter, there was a further deterioration of the markets of reference, especially in Europe and America which, combined with a peak in raw material costs reached during the period, did not make it possible to arrive at the level of operating profit reported in the same period of the prior year.

Net sales in the third quarter amount to Euros 1,062.9 million, however, with an increase on a like-for-like basis of 3.4 percent against the same period of the prior year. This was due to a reduction in total volumes of 4.2 percent, more accentuated in the mature markets, and by a further strengthening of the positive price/mix variation compared to the first half equal to 7.6 percent. The negative exchange rate effect of 1.2 percent mitigated the overall growth of sales in the period to 2.2 percent over the prior year.

Operating profit before restructuring expenses in the third quarter is Euros 40.8 million (3.8 percent of net sales) compared to Euros 79.9 million (7.7 percent of net sales) reached in the third quarter of 2007.

The unfavorable scenario on the front of volumes, combined with a sharp rise in raw material costs and other production factors, produced an increase of Euros 90 million in the third quarter alone, compared to an increase of Euros 61 million in the first half of 2008 against the corresponding periods of 2007. As a result, it was not possible to completely offset those higher costs at the level of operating profit, despite the commercial performance in price/mix terms and the positive contribution delivered by the rapidly developing and emerging markets. On the whole, the commercial variances on operating profit grew by Euros 53 million in the third quarter alone compared to a growth of Euros 61 million in the first half against the corresponding periods of the prior year.

In this negative market context, Pirelli Tyre intensified its restructuring measures within the framework of a process to continually achieve efficiency and improve the industrial organization as well as modify the structure of fixed costs to conform to the changed scenario; the impact on the income statement in third quarter was Euros 26.7 million.

Moreover, in the third quarter, minority stakes were acquired in the subsidiaries in Turkey for Euros 43.3 million. This had a positive impact on the earnings from investments of Euros 27.3 million as the purchase price was below the book value.

Net sales in the first nine months of 2008 amount to Euros 3,229.2 million, with an increase on a like-for-like basis of 3.1 percent compared to the same period of the prior year.

Net of the exchange rate effect (a negative 1.9 percent), the growth in net sales is 1.2 percent.

The individual components of the change in net sales are as follows:

• Volumes	-	2.2%
• Prices/mix	+	5.3%
Change on a like-for-like basis	+	**3.1%**
• Foreign exchange effect	-	1.9%
Total change	+	**1.2%**

The 3.1 percent growth in net sales, on a like-for-like basis, was reached notwithstanding a contraction of the North American and European markets. This was achieved thanks to the focus on higher value segments and price management.

The reduction of volumes in Europe and North America was only partly compensated by the growth of volumes in South America and in emerging areas (overall the volume variance on net sales was a negative 2.2 percent).

The composition of net sales by geographical area reflects this scenario (growth in South America and reductions in Europe and North America). This was more apparent in the U.S. dollar areas because of a weakening of the currency (-13 percent compared to the prior year).

As far as the businesses are concerned, net sales recorded a growth in Industrial Tyres and a decline in Car tyres.

Geographical area	9 months to 9/30/2008	9 months to 9/30/2007
Italy	10%	11%
Other European countries	36%	38%
North America	7%	8%
Central and South America	32%	28%
Oceania, Africa, Asia	15%	15%
Total	**100%**	**100%**

Product category	9 months to 9/30/2008	9 months to 9/30/2007
Car tyres	58%	60%
Truck tyres	28%	27%
Motorcycle tyres	9%	9%
Steelcord / other tyres	5%	4%
Total	**100%**	**100%**

Gross operating profit before restructuring expenses in the nine months to September 30, 2008 decreased 12 percent compared to 2007, reaching Euros 378.3 million (11.7 percent of net sales), compared to Euros 430.6 million (13.5 percent of net sales).

Operating profit before restructuring expenses in the nine months to September 30, 2008 is Euros 231.8 million, (7.2 percent of net sales), compared to Euros 286.2 million in the first nine months of 2007 (9.0 percent of net sales).

Despite the contribution by the price/mix product variance and higher Original Equipment volumes, especially in South America, the lower sales volumes in the Replacements channels in Europe and North America and particularly overall increases in the unit cost of production factors (raw materials, energy and labor), further increasing in the third quarter, in an unfavorable market scenario, negatively influenced the result for the first nine months of 2008 compared to the prior year. The exchange rate effect was also negative.
The intensification of restructuring measures in Europe had a progressive impact for a cost of Euros 31.7 million, in order to more quickly combat the current scenario, in terms of strengthening the group's competitive position.

After restructuring expenses, **total operating profit in the first nine months of 2008** is Euros 200.1 million compared to Euros 286.2 million in the prior year.

