

November 9, 2006

## **SECOND QUARTER AND HALF YEAR RESULTS TO SEPTEMBER 30, 2006**

### **SECOND QUARTER HIGHLIGHTS**

- Revenue of £4,941 million, up 4 per cent
- New wave revenue of £1,736 million, up 21 per cent, representing 35 per cent of total revenue compared with 30 per cent last year
- EBITDA before specific items<sup>1</sup> and leaver costs of £1,418 million, up 2 per cent
- Profit before taxation, specific items<sup>1</sup> and leaver costs of £665 million, up 12 per cent
- Earnings per share before specific items<sup>1</sup> and leaver costs of 6.0 pence, up 13 per cent
- Continued strong broadband net additions<sup>2</sup> of 626,000 of which BT Retail's share was 25 per cent

### **HALF YEAR HIGHLIGHTS**

- Revenue of £9,805 million, up 3 per cent
- New wave revenue of £3,377 million, up 20 per cent
- EBITDA before specific items<sup>1</sup> of £2,747 million, up 2 per cent
- Profit before taxation and specific items<sup>1</sup> of £1,247 million, up 17 per cent
- Earnings per share before specific items<sup>1</sup> of 11.3 pence, up 19 per cent
- Interim dividend of 5.1 pence per share, up 19 per cent
- Broadband end users<sup>2</sup> of 9.3 million at September 30, 2006 of which BT Retail now has 3 million customers

The income statement, cash flow statement and balance sheet from which this information is extracted are set out on pages 16 to 22.

<sup>1</sup>Before specific items which are material one off or unusual items as defined in note 4 on page 26.

<sup>2</sup>DSL and LLU connections.

## **Chairman's statement**

Sir Christopher Bland, Chairman, commenting on the half year results said:

“These strong half year results show sustained momentum across the business with revenues up 3 per cent and earnings per share before specific items up 19 per cent.

“I am pleased to report that we will be paying an interim dividend of 5.1 pence, up 19 per cent on last year, showing our continued commitment to improving shareholder returns and our confidence for the future.”

## **Chief Executive's statement**

Ben Verwaayen, Chief Executive, commenting on the second quarter results, said:

"These second quarter results show another strong team performance with every part of the business playing its part. We have announced today that BT Retail has passed 3 million broadband connections in a fast growing market. We have now reached 1 million LLU connections. 21CN is going live in the Cardiff area this month. The business continues to win major transformational contracts, including PepsiCo and Vodafone.

“Revenue has increased for eleven consecutive quarters and earnings per share<sup>1</sup> were up 13 per cent, the eighteenth consecutive quarter of growth. EBITDA<sup>1</sup> continues to grow and was up 2.4 per cent.

“These results underpin our confidence in our ability to grow our revenue, EBITDA, earnings per share and dividends this year.”

<sup>1</sup>Before specific items and leaver costs.

**RESULTS FOR THE SECOND QUARTER AND HALF YEAR  
TO SEPTEMBER 30, 2006**

	Second quarter			Half year		
	2006 £m	2005 £m	Better (worse) %	2006 £m	2005 £m	Better (worse) %
Revenue	4,941	4,767	4	9,805	9,498	3
<b>EBITDA</b>						
- before specific items and leaver costs	1,418	1,385	2	2,804	2,748	2
- before specific items	1,385	1,348	3	2,747	2,705	2
<b>Profit before taxation</b>						
- before specific items and leaver costs	665	596	12	1,304	1,113	17
- before specific items	632	559	13	1,247	1,070	17
- after specific items	629	489	29	1,244	988	26
<b>Earnings per share</b>						
- before specific items and leaver costs	6.0p	5.3p	13	11.8p	9.8p	20
- before specific items	5.7p	5.0p	14	11.3p	9.5p	19
- after specific items	5.7p	4.4p	30	11.3p	8.8p	28
Capital expenditure	812	694	(17)	1,527	1,410	(8)
Free cash flow	338	503	(33)	321	377	(15)
Interim dividend				5.1p	4.3p	19
Net debt				8,079	8,133	1

The commentary focuses on the results before specific items and leaver costs. This is consistent with the way that financial performance is measured by management and we believe allows a meaningful analysis to be made of the trading results of the group. Specific items are defined in note 4 on page 26.

The income statement, cash flow statement and balance sheet are provided on pages 16 to 22. A reconciliation of EBITDA before specific items to group operating profit is provided on page 31. A definition and reconciliation of free cash flow and net debt are provided on pages 28 to 30.

## **GROUP RESULTS**

Revenue was 4 per cent higher at £4,941 million in the quarter with continued strong growth in new wave revenue more than offsetting the decline in traditional revenue. EBITDA before specific items and leaver costs grew by 2.4 per cent. This is the third quarter of growth and builds on the 1.7 per cent growth reported last quarter. Earnings per share before specific items and leaver costs increased by 13 per cent to 6.0 pence, the eighteenth consecutive quarter of year on year growth.

The strong growth in new wave revenue continued and at £1,736 million was 21 per cent higher than last year. New wave revenue accounted for 35 per cent of the group's revenue compared to 30 per cent in the second quarter of last year. New wave revenue is mainly generated from networked IT services, broadband and mobility. Networked IT services revenue grew by 10 per cent to £1,001 million, broadband revenue increased by 39 per cent to £486 million and mobility revenue increased by 4 per cent to £72 million.

Networked IT services contract wins were £0.7 billion in the second quarter, with £4.0 billion achieved over the last twelve months.

BT had 9.3 million wholesale broadband connections at September 30, 2006, including 838,000 local loop unbundled lines, an increase of 2.8 million connections year on year and 626,000 connections in the quarter. Over 46 per cent of all UK homes now subscribe to broadband services, comprising both DSL and cable services (Source: Informa, Telecoms Market, September 2006).

