PIRELLI & C. S.P.A. SEPARATE FINANCIAL STATEMENTS AT DECEMBER 31, 2018

STATEMENT OF FINANCIAL POSITION

in euro

	Note	12/31/2018	*Of which related parties (Note 38)*	12/31/2017	*Of which related parties (Note 38)*
Property, plant and equipment	8	36,626,844		41,335,010	
Intangible assets	9	2,273,663,830		2,274,121,987	
Investments in subsidiaries	10	4,568,324,362		4,568,309,362	
Investments in associates	11	6,374,501		10,204,402	
Other financial assets	12	-		224,593,085	
Other financial assets at fair value through other comprehensive income	12	66,999,913		-	
Other receivables	13	600,543,719	*600,000,000*	14,819,551	
Derivative financial instruments	17	19,402,654	*19,402,654*	-	
Non-current assets		**7,571,935,823**		**7,133,383,397**	
Trade receivables	14	35,365,570	*32,352,151*	52,045,402	*43,721,766*
Other receivables	13	1,548,690,528	*1,524,041,518*	45,164,222	*13,972,980*
Cash and cash equivalents	15	101,764,103		1,749,490	
Tax receivables	16	49,745,832	*48,490,491*	110,632,072	*104,054,274*
Derivative financial instruments	17	3,749,194	*3,749,194*	94,846	*94,846*
Current assets		**1,739,315,227**		**209,686,032**	
Total assets		**9,311,251,050**		**7,343,069,429**	
Shareholders' equity:					
- Share capital		1,904,374,936		1,904,374,936	
- Other reserves		2,144,425,954		2,163,146,083	
- Retained earnings reserve		181,511,751		-	
- Net income (loss) for the year		262,362,043		170,850,918	
Total shareholders' equity	18	**4,492,674,684**		**4,238,371,937**	
Borrowings from banks and other financial institutions	19	3,921,508,709		2,331,646,999	
Other payables	23	211,511		211,511	
Provisions for liabilities and charges	20	40,530,891		45,677,712	
Provision for deferred tax liabilities	24	527,806,343		554,828,134	
Employee benefit obligations	21	2,210,239		2,071,744	
Derivative financial instruments	17	10,565,158	*10,565,158*	29,715,928	*29,715,928*
Non-current liabilities		**4,502,832,851**		**2,964,152,028**	
Borrowings from banks and other financial institutions	19	222,503,724	*6,591*	16,856,013	*9,411,654*
Trade payables	22	19,380,689	*2,986,850*	29,694,193	*4,819,768*
Other payables	23	48,351,164	*26,177,691*	75,212,817	*27,491,367*
Provisions for liabilities and charges	20	1,815,160		-	
Employee benefit obligations	21	1,964,819		-	
Tax payables	25	16,436,159	*16,207,276*	18,636,545	*18,407,661*
Derivative financial instruments	17	5,291,800	*5,291,800*	145,896	*145,896*
Current liabilities		**315,743,515**		**140,545,464**	
Total Liabilities and Equity		**9,311,251,050**		**7,343,069,429**	

INCOME STATEMENT

in euro

	Note	2018	*Of which related parties (Note 38)*	2017	*Of which related parties (Note 38)*
Revenues from sales and services	26	38,718,521	*37,363,694*	42,084,384	*41,349,034*
Other income	27	112,178,568	*102,183,610*	105,778,332	*99,323,081*
Raw materials and consumables used	28	(210,126)		(183,120)	
Personnel expenses	29	(34,130,338)	*(2,185,521)*	(26,709,830)	*(4,779,614)*
- of which non recurring events	37	-		*(1,691,015)*	
Amortisation, depreciation and impairment	30	(3,983,656)		(4,899,942)	
Other costs	31	(105,044,273)	*(20,168,662)*	(167,059,757)	*(18,618,209)*
- of which non recurring events	37	*(1,025,850)*		*(62,390,073)*	
Net impairment loss on financial assets	32	(1,930,360)		-	
Operating income (loss)		**5,598,336**		**(50,989,933)**	
Net income (loss) from equity investments	33	284,943,288		204,415,855	
- gains on equity investments		*4,006,808*		*2,752,299*	*2,564,250*
- losses on equity investments		*(3,580,191)*	*(3,580,191)*	*(13,833,292)*	*(11,479,999)*
- dividends		284,516,671	*283,549,189*	*215,496,848*	*208,870,744*
Financial income	34	60,818,832	*59,276,892*	116,744,745	*10,680,847*
Financial expenses	35	(93,669,719)	*(6,519,324)*	(240,118,416)	*(103,275,015)*
- of which non recurring events	37	*(9,964,795)*	*(21,977,000)*	(41,966,793)	
Net income (loss) before taxes		**257,690,737**		**30,052,251**	
Taxes	36	4,671,306		140,798,667	
- of which non recurring events	37	*2,677,575*		*96,107,664*	
Total net income (loss) for the year		**262,362,043**		**170,850,918**	

STATEMENT OF COMPREHENSIVE INCOME

in euro

	2018	2017
A - Net income (loss)	**262,362,043**	**170,850,918**
Other components of comprehensive income:		
B - Items that will not be reclassified to income statement:		
- Net actuarial gains (losses) on employee benefits	(8,269)	17,555
- Tax effect	1,985	-
- Fair value adjustment of other financial assets at fair value through other comprehensive income	(5,709,065)	-
Total B	**(5,715,349)**	**17,555**
C - Items reclassified / that may be reclassified to income statement:		
Fair value adjustment of derivatives designated as cash flow hedge		
- Gains / (losses) arising from adjustment to fair value	54,928,567	(7,117,489)
- (Gains) / losses reclassified to income statement	(64,453,722)	(270,006)
- Tax effect	2,286,037	1,708,197
Cost of hedging:		
- Gains /(losses) arising from adjustment to fair value	10,481,543	-
- (Gains) / losses reclassified to income statement	(4,040,529)	-
- Tax effect	(1,545,843)	-
Fair value adjustment of other financial assets available for sale:		
- Gains / (losses) arising from adjustment to fair value	-	40,486,365
- (Gains) / losses reclassified to income statement	-	1,439,103
Total C	**(2,343,947)**	**36,246,170**
B+C Total other components of comprehensive income	**(8,059,296)**	**36,263,725**
A+B+C Total comprehensive income (loss) for the year	**254,302,747**	**207,114,643**

STATEMENT OF CHANGES IN EQUITY (CONTINUED)

in euro

	Share Capital	Legal Reserve	Surplus Reserve	Concentration Reserve	Other Reserves	IAS Reserves (*)	Merger Reserve	Reserve from results carried forward	Net result of the year	Total
Total at 12/31/2016	**1,342,280,641**	**152,113,517**	**-**	**12,466,897**	**92,534,791**	**(12,302,632)**	**1,245,261,239**	**305,401,651**	**68,477,271**	**3,206,233,375**
Board resolution of 6 March, 2017	-	116,962,590	-	-	-	-	-	(116,962,590)		-
Reserve distribution assignment TP Industrial	-	-	-	-	-	-	(175,912,021)	(188,439,061)		(364,351,082)
- Retained earnings								68,477,271	(68,477,271)	-
Annulment treasury shares	3,099,893							(3,099,893)		-
Share capital increase	558,994,402	-	630,380,599	-	-	-	-		-	1,189,375,001
Board resolution of August 1, 2017	-	111,798,881	-	-	-	-	(46,421,503)	(65,377,378)	-	-
Other items of the comprehensive income statement	-	-	-	-	-	36,263,725	-	-	-	36,263,725
Result for the year	-	-	-	-	-	-	-	-	170,850,918	170,850,918
Total comprehensive income/(loss) for the year	-	-	-	-	-	*36,263,725*	-	-	*170,850,918*	*207,114,643*
Total at 12/31/2017	**1,904,374,936**	**380,874,988**	**630,380,599**	**12,466,897**	**92,534,791**	**23,961,093**	**1,022,927,715**	**-**	**170,850,918**	**4,238,371,937**
Adoption of new accounting standard IFRS 9										-
- Reclassification from *available for sale* financial assets to other financial assets at FV through income statement	-	-	-	-	-	(10,554,761)	-	10,554,761	-	-
Total at 1/1/2018	**1,904,374,936**	**380,874,988**	**630,380,599**	**12,466,897**	**92,534,791**	**13,406,332**	**1,022,927,715**	**10,554,761**	**170,850,918**	**4,238,371,937**
Result carried forward s per resolution of May 15, 2018								170,850,918	(170,850,918)	-
Other items of the comprehensive income statement	-	-	-	-	-	(8,059,296)	-	-	-	(8,059,296)
Result for the year	-	-	-	-	-	-	-	-	262,362,043	262,362,043
Total comprehensive income/(loss) for the year	-	-	-	-	-	*(8,059,296)*	-	-	*262,362,043*	*254,302,747*
Other changes	-	-	-	-	-	(106,073)	-	106,073	-	-
Total at 12/31/2018	**1,904,374,936**	**380,874,988**	**630,380,599**	**12,466,897**	**92,534,791**	**5,240,963**	**1,022,927,715**	**181,511,752**	**262,362,043**	**4,492,674,684**

STATEMENT OF CHANGES IN EQUITY

in euro

BREAKDOWN OF IAS RESERVES *							
	Reserve for fair Value adjustment of available-for-sale financial assets	Reserve for fair value adjustment of financial assets at fair value through other comprehensive income	Reserve for actuarial gains/losses	Reserve for cost of hedging	Cash flow hedge reserve	Tax effect	TOTAL
Balance at 12/31/2016	**(14,583,100)**	**-**	**2,010,462**	**-**	**270,006**	**-**	**(12,302,632)**
Other components of comprehensive income	41,925,468	-	17,555	-	(7,387,495)	1,708,197	36,263,725
Balance at 12/31/2017	**27,342,368**	**-**	**2,028,017**	**-**	**(7,117,489)**	**1,708,197**	**23,961,093**
Adoption of new accounting standard IFRS 9	(27,342,368)	16,787,607	-	394,804	(394,804)	-	(10,554,761)
Balance at 1/1/2018	**-**	**16,787,607**	**2,028,017**	**394,804**	**(7,512,293)**	**1,708,197**	**13,406,332**
Other components of comprehensive income	-	(5,709,064)	(8,269)	6,441,013	(9,525,155)	742,179	(8,059,296)
Other changes	-	(106,073)	-	-	-	-	(106,073)
Balance at 12/31/2018	**-**	**10,972,470**	**2,019,748**	**6,835,817**	**(17,037,448)**	**2,450,376**	**5,240,963**

CASH FLOW STATEMENT

in euro

		2018	*Of which related parties (Note 38)*	2017	*Of which related parties (Note 38)*
	Result before taxes	257,690,737		30,052,251	
	Reversal depreciation, amortization and write-downs	3,983,656		4,899,942	
	Reversal financial expenses	93,669,719	*6,519,324*	240,118,416	*103,275,015*
	Reversal financial income	(60,818,832)	*(59,276,892)*	(116,744,745)	*(10,680,847)*
	Reversal result from investments	(284,943,288)	*(283,549,189)*	(204,415,855)	*(199,954,995)*
	Taxes paid	-		-	
	Change in trade receivables	16,679,832	*11,369,615*	9,646,590	*13,193,646*
	Change in trade payables	(10,594,441)	*(1,832,918)*	(2,731,044)	*3,237,898*
	Change in other receivables/other payables	(9,800,604)	*(3,428,000)*	22,708,000	*12,585,217*
	Change in tax receivables/tax payables	42,775,429	*42,775,429*	22,393,548	*36,366,068*
	Change in personnel provisions and other provisions	(1,228,347)		(2,165,575)	
	(Gains)/losses from sales of tangible and intangible assets	(575,786)		11,240	
A	**Net cash generated/(used) by operating activities**	**46,838,075**		**3,772,768**	
	Investments in tangible assets	(1,384)		(338,274)	
	Disinvestments of property, plant & equipment	3,000,000		26,639	
	Investments in intangible assets	(1,024,267)		(1,550,850)	
	Disinvestments of intangible assets	-		750,000	
	Investments in shareholdings in subsidiaries	(15,000)	*(15,000)*	(9,705,361)	*(9,705,361)*
	Disinvestments of shareholdings in subsidiaries	-		7,938	*7,938*
	Investments in other financial assets	-		(2,459,092)	
	Disinvestments of other financial assets	-		2,365	
	Disinvestments of other financial assets non corrent at fair value through other comprehensive income	109,254		-	
	Disinvestments /(Investments) in other financial assets non current at fair value through other comprehensive income	152,807,660		-	
	Disinvestments of shareholdings in associated companies	249,710	*249,710*	17,209,724	*17,209,724*
	Dividends received	284,516,671	*283,549,189*	215,496,848	*208,870,744*
B	**Net cash generated/(used) by investment activities**	**439,642,644**		**219,439,937**	
	Change in share capital	-		1,189,375,000	
	Change in financial receivables	(2,103,421,000)	*(2,103,912,000)*	629,710,507	*629,710,507*
	Interest income and other financial income	15,820,233	*15,820,233*	1,817,000	
	Change in financial payables	1,744,063,616	*(9,000,000)*	(1,884,066,984)	*9,000,000*
	Interest expense and other financial expenses	(42,928,955)	*2,233,556*	(160,104,080)	*(53,865,315)*
C	**Net cash generated/(used) by financing activities**	**(386,466,106)**		**(223,268,557)**	
D	**Total net cash generated/(used) in the year (A+B+C)**	**100,014,613**		**(55,851)**	
E	**Cash and cash equivalents at the beginning of the year**	**1,749,490**		**1,805,342**	
F	**Cash and cash equivalents at the end of the year (D+E)**	**101,764,103**		**1,749,490**	

Explanatory Notes

1. GENERAL INFORMATION

Pirelli & C. S.p.A. (hereinafter also Pirelli, the "Company" or the "Parent Company") is a corporation organised under the laws of the Republic of Italy.

Founded in 1872, it is a holding company that manages, coordinates and funds the activities of subsidiaries (hereinafter Pirelli Group).

The registered office of the Company is in Viale Piero e Alberto Pirelli 25 – Milan.

As from October 4, 2017, Pirelli & C. S.p.A. shares are now traded on the Mercato Telematico Azionario (MTA Telematic Stock Market), managed by Borsa Italiana S.p.A..

Following the total non-proportional demerger of Marco Polo International Italy S.p.A., which took place in August 2018, Pirelli & C. S.p.A. is directly controlled by Marco Polo International Italy S.r.l., newly established company indirectly controlled by China National Chemical Corporation ("ChemChina"), a "state-owned enterprise" (SOE) under Chinese law, with registered office in Beijing, referring to the Central Government of the People's Republic of China.

Marco Polo International Italy S.r.l. controls the Company with 45.52% of the capital and does not exercise management and coordination activities.

On February 26, 2019, the Board of Directors authorised publication of these Annual Financial Statements ("Annual Financial Statements or Separate Financial Statements").

SIGNIFICANT EVENTS 2018

On **January 11, 2018**, Pirelli sold, through an operation reserved to qualified investors in Italy and institutional investors abroad, the entire investment held directly in Mediobanca S.p.A. - corresponding to about 1.8% of the relative share capital - with total net income of Euro 152.8 million.

On **January 22, 2018**, under the EMTN program approved at the end of 2017, Pirelli & C. S.p.A. placed a bond at international institutional investors for a nominal amount of Euro 600 million with a five-year term at fixed rate. The effective yield at maturity is 1.479% and the securities were listed on the Luxembourg Stock Exchange. Furthermore, during the first weeks of January, Pirelli undertook an operation to change the economic conditions of the Group's main banking line - involving a total notional amount of Euro 4.2 billion, including a revolving line of Euro 700 million - which allowed reducing the interest margin applied by 30 basis points.

On **March 15, 2018,** Pirelli & C. S.p.A. placed a "Floating Rate Note" bond with a value of Euro 200 million with maturity in September 2020. The variable rate bond issue - intended exclusively for institutional investors - allowed the repayment of the existing debt for an equal amount, further optimising the company's financial structure by reducing the cost of debt.

On **July 26, 2018**, Pirelli & C. S.p.A. concluded a "Schuldschein" loan for a total of Euro 525 million. The loan, guaranteed by Pirelli Tyre S.p.A. and entered into by leading market operators, consists of a tranche of Euro 82 million with maturity in 3 years, a tranche of Euro 423 million with maturity in 5 years and a tranche of Euro 20 million with maturity in 7 years. The transaction allowed repayment of part of the existing debt, further optimizing the structure and costs.

On **August 7, 2018**, the Board of Directors of Pirelli - with reference to the bond referred to as "Pirelli & C. S.p.A. Euro 600,000,000 1.375 per cent. Guaranteed Notes due 25 January 2023" (ISIN: XS1757843146) issued by Pirelli & C. S.p.A. as part of the EMTN programme of Euro 2 billion and listed on the Luxembourg Stock Exchange - resolved to proceed with the purchase of said bonds for a total nominal value of a maximum of Euro 150 million. As part of this resolution, on October 30, 2018, Pirelli conferred a mandate to Goldman Sachs International to proceed with the partial repurchase of the bond for a maximum nominal amount of Euro 50 million. At the end of the partial repurchase program that was completed on December 19, 2018, bonds were repurchased and annulled for a nominal value of Euro 47 million at an average price of 96.110% and, consequently, the total nominal value of bonds outstanding as of December 31, 2018 is equal to Euro 553 million.

2. BASIS FOR PREPARATION

The 2018 financial statements represent the separate financial statements of the Parent Company Pirelli & C. S.p.A..

These Financial Statements have been prepared on a going concern assumption since the Directors have verified the absence of financial, operational or other types of indicators that could indicate critical issues regarding the ability of the Company to meet its obligations in the foreseeable future and in particular in the next 12 months. The description of the ways in which the Company manages financial risks is contained in Chapter 4 Financial risk management policy and 6 Capital management policy of these Notes.

In application of Legislative Decree of February 28, 2005, no. 38, "Exercise of the options provided for by article 5 of regulation (EC) no. 1606/2002 on international accounting standards", issuers are required to prepare not only the consolidated financial statements but also the financial statements of the Company in compliance with the international accounting standards (IFRS) issued by the International Accounting Standards Board (IASB) and published in the Official Journal of the European Community (GUCE).

IFRS include all International Financial Reporting Standards, International Accounting Standards (IAS), all interpretations of the International Financial Reporting Interpretations Committee (IFRIC), formerly the Standing Interpretations Committee (SIC).

The financial statements have been prepared under the conventional historical cost basis, except for the following items which have been measured at fair value:

- derivate financial instruments;
- financial assets available for sale (until December 31, 2017);
- financial assets at fair value through other comprehensive income (as January 1, 2018);
- financial assets at fair value through income statement (as January 1, 2018).

FINANCIAL STATEMENTS
The separate Financial Statements at December 31, 2018 consist of the Statement of Financial Position, the Income Statement, the Statement of Comprehensive Income, the Statement of Changes in Equity, the Statement of Cash Flows and the Explanatory Notes, and are accompanied by the Directors' Report on Operations.

The Company has chosen to represent the Income Statement by nature of expense, assets and liabilities in the Statement of Financial Position are divided into current and non-current and the Cash Flow Statement has been prepared using the indirect method.

It shall also be noted that the Group has applied the provisions of Consob Resolution no. 15519 of July 27, 2006 in regard to the formats of financial statements and Consob Notice no. 6064293 of July 28, 2006 in regard to corporate disclosure.

All amounts included in the Notes, unless otherwise specified, are in thousands of Euro.

3. ACCOUNTING STANDARDS

The accounting standards used in the preparation of separate financial statements are the same as those used for the purposes of preparing the consolidated financial statements where applicable, except in relation to the assessment of investments in subsidiaries and associate companies and dividends, as indicated below.

INVESTMENTS IN SUBSIDIARIES AND ASSOCIATED COMPANIES
Investments in subsidiaries and associates are recognised at cost, net of any impairment losses.

In the presence of specific impairment indicators, the value of investments in subsidiaries and associates, determined based on the historical cost basis, is tested for impairment.

The indicators are as follows:

- The book value of the investment in the separate financial statements exceeds the book value of the investee's net assets (inclusive of any associates goodwill) expressed in the consolidated financial statements;
- The dividend distributed by the investee exceeds the total undistributed profits of the same investee;
- The operating result achieved by the investee company is significantly lower than the amount envisaged in the management plan, if this indicator can be considered significant for the reference company;
- There are expectations of significantly decreasing operating results for future years;
- Existence of changes in the technological, market, economic or regulatory environment in which the investee operates that may generate significant negative economic effects on the company's results.

The impairment test consists of comparing the book value and the recoverable value of the investment.

If the recoverable amount of an investment is lower than the carrying amount, the latter is reduced to the recoverable amount. This reduction constitutes an impairment loss recognised in the Income Statement.

The recoverable amount of an investment is identified as the greater of fair value and value in use. The value in use of an investment is the present value of future cash flows expected to originate from a cash-generating investment. The value in use reflects the effects of factors that may be entity specific, factors that may not be applicable to any entity.

If the reason for impairment ceases to exist, the carrying amount of the investment is recognised in the Income Statement, up to the original cost.

DIVIDENDS
Dividend income is recognised in the Income Statement when the right to receive payment is established, which normally corresponds to the resolution approved by the Shareholders' Meeting for the distribution of dividends.

3.1 ACCOUNTING STANDARDS AND INTERPRETATIONS ENDORSED AND IN FORCE FROM JANUARY 1, 2018
In accordance with IAS 8 "Accounting standards, changes in accounting estimates and errors", the IFRS effective from January 1, 2018 are indicated below:

- IFRS 15 - Revenues from contracts with customers
  The impacts deriving from the application of this standard, which replaces the previous IAS 18, are described in Note 3.3 "Impacts deriving from the adoption of IFRS 15 and IFRS 9" for the impacts resulting from the first application of this standard.

- IFRS 9 – Financial Instruments
  IFRS 9 replaces the previous IAS 39 standard regarding the classification and measurement of financial assets and liabilities, the impairment of financial assets and hedge accounting. See Note 3.3 "Impacts deriving from the adoption of IFRS 15 and IFRS 9" for the impacts resulting from the first application of this standard.

- Amendments to IFRS 2 - Share-based payments and Classification and measurement of transactions with share-based payment
  The objective of these amendments is to clarify the accounting treatment of some types of share-based payments. Application of these amendments will not have any impact on the separate financial statements.

- IFRIC 22 - Transactions in Foreign Currency and Advances
  The objective of this interpretation is to establish the exchange rate to be used in the conversion of advances in foreign currency, paid or received. In the presence of advances paid or received, the exchange rate to be used to convert assets, liabilities, revenues or costs recognised at a subsequent time is the same used to convert the advance. There are no impacts on the separate financial statements.

- Amendments to IAS 40 - Transfers of property investments
  These amendments further clarify the situations in which it is possible to reclassify a property asset within or outside the category of property investments. These amendments do not apply to the separate financial statements.