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

Operating profit - 9 months to 9/30/2007		**286.2**
. Foreign exchange effect	(8.8)	
. Prices/mix	137.2	
. Volumes	(22.9)	
. Production factors per unit cost	(151.1)	
. Efficiencies	(3.2)	
. Restructuring expenses	(31.7)	
. Depreciation and other	(5.6)	
		(86.1)
Operating profit - 9 months to 9/30/2008		**200.1**

The **net result** is **income** of Euros 108.3 million in the first nine months of 2008 (after net financial expenses of Euros 43.0 million and income tax expenses of Euros 76.4 million) and including earnings from investments equal to Euros 27.6 million, (purchase of minority stakes in Turkey) compared to Euros 160.0 million in the first nine months of 2007 (after net financial expenses of Euros 43.2 million and income tax expenses of Euros 83.4 million).

The **net financial position** is a net debt position of Euros 892.4 million, compared to Euros 559.6 million at December 31, 2007 after the payment of dividends for Euros 93.2 million (of which Euros 54.9 million to Pirelli & C. S.p.A.). This increase is mainly due to the purchase of minority stakes in the subsidiaries in Turkey for Euros 43.3 million in August and seasonal factors affecting working capital, with critical inventory levels reached at the end of the period owing to the contraction of volumes, with corrective actions in progress in the last quarter.

Factories number 24 and are unchanged compared to December 31, 2007.

At September 30, 2008, there are 29,151 **employees**, including 2,970 with temporary contracts and 469 temp workers. Compared to December 31, 2007 (27,224 including 2,665 with temporary contracts and 816 temp workers), the number of workers increased mainly in Brazil and Turkey and in the new areas of investment in China and Romania.

Consumer Market

Net sales were reported **in the third quarter** for Euros 713.6 million. This figure is basically the same (+0.1 percent) as last year at stable exchange rates, with an increase in the price/mix variation of 5.1 percent and a reduction in volumes equal to 5 percent mainly in North America and Europe. The change is mainly in the Winter segment (the Replacements market in Europe is down overall by 6 percent, with a contraction in the Winter segment of 14% and 2% in Original Equipment; in North America, the reduction is 10 percent in Replacements and 19 percent in Original Equipment). The negative exchange effect of 1 percent caused a global change in sales of -0.9 percent compared to the prior year.

Gross operating profit before restructuring expenses in the third quarter is Euros 50.6 million, 42.2 percent lower compared to the prior year (Euros 87.6 million). The change is due to the negative trend of sales volumes, an unfavorable sales mix channel, since reductions were mainly recorded in the replacements channel, and, as mentioned above, the sharp increase in the costs of production factors, especially raw materials. There was also a negative impact from the under-utilization of production capacity at the factories during the quarter and the presence of start-up costs incurred for the Car tyre plant facilities in Romania and China.

Operating profit before restructuring expenses in the third quarter is Euros 12.2 million, (1.7 percent of net sales), with a strong contraction compared to the prior year (Euros 52.7 million).

Net sales in the first nine months of 2008 were Euros 2,207.9 million, with a like-for-like increase of 2.2 percent compared to the prior year (the exchange rate effect is -2.4 percent).
Substantial growth was reported in the sales of the Original Equipment channel (especially in South America) and the Motorcycle segment, whereas in the Replacements channel in Europe and North America negative volumes offset the positive price/mix gains with a 5 percent contraction of the Replacements market in Europe, 6 percent in North America and 15 percent in Original Equipment).
Double-digit growth in revenues was reported in South American thanks partly to a brilliant market especially for Original Equipment; this is a positive indicator and commercial investment for the future growth of demand in Replacements.
The exchange rate effect is negative mostly on account of the translation to euros of the sales made in North America and in developing markets (Africa, Middle East and Far east) where prices increased significantly

Gross operating profit before restructuring expenses in the nine months to September 30, 2008, equal to Euros 249.1 million, shows a gross operating margin of 11.3 percent which is lower by 19% compared to 2007 (Euros 307.3 million). The change is due to the negative trend of volumes, an unfavorable sales channel mix and only a partial recovery of the increase in the cost of production factors.

Operating profit before restructuring expenses in the nine months to September 30, 2008 is Euros 139.0 million, (6.3 percent of net sales), compared to Euros 201.8 million (9.1 percent of net sales) in 2007.

In the **Car** segment, the following products were launched during the year:

- on the European market, the new Pirelli Cinturato, a modern high-tech revisitation of the tyre that made history in the tyre industry. The new Cinturato, manufactured in the P4 and P6 models, is an environmentally-friendly, high-performance tyre with excellent safety features which, thanks to new technologies, makes it possible to reduce fuel consumption and harmful emissions by up to 4 percent and improve mileage (+30 percent). Furthermore, aromatic oils have been removed from the tread, in advance of the new European regulations which will come into force in 2010.
  The new Cinturato, produced at the factories in Bollate (Italy), Izmit (Turkey), Manresa (Spain) and Carlisle (Great Britain) has already been selected as Original Equipment on the most popular models of many leading automakers such as Mercedes, Volkswagen, Fiat and Peugeot. The tyre has already received notable recognition from the most important specialized magazines and from the German, Swiss and Austrian Automobile Clubs, regarded as authoritative showcases for comparative tests on new car products in Central Europe.