### **Revenue**

Revenue from the group's traditional businesses declined by 4 per cent continuing recent trends. This reflects regulatory intervention, competition, price reductions and also technological changes that we are using to drive customers from traditional services to new wave services.

Major corporate (UK and international) revenue showed growth of 5 per cent, with 11 per cent growth in new wave revenue more than offsetting the decline in traditional services. Migration from traditional voice only services to networked IT services continued with new wave revenue representing 60 per cent of all major corporate revenue.

Revenue from smaller and medium sized (SME) UK businesses grew by 2 per cent year on year. New wave revenue grew by 23 per cent driven by continued growth in broadband and other new wave services. In the declining UK calls market, BT has gained market share in the SME sector through innovative pricing plans and a focus on propositions that bring together IT,

broadband and communications to allow business people to concentrate on running their business.

Consumer revenue in the second quarter was 6 per cent lower, primarily due to wholesale line rental (WLR) substitution. Growth in new wave revenue of 44 per cent continues to reduce our dependence on traditional revenue which has declined by 12 per cent with the strategic shift towards new wave products and services. New wave revenue now represents 17 per cent of the total consumer revenue.

The 12 month rolling average revenue per consumer household (net of mobile termination charges) of £254 increased by £1 compared to last quarter, the third successive quarter of growth. Improvements in the proportion of customers upgrading from the basic broadband package and more new customers subscribing for higher value packages has more than offset the lower call revenues. BT Total Broadband reflects our strategy to drive value into the broadband market and we reached 3 million BT Retail broadband connections in October. Contracted revenues increased by 1 percentage point to 69 per cent compared to last quarter, 3 percentage points higher than last year.

Wholesale (UK and Global Carrier) revenue increased by 14 per cent driven by WLR and LLU. UK Wholesale new wave revenue increased by 41 per cent to £339 million, mainly driven by broadband.

## **Operating results**

Group operating costs before specific items increased by 4 per cent year on year to £4,311 million. Staff costs before leaver costs increased by £64 million to £1,274 million due mainly to the additional staff needed to support networked IT services contracts, increased levels of activity in the network and 21CN activities (including capital work) as well as cost inflation. Leaver costs were £33 million in the quarter (£37 million last year). Payments to other telecommunication operators increased by £45 million to £1,034 million. Other operating costs before specific items of £1,442 million increased by £47 million mainly due to increased costs of sales from growth in networked IT and other new wave services which were partly offset by cost savings from our efficiency programmes. Depreciation and amortisation increased by 2 per cent year on year to £703 million.

Group operating profit before specific items and leaver costs increased by 3 per cent to £715 million. Operating profit margin before specific items remained flat year on year at 14 per cent.

## Earnings

Net finance costs were £55 million, an improvement of £45 million against last year. This includes net finance income associated with the group's defined benefit pension scheme which was £105 million in the second quarter, £41 million higher than last year. Repayment of maturing debt last year, fair value movements on derivatives that are economic hedges but are not fully effective hedges under the IAS 39 definitions and lower average net debt have also contributed to the reduction in net finance costs. This reduction was offset by a £31 million net gain last year on the early redemption of the US dollar 2008 LG Telecom convertible bond.

Profit before taxation, specific items and leaver costs of £665 million increased by 12 per cent.

The effective tax rate on the profit before specific items was 24.5 per cent (24.9 per cent last year) reflecting the continued focus on tax efficiency within the group.

Earnings per share before specific items and leaver costs increased by 13 per cent to 6.0 pence.

## Specific items

Specific items are defined in note 4 on page 26. There was a net charge before taxation of £3 million in the quarter (£70 million charge last year). Costs of £23 million relating to the further rationalisation of the group's office portfolio were incurred in the quarter (£nil last year). This was partly offset by a profit of £20 million arising from the group's disposal of 6 per cent of its equity interest in Tech Mahindra Limited, an associated undertaking, reducing the group's holding to 36 per cent. In the prior year, a provision of £70 million was recognised relating to the incremental and directly attributable costs in connection with creating the Openreach line of business.

Earnings per share after specific items were 5.7 pence in the quarter (4.4 pence last year).

## Cash flow and net debt

Net cash inflows from operating activities in the second quarter amounted to £1,191 million compared to £1,263 million last year, largely due to higher working capital outflows.

Free cash flow was a net inflow of £338 million in the second quarter compared to £503 million last year mainly reflecting the higher working capital outflows and increased capital expenditure. The year on year deterioration reflects the timing of receipts and payments and is expected to reverse in the second half of the year. The share buyback programme continued with

the repurchase of 48 million shares for £102 million during the quarter. Net debt was £8,079 million at September 30, 2006, £54 million below the level at September 30, 2005. Free cash flow and net debt are defined and reconciled in notes 8 and 9 on pages 28 to 30.

## **Pensions**

The IAS 19 net pension obligation at September 30, 2006 was a deficit of £2.0 billion, net of tax, being £0.6 billion lower than the level at September 30, 2005. The BT Pension Scheme had assets of £35.9 billion at September 30, 2006. The triennial funding valuation as at December 31, 2005 is currently being performed and we expect this exercise to conclude by December 31, 2006.

## **21<sup>st</sup> Century Network**

BT's 21st Century Network programme made significant progress during the quarter. The construction of 10 per cent of the UK's core communications infrastructure is in place and fully operational. Site planning and preparation has been completed in all core and metro nodes in South Wales, and at a further 100 sites across the country. Nine new fibre rings, totalling 2,100 kilometres, have been installed in South Wales and 1,500 man years of IT systems development work has been carried out. All of this preparatory work is required to support the migration of the first end user customers to 21CN. This is scheduled to take place near Cardiff at the end of November.

Readiness testing of the network, systems, services and customer premises equipment (CPE) is well advanced. A test facility in Swansea, where other communications providers can test their services, was opened on October 25, 2006. Live voice calls have already been carried over the new 21CN network, built using 21CN hardware and software, in South Wales.