- Improvements to IFRS – 2014-2016 cycle (issued by the IASB in December 2016).
  The IASB has issued a series of amendments to 3 current standards, which concern, in particular, the following aspects: clarification on the scope of application of IFRS 12 – Supplementary information relating to interests in other entities - in the presence of re-entrant entities within the scope of application of IFRS 5 – Non-current assets held for sale and discontinued operations; valuation of associates or joint ventures at fair value in the presence of investment entities in IAS 28 – Investment in associated companies; elimination of short-term exemptions for those adopting IFRS for the first time in IFRS 1 – First-time adoption of IFRS. The amendments to IAS 28 and IFRS 1 are not applicable to the Company, while the amendments to IFRS 12 are applicable only in the presence of entities classified under IFRS 5. There are no impacts on the separate financial statements due to application of these amendments.

- Amendments to IFRS 4 - Application of IFRS 9 Financial instruments in case of application of IFRS 4 Insurance contracts.
  These amendments govern the implementation of the new standard IFRS 9 Financial instruments, in case IFRS 4, still subject to further changes, is applicable. These amendments are not applicable to the Company.

3.2 INTERNATIONAL ACCOUNTING STANDARDS AND/OR INTERPRETATIONS ISSUED BUT NOT YET IN FORCE
Pursuant to IAS 8 "Accounting standards, changes in accounting estimates and errors", the following are the new Standards or Interpretations that have been issued but have not yet come into force or have not yet been endorsed by the European Union at December 31, 2018, and which are therefore not applicable, and the foreseeable impacts on the Separate Financial Statements.

None of these standards and interpretations have been adopted in advance.

- Amendments to IFRS 10 and IAS 28 – Sale or transfer of assets from an investing company to an associate or joint venture
  The IASB issued said amendments to eliminate an inconsistency between IFRS 10 and IAS 28, stating that if the assets sold/transferred constitute a business as defined by IFRS 3; the possible gain or loss must be recognised fully and any gain or loss shall be recognised only for the related portion.
  These amendments, the entry into force of which was deferred to an indefinite time, have not yet been endorsed by the European Union. No impacts are expected on the Financial Statements deriving from the future application of these amendments as the current accounting treatment followed by the Company is already compliant.

- IFRS 16 – Leases
  The new lease standard, which will replace the current IAS 17, provides a new definition of lease and

introduces a criterion based on control (right of use) of an asset to distinguish lease contracts from service provision contracts, identifying as discriminants: the identification of the asset, the right to replace the same, the right to obtain substantially all of the economic benefits arising from the use of the asset and lastly, the right to direct the use of the asset underlying the contract.
The standard establishes for the lessee a single model of recognition and evaluation of lease contracts that provides for the recognition of the asset subject to a lease, also operating, in balance sheet asset with a financial payable as balancing entry, for an amount equal to the current value of the future payments. The concept of operating leasing is no longer included. By contrast, the Standard does not include significant changes for lessors.
Said standard, endorsed by the European Union, is applicable from January 1, 2019. The Company will apply the new standard starting from the date of entry into force.
The Company completed the preliminary assessment project of potential impacts deriving from the application of the new standard on the transition date (January 1, 2019). This process was in several phases, including the complete mapping of contracts potentially suitable for containing a lease and the analysis of the same in order to understand the main clauses relevant to IFRS 16.
The Company referred to the practical expedient provided for by the standard, which makes it possible to refer to the conclusions reached in the past on the basis of IFRIC 4 and IAS 17 regarding the quantification of operating leases for a specific contract. This practical expedient was applied to all contracts.
The process of implementation of the standard is being completed, which provides for the setting up of the IT infrastructure aimed at accounting management of the standard and the alignment of administrative processes and controls to oversee critical areas concerned with the standard. This process is expected to be completed within the first quarter of 2019.
The Company has chosen to apply the standard retrospectively, with recognition of the cumulative effect deriving from the application of the standard in shareholders' equity at January 1, 2019 (modified retrospective method). In particular, the Company will recognise, for lease contracts previously classified as operational:

- a financial liability, equal to the present value of the future residual payments at the transition date, discounted using the incremental borrowing rate applicable at the transition date for each contract;
- a right of use equal to the value of the financial liability at the transition date, net of any accrued and deferred assets/liabilities related to the lease and recorded in the balance sheet at the closing date of these financial statements.

The following table shows the impacts estimated from the adoption of IFRS 16 at the transition date:

in thousands of euro

NON-CURRENT ASSETS	
Tangible assets	
- Right of use assets - buildings	33,470
- Right of use assets - car, light vehicles	1,944
Total	**35,415**
CURRENT ASSETS	
Other receivables	(127)
Total assets	**35,228**

in thousands of euro

NON-CURRENT LIABILITIES	
Borrowings from banks and other financial institutions	36,389
CURRENT LIABILITIES	
Borrowings from banks and other financial institutions	2,015
Other payables	(3,116)
Total liabilities	**35,288**

The value of non-current assets relating to operating lease contracts was increased for the balance of accrued/deferred assets recognised at December 31, 2018 for an amount equal to Euro 127 thousand (included under the item other current receivables) and decreased for the balance of accrued liabilities recognised at December 31, 2018 for an amount equal to Euro 3,116 thousand (included under the item other current payables).

In adopting IFRS 16, the Company decided to avail itself of the exemption granted by the standard in relation to short-term leases (contracts with a duration of less than 12 months) for all asset classes. For such contracts the introduction of IFRS 16 will not entail the recognition of the financial liability of the lease and the related right of use, but the lease payments will be recorded in the income statement on a linear basis for the duration of the respective contracts.

The Company also intends to avail itself of the exemption granted by the standard with regard to lease contracts for which the underlying asset is configured as a low-value asset, i.e. lease contracts for which the unit value of the underlying assets is not greater than Euro 8 thousand when new. Contracts for which the exemption was applied fall mainly within the following categories:

- computers, telephones and tablets;
- office and multifunction printers;
- other electronic devices.

For these contracts, the introduction of IFRS 16 will not entail the recognition of the financial liability of the lease and the related right of use. However, the lease payments will be recognised in the income statement on a straight-line basis for the duration of the respective contracts.

The Company intends to use the practical expedient envisaged by IFRS 16 with regard to the separation of non-lease components for vehicles. The non-lease components on these assets will not be separated and accounted separately from the lease components, but will be considered together with the latter in determining the financial liability of the lease and the related right of use.

Furthermore, with reference to the transition rules, the Company intends to avail itself of the following practical expedients available if choosing the modified retrospective transition method:

- classification of contracts that expire within 12 months from the date of transition as a short-term lease. For these contracts, lease payments will be recognised in the income statement on a straight-line basis;
- use of the information present on the transition date for the determination of the lease term, with particular reference to the exercise of extension and early closure options.

The transition to IFRS 16 introduces some elements of professional opinion and the use of assumptions and estimates in relation to the lease term, to the definition of the increase in the borrowing rate. The main ones are summarised below:

- the Company has decided not to apply IFRS 16 for contracts containing a lease that have an intangible asset as an underlying asset;
- contract renewal clauses are considered for the purposes of determining the duration of the contract when the Company has the option of exercising them without the need to obtain the consent of the counterparty and their exercise is deemed reasonably certain. In the case of clauses providing for multiple renewals that can be exercised unilaterally by the Company, only the first extension period has been considered;
- automatic renewal clauses in which both parties have the right to terminate the contract are not considered for the purposes of determining the duration of the contract, as the ability to extend the duration of the same is not under the unilateral control of the Company and the penalty to which the lessor could be exposed is not significant. However, in the event that the lessor is exposed to a significant penalty, the Company includes the renewal option in determining the duration of the contract. This assessment is also carried out considering the degree of customisation of the asset subject to leasing: if the customisation is high, the lessor may incur a significant penalty if opposing renewal;
- early termination clauses of contracts: these clauses are not considered in determining the duration of the contract if they can only be exercised by the lessor or by both parties. If they can be unilaterally exercised by the Company, specific assessments are made contract by contract (for example, the Company is already negotiating a new contract or has already given termination notice to the lessor);
- incremental borrowing rate: the Company decided to use the incremental borrowing rate as discount rate to discount lease contract payments. This rate consists of the free risk rate of the country in which the contract is negotiated and based on the duration of the contract. It is then adjusted according to the Company's credit spread and the local credit spread.

RECONCILIATION WITH COMMITMENTS FOR FUTURE MINIMUM PAYMENTS DUE FOR NON-CANCELLABLE OPERATING LEASES

In order to facilitate the understanding of the impacts arising from the first application of the standard, the following table provides a reconciliation between future commitments relating to lease contracts, which is referred to in paragraph 8, and the impact expected from the adoption of IFRS 16 as of January 1, 2019:

in thousands of euro

Future minimum lease payments for operating leases at 12/31/2018 (IAS 17)	47,796
Short term leases	(136)
Leases of low value assets	(127)
Discounting	(11,144)
Financial liabilities for leases contracts at 1/1/2019 (IFRS 16)	**36,389**

- IFRIC 23 – Uncertainty on the treatment of income taxes
  This interpretation clarifies the criteria to be applied for the recognition and measurement of current and deferred tax liabilities/assets in the event of uncertainty regarding the tax treatment, i.e. situations in which it is not certain that a specific treatment will be accepted by the tax authorities (ex. deductibility some costs or exemption of some income), but also uncertainty regarding the determination of taxable income, the tax base of assets and liabilities, tax losses and rates to be applied.
  The accounting treatment depends on the probability of whether tax authorities will accept the tax treatment or not. In the event it is not probable that the tax authority accept the uncertain tax treatment, uncertainty is recorded by recognising an additional tax liability or by applying a higher rate.
  Said interpretation, endorsed by the European Union, is applicable from January 1, 2019. No significant impacts are expected on the Financial Statements of the Company.

- Amendments to IFRS 9 – Financial Instruments: prepayment features with negative compensation and amendments to financial liabilities
  Said amendments concern the following:
  - o financial assets (financial receivables and debt securities) which, in the presence of certain characteristics, can be measured at amortised cost, whereas previously they had to be measured at fair value recorded in the income statement;
  - o accounting treatment in the presence of changes to financial liabilities that do not lead to derecognition from the financial statements: in such situations, a profit or loss calculated as the difference between the contractual cash flows of the original liability and the changed cash flows must be recorded in the income statement, both discounted at the original effective interest rate.

  These amendments, which will come into force on January 1, 2019, have not yet been endorsed by the European Union. With regard to the change relating to financial assets, assessments are underway to verify their applicability to the Group and to the Company; the change in the accounting treatment of financial liabilities in the event of changes that do not lead to derecognition is applicable to the Company and has no impact as the Company already applies this accounting treatment.

- Amendments to IAS 28 – Investments in associates and joint ventures: long-term interests in associates and joint ventures
  These amendments clarified that, if investments in associates and joint ventures are not valued using the equity method (IAS 28), they must be valued in accordance with the provisions of IFRS 9.
  These amendments, which will come into force on January 1, 2019, have not yet been endorsed by the European Union. No impacts are expected on the Financial Statements of the Company.

- "Improvements" to IFRS 2015-2017 (issued by the IASB in December 2017).
  The IASB issued a series of amendments to 4 standards in force in particular regarding the following aspects:
  - IFRS 3 – business combinations: obtaining control of a business that is classified as a joint operation must be accounted for as a business combination in phases and the investment previously held must be remeasured at fair value on the date of acquisition.
  - IFRS 11 – Joint arrangements: in the case of obtaining joint control over a business that is classified as a joint operation, the investment previously held does not have to be remeasured at fair value.
  - IAS 12 – taxes: the accounting treatment of the tax effects of dividends on financial instruments classified as equity must follow that of the transactions or events that generated the distributable dividend.
  - IAS 23 – financial expenses: if a specific loan relating to a qualifying asset is still outstanding at the time the asset is ready for use or sale, it becomes part of the generic loans.

  These amendments, which will come into force on January 1, 2019, have not yet been endorsed by the European Union. Any impacts on the financial statements of the Group and the Company are currently being analysed.

- Amendments to IAS 19 – Employee benefits
  Said amendments require that:
  - the cost for the current service and the net interest for the period following a modification and/or reduction of the plan are determined using updated assumptions;
  - any reductions in the surplus of a plan are recognised in the income statement, even if the surplus had not been recognised in the income statement due to the asset ceiling.

  These amendments, which will come into force on January 1, 2019, have not yet been endorsed by the European Union.

- Amendments to IFRS 3 – Business Combinations
  These amendments introduced a new definition of business, as the current one is too complex with the result that too many transactions qualified as a business combination.
  These amendments, which will come into force on January 1, 2020, have not yet been endorsed by the European Union.

- Amendments to IAS 1 – Presentation of Financial Statements and to IAS 8 – Accounting standards, Changes in accounting estimates and errors
  In addition to clarifying the concept of materiality, these amendments focus on the definition of a coherent and unique concept of materiality among the various accounting standards and incorporate the guidelines included in IAS 1 on intangible information.
  These amendments, which will come into force on January 1, 2020, have not yet been endorsed by the European Union.

3.3 IMPACTS DERIVING FROM THE ADOPTION OF IFRS 15 AND IFRS 9

The table below shows the effects on the opening balance sheet at January 1, 2018 following the first application of IFRS 15 and IFRS 9:

STATEMENT OF FINANCIAL POSITION

in thousands of euro

	Note	12/31/2017	IFRS 15 1st adoption	IFRS 9 1st adoption	1/1/2018
Property, plant and equipment	8	41,335			41,335
Intangible assets	9	2,274,122			2,274,122
Investments in subsidiaries	10	4,568,309			4,568,309
Investments in associates	11	10,204			10,204
Other financial assets	12	224,593		*(224,593)*	-
Other financial assets at fair value through other comprehensive income	12	-		*75,566*	75,566
Other financial assets at fair value through income statement	12	-		*149,027*	149,027
Other receivables	13	14,820			14,820
Non-current assets		**7,133,383**	**-**	**-**	**7,133,383**
Trade receivables	14	52,046			52,046
Other receivables	13	45,164			45,164
Cash and cash equivalents	15	1,749			1,749
Tax creditis	16	110,632			110,632
Derivative financial instruments	17	95			95
Current assets		**209,686**	**-**	**-**	**209,686**
Total Assets		**7,343,069**	**-**	**-**	**7,343,069**
					-
Equity attributable to owners of the Group:		**4,238,372**	**-**	**-**	**4,238,372**
- Share capital		1,904,375			1,904,375
- Reserves		2,163,146			2,163,146
- Net income (loss) for the period		170,851			170,851
Total Equity	**18**	**4,238,372**	**-**	**-**	**4,238,372**
Borrowings from banks and other financial institutions	19	2,331,647			2,331,647
Other payables	23	212			212
Provisions for liabilities and charges	20	45,677			45,677
Provisions for deferred tax liabilities	24	554,828			554,828
Employee benefit obligations	21	2,072			2,072
Derivative financial instruments	17	29,716			29,716
Non-current liabilities		**2,964,152**	**-**	**-**	**2,964,152**

	Note	12/31/2017	IFRS 15 1st adoption	IFRS 9 1st adoption	1/1/2018
Borrowings from banks and other financial institutions	19	16,856			16,856
Trade payables	22	29,694			29,694
Other payables	23	75,213			75,213
Tax payables	25	18,636			18,636
Derivative financial instruments	17	146			146
Current liabilities		**140,545**	-	-	**140,545**
Total Liabilities and Equity		**7,343,069**	-	-	**7,343,069**

IFRS 15 IFRS 15 had no impact on the methods for recognising revenues and the reporting of said revenues. Consequently, there were no impacts on the Company's shareholders' equity at the transition date.

IFRS 9 - FINANCIAL INSTRUMENTS IFRS 9 has been applied retrospectively and the date of first application coincides with January 1, 2018. The comparable data for 2017 was not subject to restatement.

→ Classification and measurement
At January 1, 2018, based on the assessment of the applicable business model and the contractual conditions of the cash flows associated with the assets, financial assets were classified in the categories envisaged by IFRS 9. Equity instruments that at December 31, 2017 were classified as available for sale financial assets (AFS) were designated as financial assets at fair value recorded in the other components of the comprehensive income statement (FVOCI), as they do not belong to the Company's core operations. The sole exception concerns the investment in Mediobanca S.p.A., which has instead been classified in financial assets for which fair value changes are recognised through profit or loss (FVPL). The investment in Mediobanca S.p.A. was sold in the first days of January 2018 and the positive fair value change of Euro 3,780 thousand was recognised in the income statement under the item "Gains on equity investments" (Note 33.1).

The following table summarises the reclassifications made:

in thousands of euro

	Other non current financial assets at FV through income statement	Other financial assets at FV through other comprehensive income (available for sale financial assets 2017)	Financial assets at amortised cost (gross trade receivables and gross other receivables)
Total at 12/31/2017	-	**224,593**	**116,235**
Reclassification from available for sale financial assets to other financial assets at FV through income statement	149,027	(149,027)	-
Total at 01/01/2018	**149,027**	**75,566**	**116,235**

→ *Impairment of financial assets*
The Company analysed the impacts of the new impairment model of IFRS 9 based on expected losses in relation to trade and financial receivables.
For trade receivables, the Company has applied the simplified approach permitted by the standard, according to which expected losses are calculated over the life of receivables and has used a matrix based on historical experience and related to credit aging, adjusted to take account of specific factors to some creditors. There are no impacts on Company assets at the transition date due to the application of the new impairment model to trade receivables.

→ Hedge accounting: the Company has adopted the new rules for hedge accounting required by IFRS 9 prospectively starting from January 1, 2018. Hedging relations outstanding at December 31, 2017 met the conditions required by IFRS 9 to continue adopting hedge accounting. It should be noted that, based on the provisions of IFRS 9, the cash flow hedge reserve relating to cash flow hedges outstanding at December 31, 2017 was partly reclassified to a new reserve for cost of hedging in equity for an amount equal to Euro 394 thousand. The reclassification relates to the change in the fair value of the cross currency basis spread which, not being hedge accounting, is separated and recorded in a separate equity reserve, while the cash flow hedge reserve only includes changes in fair value in hedge accounting.

The impacts on the individual components of Company equity deriving from the first application of IFRS 9 are summarised in the following table:

in thousands of euro

	Reserve for fair value adjustment of available for sale financial assets	Reserve for fair value adjustment of financial assets at fair value through other comprehensive income	Reserve for cash flow hedge	Reserve for cost of hedging	Other reserves / retained earnings
Total at 12/31/2017	**27,342**	-	**(7,117)**	-	**92,535**
Reclassification from available for sale financial assets to other financial assets at FV through income statement (Mediobanca)	(10,554)	-	-	-	10,554
Reclassification from available for sale financial assets to other financial assets at FV through other comprehensive income	(16,788)	16,788	-	-	-
Impairment of financial assets	-	-	-	-	-
Reclassification for hedge accounting	-	-	(394)	394	-
Total at 01/01/2018	-	**16,788**	**(7,511)**	**394**	**103,089**

It should be noted that the fair value adjustment reserve for available for sale financial assets at December 31, 2017 (positive for Euro 27,342 thousand) was reclassified to a new reserve in equity for investments designated as assets at fair value recorded in the other components of the comprehensive income statement, while it was reclassified in retained earnings for investments for which the changes in fair value are recognised in the income statement. These reserves will not be reversed to the income statement if the investments are sold.

4. FINANCIAL RISK MANAGEMENT POLICY

The measurement and management of the financial risks of Pirelli & C. S.p.A. are consistent with as defined by the Group policies.

The Pirelli Group is exposed to financial risks. These are principally associated with foreign exchange rates, fluctuations in interest rates, the price of financial assets held as investments, the ability of customers to meet their obligations to the Group (credit risk), and raising funds on the market (liquidity risk).

Financial risk management is an integral part of Group business management and is handled directly by the headquarters in accordance with guidelines issued by the Finance Department on the basis of general risk management strategies defined by the Managerial Risk Committee.

The main financial risk categories to which the Company is exposed are shown below:

EXCHANGE RATE RISK

This risk is generated by the commercial and financial transactions that are executed in currencies other than the Euro. Exchange rate fluctuations between the time when the commercial or financial relationship is established and when the transaction is completed (collection or payment) may generate foreign exchange gains or losses.

The Group's objective is to minimise the effects on the Income Statement of foreign exchange rate risk related to volatility. To achieve this objective, Group procedures make the Operating Units responsible for collecting complete information about the assets and liabilities that are subject to transaction exchange rate risk. This risk is hedged with forward contracts made with the Group Treasury.

The items subject to exchange rate risk are mainly represented by receivables and payables denominated in foreign currency.

The Group Treasury is responsible for hedging the net position for each currency and, in accordance with established guidelines and restrictions, it closes all risk positions by trading derivative contracts on the market, which typically take the form of forward contracts.

The Group has decided not to opt for hedge accounting pursuant to IFRS 9, insofar as the representation of the economic and financial effects of the hedging strategy on foreign exchange rate risk is still substantially guaranteed even without adopting such option.

Furthermore, it shall be noted that as part of the annual and three-year planning process, exchange rate forecasts are made using the best information available on the market. The fluctuation in exchange rates between the time when the forecast is made and the time when the commercial or financial transaction occurs represents the exchange rate risk on future transactions.

From time to time, the Group assesses the need to engage in hedging transactions on future transactions for which it typically uses both forward and optional purchase or sale transactions such as risk reversal (ex. zero cost collar).

The Company enters into derivative contracts, cross currency interest rate swaps, to hedge for which hedge accounting is activated when the conditions set out in IFRS 9 are fulfilled.

INTEREST RATE RISK

Interest rate risk is the risk that the fair value or the future cash flows of a financial asset or liability will change due to fluctuations in market interest rates.

The Group assesses based on market circumstances whether to enter into derivative contracts, typically interest rate swaps, to hedge for which hedge accounting is activated when the conditions set out in IFRS 9 are fulfilled.

At December 31, 2018, the Company had a negative net financial position, with all financial payables at variable rates.

In other conditions being equal, a hypothetical increase or a decrease of 0.50% in the level of interest rates would result, year on year, respectively in a net negative and positive impact on the Income Statement of Euro 7,110 thousand.

in thousands of euro

	+0.50%		-0.50%	
	2018	2017	2018	2017
Impact on the net result	(7,110)	(8,920)	7,110	8,920

The effects on the Company shareholders' equity resulting from changes in the LIBOR and EURIBOR rates calculated on the interest rate hedging instruments outstanding at December 31, 2018 are described in note 17 "Derivative financial instruments".

PRICE RISK ASSOCIATED WITH FINANCIAL ASSETS

The company is exposed to price risk, which is limited to the volatility of financial assets such as listed and unlisted stocks and bonds; these assets are classified as financial assets at fair value recognised as other components of the comprehensive income statement.

Derivatives hedges are not set up to limit the volatility of these assets.

FINANCIAL ASSETS MEASURED AT FAIR VALUE THROUGH THE INCOME STATEMENT

Financial assets at fair value recognised as other components of the comprehensive income statement consist of listed securities amounted to Euro 28,448 thousand (Euro 30,177 thousand at December 31, 2017) and those represented by securities indirectly associated with listed shares (Fin. Priv. S.r.l.) amounted to Euro 15,604 thousand (Euro 19,908 thousand at December 31, 2017); these financial assets represent 66% of total financial assets subject to price risk; a +5% price change in the above listed securities, other things being equal, would result in a positive change of Euro 1,422 thousand of the Company's shareholders' equity (positive for Euro 8,960 thousand at December 31, 2017), while a -5% change of these listed securities, other things being equal, would result in a negative change of Euro 1,422 thousand of the Company's shareholders' equity (at December 31, 2017, negative for Euro 8,960 thousand of the Company's shareholders' equity).