- In the Winter segment, the new Winter Sottozero Series 2, a tyre characterized by a special, performing grip in conditions of snow and wet asphalt, which generally contributes to safe driving in winter, while ensuring driver comfort in normal conditions.

In the **Motorcycle** segment**,** sales increased for both the Pirelli and Metzeler brands.
In the Replacements channel, significant growth was reported in Latin America, where there was a positive trend in demand in almost all the main markets.
Sales in Europe continued to increase, despite a fall in the market, particularly in the second quarter.
Positive results were reported in sales of Original Equipment, especially in Latin America.
In terms of products, with regard to the Pirelli brand, in July, the Scorpion Trail was introduced for Enduro-street motorcycles (Suzuki V-Strom, Yamaha Tenerè and BMW R1200 GS). With regard to the Metzeler brand: the new Roadtec Z6 Interact (for the Sport Touring segment) was introduced in the Isle of Man.

As for Pirelli's performance on the racing circuit, it was confirmed that Pirelli will be the official supplier in the World Superbike Championship for the next three years 2010-2012. In off-road, Pirelli led the field in all three categories (MX1, MX2 and MX3) in the Motocross World Championship. The number of world titles won rose to 51. There were victories for the Metzeler brand in the Enduro World Championship in the Junior, E1 and E3 categories. Pirelli also achieved brilliant results in National Championships.

Industrial market

In the industrial market, **net sales** amount to Euros 349.3 million **in the third quarter of 2008**, an increase of 10.7 percent compared to the same period of 2007 at stable exchange rates (the exchange rate effect is -1.6 percent). This was achieved largely on account of the price/mix lever (13.1 percent) principally in rapidly developing markets where the Business Unit's focus is highest. Growth was attenuated by a negative change in volumes of 2.4 percent, mainly concentrated in the mature markets, a market which fell by 4 percent in Europe.

Gross operating profit before restructuring expenses in the third quarter of 2008 is Euros 41.2 million (11.8 percent of net sales), in line with the prior year (Euros 41.3 million, or 12.9 percent of net sales). The growth of volumes in Latin America and in the emerging markets, which have assured full production capacity, and the positive change in the price/mix made it possible to compensate the considerable increase in the costs of production factors during the quarter which, nevertheless, was mitigated by the positive exchange effect in the markets of reference.

Operating profit before restructuring expenses in the third quarter of 2008 is Euros 28.6 million (8.2 percent of net sales), compared to Euros 27.2 million in 2007 (8.5 percent of net sales).

Net sales for the first nine months of 2008 reached Euros 1,021.3 million, with a like-for-like increase of 5.2 percent compared to the prior year (an exchange effect of -0.9 percent), composed of a positive price/mix change of 7.2 percent and a reduction in volumes of 2 percent.

Gross operating profit before restructuring expenses for the nine months to 2008 is Euros 129.2 million (12.7 percent of net sales), an increase Euros 5.9 million over the prior year (Euros 123.3 million, or 12.6 percent of net sales).

Operating profit before restructuring expenses for the nine months to September 30, 2008 is Euros 92.8 million (9.1 percent of net sales), compared to Euros 84.4 million (8.6 percent of net sales) in 2007.

Steelcord products closed the first nine months with sales in line with those of the prior year.

Outlook for the current year

In a market context where problems became more accentuated in terms of demand for Replacements in mature markets, and in which the automobile industry is announcing drastic cuts in production for the latter part of the year, with the costs of raw materials beginning to reverse their upward trend (although the positive effects of this will still be limited in the last part of the year), Pirelli Tyre has stepped up its restructuring measures and will continue to do so in the last quarter of the year, especially in Europe.

In July 2008, Pirelli announced a restructuring plan for the Manresa factory. Furthermore, production was cut in other European factories, both for tactical reasons, in order to raise efficiency by the year-end in working capital with regard to the management of inventories of finished products for the Car segment, and structurally, in order to improve its competitive position to the benefit of future years. In addition, measures were implemented to contain structural costs in Italy and the main European countries.

In the light of the current market scenario and the actions taken to cut production in the last quarter, and the fact that the fall in the costs of raw materials will begin to have a positive effect particularly starting from the first quarter of 2009, in the last quarter of 2008, Pirelli Tyre expects to report an operating result before restructuring expenses that will still be negatively affected by the current market scenario, with a trend similar to the third quarter in comparison with the prior year.

PIRELLI & C. REAL ESTATE

The Pirelli RE group is an alternative asset manager specialized in the real estate sector. It manages investment funds and companies that own real estate and non-performing loans in which it co-invests by acquiring minority stakes, aligning its own interests to those of investors, and to which it provides, as it does to other third-party customers, a full-range of specialized real estate services.
The group's principal activities are: identifying investment opportunities based on different types of products (residential, commercial and non-performing loans) and geographical location (Italy, Germany and Poland), performing management services and supplying quality specialized services.