BT and representatives from across industry have agreed a single end user communications programme to help consumers and single site small and medium enterprises understand better what next generation networks are and to provide a single source of detail and further information. The programme, which launched in October, operates under a single independent brand – “Switched-On”.

**Shareholder distributions**

An interim dividend of 5.1 pence per share, an increase of 19 per cent on last year, will be paid on February 12, 2007 to shareholders on the register on December 29, 2006. The ex dividend date is December 27, 2006. During the first half year 69 million shares were repurchased for £167 million under the group's share buyback programme.

**Prospects**

Our performance underpins our confidence that we will continue to grow revenue, EBITDA, earnings per share and dividends this financial year. Revenue growth will continue to be fuelled by new wave services; the EBITDA improvement will be driven by the continued growth in BT Retail's profitability and an acceleration through the year of the EBITDA growth in BT Global Services.

We are confident in our ability to improve shareholder returns and accelerate the strategic transformation of the business.

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The half year report, which contains the independent review report of the auditors, will be published in The Times on November 10, 2006.

The third quarter results are expected to be announced on February 8, 2007.



## LINE OF BUSINESS RESULTS

Openreach, a new line of business created in accordance with the regulatory framework agreed with Ofcom (the Undertakings), was launched on January 21, 2006. It is responsible for ensuring that all communications providers have transparent and equivalent access to the BT local network, and comprises a work force of approximately 30,000 people. Its primary products are wholesale line rental (WLR) and local loop unbundling (LLU).

In order to assist readers in understanding the year on year performance, we have restated the comparative line of business results. These restatements also reflect the impact of the new internal trading arrangements that have been implemented due to the creation of Openreach. There is no change to the overall group reported results.

### BT Global Services

	Second quarter ended September 30				Half year ended September 30	
	2006	2005*	Better (worse)		2006	2005*
	£m	£m	£m	%	£m	£m
Revenue	2,157	2,102	55	3	4,312	4,169
Gross profit	638	612	26	4	1,266	1,224
SG&A before leaver costs	<u>409</u>	<u>392</u>	(17)	(4)	<u>809</u>	<u>783</u>
EBITDA before leaver costs	229	220	9	4	457	441
Leaver costs	<u>5</u>	<u>22</u>	17	77	<u>22</u>	<u>24</u>
EBITDA	224	198	26	13	435	417
Depreciation and amortisation	<u>157</u>	<u>158</u>	1	1	<u>305</u>	<u>310</u>
Operating profit	<u>67</u>	<u>40</u>	27	68	<u>130</u>	<u>107</u>
Capital expenditure	<u>176</u>	<u>171</u>	(5)	(3)	<u>325</u>	<u>313</u>

\*Restated to reflect changes in intra-group trading arrangements.

BT Global Services revenue grew in the second quarter by 3 per cent to £2,157 million. New wave and non UK revenue was £1,661 million, an increase of 6 per cent year on year. UK traditional revenues decreased 8 per cent year on year, with continuing falls experienced in voice related and dial IP revenues. MPLS revenue rose by 33 per cent to £134 million, with the growth split evenly between the UK and overseas. Our IP network infrastructure currently extends to 128 countries.

Order intake remained firm with networked IT services contract orders of £0.7 billion, which included a 7 year agreement with PepsiCo to provide and manage an integrated portfolio of services for their international division. Total orders in the quarter amounted to £1.6 billion, £0.1 billion higher than last year, taking the value of total orders achieved over the last twelve

months to £8.1 billion. Over 40 per cent of the total order intake was generated outside the UK. During the quarter 223 new customers were signed, bringing the total for the year to 453.

EBITDA before leaver costs increased year on year by £9 million to £229 million, growth of 4 per cent year on year. Gross profit improved by £26 million to £638 million, an increase of 4 per cent, while gross profit margin improved by 0.5 percentage points to 30 per cent. SG&A costs rose 4 per cent reflecting pay inflation, increased IP networking costs and also transformation costs incurred in creating a single global services organisation. Depreciation charges fell by £1 million compared with the previous year to £157 million while leaver costs were £17 million lower at £5 million. Overall, this contributed to operating profit of £67 million, 68 per cent higher than last year.

BT continues to make good progress on its NHS National Programme for Information Technology contracts. For N3, the broadband network that underpins the programme, we have installed more than 15,500 connections and are on schedule to complete the 18,000 rollout by March 2007. BT now has more than 287,000 registered users on Spine, one of the world's largest transactional database and messaging services. In London, where we are the Local Service Provider, BT has delivered capability to 40 per cent of trusts.

## BT Retail

	Second quarter ended September 30				Half year ended September 30	
	2006	2005*	Better (worse)		2006	2005*
	£m	£m	£m	%	£m	£m
Revenue	<u>2,077</u>	<u>2,136</u>	(59)	(3)	<u>4,145</u>	<u>4,256</u>
Gross profit	592	555	37	7	1,152	1,091
SG&A before leaver costs	<u>357</u>	<u>364</u>	7	2	<u>735</u>	<u>742</u>
EBITDA before leaver costs	235	191	44	23	417	349
Leaver costs	<u>7</u>	<u>2</u>	(5)	n/m	<u>9</u>	<u>5</u>
EBITDA	228	189	39	21	408	344
Depreciation and amortisation	<u>39</u>	<u>39</u>	-	-	<u>79</u>	<u>73</u>
Operating profit	<u>189</u>	<u>150</u>	39	26	<u>329</u>	<u>271</u>
Capital expenditure	<u>40</u>	<u>33</u>	(7)	(21)	<u>80</u>	<u>68</u>

\*Restated to reflect changes in intra-group trading arrangements.