CREDIT RISK

Credit risk represents the Company's exposure to contingent losses resulting from default by commercial and financial counterparties. The Company's exposure for commercial obligations is mainly towards Group companies, for financial obligations totally towards Group companies.

To limit the risk for commercial obligations towards third parties, the Company has implemented procedures to evaluate its customers' potential and financial solidity, for the monitoring of expected cash flows and taking credit recovery action if necessary. The Company operates only with highly rated financial counterparties for the management of its temporary cash surpluses and constantly monitors its exposure to individual counterparties.

The Company does not hold public debt instruments from any European country, and constantly monitors its net credit exposure to the banking system.

LIQUIDITY RISK

Liquidity risk represents the risk that the financial resources available are insufficient to meet the financial and commercial obligations pursuant to the contractual terms and conditions.

The principal instruments used by the Group to manage liquidity risk are comprised by its annual and three-year financial and cash-pooling plans. These allow complete and fair detection and measurement of incoming and outgoing cash flows. The differences between plans and actual data are constantly analysed.

The Group has implemented a centralised cash pooling system for the management of collection and payment flows in compliance with various local currency and tax laws. Banking relationships are negotiated and managed centrally, in order to ensure coverage of short and medium-term financial needs at the lowest possible cost. The procurement of medium and long-term resources on the capital market is also streamlined through centralised management.

Prudent management of the risk described above requires maintaining an adequate level of cash or cash equivalents and/or highly liquid short-term financial instruments, and the availability of funds through an adequate amount of committed credit facilities and/or recourse to the capital market, while diversifying the products and their maturities to seize the best available opportunities.

At December 31, 2018, the Company had, aside from cash equal to Euro 101,764 thousand (Euro 1,749 thousand at December 31, 2017), unused credit lines equal to Euro 700,000 thousand (Euro 100,000 thousand at December 31, 2017) maturing in the second quarter of 2022, due to the transfer of all the Facilities that included an RCF line not used at the transfer date equal to 600,000 thousand.

The maturities of financial liabilities at December 31, 2018 may be broken down as follows:

in thousands of euro

	12/31/2018				
	up to 1 year	from 1 to 2 years	from 2 to 5 years	over 5 years	Total 12/31/2017
Payables to banks and other lenders	295,729	1,316,688	2,859,928	21,029	4,493,374
Trade payables	19,381	-	-	-	19,381
Other payables	48,351	-	-	-	48,351
Derivative financial instruments	(19,608)	(24,403)	(37,148)	(62)	(81,221)
Total	**343,853**	**1,292,285**	**2,822,780**	**20,967**	**4,479,885**

The maturities of financial liabilities at December 31, 2017 could be broken down as follows:

in thousands of euro

	12/31/2017				
	up to 1 year	from 1 to 2 years	from 2 to 5 years	over 5 years	Total 12/31/2017
Payables to banks and other lenders	57,667	53,314	2,447,334	-	2,558,315
Trade payables	29,694	-	-	-	29,694
Other payables	75,213	212	-	-	75,425
Derivative financial instruments	146	3,638	26,077	-	29,861
Total	**162,720**	**57,164**	**2,473,411**	**-**	**2,693,295**

5. INFORMATION ON FAIR VALUE

5.1 FAIR VALUE MEASUREMENT

In relation to financial instruments measured at fair value, the following table shows the classification of these instruments on the basis of the hierarchy of levels pursuant to IFRS 13, reflecting the significance of the inputs used in determining the fair value. The levels are as follows:

→ level 1 – unadjusted quotations recorded on an active market for assets or liabilities subject to valuation;
→ level 2 – inputs different from the quoted prices referred to at the preceding level, which are observable on the market either directly (as in the case of prices) or indirectly (because they are derived from prices);
→ level 3 – inputs that are not based on observable market data.

The following table shows assets measured at fair value as at December 31, 2018, divided into the three levels defined above:

in thousands of euro

	Nota	12/31/2018	Level 1	Level 2	Level 3
FINANCIAL ASSETS					
Other financial assets at fair value through income statement					
Non current derivative financial instruments	17	-	-	-	-
Current derivative financial instruments	17	325	-	325	-
Other financial assets at fair value through other comprehensive income					
Equities and shares	12	51,425	28,449	15,604	7,372
Investment funds	12	15,575	-	15,575	-
Derivative hedging instruments					
Non current derivative financial instruments	17	19,403	-	19,403	-
Current derivative financial instruments	17	3,424	-	3,424	-
TOTAL ASSETS		**90,152**	**28,449**	**54,331**	**7,372**
FINANCIAL LIABILITIES					
Financial liabilities at fair value through profit or loss					
Current derivative financial instruments	17	(44)	-	(44)	-
Derivative hedging instruments					
Non current derivative financial instruments	17	(5,248)	-	(5,248)	-
Current derivative financial instruments	17	(10,565)	-	(10,565)	-
TOTAL LIABILITIES		**(15,857)**	**-**	**(15,857)**	**-**

At December 31, 2017, the breakdown was as follows:

in thousands of euro

	Nota	12/31/2017	Level 1	Level 2	Level 3
FINANCIAL ASSETS					
Available-for-sale financial assets:					
Other financial assets					
Equities and shares	12	209,323	179,204	19,909	10,210
Investment funds	12	15,270	-	15,270	-
Derivative hedging instruments					
Current derivative financial instruments	17	95	-	95	-
TOTAL ASSETS		**224,688**	**179,204**	**35,274**	**10,210**
FINANCIAL LIABILITIES					
Financial liabilities at fair value through profit or loss					
Current derivative financial instruments	17	(146)	-	(146)	-
Derivative hedging instruments					
Non current derivative financial instruments	17	(29,716)	-	(29,716)	-
TOTAL LIABILITIES		**(29,862)**	**-**	**(29,862)**	**-**

The following table shows the changes of financial assets that occurred in level 3:

in thousands of euro

	12/31/2018	12/31/2017
Opening balance	**10,210**	**7,248**
Increases	-	781
Decreases	(2,857)	-
Reclassification	-	-
Transfer from level 2 to level 3	-	2,730
Impairment	-	(912)
Fair value adjustments through other comprehensive income	19	363
Closing balance	**7,372**	**10,210**

These financial assets mainly consist of the equity investment in Istituto Europeo di Oncologia (European Institute of Oncology) (Euro 6,961 thousand).

Decreases mainly refer to the liquidation of the investment in Emittenti Titoli S.p.A..

In the year ended December 31, 2018, there were no transfers from level 1 to level 2 and vice versa, nor from level 3 to other levels and vice versa.

The fair value of financial instruments traded on active markets is based on the price quotations published at the reporting date. These instruments, included in level 1, comprise primarily financial assets at fair value through other comprehensive income.

The fair value of financial instruments not traded on active markets (e.g. derivatives) is measured by means of techniques that maximise the use of observable and available market data, using widely applied financial measurement techniques:

→ market prices for similar instruments;
→ the fair value of cross currency interest rate swaps is calculated by discounting estimated future cash flows based on observable yield curves;
→ the fair value of foreign exchange derivatives (forward contracts) is determined by using the forward exchange rate at the reporting date.

5.2 CATEGORIES OF FINANCIAL ASSETS AND LIABILITIES

The following are the carrying amounts for each class of financial asset and liability identified by IFRS 9:

in thousands of euro

	Note	12/31/2018	12/31/2017
FINANCIAL ASSETS			
Financial assets at fair value through profit or loss			
Derivative financial instruments	17	325	-
Financial assets at amortized cost			
Other non-current receivables	13	600,544	14,820
Current trade receivabels	14	35,366	52,045
Other current receivables	13	1,548,690	45,164
Cash	15	101,764	1,749
Available-for-sale financial assets			
Other financial assets	12	-	224,593
Financial assets at fair value through other comprehensive income	**12**	67,000	-
Derivative hedging instruments			
Current derivative financial instruments	17	3,424	95
Non current derivative financial instruments	17	19,403	-
Total financial assets		**2,376,516**	**338,466**

	Note	12/31/2018	12/31/2017
FINANCIAL LIABILITIES			
Financial liabilities at fair value through profit or loss			
Derivative financial instruments	17	44	146
Financial liabilities at amortized cost			
Non-current borrowings from banks and other financial institutions	19	3,921,509	2,331,647
Current borrowings from banks and other financial institutions	19	222,504	16,856
Current trade payables	22	19,380	29,694
Other non-current payables	23	212	212
Other current payables	23	48,351	75,213
Derivative hedging instruments			
Current derivative financial instruments	17	5,248	-
Non current derivative financial instruments	17	10,565	29,716
Total financial liabilities		**4,227,813**	**2,483,484**

6. CAPITAL MANAGEMENT POLICY

The Company's objective is to maximise the return on net invested capital while maintaining the ability to operate over time, ensuring adequate returns for its shareholders and benefits for the other stakeholders, with progressive deleverage of the financial structure in the short/medium term.

In order to achieve these objectives, as well as pursuing satisfactory earnings results and generating cash flows, the Company may adjust its policy regarding dividends and the configuration of the Company's capital.

7. ESTIMATES AND ASSUMPTIONS

The preparation of the Financial Statements requires Directors to apply accounting standards and methodologies which, under certain circumstances, are based on subjective assessments and estimates that are based on historical experience and assumptions that are considered reasonable and realistic from time to time depending on the circumstances. The final results of the items of the financial statements for which said estimates and assumptions were used may differ from those in the financial statements that show the effects of the occurrence of the event subject of the estimate due to the uncertainty that characterizes the assumptions and conditions on which the estimates are based.

Below is a brief description of the accounting standards that, in relation to Pirelli & C. S.p.A., involve more than others a higher level of subjectivity by the management in making estimates and for which a change in the conditions underlying the assumptions used could have a significant impact on the financial information.

PIRELLI BRAND (INTANGIBLE ASSET WITH AN INDEFINITE USEFUL LIFE)

The Pirelli Brand is intangible fixed asset with an indefinite useful life are not subject to amortisation, but pursuant to IAS 36, is tested for impairment annually or more frequently, if specific events or circumstances arise that may indicate a reduction in value.

The impairment test at December 31, 2018 was performed using the assistance of an independent third-party professional.

The configuration of the recoverable amount for impairment testing purposes at December 31, 2018 was the fair value, calculated on the basis of the income approach (the so-called Level 3 of the hierarchy of IFRS 13 – Fair Value measurement).

For the purposes of impairment testing, the recoverable amount of the Pirelli Brand *cum*-TAB was compared with the carrying amount of the Brand *cum*-TAB and no impairment emerged.

INVESTMENTS IN SUBSIDIARIES Investments are assessed to establish whether there was a decrease in value, if there are indications that it will be difficult to recover their net accounting value through use. To establish the presence of said indications, Directors must make subjective assessments on the basis of information available within the Company and the market, as well as historical experience. Moreover, if it is determined that a potential impairment may be generated, the Company calculates this loss using appropriate measurement techniques. The proper identification of elements indicating the existence of a potential impairment loss, and the estimates for calculating the amount of such losses, depend on factors that may vary over time, affecting the assessments and estimates made by Directors.

PROVISIONS FOR RISKS AND CHARGES Provisions are set aside against contingent legal and fiscal liabilities related to indirect tax, representing the risk of negative outcome. The value of the provisions recorded in the financial statements relating to these risks represents the best estimate at the date made by the directors. Such an estimate entails making assumptions that depend on factors that may change over time and which could therefore have a material impact with respect to the current estimates made by Directors for the preparation of the Company's Financial Statements.

TAXES Significant elements of estimation are necessary in defining the forecasts of current taxes for the year and deferred tax assets and liabilities.

8. PROPERTY, PLANT AND EQUIPMENT

The items in question and the related changes are detailed as follows:

in thousands of euro

	Land	Buildings	Plant and machinery	Industrial and commercial equipment	Other assets	Assets in progress and advances	Total
Net value as of December 31, 2016	**9,021**	**28,306**	**880**	**17**	**4,722**	**475**	**43,421**
Increases	-	332	-	-	118	-	450
Decreases	-	(112)	-	-	(37)	-	(149)
Reclassification	-	475	-	-	-	(475)	-
Depreciation	-	(1,705)	(219)	(5)	(458)	-	(2,387)
At 31 December 2017	**9,021**	**27,296**	**661**	**12**	**4,345**	**-**	**41,335**
Of which:							
- Historical cost	9,021	55,639	4,686	985	14,693	-	85,024
- Accumulated depreciation	-	(28,343)	(4,025)	(973)	(10,348)	-	(43,689)
Net value as of December 31, 2017	**9,021**	**27,296**	**661**	**12**	**4,345**	**-**	**41,335**
Increases	-	-	-	-	1	-	1
Decreases	(2,437)	(53)	-	-	-	-	(2,490)
Reclassification	-	-	-	-	-	-	-
Depreciation	-	(1,708)	(208)	(3)	(300)	-	(2,219)
At 31 December 2018	**6,584**	**25,535**	**453**	**9**	**4,046**	**-**	**36,627**
Of which:							
- Historical cost	6,584	48,974	3,628	942	14,430	-	74,558
- Accumulated depreciation	-	(23,439)	(3,175)	(933)	(10,384)	-	(37,931)
Net value as of December 31, 2018	**6,584**	**25,535**	**453**	**9**	**4,046**	**-**	**36,627**

No investments were made in 2018.

The decreases for the year refer to the sale of a piece of land in Milan, against which a gain of Euro 563 thousand was realised.

The total of the future minimum payments due for non-cancellable operating leases amount to Euro 47,796 thousand, of which:

- Euro 3,465 thousand within one year;
- Euro 31,049 thousand between one and five years;
- Euro 13,200 thousand over 5 years.

9. INTANGIBLE ASSETS

The items in question and the related changes are detailed as follows:

in thousands of euro

	Brand	Software Licenses	Other assets	Assets in progress and advances	Total
At 31 December 2016	**2,270,000**	**1,078**	**4,007**	**750**	**2,275,835**
Increases	-	311	1,084	156	1,551
Decreases	-	-	-	(750)	(750)
Amortisation	-	(387)	(2,127)	-	(2,514)
At 31 December 2017	**2,270,000**	**1,002**	**2,964**	**156**	**2,274,122**
Increases	-	224	1,081	-	1,305
Decreases	-	-	-	-	-
Reclassification	-	-	156	(156)	-
Amortisation	-	(393)	(1,370)	-	(1,763)
At 31 December 2018	**2,270,000**	**833**	**2,831**	**-**	**2,273,664**

The item Trademark refers to the value of the Pirelli Brand (asset with indefinite useful life) for Euro 2,270,000 thousand, which originated following the allocation of the merger deficit, generated as a result of the incorporation of the parent company Marco Polo International Holding Italy S.p.A. in 2016. The allocation of the deficit was made consistently with the consolidated financial statements as a result of the completion of the Purchase Price Allocation.

The valuation of the useful life of the brands is based on a series of factors including the competitive environment, market share, history of the brand, life cycles of the underlying product, operational plans and macroeconomic environment of the countries in which the related products are sold. In particular, the useful life of the Pirelli Brand was assessed as indefinite based on its history of over one hundred years of success (created in 1872) and the intention and ability of the Group to continue investing to support and maintain the brand.

The increases in the year mainly include charges for the purchase of software applications (Euro 746 thousand), licenses (Euro 224 thousand), systems for personnel management (Euro 256 thousand) and treasury (Euro 79 thousand).

No impairment was carried out during the 2018 financial year.

THE IMPAIRMENT TESTING OF THE PIRELLI BRAND (INTANGIBLE FIXED ASSET WITH AN INDEFINITE USEFUL LIFE)

The Pirelli Brand at euro 2,270,000 thousand is an intangible fixed asset with an indefinite useful life and as such is not subject to amortisation, but pursuant to IAS 36, is tested for impairment annually or more, frequently, if specific events or circumstances arise that may indicate an impairment.

The impairment test as at December 31, 2018 was carried out with the assistance of an independent third party professionals.

The configuration for the recoverable amount for the purposes of impairment testing at December 31, 2018 was the fair value, calculated on the basis of the income approach (the so-called Level 3 of the hierarchy of IFRS 13 – Fair Value measurement) and is based on:

- the consensus forecasts by equity analysts with respect to the forecast revenues for the period 2019-2020 in that they were more prudent than the projections made by management;
- an evaluation criterion is obtained by the sum of parts which also takes into account the contribution of royalties from the Prometeon Tyre Group for the use the Pirelli trademark in relation to the industrial segment;
- the royalty rate applied to the revenues of the Consumer High Value and Consumer Standard segment was deduced from the royalty rates implicit in the valuations made by an independent entity relative to the main brands of the listed companies of the Tyre sector and was equal to an average royalty rate of 5.01%. With reference to the contribution in terms of royalties from the Prometeon Tyre Group, the royalty rates used were those provided for by the license agreement subject to the reshaping of the contract as approved by the Board of Directors on February 14, 2019;
- a discount rate of 8.38%, which included a premium determined on the basis of the risk of the specific asset;
- a growth rate of g in the terminal value assumed to be equal to zero;
- the TAB (Tax Amortisation Benefit) that is, the tax benefit that could potentially benefit the market participant due to the possibility of fiscally amortising the asset.

For the purposes of impairment testing, the recoverable amount of the Pirelli Brand *cum* TAB was compared with the carrying amount of the Brand *cum*-TAB and no impairment emerged.

A sensitivity analysis was also carried out in relation to the Key Assumptions used in the valuation of the royalty rate (for the Consumer evaluation unit and for the contribution in terms of royalties from the Prometeon Group); the discount rate, and the g growth factor. The fair value remained higher than the carrying amount even assuming the following changes in the sole Key assumption:

- a downward change in the royalty rates for the Consumer evaluation units of 50 basis points and the simultaneous zero balance for royalties from the license agreement with Prometeon Tyre Group;
- an upward change in the discount rate of150 basis points;
- a downward change in the g growth rate of 150 basis points.

10. INVESTMENTS IN SUBSIDIARIES

At December 31, 2018, this item amounted to Euro 4,568,324 thousand (Euro 4,568,309 thousand at December 31, 2017) and the breakdown is as follows:

in thousands of euro

	12/31/2018	12/31/2017
HB Servizi S.r.l.	230	230
Maristel S.p.A.	1,315	1,315
Pirelli & C. Ambiente S.r.l.	-	2,095
Pirelli Group Reinsurance Company S.A.	6,346	6,346
Pirelli Ltda	9,666	9,666
Pirelli Servizi Amministrazione e Tesoreria S.p.A.	3,238	3,238
Pirelli Sistemi Informativi S.r.l.	1,655	1,655
Pirelli Tyre S.p.A.	4,523,887	4,521,792
Pirelli UK Ltd.	21,871	21,871
Servizi Aziendali Pirelli S.C.p.A.	101	101
Pirelli International Treasury S.p.A.	15	-
Total	**4,568,324**	**4,568,309**

Below are the changes during the year:

in thousands of euro

	12/31/2018	12/31/2017
Opening balance	**4,568,309**	**4,930,701**
Increases	15	9,707
Impairment	-	(2,262)
Decreases	-	(364,360)
Reclassification from provision for risks and charges	-	(5,477)
Closing balance	**4,568,324**	**4,568,309**

The increases refer for Euro 15 thousand to the subscription of 30 percent of the share capital of Pirelli International Treasury S.p.A., established on October 25, 2018; the residual 70 per cent was subscribed by the subsidiary Pirelli Tyre S.p.A..

In April 2018 the Company Pirelli & C. Ambiente S.r.l. was merged by incorporation into the subsidiary Pirelli Tyre S.p.A..

The company checks the recognised values of its investments and the existence of impairment indicators on the basis of as set out in paragraph 3 Accounting standards – Investments in subsidiaries and associated companies For investments in subsidiaries, no impairment indicators were identified and therefore no impairment tests were necessary.

Further details are set out in the Annexes to the explanatory notes.

11. INVESTMENTS IN ASSOCIATES

At December 31, 2018, this item amounted to Euro 6,375 thousand (Euro 10,204 thousand at December 31, 2017) and the breakdown is as follows:

in thousands of euro

	12/31/2018	12/31/2017
Consorzio per le Ricerche sui Materiali Avanzati (CORIMAV)	104	104
Eurostazioni S.p.A. - Roma	6,271	6,271
Fenice S.r.l.	-	2,477
Focus Investments S.p.A.	-	1,352
Total	**6,375**	**10,204**

The breakdown of changes is indicated below:

in thousands of euro

	12/31/2018	12/31/2017
Opening balance	**10,204**	**33,078**
Increases	-	-
Decreases	(249)	(13,655)
Impairment	(3,580)	(9,219)
Closing balance	**6,375**	**10,204**

The write-downs refer:

- → for Euro 2,229 thousand to the investment in Fenice S.r.l. which, following the sale of the investment of Prelios S.p.A. on December 28, 2017 to Lavaredo S.p.A., a newly established joint-stock company designated by the Burlington fund counterparty in the transaction was placed in liquidation; the liquidation was concluded in July 2018 with the distribution of as resulting from the allocation plan of Euro 249 thousand;
- → for Euro 1,351 thousand is attributable to the adjustment of the carrying amount to the fair value, including the liquidation preference.

Further details are set out in the Annexes to the explanatory notes.

12. OTHER FINANCIAL ASSETS – OTHER FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME – OTHER FINANCIAL ASSET AT FAIR VALUE THROUGH PROFIT OR LOSS – NON CURRENT PORTION

OTHER FINANCIAL ASSETS

Following the entry into force on January 1, 2018 of IFRS 9, other financial assets, consisting of financial assets available for sale and equal to Euro 224,593 thousand at December 31, 2017, have been designated as financial assets at fair value recorded in the other components of the comprehensive income statement (FVOCI) for Euro 75,566 thousand and as financial assets for which fair value changes are through profit or loss (FVPL) for Euro 149,027 thousand.

in thousands of euro

Total financial assets at fair value (IAS 39) at 12/31/2017	**224,593**
Reclassification to other financial assets at fair value through other comprehensive income	(75,566)
Reclassification to other financial assets at fair value through income statement	(149,027)
Total financial assets at fair value (IFRS 9) at 01/01/2018	**-**

OTHER FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME (FVOCI)

Other financial assets at fair value recorded in the other components of the comprehensive income statement amount to Euro 67,000 thousand at December 31, 2018.

The breakdown of the item for each security is as follows:

in thousands of euro

	12/31/2018	01/01/2018
Listed securities		
RCS Mediagroup S.p.A. - Milano	28,449	30,177
Unlisted securities		
Fin. Priv Srl	15,604	19,908
Fondo Comune di Investimento Immobiliare Anastasia	15,575	15,270
Istituto Europeo di Oncologia S.r.l.	6,961	6,599
Emittenti Titoli S.p.A.	-	2,748
Other companies	411	864
Total	**67,000**	**75,566**

The changes in the year are shown below.

in thousands of euro

Other financial assets at fair value in through other components of comprehensive income (FVOCI) at 01/01/2018	**75,566**
Decreases	(2,863)
Adjustment to fair value recognized in other components of comprehensive income	(5,703)
Total	**67,000**

Decreases mainly refer to the liquidation of the investment in Emittenti Titoli S.p.A..