Economic and equity/financial review

The economic and equity/financial review of the company for the first nine months of 2008 is presented below. It should be noted that the operating profit including earnings (losses) from investments is considered to be the most important indicator given the type of business, expressing the trend of earnings.

Economic review

(in millions of euros)	9 months to 9/30/2008	9 months to 9/30/2007 net of DGAG's temporary consolidation (3)	9 months to 9/30/2007
Pro rata aggregate revenues (1)	**938.3**	**982.8**	**1,071.9**
Consolidated revenues (1)	527.1	523.5	612.5
Operating profit before restructuring expenses	30.0	3.3	26.1
Earnings (losses) from investments	3.0	137.9	137.9
Operating profit including earnings from investments before restructuring expenses	**33.0**	**141.2**	**164.0**
Restructuring expenses	(17.6)	-	-
Operating profit including earnings from investments (2)	**15.4**	**141.2**	**164.0**
Income (loss) attributable to the equity holders of the company	**(12.9)**	**111.6**	**95.8**

(1) Pro rata aggregate revenues express the total business volumes of the Group, calculated as the sum of consolidated revenues and the share of the revenues of the associates, joint ventures and funds in which the Group has holdings. The amount for the first nine months of 2007 is presented net of sales at cost of DGAG real estate properties to the joint ventures with RREEF and MSREF for Euros 1,283.2 million.

(2) Operating profit including earnings (losses) from investments comprises the operating profit (Euros 12.4 million) in addition to the share of the earnings of the companies accounted for by the equity method and the loss on the sale of investment holdings (Euros -5.5 million), dividends and income from real estate investment funds (Euros 2.9 million), as well as the gain realized on the sale of shares of real estate investment funds (Euros 5.6 million).

(3) The DGAG Group, purchased at the beginning of 2007, was consolidated line-by-line until control ceased following its partial sale to third-party counterparts in a progressive manner during the course of the year.

The **pro rata aggregate revenues** amounts to Euros 938.3 million compared to Euros 982.8 million in the nine month to September 30, 2007, net of sales at cost of DGAG properties to the joint ventures with RREEF (Deutsche Bank Group) and MSREF (Morgan Stanley Group) for Euros 1,283.2 million and net of the effect of temporarily consolidating DGAG.

Consolidated revenues amount to Euros 527.1 million compared to Euros 523.5 million in the first nine months of 2007, net of sales at cost of DGAG properties to the joint ventures with RREEF (Deutsche Bank Group) and MSREF (Morgan Stanley Group) for Euros 1,283.2 million and net of the effect of temporarily consolidating DGAG.

Operating profit including earnings (losses) from investments before restructuring expenses amounts to Euros 33 million (Euros 15.4 million post-restructuring) compared to Euros 141.2 million in the first nine months of 2007 (net of the effect of temporarily consolidating DGAG), which included Euros 42 million from the sale of the 49% stake in Pirelli RE Facility and Euros 51.5 million for the revaluation of properties to fair value. Real estate sales in the first nine months of 2008 are down to Euros 714.5 million (Euros 1,186.6 million in the first nine months of 2007).

In 2008, the company commenced a restructuring plan (for which Euros 17.6 million has been spent up to September 30, 2008) with the aim initially of saving Euros 25/30 million in 2009. The plan, announced in the quarterly report at March 31, 2008, is proceeding according to schedule and will generate more than Euros 30 million already from the beginning of 2009.

The **consolidated net result before restructuring expenses** for the nine months to September 30, 2008 is a breakeven; instead, the **total consolidated net result** is a **loss** of Euros 12.9 million compared to income of Euros 95.8 million in the first nine months of last year, including a net Euros 90.1 million from the transactions above.

Equity and financial review

(in millions of euros)	9/30/2008	12/31/2007	9/30/2007
Equity	**616.7**	**720.1**	**687.8**
. of which attributable to the equity holders of the company	*609.8*	*715.7*	*684.6*
Net financial (liquidity)/debt position	**323.8**	**289.7**	**337.4**
Shareholder loans	610.7	526.4	589.5
Net financial (liquidity)/debt position before shareholder loans	**934.5**	**816.1**	**926.9**
Gearing ratio	**1.52**	**1.13**	**1.35**

Equity attributable to the equity holders of the company is Euros 609.8 million compared to Euros 715.7 million at the end of 2007. The reduction of Euros 105.9 million is basically attributable to the payment of dividends (Euros 85.1 million) and the loss for the period of Euros 12.9 million.

The **net financial position** shows a net debt position of Euros 323.8 million at September 30, 2008 compared to Euros 337.4 million at September 30, 2007 (Euros 270.5 million at June 30, 2008). The **adjusted net financial position** (expressed gross of shareholder loans made to minority-owned companies) is a net debt position of Euros 934.5 million compared to Euros 926.9 million at September 30, 2007 (Euros 809.8 million at June 30, 2008). The increase over June 30, 2008 is due to the investment acquired in Highstreet for about Euros 110 million.