BT Retail's EBITDA before leaver costs was 23 per cent higher than last year, continuing our recent trend of growth. Gross profit increased by 7 percentage points reflecting the improved consumer broadband margins, the impact of cost efficiency programmes, lower input costs and an improved product mix. This more than compensated for the 3 per cent decline in revenues. SG&A costs before leaver costs fell by 2 per cent driven by the increased

effectiveness in serving our customers. Operating profit improved by 26 per cent to £189 million.

Traditional revenue declined by 9 per cent whilst new wave revenue grew by 34 per cent, driven primarily by broadband and other new wave services. New wave revenue was 21 per cent of total revenue in the quarter, up from 15 per cent last year.

During the quarter, following the relaxation of the regulatory environment, we introduced the biggest ever cuts to our inclusive call packages, maximising value to our customers. In the consumer market, BT Together Options 2 and 3 have reduced prices by almost one third and we have seen a significant increase in the proportion of customers moving up to higher value packages.

In the SME market, BT Business Plan is now available with mobile and BT Assurance Plus bringing SMEs a high level of care, attention and quick response and includes calls answered 24/7, access to a qualified team of experts and immediate diagnosis of faults at no extra cost. In line with our strategy to simplify the customer experience and eliminate the hassle for SMEs, in October we launched Business Manager and Business One Plan. With Business Manager, an SME can choose from a range of options to get the level of service that suits their business and Business One Plan combines landline, mobile and broadband services into one package, giving customers a wide range of benefits by delivering cost and time savings.

Broadband revenue grew by 28 per cent to £229 million with BT Retail connections at September 30, 2006 growing to 2,980,000 an increase of 5 per cent in the quarter, and in October we exceeded 3 million connections. BT Retail's share of broadband net additions (DSL and LLU) was 25 per cent in the quarter and BT Retail's share of the installed base was 32 per cent at September 30, 2006.

BT Total Broadband, launched towards the end of the first quarter, reflects our strategy to drive value into the Broadband market. The proportion of customers opting for higher value Options 2 and 3 packages increased by 29 per cent in the quarter and almost 60 per cent of orders are for these higher value packages. These customers benefit from increased security, wireless hubs and inclusive IP calls. The BT Home Hub brings together the BT Total Broadband experience and at September 30, 2006 over 250,000 Hubs had been installed, providing the platform for a range of new services.

Our strategy of adding value in the broadband arena continues with the announcement made in September of our partnership with US media entrepreneurs Podshow to launch BT Podshow. This enables UK internet users and independent media producers to create and share their content with an audience of millions in the UK and around the world.

In October we launched BT Digital Vault, an innovative new online storage service which enables BT Total Broadband customers to securely store online, back-up, share and remotely access their digital content such as photos, music and video via broadband.

Enjoying the broadband revolution is now easier than ever with the launch in August of the competitively priced BT Home IT Visit and BT Total Broadband installation services. Specially trained engineers can set up customers' broadband, a wireless home network or help resolve IT problems including PC viruses. This follows the pilot in March of BT Home IT Advisor, offering remote helpdesk support for a range of home IT issues, which was being purchased by one in ten new broadband customers, via our call centres, at the end of the quarter.

The advanced VoIP service with high-definition sound is reflected in the increased net additions and installed base. At the end of the quarter the installed base was about 400,000 customers reflecting strong growth of Broadband Talk customers.

BT Vision remains on track for launch this autumn. This service will offer a compelling line-up of entertainment programming as well as interactive services, all available on-demand and with no compulsory subscription. To date a wide range of content deals have been announced with partners including NBC Universal, Paramount, Dream Works, BBC Worldwide, MTV, History Channel, Nickelodeon, Sony BMG and many others.

**BT Wholesale**

	Second quarter ended September 30				Half year ended September 30	
	2006	2005*	Better (worse)		2006	2005*
	£m	£m	£m	%	£m	£m
External revenue	1,030	964	66	7	2,027	1,932
Internal revenue	855	849	6	1	1,705	1,695
Revenue	1,885	1,813	72	4	3,732	3,627
Variable cost of sales	963	901	(62)	(7)	1,883	1,832
Gross variable profit	922	912	10	1	1,849	1,795
Network and SG&A before leaver costs	438	442	4	1	887	857
EBITDA before leaver costs	484	470	14	3	962	938
Leaver costs	15	6	(9)	n/m	16	6
EBITDA	469	464	5	1	946	932
Depreciation and amortisation	291	274	(17)	(6)	576	545
Operating profit	178	190	(12)	(6)	370	387
Capital expenditure	266	198	(68)	(34)	466	428

\*Restated to reflect changes in intra-group trading arrangements.

BT Wholesale external revenue in the second quarter of £1,030 million increased by 7 per cent reflecting strong growth in broadband, transit and other traditional revenue. External revenue from new wave services increased to £268 million and now accounts for 26 per cent of external revenue.

Internal revenue increased marginally to £855 million due to strong growth in internal broadband revenue more than offsetting the impact of lower call volumes and lower regulatory prices being reflected in internal charges.

Gross variable profit increased £10 million although gross variable profit margin decreased by 1 percentage point to 49 per cent due to a changing sales mix. Despite greater 21CN expenditure, network and SG&A costs have decreased as a result of savings through network efficiencies. These efficiencies have yielded headcount reductions of over 1,100 employees since the prior year and these reductions are partly reflected in leaver costs of £15 million in the quarter.

Overall, EBITDA before leaver costs has increased 3 per cent to £484 million. Higher depreciation due to the shortening of the useful economic lives of legacy transmission assets to be replaced by 21CN and higher leaver costs has resulted in a 6 per cent decline in operating profit.

Capital expenditure in the quarter was 34 per cent higher than last year due to increased investment in 21CN whilst BT Wholesale has been successful in managing its legacy infrastructure on a lower level of capital investment.

In September, Vodafone UK announced it had signed Heads of Terms with BT Wholesale to provide its UK customers with Vodafone branded, consumer fixed-line broadband services. BT Wholesale and Vodafone UK have been making excellent progress and details of the service will be announced shortly.