The **fair value adjustments in other components of the comprehensive income statement** mainly refer to the investment in Fin.Priv. S.r.l. (negative for Euro 4,305 thousand), in RCS Mediagroup S.p.A. (negative for Euro 1,729 thousand), in Genextra (negative for 442 thousand), in Fondo Comune di investimento Anastasia (positive for Euro 305 thousand) and in Istituto Europeo di Oncologia (positive for Euro 362 thousand).

For listed securities, the fair value corresponds to the Stock Exchange listing at December 31, 2018. For unlisted securities and real estate funds, the fair value was estimated according to available information.

Further details are set out in the Annexes to the explanatory notes.

OTHER FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS (FVPL) – NON CURRENT PORTION

The changes in the fair value of other financial assets at fair value recorded in the income statement in the year are shown below:

in thousands of euro

Other financial assets at fair value through other comprehensive income (IFRS 9) at 01/01/2018	**149,027**
Fair value through income statement	3,780
Disposal	(152,807)
Closing balance	-

The initial value of other non-current financial assets at fair value recorded in the income statement refers to the investment in Mediobanca S.p.A. sold in January 2018.

13. OTHER RECEIVABLES

The breakdown of other receivables is as follows:

in thousands of euro

	12/31/2018			12/31/2017		
	Total	**Non-current**	**Current**	**Total**	**Non-current**	**Current**
Other receivables from subsidiaries	3,921	-	3,921	2,040	-	2,040
Financial receivables from subsidiaries	2,112,705	600,000	1,512,705	8,793	-	8,793
Guarantee deposits	221	221	-	712	712	-
Other receivables from third parties	2,221	323	1,898	18,604	14,108	4,496
Receivables from tax authorities for taxes not related to income	21,976	-	21,976	26,224	-	26,224
Financial accrued interest income	7,415	-	7,415	3,122	-	3,122
Financial prepaid expenses	776	-	776	489	-	489
Total	**2,149,235**	**600,544**	**1,548,691**	**59,984**	**14,820**	**45,164**

Financial receivables from subsidiaries mainly include the loan granted to Pirelli Tyre S.p.A. for a total amount of Euro 1,540 million, of which a current portion of Euro 940 million and a non-current portion of Euro 600 million, entered into on January 31, 2018 and maturing on January 31, 2020 and the receivable for interest accrued and not yet paid for Euro 4,329 thousand.

Financial receivables also include receivables with Pirelli International Plc related to the interest-bearing current account, settled at market rates, for Euro 561,399 thousand (at December 31, 2017 equal to Euro 4,082 thousand) and related to the charge-back of guarantee commissions for Euro 3,259 thousand.

For the purpose of applying the IFRS 9 accounting standard for intercompany loans, the analysis carried out take into account qualitative, quantitative, historical and prospective information, to determine the credit risk of an intragroup loan as of 31 December 2018. As a consequence, using a probability of default of an investment grade loan, the company management has concluded that any write-down required by the standard would be not-material.

Receivables from the tax authorities for taxes not related to income for Euro 21,976 thousand mainly refer to receivables for VAT.

Accrued financial assets refer to portions of interest accrued but not yet collected on cross currency interest swap derivative contracts related to the unsecured syndicated financing "Facilities" granted to Pirelli & C. S.p.A..

Deferred financial assets relate mainly to the commissions on the revolving and term loan credit line.

The book value of financial receivables and other receivables approximates their fair value.

14. TRADE RECEIVABLES

Trade receivables amount to Euro 35,366 thousand compared to Euro 52,045 thousand of the previous year and the breakdown is as follows:

in thousands of euro

	12/31/2018	12/31/2017
Receivables from subsidiaries	32,229	42,159
Receivables from associates	3	3
Receivables from other companies	6,105	14,088
Total receivables - gross amount	**38,336**	**56,250**
Provision for bad debt	(2,970)	(4,205)
Total	**35,366**	**52,045**

Below is the breakdown of trade receivables based on the currency in which they are expressed:

in thousands of euro

	12/31/2018	% of total trade receivables	12/31/2017	% of total trade receivables
EUR	34,180	89%	48,139	86%
USD (Dollar USA)	2,083	6%	2,381	4%
RUB (Ruble Russia)	2,039	4%	5,699	10%
Other currencies	33	-	31	-
Total	**38,336**		**56,250**	

Receivables from subsidiaries at December 31, 2018 mainly include the amounts that Pirelli & C. S.p.A. charges for services rendered through Corporate functions. The aforementioned receivables are due within the financial year and do not show overdue balances significant amount.

Receivables from other companies of Euro 6,105 thousand (Euro 14,088 thousand at December 31, 2017), shown gross of the bad debt provision of Euro 2,970 thousand, are past due for Euro 2,119 thousand.

Overdue receivables and receivables due have been valued in accordance with the Group policies described in the paragraph relating to credit risk management within the "Financial risk management policy".

The impaired receivables include both significant positions written down separately, and positions with similar characteristics in terms of credit risk, grouped and written down on a collective basis.

The change in the provision for bad debts is shown below:

in thousands of euro

	12/31/2018	12/31/2017
Opening balance	**4,205**	**4,059**
Accruals	2,962	275
Utilisations/reversals	(4,197)	(129)
Closing balance	**2,970**	**4,205**

Accruals to the provision for bad debts are recognised in the Income Statement as "Impairment of financial assets" (Note 32).

For trade receivables, the carrying amount is considered to approximate the applicable fair value.

15. CASH AND CASH EQUIVALENTS

At December 31, 2018, they amount to Euro 101,764 thousand, against Euro 1,749 thousand at December 31, 2017 and refer to balances of bank accounts in Euro repayable on demand.

The credit risk associated with cash and cash equivalents is to be considered limited because the counterparties

are represented by leading national and international banking institutions.

It is believed that the value of cash and cash equivalents is in line with their fair value.

16. TAX RECEIVABLES

At December 31, 2018, they amount to Euro 49,746 thousand (Euro 110,632 thousand at December 31, 2017).

The amount mainly includes:

- receivables from Group companies participating in the tax consolidation for Euro 48,489 thousand (Euro 104,054 thousand at December 31, 2017). The decrease compared to the previous year substantially depends on the lower contribution of the positive taxable result by the subsidiary Pirelli Tyre S.p.A., deriving from the Patent Box benefit;
- receivables for IRAP advances paid for Euro 925 thousand, unchanged compared to the previous year.

17. DERIVATIVE FINANCIAL INSTRUMENTS

The item includes the fair value of derivative instruments. The breakdown is as follows:

in thousands of euro

	12/31/2018				12/31/2017			
	Non Current Assets	Current Assets	Non Current Liabilities	Current Liabilities	Non Current Assets	Current Assets	Non Current Liabilities	Current Liabilities
Without adoption of hedge accounting								
Forex instruments - trade positions	-	325	-	(44)	-	95	-	(146)
In hedge accounting								
- cash flow hedge:								
Derivatives for interest rate	-	-	(2,824)	-	-	-	-	-
Other derivatives instruments	19,403	3,424	(7,741)	(5,248)	-	-	(29,716)	-
Total	**19,403**	**3,749**	**(10,565)**	**(5,292)**	**-**	**95**	**(29,716)**	**(146)**

The above derivatives are fully stipulated with the Group's treasury company, Pirelli International PLC.

DERIVATIVE FINANCIAL INSTRUMENTS NOT IN HEDGE ACCOUNTING

The value of **exchange rate derivatives** corresponds to the fair value of forward currency purchases/sales outstanding at the closing date of the year. These involve hedges of the Company's commercial transactions for which hedge accounting was not adopted. The fair value is determined by using the forward exchange rate at the reporting date.

DERIVATIVE FINANCIAL INSTRUMENTS IN HEDGE ACCOUNTING

The value of **derivatives on interest rates**, recorded as non-current liabilities for Euro 2,824 thousand, refers to the fair value measurement of 4 interest rate swaps forward start contracts with a notional of Euro 550 million and that exchange fixed rate against variable EURIBOR to hedge both future transactions and liabilities already recognised in the financial statements.

in thousands of euro

Instrument	Underlying item	Notional (in thousands of euro)	Start date	Deadline	
IRS forward start	Forecast transaction	250,000	June 2019	June 2022	receive fix / pay floating
IRS forward start	Term loan	100,000	October 2019	June 2022	receive fix / pay floating
IRS forward start	Schuldschein	180,000	July 2020	July 2023	receive fix / pay floating
IRS forward start	Schuldschein	20,000	July 2020	July 2025	receive fix / pay floating
Total		**550,000**			

The change in fair value of IRS for the period, negative for Euro 2,824 thousand, was entirely suspended in equity for Euro 2,810 thousand.

A +0.5% change in the EURIBOR curve, other things being equal, would result in a positive change of Euro 8,152 thousand in the Group's shareholders' equity, while a -0.5% change in the same curve would result in a negative change of Euro 8,527 thousand in the Group's shareholders' equity.

The value of **other derivatives**, recognised as non-current assets for Euro 19,403 thousand, current asset for Euro 3,424 thousand, non-current liabilities for Euro 7,741 thousand and current liabilities for 5,248 thousand, refers to the fair value measurement of 6 cross currency interest rate swaps with the following characteristics:

in thousands of USD

Instrument	Notional	Start date	Deadline	Description
CCIRS	170,422	July 2017	July 2019	pay floating EURIBOR / receive floating LIBOR
CCIRS	284,037	July 2017	June 2020	pay floating EURIBOR / receive floating LIBOR
CCIRS	681,690	July 2017	June 2022	pay floating EURIBOR / receive floating LIBOR
CCIRS	908,920	November 2018	July 2019	pay floating EURIBOR / receive floating LIBOR
	2,045,069			
CCIRS forward start	170,422	July 2019	June 2022	pay fix EURIBOR / receive floating LIBOR
CCIRS forward start	908,920	July 2019	June 2022	pay fix EURIBOR / receive floating LIBOR
	1,079,342			

The objective of these derivatives, for which hedge accounting of the cash flow hedge type was adopted, is to hedge the Company against the risk of fluctuations in cash flows associated with changes in the LIBOR rate and changes in the USD/EUR exchange rate, generated by a liability in USD at variable rate with a notional value of USD 2,045,069 thousand, equivalent to Euro 1,786,072 thousand (see note 19 Payables to banks and other lenders).

The positive change in fair value for the period was suspended in equity for Euro 68,220 thousand (cash flow hedge reserve for Euro 57,739 thousand and cost of hedging reserve for Euro 10,482 thousand), while Euro 39,973 thousand was reversed to the income statement in the item "net profits on derivatives" (Note 34 "Financial income") to offset unrealised exchange rate losses recorded on liabilities hedged and Euro 28,523 thousand was instead reversed in the item "Financial expenses" (Note 35) correcting the financial expenses recorded on the liability hedged.

Other things being equal, a hypothetical increase and decrease of 0.50% of the EURIBOR and LIBOR curves would have respectively a positive net impact of Euro 12,412 thousand and a negative net impact of Euro 12,730 thousand on the shareholders' equity of the Company.

Hedging relationships relating to IRS and CCIRS are considered effective prospectively as the following conditions are met:

- → there is an economic relationship between the hedging instrument and the hedged item, as the characteristics of the hedging instrument (nominal interest rate, reset of the interest rate and frequency of the payment of interest) are substantially in line with those of the hedged item. As a consequence, changes in the fair value of the hedging instrument regularly offset those of the hedged item;
- → the effect of credit risk is not predominant within the hedging relationship: based on the Group's operating rules, derivatives are traded only with high standing banking counterparties and the credit quality of the existing derivatives portfolio is constantly monitored;
- → the designated hedge ratio is in line with the one used for financial risk management and is 100% (1:1).

The ineffectiveness of the hedging relationship is calculated at each reporting date with the Dollar Offset method, which provides for the comparison of changes in the fair value risk adjusted of the hedging instrument (with the exception of those attributable to the spread referring to the currency basis) with changes in the fair value risk free of the hedged item, through the identification of a hypothetical derivative with the same characteristics of the underlying financial liability.

Possible causes of ineffectiveness are as follows:

- → application of adjustment for credit risk only to the hedging instrument but not to the hedged item;
- → the hedged item incorporates a floor that is not reflected in the hedging instrument;
- → misalignment between the actual contractual conditions of the future transaction and those of the hedging instrument.

At December 31, 2018, no ineffectiveness was recognised with reference to the aforementioned hedging relationships.

18. SHAREHOLDERS' EQUITY

Equity amounts to Euro 4,492,675 thousand (Euro 4,238,372 thousand at December 31, 2017).

The statement of changes in equity is shown in the main financial statements.

Equity went from Euro 4,238,372 thousand at December 31, 2017 to Euro 4,492,675 thousand at December 31, 2018. The positive change is essentially due to the net result for the year (positive for Euro 262,362 thousand), offset by the adjustment to the fair value of derivatives designated as cash flow hedges (negative for 3,084 thousand) and to the adjustment to the fair value of financial assets at fair value recognised as other components of the comprehensive income statement (negative for Euro 5,709 thousand).

SHARE CAPITAL

The share capital at December 31, 2018, fully subscribed and paid-in, amounts to Euro 1,904,374,935.66 divided into 1,000,000,000 ordinary shares without nominal value and unchanged compared to December 31, 2017.

LEGAL RESERVE

At December 31, 2018, the legal reserve amounted to Euro 380,875 thousand, unchanged compared to December 31, 2017.

SHARE PREMIUM RESERVE

At December 31, 2018, the share premium reserve amounted to Euro 630,381 thousand and unchanged compared to December 31, 2017.

CONCENTRATION RESERVE

At December 31, 2018, the concentration reserve amounted to Euro 12,467 thousand and unchanged compared to December 31, 2017.

OTHER RESERVES

At December 31, 2018, other reserves amounted to Euro 92,535 thousand and unchanged compared to December 31, 2017.

IAS RESERVE

At December 31, 2018, the IAS reserves amounted to Euro 5,241 thousand and refer to the reserve for the fair value adjustment recognised in the comprehensive income statement (positive for Euro 10,972 thousand), to the actuarial gains/losses reserve (positive for Euro 2,020 thousand), the cash flow hedge reserve and the cost of hedging reserve, net of the tax effect (negative for Euro 7,751 thousand).

MERGER RESERVE

At December 31, 2018, the merger reserve amounted to Euro 1,022,928 thousand, unchanged compared to December 31, 2017. The reserve was generated following the merger by incorporation of Marco Polo International Holding S.p.A. in Pirelli & C. S.p.A. in 2016.

RETAINED EARNINGS

The reserve from results carried forward amounts to Euro 181,512 thousand compared to a zero value at December 31, 2017. The increase is mainly attributable to the result for the previous year for Euro 170,851 thousand, which has been carried forward and to the classification to retained earnings for Euro 10,554 thousand of the fair value adjustment reserve for available for sale financial assets at December 31, 2017, for investments for which the changes in fair value are recognised in the income statement.

In accordance with the provisions of article 2427, no. 7-*bis* of the Italian Civil Code, in the following table each item of equity is indicated analytically, with indication of its origin, possibility of use and distributability, as well as of its use in previous years:

in thousands of euro

Equity items	Amount	Possible use	Available portion	Summary of reserves uses in the last 3 previous years
Share capital	1,904,375		-	-
Surplus reserve	630,381	A, B, C	630,381	-
Legal reserve	380,875	B	380,875	-
Other reserves				
- Concentration reserve	12,467	A, B, C	12,467	-
- Other Reserves	92,535	A, B	92,535	-
- IAS Reserves	5,241	-	-	-
- Merger Reserve	1,022,928	A, B, C	1,022,928	175,912
- Retained earnings	181,512	A, B, C	181,512	188,439
Total	**4,230,314**		**2,320,698**	**364,351**
Non distributable			473,410	
Residual available share			**1,847,288**	

A to increase the share capital
B to cover losses
C to distribute to the shareholders

19. BORROWINGS FROM BANKS AND OTHER FINANCIAL INSTITUTION

The breakdown of the item borrowings from banks and other financial institutions is as follows:

in thousands of euro

	12/31/2018			12/31/2017		
	Total	Not currents	Currents	Total	Not currents	Currents
Bonds	1,269,514	1,269,514	-	-	-	-
Borrowings from banks	2,851,995	2,651,995	200,000	2,331,086	2,331,086	-
Other financial payables	2,949	-	2,949	12,021	561	11,460
Accrued liabilities	19,555	-	19,555	5,396	-	5,396
Total	**4,144,013**	**3,921,509**	**222,504**	**2,348,503**	**2,331,647**	**16,856**

The item **bonds** refers to:

- unrated public bonds, for a total nominal amount of Euro 753 million of which Euro 553 million (originally Euro 600 million partially repurchased for a total amount of Euro 47 million during the last quarter of the year) placed on January 22, 2018 with a fixed coupon of 1.375% and with an original maturity of 5 years and a second security issued on March 15, 2018 for a nominal amount of Euro 200 million at variable rate with an original maturity of 2.5 years. Both loans, placed with international institutional investors, were issued under the EMTN program approved by the Board of Directors at the end of 2017, entered into on January 10, 2018 and updated on December 19, 2018.
- "Schuldschein" loan at variable rate entered into for a total of Euro 525 million on July 26, 2018. The loan, guaranteed by Pirelli Tyre S.p.A. and entered into by leading market operators, consists of a tranche of Euro 82 million with maturity in 3 years, a tranche of Euro 423 million with maturity in 5 years and a tranche of Euro 20 million with maturity in 7 years.

The carrying amount of the item bonds was determined as follows:

in thousands of euro

	12/31/2018
Nominal value	1,278,000
Transaction costs	(7,683)
Bond discount	(2,988)
Amortisation of effective interest rate	2,185
Total	**1,269,514**

Borrowings from banks mainly refers to:

- use of the unsecured loan ("Facilities") granted to Pirelli & C. S.p.A. and Pirelli International Plc for Euro 2,651,994 thousand. The contractual amount of the refinancing operation, signed on June 27, 2017 (with closing on June 29, 2017), is equal to Euro 3.4 billion (net of reimbursements made from the signing date – original amount of lines granted equal to Euro 4.2 billion). The loan was repriced in January 2018 with the recognition of a benefit in the income statement related to the debt remeasurement (see Note 35 "Financial expenses"). The loan had an original maturity of three and five years and is entirely classified as non-current payables to banks. On November 29, 2018, the loan was modified to include the right of the Pirelli Group to extend the maturity of the individual lines of the loan up to 2 years at its discretion with respect to their original contractual maturity of 3 and 5 years. Lastly, it is noted that also on November 29, 2018 was the conclusion of the transfer to Pirelli & C. S.p.A. of all the lines of the loan granted to Pirelli International Plc and therefore at December 31, 2018, the entire financing line is held by the Parent Company;
- Euro 200,000 thousand relating to the loan granted by Intesa Sanpaolo to Pirelli & C. S.p.A. at a fixed rate and maturing in January 2019, classified as current payables to banks. It should be noted that in July 2018, the maturity of the loan was extended until July 19, 2019.

The item **other financial payables** includes the payable to shareholders for Euro 2,460 thousand following the squeeze out operation. The decrease compared to the previous year is due to the closure of the payable of Euro 9,000 thousand to the subsidiary Pirelli International Plc.

The item **accrued liabilities** essentially refers to interest that has accrued on the term loans but has not yet been paid (Euro 10,144 thousand) and to interest accrued on bonds for Euro 9,269 thousand.

Below are the changes in payables to banks:

in thousands of euro

Borrowings from banks at December 31, 2017	**2,331,086**
Reimbursements of secured loan *(Senior Facilities)*	(700,000)
Transfer of loan from Pirelli International Plc	986,965
Additional financing from Intesa	200,000
Amortisation of bank/financial expenses (including repricing)	(6,590)
Translation differences	40,533
Borrowings from banks at December 31, 2018	**2,851,994**

Below is the change in total borrowing from banks for to the previous year:

in thousands of euro

Borrowings from banks at December 31, 2016	**4,267,340**
Drawdowns of secured financing (Senior Facilities)	249,108
Reimbursements of secured financing (Senior Facilities)	(4,509,537)
Drawdowns of unsecured financing (Facilities)	2,879,641
Reimbursements of unsecured financing (Facilities)	(499,450)
Amortisation of bank/financial expenses	57,265
Translation differences	(113,281)
Borrowings from banks at December 31, 2017	**2,331,086**

For current financial payables, it is maintained that the book value is approximately the fair value. The table below compares the fair value of non-current financial payables with their book value:

in thousands of euro

	12/31/2018		**12/31/2017**	
	Carrying amount	**Fair value**	**Carrying amount**	**Fair value**
Bonds	1,269,514	1,252,468	-	-
Borrowings from banks	2,651,995	2,686,087	2,331,086	2,364,230
Other financial payables	-	-	561	561
Total borrowings from banks and other financial institutions - non current	**3,921,509**	**3,938,555**	**2,331,647**	**2,364,791**

The unrated public bonds issued by Pirelli & C. S.p.A. are listed on an active market and the related fair value was measured with reference to its prices at the end of the year. Therefore, it is classified in level 1 of the hierarchy required by IFRS 13 – Fair Value Measurement. The fair value of the "Schuldschein" loan and payables to banks was calculated by discounting each debtor cash flow expected at the market swap rate for the currency and at the reference maturity date, increased by the Group credit rating for similar debt instruments by nature and technical characteristics and is therefore classified as level 2 in the hierarchy required by IFRS 13 – Fair Value Measurement.

The distribution of payables to banks and other lenders by currency of origin of the payable at December 31, 2018 and December 31, 2017 is as follows:

in thousands of euro

	12/31/2018	**12/31/2017**
EUR	2,368,434	1,403,382
USD (Dollar USA)	1,775,578	945,121
Total	**4,144,012**	**2,348,503**

At December 31, 2018, there are hedging derivatives for interest rate and exchange rate on payables at variable rate in foreign currency.

With reference to the presence of financial covenants, it should be noted that the main bank financing of the Group ("Facilities") granted to Pirelli & C. S.p.A. and Pirelli International Plc (currently entirely held by the Parent Company) and the "Schuldschein" loan require compliance with a maximum ratio ("Total Net Leverage") between net indebtedness and gross operating profit as resulting from the Consolidated Financial Statements of Pirelli & C. S.p.A..

As part of the bank financing, failure to comply with the financial covenant is identified as an event of default which, if exercised according to the contract terms by a number of lending banks representing at least 66 2/3% percent of the total commitment, would result in early repayment (partial or total) of the loan with simultaneous cancellation of the related commitment. This parameter was fully satisfied at December 31, 2018.

Also in the case of the Schuldschein loan, failure to comply with the financial covenant is identified as an event of default. However, unlike as occurs in the case of the bank financing, qualified majorities are not required for the early repayment request as each lender may proceed independently for the relative portion.