Assets under management (stated at book value) total Euros 17.4 billion (of which Euros 4.6 billion is under co-management) and increased by Euros 3.7 billion compared to December 31, 2007.

After the above transactions, the **gearing** ratio rose to 1.52 from 1.23 at June 30, 2008 (1.35 at September 30, 2007).

Net cash flows before dividends are positive for Euros 51.0 million compared to negative cash flows for Euros 109.0 million in the first nine months of 2007, while net cash flows from ordinary operations are negative for Euros 34.1 million compared to a negative Euros 196.0 million in the nine months to September 2007.

Performance by Pirelli RE divisions

In the **Residential Division,** pro rata aggregate revenues in the first nine months of 2008 total Euros 248.8 million (Euros 223.8 million in the first nine months of 2007). These revenues are composed of Euros 181.1 million from Capital activities (Euros 171.7 million in the first nine months of 2007) and Euros 67.7 million from Management and Specialized services (Euros 52.1 million in the first nine months of 2007). The operating result including earnings (losses) of investments, before restructuring expenses, for the first nine months of 2008 is a loss of Euros 11.9 million compared to a loss of Euros 1.1 million in the first nine months of 2007, net of the temporary consolidation of DGAG.

In the **Commercial Division (offices, retail and industry)** pro rata aggregate revenues amount to Euros 340.0 million in the first nine months of 2008 (Euros 379.7 million in the first nine months of 2007). These revenues are composed of Euros 246.0 million from Capital activities (Euros 285.6 million in the first nine months of 2007) and Euros 94 million from Management and Specialized services (Euros 94.1 million in the first nine months of 2007). The operating profit including earnings (losses) of investments, before restructuring expenses, is Euros 35.7 million in the first nine months of 2008 compared to an operating profit of Euros 96.0 million in the first nine months of 2007, which comprises Euros 51.5 million in fair value revaluations, net of the temporary consolidation of DGAG.

The **Non-performing Loans Division** posted pro rata aggregate revenues of Euros 27.3 million in the first nine months of 2008 (Euros 31.7 million in the first nine months of 2007). These revenues are composed of Euros 4.1 million from co-investment activities (Euros 2.1 million for the nine months to September 30, 2007) and Euros 23.2 million from Management and Specialized services (Euros 29.6 million for the nine months to September 30, 2007). Collections of Non-performing Loans are equal to Euros 321.3 million (Euros 319 million in the same period of 2007). The operating profit including earnings (losses) of investments is Euros 14.7 million in the first nine months of 2008 and is basically in line with Euros 15.5 million in the first nine months of 2007.

Integrated Facility Management records pro rata aggregate revenues realized by joint ventures of Euros 338.9 million in the first nine months of 2008 compared to Euros 357 million in the first nine months of 2007. The operating profit including earnings (losses) of investments increased to Euros 16.2 million in the first nine months of 2008 from Euros 14.4 million in the first nine months of 2007, on a comparable consolidation basis.

Outlook for the current year

Given the financial crisis, which caused a severe market slowdown, the company does not believe that it will meet its EBIT 2008 target. The company nevertheless expects its net result to reach a breakeven, inclusive of extraordinary income and expenses.

BROADBAND ACCESS

The highlights can be summarized as follows:

(in millions of euros)

	3rd Quarter 2008	3rd Quarter 2007	**9 months to 9/30/2008**	9 months to 9/30/2007	Year 2007
. Net sales	28.9	35.0	**92.3**	86.7	112.5
. Gross operating profit	0.2	1.9	**3.8**	2.7	1.9
. Operating profit	-	1.7	**3.2**	2.0	0.9
. Earnings (losses) from investments	-	-	**-**	-	-
. Operating profit incl. earnings (losses) from investments	-	1.7	**3.2**	2.0	0.9
. Financial income (expenses)	1.5	(1.5)	**(1.3)**	(2.5)	(3.5)
. Income taxes	0.6	-	**0.4**	-	-
. Income (loss)	2.1	0.2	**2.3**	(0.5)	(2.6)
. Net financial (liquidity)/debt position			**32.0**	37.6	21.5
. Employees (number at period-end)			**113.0**	89.0	94.0

Net sales in the nine months ending September 30, 2008 amount to Euros 92.3 million, an increase of 6.5 percent compared to the first nine months of 2007 (Euros 86.7 million).

Gross operating profit is Euros 3.8 million, increasing from Euros 2.7 million in the corresponding period of the prior year.

Operating profit is Euros 3.2 million, compared to Euros 2.0 million recorded in the same period of the prior year. The improvement in operating profit reflects a positive effect of the product mix sold as well as a favorable trend in the U.S. dollar/Euro exchange rate.