In September, BT Wholesale also launched the UK's first broadcast mobile TV service, BT Movio, with Virgin Mobile as the initial customer. BT Movio's service line-up includes live versions of TV channels from the BBC, ITV and Channel 4, as well as all the UK's DAB Digital Radio stations, a 7 day programme guide and 'red button' interactivity. BT Movio also announced an agreement with ZTE, a leading global provider of telecommunications equipment and network solutions, to develop the world's first 3G mobile handset compatible with the BT Movio service. When available, the new handset will enable 3G operators to offer the Movio service.

## Openreach

	Second quarter ended September 30				Half year ended September 30	
	2006 £m	2005* £m	Better (worse) £m %		2006 £m	2005* £m
External revenue	162	60	102	170	292	113
Revenue from other BT lines of business	<u>1,117</u>	<u>1,211</u>	(94)	(8)	<u>2,246</u>	<u>2,452</u>
Revenue	1,279	1,271	8	1	2,538	2,565
Operating costs before leaver costs	<u>819</u>	<u>789</u>	(30)	(4)	<u>1,606</u>	<u>1,576</u>
EBITDA before leaver costs	460	482	(22)	(5)	932	989
Leaver costs	<u>-</u>	<u>-</u>	-	-	<u>2</u>	<u>-</u>
EBITDA	460	482	(22)	(5)	930	989
Depreciation and amortisation	<u>178</u>	<u>188</u>	10	5	<u>353</u>	<u>374</u>
Operating profit	<u>282</u>	<u>294</u>	(12)	(4)	<u>577</u>	<u>615</u>
Capital expenditure	<u>279</u>	<u>246</u>	(33)	(13)	<u>550</u>	<u>503</u>

\*Restated to reflect changes in intra-group trading arrangements.

Openreach's revenue in the second quarter was £1,279 million, a 1 per cent increase from the prior year driven by market volume growth. External revenue has increased by £102 million predominantly due to WLR and LLU volume growth which has more than offset the price reductions. Revenues from other BT lines of business decreased by 8 per cent to £1,117

million reflecting the volume shift to external revenues and also the regulatory LLU and WLR prices reductions in prior periods.

At September 30, 2006 Openreach had over 838,000 external LLU lines and 4.0 million external WLR lines. These have grown significantly from June 30, 2006 with net additions being 258,000 LLU connections and 446,000 WLR connections in the quarter.

During the quarter, Openreach launched a number of products to enhance the fully unbundled Metallic Path Facilities (MPF), the most significant being the Mass Migration product which enables Openreach to project manage multiple migrations of a Communications Provider's customer base on to MPF.

On September 30, 2006, a key milestone in the Undertakings was achieved as Openreach successfully started to provide Wholesale Extension Services (WES) and Backhaul Extension Services (BES) on an equivalent basis. At the same time, a number of new Ethernet products were launched. These include Wholesale End to End Ethernet Services (WEES) which are high speed, permanently connected, point-to-point data circuits that are available 24 hours a day, 365 days per year.

Operating costs increased by 4 per cent to £819 million due to increased volumes, inflationary pressures and focus on service levels. However these have been partially offset by cost savings from efficiency programmes across the business.

Overall this has resulted in a £22 million decrease in EBITDA before leaver costs. The decrease in depreciation and amortisation costs of £10 million is due to the lengthening of the useful economic life of copper, consistent with Ofcom's review, which is partially offset by higher systems depreciation.

Capital expenditure in the quarter was 13 per cent higher than last year reflecting increased investment in new systems to ensure compliance with the Undertakings and increased network infrastructure spend to meet LLU demand.

**GROUP INCOME STATEMENT**  
**for the three months ended September 30, 2006**

(unaudited)	Notes	Before specific items £m	Specific items (note 4) £m	Total £m
<b>Revenue</b>	2	4,941	-	4,941
Other operating income		52	-	52
Operating costs	3	<u>(4,311)</u>	<u>(23)</u>	<u>(4,334)</u>
<b>Operating profit</b>	2	682	(23)	659
Finance costs		(651)	-	(651)
Finance income		<u>596</u>	-	<u>596</u>
Net finance costs	5	(55)	-	(55)
Share of post tax profits of associates and joint ventures		5	-	5
Profit on disposal of associate		-	<u>20</u>	<u>20</u>
<b>Profit before taxation</b>		632	(3)	629
<b>Taxation</b>		<u>(155)</u>	<u>1</u>	<u>(154)</u>
<b>Profit for the period attributable to equity shareholders</b>		<u>477</u>	<u>(2)</u>	<u>475</u>
<b>Earnings per share</b>	7			
- basic		<u>5.7p</u>		<u>5.7p</u>
- diluted		<u>5.6p</u>		<u>5.6p</u>



**GROUP INCOME STATEMENT**  
**for the three months ended September 30, 2005**

(unaudited)	Notes	Before specific items £m	Specific items (note 4) £m	Total £m
<b>Revenue</b>	2	4,767	-	4,767
Other operating income		53	-	53
Operating costs	3	<u>(4,164)</u>	<u>(70)</u>	<u>(4,234)</u>
<b>Operating profit</b>	2	656	(70)	586
Finance costs		(676)	-	(676)
Finance income		<u>576</u>	<u>-</u>	<u>576</u>
Net finance costs	5	(100)	-	(100)
Share of post tax profits of associates and joint ventures		<u>3</u>	<u>-</u>	<u>3</u>
<b>Profit before taxation</b>		559	(70)	489
<b>Taxation</b>		<u>(139)</u>	<u>21</u>	<u>(118)</u>
<b>Profit for the period attributable to equity shareholders</b>		<u>420</u>	<u>(49)</u>	<u>371</u>
<b>Earnings per share</b>	7			
- basic		<u>5.0p</u>		<u>4.4p</u>
- diluted		<u>4.9p</u>		<u>4.3p</u>