The Facilities and the "Schuldschein" loan envisage a Negative Pledge clause the terms of which are in line with the market standards for this type of credit facility.

The other outstanding financial payables at December 31, 2018 do not contain financial covenants.

NET FINANCIAL POSITION (ALTERNATIVE PERFORMANCE INDICATOR NOT REQUIRED BY IFRS ACCOUNTING STANDARDS)

The table below shows the breakdown of the net financial position and net financial debt, determined in accordance with the provisions of Consob communication DEM/6064293 of July 28, 2006 and in compliance with the ESMA/2013/319 Recommendations.

in thousands of euro

	Note	12/31/2018	*Of which related parties (note 38)*	12/31/2017	*Of which related parties (note 38)*
Current borrowings from banks and other financial institutions	**19**	222,504	*7*	16,856	*9,001*
Non-current borrowings from banks and other financial institutions	**19**	3,921,509	-	2,331,647	-
Current derivative financial instruments (liabilities)	**17**	5,248	*5,248*	29,716	*29,716*
Non-current derivative financial instruments (liabilities)	**17**	10,252	*10,252*	-	-
Total gross debt		**4,159,513**		**2,378,219**	
Cash and cash equivalents	**15**	(101,764)	-	(1,749)	-
Current financial receivables and other assets	**13**	(1,520,896)	*(1,520,120)*	(12,404)	*(11,915)*
Derivative financial instruments - assets	**17**	(3,424)	*(3,424)*	-	-
Net financial debt *		**2,533,429**		**2,364,066**	
Non-current financial receivables and other assets	**13**	(600,221)	*(600,000)*	(712)	-
Derivative financial instruments	**17**	(19,403)	*(19,403)*	-	-
Total net financial (liquidity)/debt position		**1,913,805**		**2,363,354**	

* Pursuant to Consob Notice of July 28, 2006 and in compliance with CESR recommendation of February 10, 2005 "Recommendations for the consistent implementation of the European Commission regulation on Prospectuses".

20. PROVISIONS FOR LIABILITIES AND CHARGES

The following is a detail of changes of the item in question:

in thousands of euro

	12/31/2018			12/31/2017		
	Total	**Non-current**	**Current**	**Total**	**Non-current**	**Current**
Opening balance	**45,678**	**45,678**	**-**	**51,427**	**45,950**	**5,477**
Increases	5,000	3,497	1,503	3,656	3,656	-
Reversals	(4,082)	(4,082)	-	(530)	(530)	-
Uses	(4,562)	(4,562)	-	(8,875)	(3,398)	(5,477)
Reclassification	312	-	312	-	-	-
Closing balance	**42,346**	**40,531**	**1,815**	**45,678**	**45,678**	**-**

Provisions for risks and charges refer for Euro 33,500 thousand to contingent liabilities (whose outlay is not considered probable) identified in the Purchase Price Allocation following the acquisition of the Pirelli Group by Marco Polo Industrial Holding S.p.A. and the subsequent reverse merger in Pirelli & C.S.p.A.; they refer to the decision taken by the European Commission – and subsequently confirmed by the sentence of the Tribunal of the European Union of July 12, 2018 – at the conclusion of the antitrust investigation initiated with respect to the business of energy cables, which provides for a fine for Prysmian Cavi e Sistemi S.r.l. ("Prysmian") of about Euro 104 million for a portion of which, equal to Euro 67 million, Pirelli & C. S.p.A., although not involved in the alleged cartel, is called to respond jointly with Prysmian exclusively in application of the so-called "parental liability" principle, because, during part of the period of the alleged infringement, Prysmian was controlled by Pirelli. The amount set aside corresponds to the amount of the first demand bank guarantee issued by Pirelli - similar to as was carried out by Prysmian - for the benefit of the Commission (and at the request of the latter) for an amount equal to 50% of the aforementioned Euro 67 million.

The **non-current portion** also mainly includes provisions for labour disputes (Euro 3,586 thousand), reclamation of abandoned areas (Euro 1,922 thousand) and legal and tax disputes (Euro 1,523 thousand).

Increases mainly refer to provisions for environmental reclamation and labour disputes.

Uses are mainly attributable to the closure of pending disputes relating to occupational diseases and reclamation of abandoned areas.

Reversals of excess funds are mainly related to the adjustment of provisions for tax risks.

21. EMPLOYEE BENEFIT OBLIGATIONS

Personnel provisions amount to Euro 4,175 thousand (Euro 2,072 thousand at December 31, 2017). This item includes provision for severance pay which amounts to Euro 1,077 thousand (Euro 1,385 thousand at December 31, 2017) and other employee benefits of Euro 3,098 thousand (Euro 687 thousand at December 31, 2017).

The increase compared to the previous year is attributable for Euro 1,964 thousand to the portion accrued at December 31, 2018 of the second instalment of the retention plan, assessed in accordance with the accounting standard IAS 19 – Employee Benefits – which will be liquidated in the first half of 2019. The plan was approved by the Board of Directors on February 26, 2018 and is intended for Key Managers and a selected number of Senior Managers and Executives whose contribution for the implementation of the Strategic Plan is considered particularly significant.

Personnel provisions also include the portion pertaining to the 2018-2020 three-year monetary incentive plan (LTI Plan) for Group management, approved by the Board of Directors on February 26, 2018. This incentive plan is monetary (cash settled), as it does not provide for the allocation of shares or options on shares or other securities but exclusively a cash incentive, partly linked to the performance of the ordinary share of Pirelli & C. S.p.A.

EMPLOYEE SEVERANCE INDEMNITY (TFR)

The changes in the year 2018 for the employee severance indemnity are the following:

in thousands of euro

	12/31/2018	12/31/2017
Opening balance	**1,385**	**1,248**
Movements through income statement	934	1,136
Actuarial (gains)/losses recognized in equity	8	17
Indemnities, advance payments, relocations, payment to funds	(1,250)	(1,016)
Closing balance	**1,077**	**1,385**

The amounts recognised in the income statement are included in the item "Personnel Costs" (note 29).

Net actuarial gains accrued in 2018, recognised directly in equity, amount to Euro 8 thousand and are essentially related to the change in the economic parameters of reference (discount rate and inflation rate).

In accordance with national legislation, the amount due to each employee accrues based on the service provided and is paid when the employee leaves the company. The treatment due to the termination of the employment relationship is calculated based on its duration and the taxable remuneration of each employee. The liability, annually revalued on the basis of the official cost of living and statutory interest rate, is not associated with any accrual condition or period, nor with any financial funding obligation; therefore, there is no activity at the service of the fund.

The discipline was supplemented by Legislative Decree no. 252/2005 and by Law no. 296/2006 (Finanziaria 2007) which, for companies with at least 50 employees, has established that the portions accrued since 2007 be allocated, on the employees' option, either to the INPS Treasury Fund or to supplementary pension schemes, assuming the nature of "Defined contribution plan". In any case, for all companies, the revaluations of the amounts outstanding at the option dates are still accounted for under staff severance indemnities as well as, for companies with less than 50 employees, also the portions accrued and not allocated to supplementary pensions.

The principal actuarial assumptions used at December 31, 2018 are as follows:

	2018
Discount rate	1.5%
Inflation rate	1.5%

The principal actuarial assumptions used at December 31, 2017 were as follows:

	2017
Discount rate	1.6%
Inflation rate	1.5%

Hired employees at December 31, 2018 amount to 151 units (141 units at December 31, 2017).

In other conditions being equal, a hypothetical change of 0.25% in the discount rate would result in a decrease in liabilities equal to 1.82%, in the case of an increase (1.78% at December 31, 2017), and an increase in liabilities of 1.83%, in the case of a decrease (1.84% at December 31, 2017).

22. TRADE PAYABLES

The breakdown of trade payables is as follows:

in thousands of euro

	12/31/2018	12/31/2017
Payables to subsidiaries	2,392	4,755
Payables to associates	60	64
Payables to other companies	16,929	24,875
Total	**19,381**	**29,694**

The carrying amount of trade payables is considered to approximate their fair value.

23. OTHER PAYABLES

The breakdown of other payables is as follows:

in thousands of euro

	12/31/2018			12/31/2017		
	Total	Non-current	Current	Total	Non-current	Current
Payables to subsidiaries	25,944	-	25,944	27,491	-	27,491
Payables to social security and welfare institutions	1,905	-	1,905	3,067	-	3,067
Payables to employees	8,275	-	8,275	8,303	-	8,303
Other payables	9,088	211	8,877	35,377	211	35,166
Accrued liabilities	3,343	-	3,343	1,177	-	1,177
Deferred income	7	-	7	8	-	8
Total	**48,562**	**211**	**48,351**	**75,423**	**211**	**75,212**

Payables to subsidiaries mainly refer to receivables related to VAT consolidation.

Payables to pension and social security institutions are mainly constituted by contributions to be paid to the INPS (National Social Welfare Institute) and INAIL (National Institute for Insurance against Industrial Accidents).

Payables to employees refer to contributions for fees to be paid to employees.

The item Other payables includes payables for fees to be paid to directors and auditors, for withholding taxes on income from self-employed and employed work and payables to advisors for commissions related to the IPO.

For other current payables it is considered that the carrying value approximates their fair value.

24. PROVISION FOR DEFERRED TAX LIABILITIES

The deferred tax provision amounted to Euro 527,807 thousand at December 31, 2018 (Euro 554,828 thousand at December 31, 2017).

The breakdown of deferred tax provisions gross of the offsets made is as follows:

in thousands of euro

	12/31/2018	12/31/2017
Deferred tax assets	**113,005**	**85,983**
- of which within 12 months	55,649	52,964
- of which over 12 months	57,356	33,019
Provision for deferred tax liabilities	**(640,811)**	**(640,811)**
- of which within 12 months	-	-
- of which over 12 months	(640,811)	(640,811)
Total	**(527,806)**	**(554,828)**

The tax effect of temporary differences and of tax losses carried forward which make up the item is shown in the following table:

in thousands of euro

	12/31/2018	12/31/2017
Deferred tax assets		
Provision for risk and charges	1,897	2,103
Property, plant and equipment	65	422
Employees provision	864	189
Provision for bad debt	713	1,009
Tax losses carried forward	50,339	35,421
ACE Benefit	43,498	30,913
Interests	13,180	14,218
Derivatives	2,448	1,708
Total deferred tax assets	**113,005**	**85,983**
Provision for deferred tax liabilities		
Brand Pirelli	(633,330)	(633,330)
Exchange differences not realised	(7,481)	(7,481)
Total provision for deferred tax liabilities	**(640,811)**	**(640,811)**
Total	**(527,806)**	**(554,828)**

25. TAX PAYABLES

These amounted to Euro 16,436 thousand (Euro 18,636 thousand at December 31, 2017) and mainly include payables for withholding taxes incurred abroad (WHT), transferred from subsidiaries that adhere to the tax consolidation by the Company.

INCOME STATEMENT

26. REVENUES FROM SALES AND SERVICES

Revenues from sales and services amount to Euro 38,719 thousand for 2018 compared to Euro 42,084 thousand in 2017 and the breakdown is as follows:

in thousands of euro

	2018	2017
Sales of services to subsidiaries	37,054	40,070
Sales of services to other companies	1,665	2,014
Total	**38,719**	**42,084**

Revenues from subsidiaries refer to services provided through Corporate functions.

27. OTHER INCOME

Other income amounts to Euro 112,179 thousand (Euro 105,778 thousand in 2017) and the breakdown is as follows:

in thousands of euro

	2018	2017
Other income from subsidiaries	102,110	98,903
Other revenues from third parties	10,069	6,875
Total	**112,179**	**105,778**

Other income from subsidiaries mainly include royalties paid by Group companies for the use of the brand (Euro 69,562 thousand in 2018 compared to Euro 71,897 thousand in 2017). They also include other revenues deriving from the charge-back of costs to Group companies and revenues for sub-leases and related accessory charges.

Other revenues from other companies mainly include royalties paid by other companies for the use of the Pirelli brand (Euro 1,409 thousand in 2018 compared to Euro 2,221 thousand in 2017) and the gain of Euro 575 thousand deriving from the sale of the land located in Milan.

28. RAW MATERIALS & CONSUMABLES USED

They amount to Euro 210 thousand in 2018 (Euro 183 thousand in 2017) and include purchases of advertising material, fuels and various materials.

29. PERSONNEL COSTS

Personnel costs amount to Euro 34,130 thousand (Euro 26,710 thousand in 2017) and the breakdown is as follows:

in thousands of euro

	2018	2017
Wages and salaries	23,744	19,969
Social security and welfare contributions	4,982	5,129
Employee leaving indemnities (TFR)	973	1,027
Retirement and similar obbligations	241	232
Other costs	4,190	353
Total	**34,130**	**26,710**

The average staff headcount is the following:

- → Executives 39
- → Employees 109
- → Workers 3

30. AMORTISATION, DEPRECIATION AND IMPAIRMENTS

The breakdown is as follows:

in thousands of euro

	2018	2017
Amortisation - intangible assets	1,764	2,514
Depreciation - property, plant and equipment	2,220	2,386
Total	**3,984**	**4,900**

31. OTHER COSTS

The breakdown of other costs is the following:

in thousands of euro

	2018	2017
Services rendered by subsidiaries	10,840	16,032
Advertising	31,243	33,249
Consultancy and collaboration services	8,551	11,863
Accruals to provisions (net of reversals)	(786)	3,931
Legal and notarial expenses	671	4,434
Travel expenses	11,119	10,653
Remuneration of Directors and supervisory bodies	8,449	2,515
Membership fees and contributions	2,251	1,484
Rental and lease instalments	10,854	10,662
IT expenses	2,551	2,946
Energy, gas and water expenses	1,332	1,483
Security service	2,634	2,863
Insurance premiums	3,056	3,796
Patents and trademarks expenses	845	719
Cleaning and property ordinary maintenance expenses	689	1,381
Property maintenance	2,124	901
Bank charges for IPO	163	44,274
Other	8,458	13,874
Total	**105,044**	**167,060**

Other costs include non-recurring costs for an amount of Euro 1,025 thousand and refer mainly to the queue of costs related to the listing project occurred in 2017. The reduction of other costs compared to 2017 is mainly attributable to advisors and fee costs related to the IPO incurred in 2017 for Euro 62,390 thousand.

32. NET IMPAIRMENT LOSS ON FINANCIAL ASSETS

The item, negative for Euro 1,930 thousand, mainly includes the net impairment of trade receivables.
At December 31, 2017, the net write-down of trade receivables amounted to Euro 275 thousand and was included in the item "Other costs" (Note 31).

33. NET INCOME(LOSS) FROM EQUITY INVESTMENTS

33.1 GAINS ON EQUITY INVESTMENTS

They amount to Euro 4,007 thousand in 2018 (Euro 2,752 thousand in 2017) and the breakdown is as follows:

in thousands of euro

	2018	2017
- Capital gain on disposal of investment in Prelios S.p.A.	-	2,564
- Fair value adjustment of investment in Mediobanca S.p.A.	3,780	-
- Other gains on equity investments	227	188
Total	**4,007**	**2,752**

For further details, reference is made to Note 11 – Investments in associated companies.

The item mainly refers to the positive impact of Euro 3,780 thousand related to the investment in Mediobanca S.p.A., classified as "Other financial assets at fair value through profit or loss" (Note 12) and sold on January 11, 2018.

33.2 LOSSES ON EQUITY INVESTMENTS

They amount to Euro 3,580 thousand (Euro 13,833 thousand in 2017) and the breakdown is as follows:

in thousands of euro

	2018	2017
Impairment losses on equity investments in subsidiaries:		
- Pirelli & C. Ambiente S.r.l.	-	1,128
- Hb Servizi S.r.l.	-	1,134
Impairment losses on equity investments in associates:		
- Prelios S.p.A.	-	-
- Focus Investments S.p.A.	1.,351	2,648
- Fenice S.r.l.	2,229	6,570
Impairment losses on other financial assets:		
- Alitalia S.p.A.- Compagnia Aerea Italiana S.p.A.	-	781
- Movincom Servizi S.p.A.	-	120
- Emittente Titoli S.p.A.	-	1,441
- Others	-	11
Total	**3,580**	**13,833**

For further details, reference shall be made to the notes related to investments in subsidiaries (note 10), associates (note 11) and other financial assets (note 12).

33.3 DIVIDENDS

They amount to Euro 284,517 thousand in 2018 compared to Euro 215,497 thousand in 2017 and the breakdown is as follows:

in thousands of euro

	2018	2017
From subsidiaries:		
- Pirelli Tyre S.p.A. - Italy	270,000	200,000
- Pirelli Group Reinsurance Company SA - Switzerland	5,025	-
- Pirelli Servizi Amministrazione e Tesoreria S.p.A. - Italia	500	-
- Pirelli Sistemi Informativi S.r.l. - Italy	5,800	300
From associates:		
- Fenice Srl - Italy	2,225	8,556
- International Media Holding S.p.A. - Italy	-	15
From other financial assets:		
- Mediobanca S.p.A. - Italy	-	5,829
- ECA Ltd - United the Kingdom	10	10
- Fin. Priv. S.r.l. - Italy	957	757
- Emittenti Titoli S.p.A. - Italy	-	30
Total	**284,517**	**215,497**

34. FINANCIAL INCOME

The breakdown is as follows:

in thousands of euro

	2018	2017
Interests	15,419	1,686
Other financial income	5,108	4,744
Net gains on derivatives	40,292	-
Net gains on exchange rates	-	110,315
Total	**60,819**	**116,745**

Interest mainly refers to interest accrued on loans granted in 2018 to the subsidiary Pirelli Tyre S.p.A.

The item **other financial income** mainly includes Euro 3,259 thousand of guarantee fees charged to other Group companies and Euro 1,828 thousand relating to the gain realised on the early partial repayment of the unrated bond completed on December 19, 2018 for a total amount of Euro 47 million.

Net profits on derivatives refer to forward purchases/sales of foreign currencies to hedge the financial payables in foreign currency of the Company, in accordance with the Group foreign exchange risk management policy. For transactions outstanding at the end of the period, the fair value is determined using the forward exchange rate at the reporting date. The fair value assessment includes two elements: the interest component linked to the interest rate spread between the currencies subject to the individual hedges, a net cost of Euro 365 thousand, and the exchange rate component, a net revenue of Euro 40,657 thousand.

Comparing net foreign exchange losses, equal to Euro 40,841 thousand, with the exchange rate component of net profits on derivatives (equal to Euro 40,657 thousand), the impact is almost nil.

35. FINANCIAL EXPENSES

The breakdown is as follows:

in thousands of euro

	2018	2017
Interests	51,416	136,839
Commissions	1,228	1,147
Net interest on the personal provision	185	24
Net losses on exchange rates	40,841	-
Net losses on derivative financial instruments	-	102,108
Total	**93,670**	**240,118**

Interest and other financial expenses for a total of Euro 51,416 thousand mainly include:

- → Euro 56,760 thousand of financial expenses for the unsecured financing line (“Facilities”) granted to Pirelli & C. S.p.A. and Pirelli International Plc (as of November 29, 2018, held entirely by the Parent Company) entered into on June 27, 2017;
- → Euro 12,585 thousand of financial expenses related to bonds, of which Euro 10,256 thousand related to unrated bonds and Euro 2,329 thousand related to the “Schuldschein” loan, both issued by Pirelli & C. S.p.A.;
- → Euro 21,977 thousand of indemnity paid to Pirelli International Plc for costs incurred for early closing of the bond (from Euro 600 million, 1.75% coupon and original maturity in November 2019), which took place through the exercise of the so-called make-whole option.

The components above are partially offset by:

- → Euro 28,523 thousand for net interest income on Cross Currency Interest Rate Swaps to adjust the flow of interest expense on the liability hedged;
- → Euro 12,012 thousand of positive effect deriving from the repricing of the unsecured financing line (“Facilities”) in January 2018 and which entailed a re-measurement of the related debt.

At December 31, 2017, the item “interest and other financial expenses” included Euro 41,967 thousand of wash down of the fees not yet amortised relating to the bank loan, repaid in advance in June 2017.

Net exchange rate losses of Euro 40,841 thousand refer to the adjustment to the exchange rate at the end of the year of the items expressed in the currency other than the functional one still in effect at the closing date of the Financial Statements and the net losses on items closed during the year.

Financial expenses include non-recurring events for a total negative impact of Euro 9,964 thousand, which include Euro 21,977 thousand related to the indemnity paid to Pirelli International Plc for costs incurred for early closing of the bond, net of gains for Euro 12,012 thousand (already net of the relative amortised portion) relating to the repricing of the unsecured bank line ("Facilities") in January 2018.

36. TAXES

The breakdown of taxes is as follows:

in thousands of euro

	2018	2017
Current taxes	21,608	(64,005)
Deferred taxes	(26,279)	(76,794)
Total	**(4,671)**	**(140,799)**

Current taxes for the year 2018 mainly include a negative effect of expenses deriving from tax consolidation relating to previous years (Euro 53,836 thousand), essentially due to the reduction in the taxable income of the subsidiary Pirelli Tyre thanks to the benefit deriving from the application of the Patent Box facilitated tax regime, offset by a positive effect mainly deriving from income from tax consolidation for the year 2018 (Euro 32,363 thousand).

Deferred tax assets include the recognition of deferred tax assets on previous tax losses, on the ACE benefit and excess non-deducted interest expense, which was partially used during the year.

The significant change in the tax burden compared to the previous year is mainly due to the recognition in 2017 of deferred tax assets on previous tax losses, excess non-deducted interest expense, ACE benefit and other temporary differences.

The table below shows the reconciliation of the effective tax rate with the theoretical rate of the Parent Company:

in thousands of euro

	2018	2017
A) Profit/(loss) before taxes	257,691	30,052
B) Theoretical taxes	**61,846**	**7,212**
Main causes that give rise to changes between theoretical and effective taxes,		
Tax incentives	(3,482)	(7,864)
Dividends and gains from investments not subject to taxation	(65,571)	(49,897)
Non-deductible costs	2,209	19,837
Uses losses previous years not activated	-	(37,648)
Deferred tax assets on previous tax losses and other temporary differences	-	(80,552)
Taxes relating to previous years	327	8,112
C) Effective taxes	**(4,671)**	**(140,799)**
Theoretical tax rate (B/A)	24%	24%
Effective tax rate (C/A)	-1.8%	-468.5%

TAX CONSOLIDATION

It shall be noted that starting from 2004, the Company exercised the option for consolidated taxation as consolidator, pursuant to article 117 and following of the TUIR, with regulation of relations arising from adhesion to consolidation through a special Regulation, which involves a common procedure for the application of laws and regulations.

Said regulation was updated in subsequent years as a result of amendments made within the companies participating in the agreement and the related shareholding structure, as well as in light of the corrective and supplementary interventions of the relevant legislation.

The above amendments particularly concerned the remuneration of the tax losses used by the companies adhering to the consolidation. The adoption of the consolidation makes it possible to compensate, with regard to the parent company Pirelli & C. S.p.A., the taxable income or loss of the same parent company with those of its resident subsidiaries which have exercised the option, given that the tax losses accrued during periods prior to the introduction of Group taxation can be used by those companies which are eligible.