The **net result** is **income** of Euros 2.3 million (after financial and income tax expenses of Euros 0.9 million) compared to a loss of Euros 0.5 million in the first nine months of 2007 (after financial and income tax expenses of Euros 2.5 million). A tax credit of Euros 1.0 million recognized for research and development costs sustained in 2007 also had a favorable effect on the net result.

The **net financial position** is a net debt position of Euros 32 million compared to a net debt position of Euros 21.5 million at December 31, 2007.

At September 30, 2008, there are 113 **employees**, compared to 94 employees at December 31, 2007.

In the first nine months of 2008, Pirelli Broadband Solutions reported a significant increase in revenues compared to the prior year. The change is particularly due to the increase in the sales volumes of Set-top Boxes, following the completion of the product range for IPTV (Internet Protocol Television). In terms of geographic positioning, the company is continuing its expansion towards Europe (especially targeting the markets in the eastern area), Russia and South America.
During the first nine months of the year the corporate portfolio grew further and was consolidated and now consists of six different product lines: Residential Access Gateways, Small Business Gateways, Set-top Box, Extenders (products for implementing domestic broadband networks), Terminals (mobile and combined fixed-mobile convergence broadband solutions) and PMP (Pirelli Management Platform, a remote software platform for device management).

Finally, during the first part of the year, Pirelli Broadband Solutions sealed a cooperation agreement with Nokia Siemens in the field of “femtocells”, a technology that will encourage the development third-generation broadband communications in the domestic environment.

Outlook for the current year

The current year shows the company concentrating its efforts mainly on consolidating the Access Gateways line, increasing volumes in the Set-top Box line by completing the IPTV optical product range, and developing the Small Business line with a modular product capable of supporting various configurations of service models.

These development lines should enable the company to continue the good performance recorded in the first nine months for the rest of the year and to preserve business profits despite the trend of the U.S. dollar/Euro exchange rate which is less favorable than in the first part of the year, and the increasingly critical world economic situation which is tending to exacerbate phenomena that are already typical of the reference market such as the erosion of prices.

OTHER BUSINESSES

The other businesses of the group in the sectors of renewable energy sources (Pirelli Ambiente), sustainable mobility (Pirelli Eco Technology) and fashion (Pirelli PZero) reported **net sales** of Euros 54.1 million in the first nine months of 2008, up 6.7 percent up compared to the first nine months of 2007 (Euros 50.7 million).

The **operating loss** of Euros 11 million (Euros 5 million in the first nine months of 2007) was particularly affected by the start-up costs for the new manufacturing and marketing activities of antiparticulate filters.

The sales of these businesses were linked mainly to the development of the new business line of antiparticulate filters to reduce emissions from diesel-run vehicles and the marketing of fuel with a low environmental impact, Gecam – "the white diesel", also sold on the French market through the subsidiary Gecam France.
During the period, sales of filter systems for light and heavy vehicles continued in Italy, where Pirelli is the first company to have obtained homologation for five product lines. Marketing has also begun in certain European countries (Benelux, Germany, the United Kingdom). On the Chinese market, testing is being conducted on some of the heavy vehicles used by the City of Beijing. During the period, building work continued on the new antiparticulate filter production plant in Gorj county in Romania, which will become operational by the end of the year. Activities continued in the spheres of producing renewable energy from solid waste through the high-quality fuel CDR-Q, in photovoltaic cells and in environmental reclamation.

The Board of Directors
Milan, November 7, 2008

INTERIM CONSOLIDATED FINANCIAL STATEMENTS

AND

COMMENTS

(in thousands of euros)

	CONSOLIDATED BALANCE SHEET	30/09/2008	31/12/2007
3	Property, plant and equipment	1,647,539	1,650,485
4	Intangible assets	1,043,414	672,540
5	Investments in associates and joint ventures	634,937	534,194
6	Other financial assets	582,603	958,272
7	Deferred tax assets	61,073	58,524
9	Other receivables	778,661	672,894
	Tax receivables	11,924	12,278
	Financial instruments	5,497	3,849
	NON-CURRENT ASSETS	4,765,648	4,563,036
10	Inventories	902,197	776,474
8	Trade receivables	1,045,892	1,098,927
9	Other receivables	255,353	241,475
11	Securities held for trading	143,894	114,039
12	Cash and cash equivalents	218,604	2,057,682
	Tax receivables	43,196	43,281
	Financial instruments	58,990	58,326
	CURRENT ASSETS	2,668,126	4,390,204
	TOTAL ASSETS	7,433,774	8,953,240
14.1	Attributable to the equity holders of the company:	2,499,617	2,980,231
	Share capital	1,554,631	1,555,934
	Reserves	996,312	1,259,746
	Income (loss) for the period	(51,326)	164,551
14.2	Attributable to the minority interest:	309,342	823,840
	Reserves	294,314	664,799
	Income for the period	15,028	159,041
14	**TOTAL EQUITY**	2,808,959	3,804,071
18	Borrowings from banks and other financial institutions	545,192	788,198
20	Other payables	58,487	23,300
16	Provisions for other liabilities and charges	141,881	146,331
	Deferred tax liabilities	39,506	44,625
17	Employee benefit obligations	413,065	349,142
	Tax payables	10,036	11,211
21	Financial instruments	5,003	6,782
	NON-CURRENT LIABILITIES	1,213,170	1,369,589
18	Borrowings from banks and other financial institutions	1,581,520	871,759
19	Trade payables	1,111,336	1,323,588
20	Other payables	506,245	1,394,673
	Provisions for other liabilities and charges	91,382	71,340
	Tax payables	57,643	45,707
21	Financial instruments	63,519	72,513
	CURRENT LIABILITIES	3,411,645	3,779,580
	TOTAL EQUITY AND LIABILITIES	7,433,774	8,953,240