**GROUP INCOME STATEMENT**  
**for the six months ended September 30, 2006**

(unaudited)	Notes	Before specific items £m	Specific items (note 4) £m	Total £m
<b>Revenue</b>	2	9,805	-	9,805
Other operating income		102	-	102
Operating costs	3	<u>(8,566)</u>	<u>(23)</u>	<u>(8,589)</u>
<b>Operating profit</b>	2	1,341	(23)	1,318
Finance costs		(1,293)	-	(1,293)
Finance income		<u>1,192</u>	<u>-</u>	<u>1,192</u>
Net finance costs	5	(101)	-	(101)
Share of post tax profits of associates and joint ventures		7	-	7
Profit on disposal of associate		<u>-</u>	<u>20</u>	<u>20</u>
<b>Profit before taxation</b>		1,247	(3)	1,244
<b>Taxation</b>		<u>(306)</u>	<u>1</u>	<u>(305)</u>
<b>Profit for the period attributable to equity shareholders</b>		<u>941</u>	<u>(2)</u>	<u>939</u>
<b>Earnings per share</b>	7			
- basic		<u>11.3p</u>		<u>11.3p</u>
- diluted		<u>11.1p</u>		<u>11.1p</u>

**GROUP INCOME STATEMENT**  
**for the six months ended September 30, 2005**

(unaudited)	Notes	Before specific items £m	Specific items (note 4) £m	Total £m
<b>Revenue</b>	2	9,498	-	9,498
Other operating income		95	-	95
Operating costs	3	<u>(8,289)</u>	<u>(82)</u>	<u>(8,371)</u>
<b>Operating profit</b>	2	1,304	(82)	1,222
Finance costs		(1,392)	-	(1,392)
Finance income		<u>1,150</u>	<u>-</u>	<u>1,150</u>
Net finance costs	5	(242)	-	(242)
Share of post tax profits of associates and joint ventures		<u>8</u>	<u>-</u>	<u>8</u>
<b>Profit before taxation</b>		1,070	(82)	988
<b>Taxation</b>		<u>(268)</u>	<u>25</u>	<u>(243)</u>
<b>Profit for the period attributable to equity shareholders</b>		<u>802</u>	<u>(57)</u>	<u>745</u>
<b>Earnings per share</b>	7			
- basic		<u>9.5p</u>		<u>8.8p</u>
- diluted		<u>9.3p</u>		<u>8.7p</u>

**GROUP STATEMENT OF RECOGNISED INCOME AND EXPENSE**  
**for the six months ended September 30, 2006**

(unaudited)	Half year ended September 30	
	2006 £m	2005 £m
<b>Profit for the period</b>	<u>939</u>	<u>745</u>
Actuarial (losses) gains on defined benefit pension schemes	(369)	1,090
Net gains on revaluation of available-for-sale investments	-	1
Net gains (losses) on cash flow hedges	61	(5)
Exchange differences on translation of foreign operations	(72)	(4)
Tax on items taken directly to equity	<u>82</u>	<u>(327)</u>
<b>Net (losses) gains recognised directly in equity</b>	<u>(298)</u>	<u>755</u>
<b>Total recognised income for the period attributable to equity shareholders</b>	<u>641</u>	<u>1,500</u>

**GROUP CASH FLOW STATEMENT**  
**for the three months and six months ended September 30, 2006**

(unaudited)	Second quarter ended September 30		Half year ended September 30	
	2006 £m	2005 £m	2006 £m	2005 £m
<b>Cash flow from operating activities</b>				
Cash generated from operations (note 8 (a))	1,281	1,374	2,373	2,346
Income taxes paid	<u>(90)</u>	<u>(111)</u>	<u>(180)</u>	<u>(242)</u>
<b>Net cash inflow from operating activities</b>	1,191	1,263	2,193	2,104
<b>Cash flow from investing activities</b>				
Net sale (acquisition) of subsidiaries, associates and joint ventures	13	-	(25)	(88)
Net purchase of property, plant, equipment and software	(794)	(671)	(1,596)	(1,357)
Interest received	22	59	37	96
Dividends received from associates and joint ventures	2	-	5	-
Net sale (purchase) of short term investments and non current asset investments	<u>249</u>	<u>732</u>	<u>(480)</u>	<u>582</u>
<b>Net cash (used) received in investing activities</b>	(508)	120	(2,059)	(767)
<b>Cash flows from financing activities</b>				
Repurchase of ordinary share capital	(52)	(88)	(114)	(109)
Net repayments of borrowings	(140)	(10)	(162)	(24)
Net movement on commercial paper	(77)	-	227	-
Interest paid	(83)	(147)	(318)	(465)
Equity dividends paid	<u>(625)</u>	<u>(540)</u>	<u>(630)</u>	<u>(540)</u>
<b>Net cash used in financing activities</b>	(977)	(785)	(997)	(1,138)
Effects of exchange rate changes	-	(6)	-	23
<b>Net (decrease) increase in cash and cash equivalents</b>	<u>(294)</u>	<u>592</u>	<u>(863)</u>	<u>222</u>
<b>Cash and cash equivalents at beginning of period</b>	1,215	940	1,784	1,310
<b>Cash and cash equivalents, net of bank overdrafts, at end of period (note 8 (c))</b>	<u>921</u>	<u>1,532</u>	<u>921</u>	<u>1,532</u>
Free cash flow (note 8 (b))	<u>338</u>	<u>503</u>	<u>321</u>	<u>377</u>
Increase in net debt from cash flows (note 9 (b))	<u>326</u>	<u>125</u>	<u>448</u>	<u>360</u>