37. NON-RECURRING EXPENSES AND INCOME

Pursuant to Consob Communication no. DEM/6064293 of July 28, 2006, information is provided below regarding the economic impacts of non-recurring events and transactions of the Company equal to net expenses of Euro 8,312 thousand in 2018 and net expenses of Euro 9,940 thousand in 2017:

in thousands of euro

	2018	2017
Personnel costs:		
- Retention Plan	-	(1,691)
Other costs:		
- IPO costs	(841)	(62,390)
- Other	(184)	-
Impact on operating result	**(1,025)**	**(64,081)**
Financial expenses:		
- Refinancing impact June 2017 transaction costs	-	(41,967)
- Indemnification to Pirelli Internation Plc against costs incurred for early repayment of the bond	(21,977)	-
- Impact of repricing of unsecured debt ("Facilities")	12,012	-
Impact on result before taxes	**(10,990)**	**(106,048)**
Taxes:		
- Recognition of deferred tax assets on previous losses and other temporary differences	-	80,552
- Tax impact on operating result adjustments and financial expenses	2,678	15,556
Impact on net result	**(8,312)**	**(9,940)**

38. TRANSACTIONS WITH RELATED PARTIES

Transactions between Pirelli & C. S.p.A. and the subsidiaries mainly concern:

- → services (technical, organisational, general) provided by the headquarters to subsidiaries;
- → royalties for the use of patents for Group companies benefiting from them.

All the transactions listed above are part of the ordinary management of relations between the Parent Company and its subsidiaries.

Transactions with related parties also included the fees paid to Directors and Key Managers.

The statement below shows a summary of the Statement of Financial Position and the Income Statement that include transactions with related parties and their impact.

in thousands of euro

	12/31/2018	Of which related parties	*% share*	12/31/2017	Of which related parties	*% share*
BALANCE SHEET						
Non current assets						
Other receivables	600,544	*600,000*	99.9%	-	-	0.0%
Derivative financial instruments	19,403	*19,403*	100%	-	-	0.0%
Current assets						
Trade receivables	35,366	*32,352*	91.5%	52,045	*43,722*	84.0%
Other receivables	1,548,691	*1,524,042*	98.4%	45,164	*13,973*	30.9%
Tax receivables	49,746	*48,490*	97.5%	110,632	*104,054*	94.1%
Derivative financial instruments	3,749	*3,749*	100%	95	*95*	100%
Non-current liabilities						
Derivative financial instruments	10,565	*10,565*	100%	29,716	*29,716*	100%
Current liabilities						
Payables to banks and other financial lenders	222,504	*7*	0.0%	16,856	*9,412*	55.8%
Trade payables	19,381	*2,987*	15.4%	29,694	*4,820*	16.2%
Other payables	48,351	*26,178*	54.1%	75,213	*27,491*	36.6%
Tax payables	16,436	*16,207*	98.6%	18,637	*18,408*	98.8%
Derivative financial instruments	5,292	*5,292*	100%	146	*146*	100%

in thousands of euro

	2018	Of which related parties	*% share*	2017	Of which related parties	*% share*
INCOME STATEMENT						
Revenues from sales and services	38,719	*37,364*	96.5%	42,084	*41,349*	98.3%
Other income	112,179	*102,184*	91.1%	105,778	*99,323*	93.9%
Personnel expenses	(34,130)	*(2,186)*	0.0%	(26,710)	*(4,780)*	17.9%
Other costs	(105,044)	*(20,169)*	19.2%	(167,060)	*(18,618)*	11.1%
Income on equity investments	-	-	0,0%	2,752	*2,564*	93.2%
Losses on equity investments	(3,580)	*(3,580)*	100%	(13,833)	*(11,480)*	83.0%
Dividends	284,517	*283,549*	99.7%	215,496	*208,871*	96.9%
Financial income	60,819	*59,277*	97.5%	116,745	*10,681*	9.1%
Financial expenses	(93,670)	*(6,519)*	7.0%	(240,118)	*(103,275)*	43.0%

TRANSACTIONS WITH RELATED PARTIES

The tables below shows the main equity transactions with related parties for the years ended December 31, 2018 and December 31, 2017.

in thousands of euro

	Subsidiaries	Associates	Other related parties	Total 31 December 2018
Trade receivables	32,229	3	120	32,352
Other current receivables	1,524,042	-	-	1,524,042
Other non current receivables	600,000	-	-	600,000
Tax receivables	48,490	-	-	48,490
Derivative financial instruments (current assets)	3,749	-	-	3,749
Derivative financial instruments (non current assets)	19,403	-	-	19,403
Payables to banks and other lenders (current liabilities)	7	-	-	7
Trade payables	2,393	60	535	2,987
Other payables	25,944	-	234	26,178
Tax payables	16,207	-	-	16,207
Derivative financial instruments (current liabilities)	5,292	-	-	5,292
Derivative financial instruments (non-current liabilities)	10,565	-	-	10,565

in thousands of euro

	Subsidiaries	Associates	Other related parties	Total 31 December 2017
Trade receivables	42,159	3	1,560	43,722
Other current receivables	13,973	-	-	13,973
Tax receivables	104,054	-	-	104,054
Derivative financial instruments (current assets)	95	-	-	95
Payables to banks and other lenders (current liabilities)	9,412	-	-	9,412
Trade payables	4,755	64	-	4,820
Other payables	26,814	-	677	27,491
Tax payables	8,513	-	9,895	18,408
Derivative financial instruments (current liabilities)	146	-	-	146
Derivative financial instruments (non-current liabilities)	29,716	-	-	29,716

Trade receivables amounted to Euro 32,352 thousand (Euro 43,722 thousand at December 31, 2017) and mainly refer to receivables for services/provisions provided to Group companies (Euro 29,354 thousand from Pirelli Tyre S.p.A., Euro 2,163 thousand from Limited Liability Company Pirelli Tyre Russia, Euro 400 thousand from Pirelli Tyre Trading (Shanghai) Co. Ltd., Euro 163 thousand from Pirelli International Plc).

Other current receivables amounted to Euro 1,524,042 thousand (Euro 13,973 thousand at December 31, 2017) and mainly refer: for Euro 944,329 thousand to the loan granted to Pirelli Tyre S.p.A.; for Euro 561,400 thousand to the intra-group current account with Pirelli International Plc; for Euro 3,259 thousand to guarantee fees charged to Pirelli International Plc; for Euro 7,415 thousand to the interest accrual accrued on CCIRS stipulated with Pirelli International Plc; for Euro 3,310 thousand to VAT receivables transferred to the consolidation (Euro 2,695 thousand from Pirelli Industrie Pneumatici S.r.l., Euro 227 thousand from Pirelli Sistemi Informativi S.r.l., Euro 224 thousand from Pirelli Servizi Amministrazione e Tesoreria S.p.A., Euro 101 thousand from HB Servizi S.r.l., Euro 63 thousand from Servizi Aziendali Pirelli S.C.p.A.).

Other non-current receivables amount to Euro 600,000 thousand (zero amount at December 31, 2017) and refer to the loan granted to Pirelli Tyre S.p.A. with maturity January 31, 2020.

Tax receivables amounted to Euro 48,490 thousand (Euro 104,054 thousand at December 31, 2017) and refer to receivables from Group companies that adhere to tax consolidation (mainly Euro 46,102 thousand from Pirelli Tyre S.p.A., Euro 2,313 thousand from Pirelli Industrie Pneumatici S.r.l.)

Derivative financial instruments (current assets) for Euro 3,749 thousand (Euro 95 thousand at December 31, 2017) refer to hedging transactions with Pirelli International Plc. The most significant amount refers for Euro 3,424 thousand to the fair value measurement of the Cross Currency Interest Rate Swap.

Derivative financial instruments (non-current assets) for Euro 19,403 thousand (zero amount at December 31, 2017) refer to the hedging transaction of the Cross Currency Interest Rate Swap with Pirelli International Plc.

Payables to banks and other lenders (current) amounted to Euro 7 thousand (Euro 9,412 thousand at December 31, 2017) and refer to guarantee fees to Pirelli International Plc.

Trade payables amounted to Euro 2,987 thousand (Euro 4,820 thousand at December 31, 2017) and mainly refer to payables for the provision of services. The main ones are: Euro 1,525 thousand to HB Servizi S.r.l., Euro 617 thousand to Pirelli Tyre S.p.A..

The amount recorded under other related parties for Euro 535 thousand refers to the current relationship with TP Trading (Beijing) Co. Ltd.

Other payables amounted to Euro 26,178 thousand (Euro 27,491 thousand at December 31, 2017) and mainly refer to payables with Group companies that adhere to the VAT consolidation. The main ones are: Euro 25,128 thousand to Pirelli Tyre S.p.A., Euro 115 thousand to Driver Italia S.p.A.

Tax payables amounted to Euro 16,207 thousand (Euro 18,408 thousand at December 31, 2017) and refer to payables to subsidiaries that adhere to tax consolidation (Euro 16,126 thousand Pirelli Tyre S.p.A., Euro 81 thousand Driver Italia S.p.A.).

The amount of Euro 5,292 thousand (Euro 146 thousand at December 31, 2017) of **derivative financial instruments – current liabilities** refers to the hedging transaction with Pirelli International Plc and is mainly represented for Euro 5,248 thousand by the fair value measurement of the Cross Currency Interest Rate Swap.

The amount of Euro 10,565 thousand (Euro 29,716 thousand at December 31, 2017) of **derivative financial instruments (non-current liabilities)** refers to the fair value measurement of the Cross Currency Interest Rate Swap (Euro 7,741 thousand) and IRS (Euro 2,511 thousand) with Pirelli International Plc.

TRANSACTIONS WITH RELATED PARTIES

The tables below show the main financial transactions with related parties for the years 2018 and 2017.

in thousands of euro

	Subsidiaries	Associates	Other related parties	Total 2018
Revenues from sales and services	37,054		310	37,364
Other income	102,110	-	74	102,184
Personnel expenses	-	-	(2,186)	(2,186)
Other costs	(10,579)	(261)	(9,328)	(20,168)
Losses from investments	-	(3,580)	-	(3,580)
Dividends	281,325	2,224	-	283,549
Financial income	59,277	-	-	59,277
Financial expenses	(6,519)	-	-	(6,519)

in thousands of euro

	Subsidiaries	Associates	Other related parties	Total 2017
Revenues from sales and services	40,070		1,279	41,349
Other income	98,903	384	36	99,323
Personnel expenses	-	-	(4,780)	(4,780)
Other costs	(15,773)	(259)	(2,586)	(18,618)
Gains on equity investments	-	2,564	-	2,564
Losses from investments	(2,262)	(9,218)	-	(11,480)
Dividends	200,300	8,571	-	208,871
Financial income	10,681	-	-	10,681
Financial expenses	(103,275)	-	-	(103,275)

Revenues from sales and services amounted to Euro 37,364 thousand in 2018 (Euro 41,349 thousand in 2017) and mainly refer to service contracts. The main transactions with subsidiaries are: Euro 36,139 thousand - Pirelli Tyre S.p.A., Euro 301 thousand - Pirelli Sistemi Informativi S.r.l., Euro 270 thousand - HB Servizi S.r.l..

Transactions with other related parties refer for Euro 310 thousand to the service/provisions contract with Prometeon Tyre Group S.r.l..

Other income of Euro 102,184 thousand in 2018 (Euro 99,323 thousand in 2078) mainly refers to: royalties (Euro 67,388 thousand with Pirelli Tyre S.p.A., Euro 2,164 thousand with Limited Liability Company Pirelli Tyre Russia); other recoveries (Euro 25,674 thousand from Pirelli Tyre S.p.A., Euro 548 thousand from Pirelli International Plc, Euro 237 thousand from Pirelli Sistemi Informativi S.r.l., Euro 78 thousand from Pirelli Servizi Amministrazione e Tesoreria S.p.A.); lease contracts (Euro 5,572 thousand with Pirelli Tyre S.p.A., Euro 231 thousand with Pirelli Servizi Amministrazione e Tesoreria S.p.A., Euro 170 thousand with Pirelli Sistemi Informativi S.r.l.).

The amount recorded under related parties for Euro 74 thousand mainly refers to service contracts with Camfin S.p.A. (Euro 30 thousand) and with Marco Tronchetti Provera & C. S.p.A. (Euro 25 thousand).

The item **labour costs** includes the emoluments related to key managers.

Other costs for Euro 20,169 thousand in 2018 (Euro 18,618 thousand in 2017) mainly refer to expenses for services and miscellaneous costs (Euro 5,000 thousand HB Servizi S.r.l., Euro 3,178 thousand Pirelli Sistemi Informativi S.r.l., Euro 1,082 thousand Pirelli Servizi Amministrazione e Tesoreria S.p.A., Euro 559 thousand Pirelli Tyre S.p.A., Euro 345 thousand Servizi Aziendali Pirelli S.C.p.a.).

In the item associates, the amount shown refers to relations with the Consortium for Research on Advanced Materials – Corimav.

The item other related parties includes transactions with TP Trading (Beijing) Co. Ltd. for Euro 1,099 thousand, and the remuneration of directors and key managers for Euro 8,229 thousand.

Losses from investments for Euro 3,580 thousand in 2018 (Euro 11,480 thousand in 2017) refer to the write-downs of the investments in Fenice S.r.l. for Euro 2,229 thousand and Focus Investments S.p.A. for Euro 1,351 thousand. For further details, reference is made to note 33.

Dividends for Euro 283,549 thousand in 2018 (Euro 208,871 thousand in 2017) refer to dividends collected during the year (Euro 270,000 thousand from Pirelli Tyre S.p.A., Euro 5,800 thousand from Pirelli Sistemi Informativi S.r.l., Euro 5,025 thousand from Pirelli Group Reinsurance Company SA and Euro 500 thousand from Pirelli Servizi Amministrazione and Tesoreria S.p.A.).

The amount recorded in the item associates mainly refers to the dividends distributed by Fenice S.r.l. (Euro 2,224 thousand).

Financial income for Euro 59,277 thousand in 2018 (Euro 10,681 thousand in 2017) refers for Euro 40,292 to net profits on derivatives made with Pirelli International Plc, Euro 3,259 thousand to the charge-back of fees to Pirelli International Plc and for Euro 15,406 thousand for interest income on loans to Pirelli Tyre S.p.A..

Financial expenses of Euro 6,519 thousand in 2018 (Euro 103,275 thousand in 2017) mainly refer to Euro 21,977 thousand for the indemnity paid to Pirelli International Plc for costs incurred for the early termination of the loan offset for Euro 28,523 thousands from net interest income on Cross Currency Interest Rate Swap.

BENEFITS FOR KEY MANAGERS

At December 31, 2018, remuneration payable to key managers amounted to Euro 10,415 thousand. The portion relating to employee benefits was recognised in the Income Statement item "personnel costs" for Euro 2,186 thousand and for Euro 8,229 thousand in the Income Statement item "other costs".

39. OTHER INFORMATION

REMUNERATION OF DIRECTORS AND STATUTORY AUDITORS

The fees due to Directors of Pirelli & C. S.p.A. amounted to Euro 4,440 thousand in 2018 and Euro 2,133 thousand in 2017. The fees due to the Statutory Auditors for the function performed at Pirelli & C. S.p.A. amounted to Euro 275 thousand in 2018 (Euro 296 thousand in 2017).

AUDITORS' FEES

Pursuant to applicable regulation, the following table shows the fees pertaining to 2018 for the auditing activities and other services rendered by the Auditing Company PricewaterhouseCoopers S.p.A. and by the companies of the PricewaterhouseCoopers network:

in thousands of euro

	Company that provided the service	Company that received the service	Partial fees	Total fees
Independent auditing services	PricewaterhouseCoopers S.p.A.	Pirelli & C. S.p.A.	71	
Independent certification services (1)	PricewaterhouseCoopers S.p.A.	Pirelli & C. S.p.A.	220	
Services other than auditing	PricewaterhouseCoopers S.p.A.	Pirelli & C. S.p.A.	46	
				337

(1) the item "independent certification services" includes amounts paid for other services that envisage the issuance of an auditor's report as well as amounts paid for the so called certification services since they create synergies with the auditing services.

INFORMATION REQUIRED BY THE LAW N.124/2017 ART.1 – PARAGRAPHS 125-129

There is no information to be highlighted pursuant to the law in question referring to Pirelli & C. S.p.A. for the financial year 2018.

Any information referring to the subsidiaries of Pirelli & C. S.p.A. they are included in the consolidated financial statements.

40. ATYPICAL AND/OR UNUSUAL TRANSACTIONS

Pursuant to Consob Communication no. 6064293 of July 28, 2006, the Company certifies that no atypical and/or unusual transactions as defined in said Communication were carried out in 2018.

41. SIGNIFICANT EVENTS SUBSEQUENT TO THE END OF THE YEAR

Effective January 1, 2019 was the sale by the subsidiary Pirelli Tyre to the parent company Pirelli & C. S.p.A. of the business unit consisting of all the staff and business support functions related to Human Resources, Health and Safety, Security, Planning and Controlling, CFO, Legal Affairs, Digital, Communication. This operation is part of a large project for the reorganization of activities within the Group.

ANNEXES TO THE EXPLANATORY NOTES

MOVEMENTS OF INVESTMENTS IN SUBSIDIARIES FROM 12/31/2017 TO 12/31/2018

in thousands of euro

	12/31/2017				Changes		12/31/2018			
	Number of shares	Carrying amount (€/thousands)	% of total investments	Of which direct	Number of shares	(€/thousand)	Number of shares	Carrying amount (€/thousands)	% of total investments	Of which direct
INVESTMENTS IN SUBSIDIARIES										
ITALY										
Unlisted:										
Pirelli Servizi Amministrazioni e Tesoreria S.p.A.	2,047,000	3,237	100	100	-	-	2,047,000	3,237	100	100
Maristel S.r.l. - Milan	1,020,000	1,315	100	100	-	-	1,020,000	1,315	100	100
Pirelli International Treasury SpA	-	-	-	-	15,000	15	15,000	15	100	30
Pirelli Sistemi Informativi S.r.l. - Milan	1 quota	1,655	100	100	-	-	1 quota	1,655	100	100
Pirelli & C. Ambiente S.r.l.	1 quota	2,095	100	100	-	(2,096)	-	-	-	-
Pirelli Tyre S.p.A. - Milan	558,154,000	4,521,792	100	100	-	2,096	558,154,000	4,523,888	100	100
Servizi Aziendali Pirelli S.C.p.A. - Milan	94,978	101	100	91.3	-	-	94,978	101	100	91.3
HB Servizi Srl	1 quota	230	100	100	-	-	1 quota	230	100	100
Total investments in Italian subsidiaries		**4,530,427**				**15**		**4,530,442**		

	12/31/2017				Changes		12/31/2018			
	Number of shares	Carrying amount (€/thousands)	% of total investments	Of which direct	Number of shares	(€/thousand)	Number of shares	Carrying amount (€/thousands)	% of total investments	Of which direct
FOREIGN COMPANIES										
Brazil										
Pirelli Ltda - Sao Paulo	14,000,000	9,666	100	100	-	-	14,000,000	9,666	100	100
T3 Brasil Industrial de Pneus Agricol	-	-	-	-	-	-	-	-	-	-
Pirelli Latam Participações Ltda.	1	-	-	-	-	-	1	-	-	-
Pirelli Pneus Ltda	1	-	-	-	-	-	1	-	-	-
Pirelli Comercial de Pneus Brasil Ltda.	1	-	-	-	-	-	1	-	-	-
France										
Pirelli Solutions France Sarl - Villepinte	1 quota	-	-	100	-	-	1 quota	-	-	100
UK										
Pirelli UK ltd. - London - ordinary	163,991,278	21,871	100	100	-	-	163,991,278	21,871	100	100
Switzerland										
Pirelli Group Reinsurance Company S.A.	800,000	6,346	100	100	(500,000)	-	300,000	6,346	100	100
Total investments in foreign subsidiaries		**37,883**				**-**		**37,883**		
Total investments in subsidiaries		**4,568,309**				**15**		**4,568,324**		

MOVEMENTS OF INVESTMENTS IN ASSOCIATES FROM 12/31/2017 TO 12/31/2018

in thousands of euro

	12/31/2017				Changes		12/31/2018			
	Number of shares	Carrying amount (€/ thousands)	% of total investments	Of which direct	Number of shares	(€/ thousand)	Number of shares	Carrying amount (€/ thousands)	% of total investments	Of which direct
INVESTMENTS IN ASSOCIATES										
ITALY										
Unlisted:										
Fenice Srl - in liquidazione	1 quota	2,478	69.9	69.9	-	(2,478)	-	-	-	-
Consorzio per le Ricerche sui Materiali Avanzati (CORIMAV)	1 quota	104	100	100	-	-	1 quota	104	100	100
Eurostazioni S.p.A. - Roma	52,333,333	6,271	32.7	32.7	-	-	52,333,333	6,271	32.7	32.7
Focus Investments S.p.A.	111,111	1,352	8.3	8.3	-	(1,352.)	111,111	-	8.3	8.3
Total unlisted companies		**10,204**				**(3,830)**		**6,375**		
Total investments in associates - Italy		**10,204**				**(3,830)**		**6,375**		
Total investments in associates		**10,204**				**(3,830)**		**6,375**		

MOVEMENTS OF OTHER FINANCIAL ASSETS AT FAIR VALUE THROUGH INCOME FROM 01/01/2018 TO 12/31/2018

in thousands of euro

	1/1/2018				Changes		12/31/2018			
	Number of shares	Carrying amount (€/ thousands)	% of total investments	Of which direct	Number of shares	(€/ thousand)	Number of shares	Carrying amount (€/ thousands)	% of total investments	Of which direct
INVESTMENTS IN OTHER COMPANIES										
ITALIAN LISTED COMPANIES										
Mediobanca S.p.A. - Milan	15,753,367	149,027	1.8	1.8	(15,753,367)	(149,027)	-	-	-	-
Total other Italian listed companies		**149,027**				**(149,027)**		-		
Total other listed companies		**149,027**				**(149,027)**		-		

MOVEMENTS OF OTHER FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME FROM 01/01/2018 TO 12/31/2018 (CONTINUED)

in thousands of euro

	1/1/2018				Changes		12/31/2018			
	Number of shares	Carrying amount (€/ thousands)	% of total investments	Of which direct	Number of shares	(€/ thousand)	Number of shares	Carrying amount (€/ thousands)	% of total investments	Of which direct
INVESTMENTS IN OTHER COMPANIES										
ITALIAN LISTED COMPANIES										
RCS Mediagroup S.p.A. - Milan	24,694,918	30,177	4.7	4.7	-	(1,729)	24,694,918	28,449	4.7	4.7
Total other Italian listed companies		**30,177**				**(1,729)**		**28,449**		
Total other listed companies		**30,177**				**(1,729)**		**28,449**		