(in thousands of euros)

	CONSOLIDATED INCOME STATEMENT	9 months to September 30, 2008	9 months to September 30, 2007
23	Revenues from sales and services	**3,898,573**	5,229,164
24	Other income	**130,102**	235,186
	Change in inventories of work in process, semifinished and finished products	**70,140**	(1,076)
	Raw materials and consumables used (net of change in inventories)	**(1,435,041)**	(2,581,990)
25	Personnel costs	**(874,142)**	(870,180)
26	Amortization, depreciation and impairments	**(160,443)**	(162,513)
27	Other expenses	**(1,440,496)**	(1,558,935)
	Increase in property, plant and equipment from internal work	**3,563**	7,636
	OPERATING PROFIT	**192,256**	**297,292**
28	Financial income	**347,722**	238,194
29	Financial expenses	**(472,480)**	(283,195)
30	Dividends	**20,204**	19,285
31	Gains (losses) from changes in fair value of financial assets	**(9,758)**	(17,347)
32	Share of earnings (losses) of associates and joint ventures	**(7,311)**	74,616
	INCOME BEFORE INCOME TAXES	**70,633**	**328,845**
33	Income taxes	**(94,819)**	(109,617)
	INCOME FROM CONTINUING OPERATIONS	**(24,186)**	**219,228**
34	Income (loss) from discontinued operations	**(12,110)**	24,106
	INCOME (LOSS) FOR THE PERIOD	**(36,296)**	**243,334**
	Attributable to:		
	equity holders of the company	**(51,324)**	129,813
	minority interest	**15,028**	113,521

FORM AND CONTENT

The quarterly report at September 30, 2008 of the Pirelli & C. Group has been prepared in accordance with art. 154 ter of Legislative Decree 58/1998 and Consob regulations on the subject.

The valuation and measurement of accounting amounts are based upon International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB) and relevant interpretations of the International Financial Reporting Interpretations Committee (IFRIC), endorsed by the European Commission and in force at the time of the approval of this report

The accounting policies and principles adopted in the preparation of this quarterly report are consistent with those used in the preparation of the financial statements at December 31, 2007, to which reference should be made for additional details. The exceptions are in respect of IFRIC 11 – Group and Treasury Share Transactions, in effect as from January 1, 2008, and the amendment to IAS 39 – Financial Instruments: Recognition and Measurement and IFRS 7 – Financial instruments: Disclosures, in effect as from July 1, 2008, the application of which did not have a significant quantitative impact for the group.

COMMENTS

Intangible assets

The increase in intangible assets compared to December 31, 2007 is mainly due to the goodwill generated on the repurchase of the 38.9 percent stake of Pirelli Tyre S.p.A. through the acquisition of Speed S.p.A. and the inclusion of some companies of the BauBeCon group in the scope of consolidation of Pirelli Real Estate.

Other financial assets

The reduction in other financial assets compared to December 31, 2007 is due to the change in fair value (Euros 366 million), of which Euros 201 million is recognized in equity and Euros 155 million in profit and loss and relates to the writedown of the investment in the shares held in Telecom Italia S.p.A..

<u>Net financial position</u>

(non-GAAP measure)

The composition of the net financial position is as follows:

(in millions of euros)

	30/09/2008	31/12/2007
. Borrowings from banks and other financial institutions - current	1,547	854
. Financial accrued liabilities and deferred income - current	58	46
. Borrowings from banks and other financial institutions - non-current	550	795
. Payables to shareholders for capital reduction	-	826
Total gross debt	**2,156**	**2,521**
. Cash and cash equivalents	(219)	(2,058)
. Securities held for trading	(144)	(114)
. Financial receivables - current	(24)	(19)
. Financial accrued income and prepaid expenses - current	(12)	(18)
Net financial debt	**1,757**	**312**
. Financial receivables - non-current	(695)	(609)
. Financial accrued income and prepaid expenses - non-current	(7)	(5)
Total net financial (liquidity)/debt position	**1,056**	**(302)**

The change during the period is mainly due to the effects of the repurchase of the minority stake in Pirelli Tyre (Euros 835 million), the payment of dividends (Euros 168 million), the purchase of Pirelli Real Estate shares (Euros 20 million), the deconsolidation of the Facility Management business (Euros 102 million) in addition to, in the quarter, the purchase of the minority stakes in the subsidiaries of the tyre business in Turkey (Euros 43.3 million), the acquisition of the stake in Highstreet by Pirelli RE (Euros 59.8 million), the impact of the CyOptics transaction in photonics (Euros 12.7 million) and the increase in working capital partly as a result of the weak business climate.