**GROUP BALANCE SHEET**  
**at September 30, 2006**

(unaudited)	September 30 2006 £m	<i>September 30</i> 2005 £m	<i>March 31</i> 2006 £m
<b>Non current assets</b>			
Goodwill and other intangible assets	1,861	1,385	1,641
Property, plant and equipment	15,350	15,386	15,489
Other non current assets	100	101	84
Deferred tax assets	<u>853</u>	<u>1,105</u>	<u>764</u>
	<u>18,164</u>	<u>17,977</u>	<u>17,978</u>
<b>Current assets</b>			
Inventories	131	126	124
Trade and other receivables	4,684	4,060	4,199
Other financial assets	778	3,217	434
Cash and cash equivalents	<u>993</u>	<u>1,727</u>	<u>1,965</u>
	<u>6,586</u>	<u>9,130</u>	<u>6,722</u>
<b>Total assets</b>	24,750	27,107	24,700
<b>Current liabilities</b>			
Loans and other borrowings	2,729	4,667	1,940
Trade and other payables	6,343	5,552	6,540
Other current liabilities	<u>981</u>	<u>1,377</u>	<u>1,000</u>
	<u>10,053</u>	<u>11,596</u>	<u>9,480</u>
<b>Total assets less current liabilities</b>	<u>14,697</u>	<u>15,511</u>	<u>15,220</u>
<b>Non current liabilities</b>			
Loans and other borrowings	6,948	8,171	7,995
Deferred tax liabilities	1,547	1,453	1,505
Retirement benefit obligations	2,842	3,682	2,547
Other non current liabilities	<u>1,819</u>	<u>1,449</u>	<u>1,566</u>
	<u>13,156</u>	<u>14,755</u>	<u>13,613</u>
<b>Capital and reserves</b>			
Called up share capital	432	432	432
Reserves	<u>1,062</u>	<u>275</u>	<u>1,123</u>
<b>Total equity shareholders' funds</b>	1,494	707	1,555
Minority interest	<u>47</u>	<u>49</u>	<u>52</u>
<b>Total equity</b>	<u>1,541</u>	<u>756</u>	<u>1,607</u>
	<u>14,697</u>	<u>15,511</u>	<u>15,220</u>

**NOTES (unaudited)**

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**1 Basis of preparation and accounting policies**

These primary statements and selected notes comprise the unaudited interim consolidated financial results of BT Group plc for the quarters and half years ended September 30, 2006 and 2005, together with the audited results for the year ended March 31, 2006. These interim financial results do not comprise statutory accounts within the meaning of Section 240 of the Companies Act 1985. Statutory accounts for the year ended March 31, 2006 were approved by the Board of Directors on May 17, 2006, published on May 31, 2006 and delivered to the Registrar of Companies. The report of the auditors on those accounts was unqualified and did not contain any statement under Section 237 of the Companies Act 1985.

The financial information set out in these interim financial results has been prepared in accordance with the Listing Rules of the Financial Services Authority. The accounting policies which have been applied to prepare the interim financial results are the same as those used for the preparation of the consolidated financial statements for the year ended March 31, 2006.

In order to assist readers in understanding the year on year performance, we have restated the comparative line of business results to reflect the creation of Openreach which is now reported as a separate line of business. These restatements also reflect the impact of the new internal trading arrangements that have been implemented. There is no change to the overall group reported results.

## 2 Results of businesses

### (a) Operating results

	External revenue £m	Internal revenue £m	Group revenue £m	EBITDA (ii) £m	Group operating profit (loss) (ii) £m
<i>Second quarter ended</i>					
<i>September 30, 2006</i>					
BT Global Services	1,763	394	2,157	224	67
BT Retail	1,982	95	2,077	228	189
BT Wholesale	1,030	855	1,885	469	178
Openreach	162	1,117	1,279	460	282
Other	4	-	4	4	(34)
Intra-group items (i)	-	(2,461)	(2,461)	-	-
<b>Total</b>	<u>4,941</u>	<u>-</u>	<u>4,941</u>	<u>1,385</u>	<u>682</u>
<i>Second quarter ended</i>					
<i>September 30, 2005</i>					
<i>(restated – note 1)</i>					
BT Global Services	1,703	399	2,102	198	40
BT Retail	2,036	100	2,136	189	150
BT Wholesale	964	849	1,813	464	190
Openreach	60	1,211	1,271	482	294
Other	4	-	4	15	(18)
Intra-group items (i)	-	(2,559)	(2,559)	-	-
<b>Total</b>	<u>4,767</u>	<u>-</u>	<u>4,767</u>	<u>1,348</u>	<u>656</u>
<i>Half year ended</i>					
<i>September 30, 2006</i>					
BT Global Services	3,517	795	4,312	435	130
BT Retail	3,959	186	4,145	408	329
BT Wholesale	2,027	1,705	3,732	946	370
Openreach	292	2,246	2,538	930	577
Other	10	-	10	28	(65)
Intra-group items (i)	-	(4,932)	(4,932)	-	-
<b>Total</b>	<u>9,805</u>	<u>-</u>	<u>9,805</u>	<u>2,747</u>	<u>1,341</u>
<i>Half year ended</i>					
<i>September 30, 2005</i>					
<i>(restated – see note 1)</i>					
BT Global Services	3,384	785	4,169	417	107
BT Retail	4,059	197	4,256	344	271
BT Wholesale	1,932	1,695	3,627	932	387
Openreach	113	2,452	2,565	989	615
Other	10	-	10	23	(76)
Intra-group items (i)	-	(5,129)	(5,129)	-	-
<b>Total</b>	<u>9,498</u>	<u>-</u>	<u>9,498</u>	<u>2,705</u>	<u>1,304</u>

- (i) Elimination of intra-group revenue between businesses, which is included in the total revenue of the originating business.  
(ii) Before specific items.

There is extensive trading between BT's lines of business and the line of business profitability is dependent on the transfer price levels. For regulated products and services those transfer prices are market based whilst for other products and services the transfer prices are agreed between the relevant lines of business. These intra-group trading arrangements are subject to periodic review.