	1/1/2018				Changes		12/31/2018			
	Number of shares	Carrying amount (€/ thousands)	% of total investments	Of which direct	Number of shares	(€/ thousand)	Number of shares	Carrying amount (€/ thousands)	% of total investments	Of which direct
ITALIAN UNLISTED COMPANIES										
Aree Urbane S.r.l. (in liquidation) - Milan	1 quota	-	-	-	-	-	1 quota	-	-	-
C.I.R.A. - Centro Italiano di Ricerche Aerospaziali S.c.p.A. - Capua (CE)	30	-	0.1	0.1	-	-	30	-	0.1	0.1
Alitalia Compagnia Aerea Italiana S.p.A. - Rome	1,162,098,622	-	1.7	1.5	-	-	1,162,098,622	-	1.4	1.4
CEFRIEL - Società Consortile a Responsabilità limitata	1 quota	-	4.9	4.9	-	-	1 quota	-	4.9	4.9
Consorzio DIXIT (in liquidation) - Milan	1 quota	-	14.3	14.3	-	-	1 quota	-	14.3	14.3
MIP Politecnico di Milano - Graduate School of Business società consortile per azioni già Consorzio per L'Innovazione nella Gestione di Azienda -Mip - (Master Imprese Politecnico) Milan	12,000	-	3.1	3.1	-	-	12,000	-	2.9	2.9
Consorzio Milano Ricerche - Milan	1 quota	-	9.0	9.0	-	-	1 quota	-	9.0	9.0
Società Generale per la Progettazione Consulenze e Partecipazioni (ex Italconsult) S.p.A. - Rome	1,100	-	3.7	3.7	-	-	1,100	-	3.7	3.7
Emittenti Titoli S.p.A. in liquidazione - Milano	229,000	2,748	2.8	2.8	(229,000)	(2.748)	-	-	-	-
F.C. Internazionale Milano S.p.A. - Milan	55,805,625	-	0.4	0.4	-	-	55,805,625	-	0.4	0.4
Fin. Priv. S.r.l. - Milan	1 quota	19,909	14.3	14.3	-	(4.305)	1 quota	15,604	14.3	14.3
Istituto Europeo di Oncologia S.r.l. - Milan	1 quota	6,599	6.1	6.1	-	362	1 quota	6,961	6.1	6.1
Nomisma - Società di Studi Economici S.p.A. - Bologna	959,429	245	3.3	3.3	-	13	959,429	258	3.3	3.3
Redaelli Sidas S.p.A. (in liquidation) - Milan	750,000	-	4.6	4.6	(750,000)	-	-	-	-	-
Consorzio Movincom scrl	1	6	5.9	5.9	(1)	(6)	-	-	-	-
Movincom Servizi S.p.A.	1 quota	-	4.4	4.4	-	-	-	-	-	-
Tiglio I S.r.l. - Milan	1 quota	87	0.6	0.6	-	(17)	1 quota	70	0.6	0.6
Genextra S.p.A.	592,450	481	0.6	0.6	-	(442)	592,450	39	0.6	0.6
Total other Italian unlisted companies		**30,075**				**(7.142)**		**22,932**		

MOVEMENTS OF OTHER FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME FROM 01/01/2018 TO 12/31/2018

in thousands of euro

	01/01/2018				Changes		12/31/2018			
	Number of shares	Carrying amount (€/ thousands)	% of total investments	Of which direct	Number of shares	(€/ thousand)	Number of shares	Carrying amount (€/ thousands)	% of total investments	Of which direct
FOREIGN COMPANIES										
Libia										
Libyan-Italian Joint Company - ordinary shares B	300	32	1.0	1.0	-	-	300	32	1.0	1.0
Belgium										
Euroqube S.A. (in liquidation)	67,570	13	17.8	17.8	-	-	67,570	13	17.8	17.8
U.S.A.										
Gws Photonics Inc - Wilmington - private shares B	1,724,138	-	-	-	-	-	1,724,138	-	-	-
Gws Photonics Inc - Wilmington - private shares C	194,248	-	-	-	-	-	194,248	-	-	-
UK										
Eca International	100	-	2.8	2.8	-	-	100	-	2.8	2.8
Total other foreign companies		**45**				**-**		**45**		
OTHER PORTFOLIO SECURITIES										
Fondo Comune di Investimento Immobiliare - Anastasia	53 quote	15,270	-	-	-	305	53 quote	15,575	-	-
Total other portfolio securities		**15,270**				**305**		**15,575**		
TOTAL OTHER FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME		**75,566**				**(8,566)**		**67,000**		

LIST OF INVESTMENTS IN SUBSIDIARIES AND ASSOCIATES (PURSUANT TO ART. 2427 OF THE CIVIL CODE)

in thousands of euro

	Legal address	Carrying amount	Share %	Share capital	Attributable equity	Attributable net income (loss)
INVESTMENTS IN SUBSIDIARIES - ITALY						
Pirelli Servizi Amministrazione e Tesoreria S.p.A.	Milan	3,238	100%	2,047	3,386	211
Maristel S.p.A.	Milan	1,315	100%	50	2,009	(30)
Pirelli Sistemi Informativi S.r.l.	Milan	1,655	100%	1,010	2,587	356
Pirelli Tyre S.p.A.	Milan	4,523,887	100%	558,154	1,593,714	417,251
Servizi Aziendali Pirelli S.c.p.a.	Milan	101	91.3%	104	283	22
HB Servizi S.r.l.	Milan	230	100%	10	309	216
Pirelli International Treasury S.p.A.	Milan	15	30%	50	15	-
Total investments in subsidiaries - Italy		**4,530,441**				
INVESTMENTS IN FOREIGN SUBSIDIARIES						
Switzerland						
Pirelli Group Reinsurance Company S.A.	Lugano	6,346	100%	2,662	22,010	6,592
Brasil						
Pirelli Ltda	Sao Paulo	9,666	100%	3,154	1,706	286
UK						
Pirelli UK Ltd.	London	21,871	100%	183,326	18,581	(6,305)
Total investments in foreign subsidiaries		**37,883**				
Total investments in subsidiaries		**4,568,324**				
INVESTMENTS IN ASSOCIATES - ITALY						
Consortium for the Reserach into Advanced Materials (CORIMAV)	Milan	104	100%	104	104	-
Eurostazioni S.p.A. **	Rome	6,271	32.7%	16,000	6,394	129
Focus Investments S.r.l.	Milan	-	8.3%	*	*	*
Total investments in associates - Italy		**6,375**				
Total investments in associates		**6,375**				

* Data not yet available
** balance sheet at July 31, 2018

REPORT OF THE BOARD OF STATUTORY AUDITORS TO THE SHAREHOLDERS' MEETING

Dear Shareholders,
pursuant to art. 153 of Legislative Decree 58/1998 ("**TUF**") and the applicable provisions of the Italian Civil Code, the Board of Statutory Auditors (which also operates as internal control and audit committee), is called on to report to the Shareholders' Meeting convened to approve the financial statements on the supervisory activity carried out and any omissions or misconduct which it might have identified. The Board of Statutory Auditors may also make proposals regarding the financial statements and their approval and other matters under its responsibility.

During the year the Board of Statutory Auditors carried out its supervisory activities as required by the law in force, taking account of the standards of conduct for the Boards of Statutory Auditors of listed companies recommended in the document by the Consiglio Nazionale dei Dottori Commercialisti e degli Esperti Contabili (the Italian national association of chartered accountants and auditors) last updated in April 2018, and of the Consob provisions on company controls and the activity of the Boards of Statutory Auditors and its Corporate Governance Code for listed companies, to which Pirelli & C. S.p.A. (hereinafter also "**Pirelli**" or the "**Company**") has adhered.

As well as through the attendance of all or some of the Statutory Auditors at meetings of the Board of Directors and its committees, this also took place through the constant exchange of information between the Board of Statutory Auditors and the relevant administrative, audit and compliance departments, and with the Supervisory Body created pursuant to Legislative Decree no. 231 of 8 June 2001, as well as with the members of the boards of statutory auditors of the principal subsidiaries and with the firm appointed as external auditor.

APPOINTMENT AND COMPOSITION OF THE BOARD OF STATUTORY AUDITORS

The Board of Statutory Auditors in office at the date of this report was appointed by the Shareholders' Meeting held on 15 May 2018. This Meeting confirmed the appointment of all the standing members of the Board of Statutory Auditors whose mandates were due to expire, and hence the Board itself can state that it worked seamlessly throughout the whole of 2018.

In particular, the Board of Statutory Auditors is made up of Standing Auditors Francesco Fallacara

(Chairman), Fabio Artoni, Antonella Carù, Luca Nicodemi and Alberto Villani, and Alternate Auditors Franca Brusco and Elenio Bidoggia.

Pursuant to article 148, subsection 3 of the TUF, and the provisions of the Corporate Governance Code for listed companies, with which Pirelli has resolved to adhere, the Board of Statutory Auditors checked that its serving members retained, on 31 December 2018, the requirements of independence they had been ascertained to possess at the time of their appointment (see paragraph below on the considerations regarding the size and operation of the control body).

COMMENTS ON THE 2018 FINANCIAL STATEMENTS AND ON TRANSACTIONS OF MAJOR IMPORTANCE CARRIED OUT DURING THE YEAR

It should be noted that Pirelli's Financial Statements have been drawn up based on the IAS/IFRS international accounting standards issued by the International Accounting Standards Board (IASB) and endorsed by the European Union, in force on 31 December 2018 and in accordance with the instructions issued in implementation of article 9 of Legislative Decree 38/2005. The Financial Statements also include the notice required by law 124/2017 (art. 1, subsections 125-129).

The principal risks and uncertainties are summarised in the Directors' Report on Operations, and there is a section on the outlook for the coming year.

The Company's Financial Statements are made up of the Statement of Financial Position, Income Statement, Statement of Comprehensive Income, Statement of Changes in Equity, Statement of Cash Flows and Explanatory Notes.

The Financial Statements are accompanied by the Directors' Report on Operations, and include the Report on the Corporate Governance and Structure of Share Ownership – prepared pursuant to Article 123-bis of the TUF – as well as the Report on responsible management of the value chain (consolidated non-financial declaration pursuant to Legislative Decree No. 254, of 30 December 2016), drawn up by the Company in accordance with the Sustainability Reporting Standards of the Global Reporting Initiative (GRI) - Comprehensive option - and the principles of inclusiveness, materiality and compliance with the AA1000 Standard.

Pirelli's 2018 Separate Financial Statements and Consolidated Financial Statements include statements of compliance by the CEO and by the Manager responsible for the preparation of the corporate financial documents, as required by prevailing legislation.

As a result of the assignment of the shares of TP Industrial Holding S.p.A, the company that held almost all of Pirelli's industrial assets, to controlling shareholder Marco Polo International Holding Italy S.p.A., in March 2017, in continuity with the 2017 financial year, some of the residual assets of the Industrial business in China and Argentina qualify as "discontinued operations". The year's results of these discontinued operations are classified in the Income Statement as a single item "net income (loss) related to discontinued operations". The process of separation was completed in the month of June 2018 with reference to Argentina, and in the fourth quarter of 2018 with reference to China.

Pirelli's 2018 Consolidated Financial Statements present the following summary data:

Revenues	€ 5,194.5 million
Operating income (EBIT)	€ 703.1 million
Adjusted EBIT before startup costs	€ 1,002.7 million
Total consolidated net income (including divested assets)	€ 442.4 million

The consolidated net financial (liquidity)/debt position was negative to the amount of euro 3,180.1 million (euro 3,218.5 million at 31 December 2017).

Parent company Pirelli closed the financial year with positive net income to the amount of euro 262.4 million (euro 170.8 million in 2017).

Transactions of major importance are accounted for in detail in the Directors' Report on Operations, and in the financial statements. The following transactions, in particular, should be noted:

– on **11 January 2018** Pirelli disposed of its entire direct holding in Mediobanca S.p.A. - corresponding to approximately 1.8% of the bank's share capital - in an operation reserved to qualified investors in Italy and institutional investors abroad - generating income of euro 152.8 million in total;
– on **22 January 2018,** after the adoption of the *Euro Medium Term Note* (EMTN) programme approved by the Board of Directors on 21 December 2017, Pirelli placed a 5 year fixed rate bond for a nominal amount of euro 600 million with international institutional investors. The effective yield on maturity is 1.479% and the bonds were listed on the Luxembourg stock exchange;
– on **15 March 2018** Pirelli placed a "Floating Rate Note" for euro 200 million, with maturity September 2020. The floating rate bond issue - for institutional investors only - allowed the company to repay the same amount of its existing debt, further optimising financial structure by reducing the cost of debt;
– on **20 March 2018** subsidiary Pirelli International PLC reimbursed early the euro 600 million bond with maturity in November 2019. The reimbursement was at the price of euro 1,031.15 as make-whole amount for each euro 1,000 bond, plus euro 5.85 for interest accrued to the date of repayment;
– on **14 May 2018**, the Board of Directors of Pirelli approved a development of the organisational structure, intended to consolidate implementation of the integrated business model, proposed by Executive Vice President and CEO Marco Tronchetti Provera;
– on **15 May 2018**, the Pirelli Shareholders' Meeting approved the financial statements for the year to 31 December 2017 (as approved by the BoD on **26 February 2018**) and the increase in the number of members of the Board of Directors to 15, and - at the proposal of a group of institutional investors - appointed Giovanni Lo Storto as the new director. Mr Lo Storto became a member of the Audit, Risks, Sustainability and Corporate Governance Committee and the Remuneration Committee. Mr Lo Storto declared that he possessed the requirements to qualify as an independent director pursuant to the Consolidated Law on Finance and the Corporate Governance Code for listed companies. With his appointment, a majority of the members of the Board of Directors of Pirelli (8 out of 15 members) are independent. The Shareholders' Meeting also appointed the new Board of Statutory Auditors for the financial years 2018-2020, using the slate voting system. The Shareholders' Meeting also authorised the Board of Directors to stipulate a new D&O (Directors & Officers Liability Insurance) insurance policy, expressed its approval of the Remuneration Policy and approved - for the part linked to Total Shareholder Return - the adoption of the three year monetary incentive plan 2018-2020 (the "LTI Plan"), destined for all the management and linked to the 2018/2020 targets contained in the 2017/2020 business plan;
– on **22 June 2018**, the Board of Directors of Pirelli postponed the expiry (from 31 January to 31 December 2019) and extended the size of the preceding board authorisation on bonds from euro 1 billion to 1.8 billion, euro 800 million of which placed in the first quarter of 2018;
– on **26 July 2018**, Pirelli concluded a "*Schuldschein*" loan for a total of euro 525 million (approved by the Board of Directors on 22 June 2018). The loan, guaranteed by Pirelli Tyre S.p.A. and underwritten by primary market operators, is composed of a tranche of euro 82 million due in 3 years, a tranche of euro 423 million due in 5 years and a tranche of 20 million euros due in 7 years. The transaction allowed the Company to repay existing debt, further optimising its debt structure and costs;
– on **7 August 2018**, the Board of Directors of Pirelli - with reference to the Pirelli & C. S.p.A. euro 600,000,000 1.375 percent Guaranteed Notes due 25 January 2023" (ISIN: XS1757843146) issued by Pirelli under the euro 2 billion EMTN programme and listed on the Luxembourg stock exchange - resolved to proceed with the partial buyback of these bonds. At the end of the partial buyback programme, the Company announced on **19 December 2018** that - through a primary intermediary - it had bought back and at the same time cancelled bonds for a nominal value of euro 47 million;
– on **7 August 2018**, the Board of Directors of Pirelli, at the proposal of the Executive Vice President and CEO, Marco Tronchetti Provera, proceeded to co-opt Ning Gaoning and appoint him Chairman of the Board of Directors, to replace Ren Jianxin, who resigned on **30 July 2018**. The Board qualified Ning Gaoning - who declared that he was not in possession of the requirements of independence pursuant to the TUF and the Corporate Governance Code - as a non-executive director, and he was assigned legal representation of the Company pursuant to the bylaws. The Board also appointed the new director a member of the Appointments and Successions Committee;
– on **7 September 2018** Pirelli announced that it had sold its Car factory in Guacara, in Venezuela, together with all the assets the company owns in that country. The transaction, which follows the accounting deconsolidation that was carried out in 31 December 2015, had no financial effects on the group;
– on **9 October 2018**, Pirelli Tyre S.p.A. completed the acquisition of a 49% stake in the Joint Venture that,

through Jining Shenzhou Tyre Co., owns a new Consumer tyre manufacturing plant in China. The investment totalled around euro 65 million. Pirelli Tyre S.p.A. will have the right - which it can exercise in the period from 1 January 2021 to 31 December 2025 - to increase its stake to up to 70%;

- on **15 October 2018** Pirelli signed the prior agreement with the Italian Revenues Agency for access to the Patent Box tax concession, with reference to tax years 2015-2019. The tax benefit for the three-year period from 2015-2017 is approximately euro 54 million, plus the estimated benefit of euro 35 million for 2018. At the proposal of the CEO, the Board of Directors allocated the resources from the Patent Box to cost cutting actions to be implemented in 2019 to continue to support a double-digit reduction in exposure on the Standard segment and the High Value strategy;
- on **18 December 2018** Pirelli announced that - together with subsidiary Pirelli Tyre S.p.A. - it had been admitted to the Collaborative Compliance regime. This is a new way of interacting with the Italian Revenues Agency based on a transparent relationship that will further increase certainty on major tax issues. The admission came at the end of the positive assessment by the Italian Revenues Agency of the company's Tax Control Framework, the system to detect, manage, control and mitigate tax risk.

UNUSUAL OR EXCEPTIONAL TRANSACTIONS

Significant transactions in 2018 are detailed in the Directors' Report on Operations. We are unaware of any atypical or unusual transactions, as defined by Consob in notice DEM/6064293 of 28 July 2006.

INTRAGROUP OR RELATED PARTY TRANSACTIONS

Pursuant to article 2391-bis of the Italian Civil Code and Consob resolution 17221 of 12 March 2010, containing the “Regulations on Related Party Transactions”, subsequently amended by Consob Resolution 17389 of 23 June 2010, the Board of Directors of Pirelli, on 31 August 2017, unanimously approved the “Procedure for Related-Party Transactions” with effect from 4 October 2017, when listing of the Company’s ordinary shares started on the Mercato Telematico Azionario (the screen-based "Main Market") organised and managed by Borsa Italiana S.p.A.

In line with the information set out in the listing prospectus, on 6 November 2017 the Board of Directors of Pirelli, subject to the favourable opinion of the relevant Committee, comprised exclusively of Independent Directors (and entrusted with this duty under Article 4 of the aforementioned Regulations with a specific resolution passed by the Board of Directors) unanimously confirmed the text of the “Procedure for Related-Party Transactions” approved before listing.

It should be noted that, pursuant to article 4, subsection 6 of the aforementioned Regulations, the Procedure adopted by the Company (i) is coherent with the principles contained in said Regulations, and (ii) is published on the Company's website www.pirelli.com).

During the 2018 financial year there were both intra-group and third party related-party transactions.

The intra-group transactions, the effects of which are shown in the financial statements, were found to be of an ordinary nature, since they essentially consist of the reciprocal provision of administrative, financial and organisational services. They were regulated applying normal conditions determined using standard parameters that reflect the actual use made of the services and were carried out in the interests of the Company, since they were aimed at rationalising the use of the Group's resources.

The non-intragroup related-party transactions that we reviewed were also of an ordinary nature (since they were part of normal business operations or related financial activities) and/or concluded at market or standard equivalent terms and were in the interest of the Company. These transactions were reported to us periodically by the Company.

We attended the meetings of the Related-Party Transactions Committee during which the Committee expressed a favourable opinion of some related party transactions of "lesser importance", after having considered the interest of the Company in the completion of the transaction and the expediency and substantial correctness of their conditions.

Regarding such transactions, we have always expressed the view that they were in the interests of the Company.

The Board of Directors attended the meetings of the Related-Party Transactions Committee, and on 14 February 2019, attended the meeting of the Company's Board of Directors that, for all intents and purposes, approved the redrafting of some of the terms of the licence agreements with Prometeon Tyre Group S.r.l. and Aeolus Tyre Co. Ltd (companies with the same parent company as the Company), the effects of which - including in the 2018 results and in the preliminary results announced to the market - had been previously communicated to the market when the draft 2018 consolidated results were announced. It should be noted that, to ensure maximum transparency to the market, the Company prudentially decided to voluntarily publish an Information Document for these transactions, drafted pursuant to art. 5 of the Regulations on Related Party Transactions approved by Consob with resolution 17221 of 12 March 2010 (as subsequently amended) and to art. 18 of the Procedure for Related-Party Transactions adopted by the Company. The Information Document was published on 20 February 2019.

We have monitored compliance with the Procedure for Related-Party Transactions adopted by the Company and the correctness of the process followed by the Board and the competent Committee for the qualification of related parties and have nothing to report.

The transactions with related parties are detailed in the notes to the Company's separate and consolidated financial statements, including information on the consequent effects on the Income Statement and the Statement of Financial Position. The Statutory Auditors deem the information on transactions with related parties provided in the financial statements to be adequate.

IMPAIRMENT TEST PROCEDURE

It should be noted that, as suggested in the joint Banca d'Italia/Consob/ISVAP document of 3 March 2010, the Board of Directors, independently, and before the formal approval of the financial statements by the Board of Directors (which occurred at the meeting on 26 February 2019), resolved that the impairment test procedure complied with the prescriptions of international accounting standard IAS 36, after said procedure had been approved by the Audit, Risks, Sustainability and Corporate Governance Committee and the Board of Statutory Auditors.

Specifically, the Company carried out an impairment test on the goodwill allocated to the group of Consumer cash generating units and to the Pirelli brand.

Information on the assessment process conducted with the assistance of a highly qualified expert, and on its outcomes, is provided in the explanatory notes to the financial statements.

The Statutory Auditors consider the procedure adopted by the Company to be adequate.

SUPERVISORY ACTIVITY PURSUANT TO LEGISLATI|VE DECREE 39/2010 - EXTERNAL AUDITOR

The Board of Statutory Auditors, in collaboration with the Audit, Risks, Sustainability and Corporate Governance Committee and pursuant to changes to the regulations introduced by Legislative Decree 135/2016, supervised:

- the financial reporting process;
- the effectiveness of the internal control, internal audit and risk management systems;
- the external audit of the annual and consolidated accounts;
- the independence of the external auditor, in particular with regard to the provision of non-auditing services;
- the results of the external audit with specific reference to the additional report pursuant to article 11 of European regulation 537/2014.

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SUPERVISING THE FINANCIAL REPORTING PROCESS

The Board of Statutory Auditors, having verified that there are adequate rules and processes governing the process of "formulating" and "disseminating" financial information, considers that the financial reporting information process is adequate, and believes that there are no issues to raise with the Shareholders' Meeting in this regard.

In addition to the annual and half-year reports, the Company voluntarily publishes the additional periodic financial information specified in art. 82-ter of Consob Regulation 11971/99 ("interim reports on

operations") for the periods that end on 31 March and 30 September each year.

SUPERVISING THE NON-FINANCIAL REPORTING PROCESS

The Board of Statutory Auditors monitored compliance with the provisions contained in legislative decree 254/2016 with reference to the declaration of a non-financial nature (the "**NFD**"), also verifying that there are adequate rules and processes governing the process of "formulating" and "disseminating" non-financial information, and considers that the non-financial reporting information process is adequate, and believes that there are no issues to raise with the Shareholders' Meeting in this regard.