Exchange rates

	(local currency against euros)					
	Period-end		Change in	Average		Change in
	09/30/2008	12/31/2007	%	2008	2007	%
British pound	0.7903	0.7334	7.76%	0.7820	0.6765	15.59%
Swiss franc	1.5774	1.6547	(4.67%)	1.6078	1.6370	(1.79%)
Slovakian koruna	30.3000	33.5830	(9.78%)	31.5815	33.8864	(6.80%)
American dollar	1.4303	1.4721	(2.84%)	1.522	1.344	13.22%
Canadian dollar	1.4961	1.4449	3.54%	1.549	1.485	4.35%
Brazilian real	2.7380	2.6075	5.01%	2.567	2.691	(4.61%)
Venezuela bolivar	3.0752	3.1650	(2.84%)	3.272	2.890	13.23%
Argentinean peso	4.4840	4.6356	(3.27%)	4.728	4.176	13.24%
Australian dollar	1.7739	1.6757	5.86%	1.669	1.637	1.94%
Chinese renminbi	9.7918	10.7516	(8.93%)	10.630	10.302	3.18%
Singapore dollar	2.0439	2.1163	(3.42%)	2.116	2.049	3.24%
Egyptian pound	7.7916	8.1039	(3.85%)	8.216	7.629	7.70%
Turkish lira	1.8065	1.7102	5.63%	1.866	1.799	3.71%

Compliance with Article 36 of Consob Regulation 16191/2007 Concerning Market Regulations

Considering that Pirelli & C. controls, directly and indirectly, certain companies established and regulated under the law of non-EU countries*, which are deemed to be of material significance pursuant to art. 36 of Consob Regulation 16191/2007 concerning Market Regulations, the company has decided to adopt a specific and suitable "Group Operating Instruction" which ensures immediate, constant and integral respect for the provisions of the above-mentioned Consob regulation, even though there are already administrative/accounting and reporting systems of the Pirelli Group in place so that the company is substantially in line with the requirements of the market regulation.

As stated in the above Operating Instruction, the competent corporate functions of the parent, in abiding by the market regulation, at specific dates and periodically, shall identify and publicize materially significant non-EU companies as defined in the market regulation, and – with the necessary and timely collaboration of the interested companies – guarantee the collection of the data and information and the verification of the circumstances as stated in article 36, ensuring that the information and data provided by the subsidiaries are available in the event of a request by Consob.

Furthermore, a periodical flow of information shall also be provided in order to ensure that the Pirelli & C. board of statutory auditors can carry out the required and necessary tests.

Finally, the operating instruction adopted by the company, in keeping with the provisions of the market regulation**, instructs how the financial statements (the balance sheet and income statement) of the materially significant non-EU companies prepared for the purpose of the consolidated financial statements are to be made available to the public.

It can therefore be stated that the company has fully complied with the provisions of article 36 of the above Consob 16191/2007.

*Non-EU companies controlled, directly and indirectly, by Pirelli & C. S.p.A., relevant pursuant to article 36 of the Market Regulation are: **Turk Pirelli Lastikleri AS, Pirelli Tyre CO LTD, Pirelli Pneus LTDA, Pirelli Tyre (EUROPE) S.A., and Pirelli Tire LLC.**

** As elucidated by Consob – article 36, paragraph 1, letter a) of the Market Regulation "will be applied in respect of financial statements for the years in progress at the date the same comes into effect" and therefore the financial statements shall be made available to the public starting from the approval of the financial statements for year 2008 for the non-EU companies controlled by Pirelli & C. which carry material significance at December 31, 2008.

Declaration Pursuant to Article 154-bis, Paragraph 2 of Legislative Decree 58 dated February 24, 1998 ("Consolidated Law on Finance)

The undersigned, Claudio De Conto, operations general manager and the manager responsible for the preparation of the financial reports of Pirelli & C. S.p.A., with registered offices in Milan, Via Gaetano Negri 10, share capital of Euros 1,556,692,865.28, tax code, VAT number and Milan Companies Register No. 00860340157

declares

pursuant to article 154 bis, paragraph 2 of the Consolidated Law on Finance that the accounting information contained in the **Quarterly Report at September 30, 2008** corresponds to the document results, books and accounting records.

Milan, November 7, 2008

Claudio De Conto
Manager responsible for the preparation
of the financial reports of the company