In particular, the Board of Statutory Auditors acknowledged that the Company has adopted a structured system to monitor the content of the NFD which includes: (i) a dedicated operating rule to ensure adequate reporting of information of a non-financial nature; (ii) a control system to ensure greater assurance that the principal non-financial information is reported correctly; (iii) checks of the data of a non-financial nature in the NFD, after appropriate highlighting and verification; (iv) signature of a letter of attestation by the senior management on the non-financial data included in the paragraphs on this subject in the financial statements.

The Company did not avail itself of its right pursuant to art. 3, subsection 8 of legislative decree 254/2016 to omit information concerning imminent developments and transactions being negotiated.

With reference to the issue of the protection of personal data, the Board of Statutory Auditors acknowledges that the Pirelli group has put in place the activities needed to ensure that the company complies with the new provisions introduced by EU Regulation 2016/279. In particular, in the European Group companies, activities to attribute roles and responsibilities in the company organisation, formalisation of internal rules, and updating of the documents required by the law were completed over the course of 2018.

SUPERVISING THE EFFECTIVENESS OF THE INTERNAL CONTROL, INTERNAL AUDIT AND RISK MANAGEMENT SYSTEMS, AND THE EXTERNAL AUDIT OF THE ANNUAL SEPARATE AND CONSOLIDATED FINANCIAL STATEMENTS

The Board of Statutory Auditors, together with the Audit, Risks, Sustainability and Corporate Governance Committee met with the Head of Internal Audit once every quarter. At those meetings, information was provided on the results of the audits designed to ascertain the adequacy and operational effectiveness of the Internal Control System, compliance with the laws and the business procedures and processes, as well as on the implementation of the related improvement plans. The Board also received the Audit Plan for the financial year, its final results and the risk analysis, expressing a favourable opinion of their approval by the Board, where requested. During the meetings it was also constantly updated about the application of the "Whistleblowing" procedure in the Pirelli Group.

Furthermore, every six months it received the reports of the Audit, Risks, Sustainability and Corporate

Governance Committee and the Supervisory Body on the activities they had undertaken.

The Board of Statutory Auditors also took note of the report made by the Manager responsible for the preparation of the corporate financial documents who, when the draft financial statements were being approved, confirmed the adequacy and appropriateness of the powers and resources conferred on him by the Board of Directors, and also confirmed that he had been given direct access to all the information necessary to produce accounting data, without needing to obtain any authorisation. The Board of Statutory Auditors also acknowledged that the Manager Responsible had reported that he had participated in the internal flows of information for accounting purposes and had approved all corporate procedures which impacted the Company's profitability, financial position and/or assets and liabilities.

Accordingly, the Board of Statutory Auditors expresses a positive opinion of the adequacy of the internal control and risk governance system as a whole, and has no issues to raise with the Shareholders' Meeting in this regard.

The Board of Statutory Auditors also met with the external auditor at least once every quarter. No fundamental issues or significant shortcomings in the internal control system related to the financial reporting process arose in these meetings, also with regard to the provisions set out in article 19, subsection 3 of legislative decree 39/2010.

In particular, it should be noted that the Board of Statutory Auditors found that the controls specified in Law 262/2005 on the financial statements as at 31 December 2018 evidenced that the administrative-accounting procedures had been applied correctly. The prescribed controls on the application of the control framework for the NFD evidenced that the internal procedures had also been applied correctly.

The Board of Statutory Auditors considered that no "significant shortcomings" in the internal control system for the financial reporting process and the NFD emerged in the letter of recommendations to the management drafted by the external auditor.

The firm appointed to undertake the external audit of the accounts of the Company is PricewaterhouseCoopers S.p.A. ("PWC"). The appointment as external auditor of the accounts was made by the Shareholders' Meeting, on the reasoned proposal of the control body, in its meeting on 1 August 2017, for the nine year period 2017/2025, pursuant to the applicable provisions for listed companies (the appointment was effective from 4 October 2017, the date Pirelli's shares were admitted to trading). PWC was also appointed as external auditor of the accounts of the principal Pirelli Group companies in Italy and abroad.

Pursuant to art. 14 of legislative decree 39/2010 and art. 10 of Regulation EU 537/3014, PWC issued its Reports on the separate and consolidated financial statements as at 31 December 2018 on 3 April 2019. On the same date, the auditing firm issued its Additional report for the internal control and audit committee, drafted pursuant to art. 11 of Regulation EU 537/3014. On the same date, 3 April 2019, PWC issued its Report on the consolidated non-financial declaration pursuant to art. 3, subsection 10 of legislative decree 254/2016.

The texts of the aforementioned reports - drafted in accordance with the applicable legal provisions - do not contain any elements to bring to the attention of the Shareholders' Meeting.

SUPERVISING THE INDEPENDENCE OF THE EXTERNAL AUDITOR, IN PARTICULAR WITH REGARD TO THE PROVISION OF NON-AUDITING SERVICES

The Board of Statutory Auditors monitored the independence of the external auditor and in particular received periodic evidence of non-audit work assigned to PWC, also by virtue of specific regulatory provisions.

Regarding the independence of the external auditor, a structured procedure has been issued at Group level. In line with the provisions of legislative decree 39/2010, this sets out that no Pirelli Group company may assign tasks other than the external audit of the accounts, to companies that are members of the network of the appointed external auditor without the prior express authorisation of the Board of Statutory Auditors, which, with the assistance of the Chief Financial Officer and Board Secretary, has the responsibility of checking that the proposed assignment is not of a type listed among those not permitted by art. 5 of Regulation EU 537/2014, and that in any event, given its characteristics, said assignment has no impact on the independence of the external auditor.

In a letter dated 3 April 2019, PWC confirmed its independence pursuant to art. 6, paragraph 2) of Regulation EU 537/2014 and paragraph 17, letter a) of International Audit Standard (IAS) 260.

During the 2018 financial year, PWC and its network carried out the activities summarised below for the Group. These activities were the object of assignments approved by the Board of Statutory Auditors where they do not relate to tasks assigned before the Company was listed:

COMPENSATION OF INDEPENDENT AUDITORS

(In thousands of euro)	Company that provided the service	Company that received the service	Partial fees	Total fees	
Independent auditing services	PricewaterhouseCoopers S.p.A.	Pirelli & C. S.p.A.	71		
	PricewaterhouseCoopers S.p.A.	Subsidiaries	611		
	Network PricewaterhouseCoopers	Subsidiaries	1.428	**2.110**	*66%*
Independent certification services (1)	PricewaterhouseCoopers S.p.A.	Pirelli & C. S.p.A.	220		
	PricewaterhouseCoopers S.p.A.	Subsidiaries	240		
	Network PricewaterhouseCoopers	Subsidiaries	72	**532**	*17%*
Services other than auditing	PricewaterhouseCoopers S.p.A.	Pirelli & C. S.p.A.	46		
	PricewaterhouseCoopers S.p.A.	Subsidiaries	195		
	Network PricewaterhouseCoopers	Subsidiaries	293	**533**	*17%*
				3.176	100%

(1) the item "independent certification services" includes amounts paid for other services that envisage the issuance of an auditor's report as well as amounts paid for the so called certification services since they create synergies with the auditing services.

The Board of Statutory Auditors considers the fees mentioned above to be adequate to the size, complexity and characteristics of the work carried out, and also considers that the non-audit assignments (and their fees)

are not such as to have an impact on the independence of the external auditor.
In this latter regard, it should be noted that the Board of Directors, after having obtained the assessment of the Audit, Risks, Sustainability and Corporate Governance Committee, was in agreement with the Statutory Auditors' opinion.

ORGANISATIONAL STRUCTURE

The Board of Statutory Auditors considered the Company's organisational structure to be adequate for the needs of the Company and appropriate to ensure that the principles of correct administration are respected.
The Report on corporate governance and the share ownership structure describes in detail the types of powers conferred on the Executive Vice President and Chief Executive Officer Marco Tronchetti Provera and indicates the matters reserved to the competence of the Board of Directors of Pirelli & C.
The Board of Statutory Audits deemed the organisational structure to be adequate, also after the creation of the General Manager Operations role, assigned to Andrea Casaluci, approved by the Board of Directors in its meeting on 14 May 2018.
It should be noted that on 26 February 2019 the Board of Directors confirmed its preceding assessments regarding the absence of a subject that exercises direction and coordination of the Company pursuant to art. 2497 of the Italian Civil Code, without prejudice to the right of the parent company to include Pirelli within its own consolidation perimeter for accounting purposes.

REMUNERATION OF THE DIRECTORS, GENERAL MANAGER AND KEY MANAGERS WITH STRATEGIC RESPONSIBILITIES

During the year, the Board of Statutory Auditors has expressed the opinions required by law regarding proposals for the remuneration of directors holding special offices, expressing the opinions prescribed in article 2389 of the Italian Civil Code.
In particular, the Board of Statutory Auditors, in the meeting of the Board of Directors on 26 February 2018, expressed a favourable opinion of the proposal to remodulate the remuneration of the Executive Vice President and Chief Executive Officer.
In the same meeting, the Board of Statutory Auditors further expressed favourable opinions: (i) of the 2017 variable incentive paid to the Head of Internal Audit, (ii) of the achievement of the targets set for the preceding LTI Plan, (iii) of the consequent launch of the 2018-2020 LTI Plan, (iv) of the award of the 2017 MBO incentives and the 2018 MBO Plan. The part of the 2018-2020 LTI Plan linked to Total Shareholder Return was approved by the Shareholders' Meeting on 15 May 2018.
During the meeting of the Board of Directors on 14 May 2018, the Board of Statutory Auditors expressed a favourable opinion of the remuneration awarded to the "new" General Manager Operations (revised on 26 February 2019) and the Key Managers with strategic responsibilities appointed on that date.

In the meeting of the Board of Directors on 26 February 2019, the Board of Statutory Auditors expressed its positive assessment of the structure of the 2019 MBO which, among the targets set to obtain the variable annual component for the 2019 financial year, includes a new target (on Sustainability) with a weight of 10% at target, consisting of green revenues on the whole range, with a mechanism to set the targets for the MBO plan that is more challenging than the targets disclosed to the market.
For more details, see the annual Remuneration Report.

FURTHER ACTIVITIES OF THE BOARD OF STATUTORY AUDUTORS AND INFORMATION REQUIRED BY CONSOB

In exercising its duties, the Board of Statutory Auditors, as prescribed in article 149 of the TUF, monitored:

- observance of the law and the deed of incorporation;
- compliance with the principles of correct administration;
- the adequacy, for those aspects within its remit, of the organisational structure of the Company, the internal control system and the administrative-accounting system, and of the reliability of the latter to correctly represent operations;
- how the corporate governance rules contained in the codes of behaviour which the Company, in a notice to the public, declares that it complies with are actually implemented. In this respect, it should be noted that, pursuant to article 123-*bis* of the TUF, the Company has, for the 2018 financial year, drafted its annual Report on corporate governance and the structure of share ownership which provides information on (i) the corporate governance practices actually applied by the Company, over and above the obligations specified in the legal or regulatory provisions, (ii) the principal features of the risk and internal control systems that exist in relation to the financial reporting process, including the consolidate financial reports, (iii) how the Shareholders' Meeting functions, including its principal powers and shareholders' rights and how they are exercised, (iv) the composition and operation of the administration and control bodies and their committees, and the other information specified in article 123-*bis* of the TUF;
- the adequacy of the instructions imparted by the Company to its subsidiaries pursuant to article 114, subsection 2 of legislative decree 58/1998, having ascertained that the Company is able to promptly and regularly fulfil the disclosure obligations set out in law and in the EU regulations, as prescribed in the aforementioned article, also by collecting information from the heads of the organisational departments, and periodic meetings with the external auditor, to exchange relevant data and information. In this regard, we have no particular comments to make.

It should also be noted that the Directors' Report on Operations includes a paragraph containing a description of the principal features of the internal control and risk management system in relation to the financial reporting process, including the reporting of consolidated financial information.

The Board of Statutory Auditors notes:

- that the Directors' Report on Operations complies with the current laws, reflecting the resolutions made by the administrative body and the results in the financial statements, and contains adequate information on operations during the year and on intra-group transactions. The section containing the report on transactions with related parties has been included in the explanatory notes to the financial statements, in compliance with the IFRS standards;
- that the explanatory notes comply with the current standards, indicating the criteria used in determining the balance sheet items and in the value adjustments, and that the separate and consolidated financial statements of the Company appear to have been drafted in accordance with the structure and frameworks imposed by the current standards. In application of Consob's provisions, the effects of relations with related parties on the Company's profitability, financial position, assets and liabilities and cash flows;
- that Directors and/or Senior Managers of the Parent Company are members of the Boards of Directors of the principal subsidiary companies to guarantee coordinated direction and an adequate flow of information, also supported by suitable accounting information.

It should also be noted that the Board of Statutory Auditors:

- received information from the Directors at least once every quarter concerning their activity and the transactions carried out by the Company having the greatest impact on its strategy, earnings, financial position and equity, and that it received this information in compliance with the specific procedure approved by the Board of Directors. The Board of Statutory Auditors can give reasonable assurance that the resolved and executed transactions comply with the law and the Articles of Association, and are not manifestly imprudent, reckless or in conflict of interest, or in violation of the resolutions passed by the Shareholders' Meeting, or capable of compromising the integrity of the company's assets;
- received from the Supervisory Body, of which Statutory Auditor Ms. Antonella Carù is a member, information about the results of its own control activity, which did not reveal anomalies or misconduct;
- held periodic meetings with representatives of the external auditor in order to exchange important data and information for the performance of its duties, as prescribed in article 150, subsection 3 of the TUF. In this regard, it should be noted that no important data and information were identified which would require a mention in this report;
- obtained information from the corresponding bodies of the main subsidiaries with regard to their management and control systems and their general operating performance (pursuant to subsections 1 and 2 of article 151 of the TUF);
- during the 2018 financial year, issued opinions pursuant to article 2386 of the Italian Civil Code, on the

occasion of the appointment of Ning Gaoning as a Director by co-option (Mr Gaoning was then appointed Chairman of the Board of Directors) on 7 August 2018.

During the 2018 financial year the Board of Statutory Auditors did not receive any complaints.
The Board of Statutory Auditors acknowledges that it received a complaint pursuant to art. 2408 of the Italian Civil Code from shareholder Mr Marco Bava, who asked the Statutory Auditors to ascertain whether each shareholder, even if a "minority" shareholder, could submit the names of candidates for the appointment of a new Director, an item on the agenda of the Shareholders' Meeting called for 15 May 2018.
The Company - in agreement with the Board of Statutory Auditors - ensured that the shareholder received the documentation on the "Appointment of a Director" item on the agenda of the aforementioned shareholders' meeting that had previously been made available to the public pursuant to law, which indicated that not only was it possible for any shareholder to do so, but that the Board had decided to put the proposal that a new Director be appointed to the shareholders' meeting solely for the purpose of enabling the "minority" shareholders to appoint their representative on the Board.
Based on the investigation it carried out, and taking account of the above, the Board of Statutory Auditors decided that the complaint received was without merit.

With regard to the external auditor, the Board of Statutory Auditors noted that PricewaterhouseCoopers S.p.A.:

- issued its report pursuant to article 14 of legislative decree 39/2010 and article 10 of Regulation EU 537/201 on 3 April 2019. This containing its unqualified opinion stating that the separate and consolidated financial statements provide a truthful and accurate representation of the equity and financial position of Pirelli and of the Group as at 31 December 2018, and of the economic results and cash flow for the financial year that closed on that date, in compliance with applicable accounting standards, and provided evidence of key aspects of their audit;
- issued a coherence opinion indicating that the Report on Operations accompanying the separate and consolidated financial statements as at 31 December 2018, and some specific information contained in the Report on Corporate Governance and the Structure of Share Ownership, as laid down in article 123-bis, subsection 4 of the TUF have been drafted in compliance with current legislation;
- as regards possible significant errors in the Report on Operations, stated that, based on the knowledge and understanding of the company and its market that it had acquired in the course of the audit activities, it had no matters to raise;
- confirmed the Company's statement regarding the fact that no other assignments have been given to persons or entities with on-going relationships with the external auditor itself;
- on 3 April 2019, provided the Board of Statutory Auditors with the Additional Report referred to in

article 11 of regulation EU 537/2014, indicating that there were no significant shortcomings in the internal control system in relation to the financial reporting process that needed to be brought to the attention of persons responsible for "governance" activities;

- on 3 April 2019, pursuant to article 3,subsection 10 of legislative decree 254/2016, issued the Report on the responsible management of the value chain (consolidated non-financial declaration pursuant to legislative decree No. 254, of 30 December 2016), concluding that no elements had come to PWC's attention that led it to believe that the group's NFD for the year to 31 December 2018 had not been drawn up, in all significant aspects, in accordance with the requirements set out in legislative decree 254/2016 and the GRI Standards;
- annexed to the Additional Report, the external auditor provided the Board of Statutory Auditors, pursuant to article 6 of regulation EU 537/2014, with a statement from which no situations emerge that could compromise the independence of the external auditor (for more details concerning the provision of non-auditing services, see the paragraph entitled "supervising the independence of the external auditor, in particular with regard to the provision of non-auditing services" in this report).

The Board of Statutory Auditors also took note of the Transparency Report drafted by the external auditor and published on its web site, pursuant to article 18 of legislative decree 39/2010.

Furthermore, with regard to the corporate bodies, the Board of Statutory Auditors noted that:

- the current Board of Directors - the mandate of which expires with the Shareholders' Meeting called to approve the financial statements for the year to 31 December 2019 - is composed of 15 Directors, 14 of whom qualified as non-executive directors and, of these, 8 deemed to possess the requirements of independence specified in the Corporate Governance Code and the TUF. During 2018, it met 6 times.

At the date of this report:

- the Audit, Risks, Sustainability and Corporate Governance Committee is composed of four Directors, all independent. During 2018, it met 5 times;
- the Remuneration Committee is composed of four Directors, a majority of whom independent (the Chairman is an independent Director). During 2018, it met 3 times;
- the Related-Party Transactions Committee is composed of three Directors, all independent. During 2018, it met 10 times;
- the Appointments and Successions Committee is composed of four Directors, one of whom is the executive Director. It did not meet during 2018;
- the Strategies Committee is composed of seven Directors, of whom two are independent. It did not meet during 2018.

The Board of Statutory Auditors has always attended the meetings of the Board of Directors and the board committees, also in its capacity as internal control and audit committee pursuant to art. 19 of legislative

decree 39/2010.

The Board of Statutory Auditors also attended the ordinary Shareholders' Meeting that in 2018 was held on 15 May.

The percentage attendance figures of the single members of the Board of Statutory Auditors at the meetings of the above bodies are provided in the report on corporate governance and the share ownership structure.

Finally, the Statutory Auditors acknowledge:

- that they have monitored fulfilment of the requirements linked to the "Market Abuse" and "Investor Protection" regulations on the subject of corporate information and internal dealing, with particular reference to the handling of inside information and the procedure for the dissemination of press releases and information to the public;
- that they ascertained, upon their appointment and most recently in their meeting on 26 February 2019, as recommended by the Borsa Italiana Corporate Governance Code, that members possess the same independence requirements - where applicable - as those requested for the directors in the aforementioned Code;
- that they have found that the criteria and procedures to ascertain the independence requirements adopted by the Board of Directors to annually check the independence of its members are correctly applied, and have no comments to make on this point;
- that they have determined that the Director's report on the Company's financial statements describes the principle risks and uncertainties to which the Company is exposed;
- that, with reference to the provisions of article 15 of Consob Regulation 20249 of 28 December 2017 concerning market discipline, they have ascertained that the organisation of the company and the procedures adopted enable Pirelli to ensure that the companies it controls and which are constituted in and regulated by the laws of States that are not members of the European Union subject to respecting the aforementioned Consob provisions, have administrative-accounting systems appropriate to regularly provide the senior management and external auditor of the Company with the information on its profitability, financial position and assets and liabilities needed to draw up the consolidated financial statements.

During the course of its supervisory activities, and on the basis of the information obtained from the external auditor, no omissions, misconduct, irregularities or significant facts were found which are worthy of being reported or mentioned in this report.

The activities described above, conducted both collectively and individually, have been documented in the minutes of the 12 meetings of the Board of Statutory Auditors held during 2018 both before and after its renewal.

SELF-ASSESSMENT OF THE BOARD OF STATUTORY AUDITORS

During 2018 the Board of Statutory Auditors started, for the first time - as recommended by the rules of behaviour for listed companies issued by the Italian national association of chartered accountants and auditors - a self-assessment process, carried out with the assistance of independent consulting firm SpencerStuart.

This self-assessment was carried out through individual interviews, with questions on the suitability, size, composition and operation of the Board of Statutory Auditors, so as to attest that the body is operating correctly and effectively and has an adequate composition.

The Board of Statutory Auditors can report that the self-assessment provided a broadly positive picture of the composition and operation of the control body. In particular, the Board of Statutory Auditors considered that its current size, of 5 standing members, introduced before listing on the stock exchange, is perfectly adequate for the effective execution of the tasks the Statutory Auditors are required to undertake in a company of Pirelli's size.

Furthermore, the Board of Statutory Auditors particularly appreciated the Induction and training activities organised by the Company for Directors and Statutory Auditors and hopes that such activities - which provide further opportunities for the different corporate bodies to meet and exchange knowledge - might also continue in the current year.

PROPOSALS TO THE SHAREHOLDERS' MEETING

FINANCIAL STATEMENTS AT 31 DECEMBER 2018

The Board of Statutory Auditors expresses its favourable opinion on the approval of the Financial Statements at 31 December 2018 and has no objections to raise regarding the proposal made for the allocation of the profits.

GROUP REMUNERATION POLICY

We inform you that the Board of Statutory Auditors has expressed a favourable opinion on the 2019 Remuneration Policy submitted for consultation to the Shareholders' Meeting called on 15 May 2019.

OTHER ISSUES SUBMITTED TO THE SHAREHOLDERS' MEETING FOR APPROVAL

Regarding the other issues submitted to you for approval (the appointment of a director and of the Chairman of the Board of Directors), the Statutory Auditors have no comment to make.

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Pursuant to article 144-*quinquiesdecies* of the Issuer Regulations, duly approved by Consob with

resolution 11971/99, as subsequently amended and supplemented, the list of offices held by members of the Board of Statutory Auditors in the companies listed in Book V, Title V, Chapters V, VI and VII of the Italian Civil Code is published by Consob on its website (www.consob.it).

It should be noted that article 144-*quaterdecies* (Consob reporting obligations) establishes that a person who is a member of the supervisory body of just one issuer is not subject to the reporting obligations prescribed in this article, and therefore, in this case, they do not appear in the lists published by Consob.

The Company lists the main positions held by the members of the Board of Statutory Auditors in its Report on Corporate Governance and the Structure of Share Ownership.

The Board of Statutory Auditors here acknowledges that all its members were in full compliance of the aforementioned regulatory provisions laid down by Consob governing the "maximum number of positions to be held".

ssMilan, 3 April 2019

Mr Francesco Fallacara

Mr Fabio Artoni

Ms Antonella Carù

Mr Luca Nicodemi

Mr Alberto Villani