## 2 Results of businesses *continued*

### (b) Revenue analysis

	Second quarter ended September 30				Half year ended September 30	
	2006 £m	2005 £m	Better (worse) £m %		2006 £m	2005 £m
Traditional	3,205	3,328	(123)	(4)	6,428	6,674
New wave	<u>1,736</u>	<u>1,439</u>	297	21	<u>3,377</u>	<u>2,824</u>
	<u>4,941</u>	<u>4,767</u>	174	4	<u>9,805</u>	<u>9,498</u>
Major corporate	1,703	1,629	74	5	3,402	3,226
Business	593	583	10	2	1,181	1,169
Consumer	1,257	1,336	(79)	(6)	2,509	2,660
Wholesale/Carrier	1,384	1,215	169	14	2,703	2,433
Other	<u>4</u>	<u>4</u>	-	-	<u>10</u>	<u>10</u>
	<u>4,941</u>	<u>4,767</u>	174	4	<u>9,805</u>	<u>9,498</u>

### (c) New wave revenue analysis

	Second quarter ended September 30				Half year ended September 30	
	2006 £m	2005 £m	Better (worse) £m %		2006 £m	2005 £m
Networked IT services	1,001	914	87	10	1,982	1,813
Broadband	486	350	136	39	940	664
Mobility	72	69	3	4	143	135
Other	<u>177</u>	<u>106</u>	71	67	<u>312</u>	<u>212</u>
	<u>1,736</u>	<u>1,439</u>	297	21	<u>3,377</u>	<u>2,824</u>

### (d) Capital expenditure on property, plant, equipment, software and motor vehicles

	Second quarter ended September 30				Half year ended September 30	
	2006 £m	2005 £m	Better (worse) £m %		2006 £m	2005 £m
BT Global Services	176	171	(5)	(3)	325	313
BT Retail	40	33	(7)	(21)	80	68
BT Wholesale	266	198	(68)	(34)	466	428
Openreach	279	246	(33)	(13)	550	503
Other (including fleet vehicles and property)	<u>51</u>	<u>46</u>	(5)	(11)	<u>106</u>	<u>98</u>
	<u>812</u>	<u>694</u>	(118)	(17)	<u>1,527</u>	<u>1,410</u>
Transmission equipment	297	347	50	14	594	720
Exchange equipment	39	18	(21)	n/m	53	36
Other network equipment	229	148	(81)	(55)	389	310
Computers and office equipment	60	54	(6)	(11)	134	110
Software	164	101	(63)	(62)	298	166
Motor vehicles and other	13	14	1	7	27	45
Land and buildings	<u>10</u>	<u>12</u>	2	17	<u>32</u>	<u>23</u>
	<u>812</u>	<u>694</u>	(118)	(17)	<u>1,527</u>	<u>1,410</u>

### 3 (a) Operating costs

	Second quarter ended		Half year ended	
	September 30		September 30	
	2006	2005	2006	2005
	£m	£m	£m	£m
Staff costs before leaver costs	1,274	1,210	2,530	2,366
Leaver costs	<u>33</u>	<u>37</u>	<u>57</u>	<u>43</u>
Staff costs	1,307	1,247	2,587	2,409
Own work capitalised <sup>1</sup>	<u>(175)</u>	<u>(159)</u>	<u>(346)</u>	<u>(320)</u>
Net staff costs	1,132	1,088	2,241	2,089
Depreciation and amortisation	703	692	1,406	1,401
Payments to telecommunication operators	1,034	989	2,040	1,998
Other operating costs	<u>1,442</u>	<u>1,395</u>	<u>2,879</u>	<u>2,801</u>
<b>Total before specific items</b>	<b>4,311</b>	<b>4,164</b>	<b>8,566</b>	<b>8,289</b>
Specific items (note 4)	<u>23</u>	<u>70</u>	<u>23</u>	<u>82</u>
<b>Total</b>	<b><u>4,334</u></b>	<b><u>4,234</u></b>	<b><u>8,589</u></b>	<b><u>8,371</u></b>

<sup>1</sup>Own work capitalised has been restated to exclude third party costs. This has no effect on the total costs.

### (b) Leaver costs

	Second quarter ended		Half year ended	
	September 30		September 30	
	2006	2005	2006	2005
	£m	£m	£m	£m
BT Global Services	5	22	22	24
BT Retail	7	2	9	5
BT Wholesale	15	6	16	6
Openreach	-	-	2	-
Other	<u>6</u>	<u>7</u>	<u>8</u>	<u>8</u>
Total	<u>33</u>	<u>37</u>	<u>57</u>	<u>43</u>

### 4 Specific items

BT separately identifies and discloses any significant one off or unusual items (termed “specific items”). This is consistent with the way that financial performance is measured by management and we believe assists in providing a meaningful analysis of the trading results of the group. Specific items may not be comparable to similarly titled measures used by other companies. Specific items were previously referred to as exceptional items under UK GAAP.

	Second quarter ended		Half year ended	
	September 30		September 30	
	2006	2005	2006	2005
	£m	£m	£m	£m
<b>Operating costs</b>				
Creation of Openreach	-	70	-	70
Property rationalisation costs	<u>23</u>	<u>-</u>	<u>23</u>	<u>12</u>
<b>Specific operating costs</b>	<b>23</b>	<b>70</b>	<b>23</b>	<b>82</b>
Profit on partial disposal of associate	<u>(20)</u>	<u>-</u>	<u>(20)</u>	<u>-</u>
<b>Total specific items</b>	<b><u>3</u></b>	<b><u>70</u></b>	<b><u>3</u></b>	<b><u>82</u></b>

## 5 Net finance costs

	Second quarter ended September 30		Half year ended September 30	
	2006	2005	2006	2005
	£m	£m	£m	£m
Finance costs <sup>1</sup> before pension interest	182	222	357	484
Interest on pension scheme liabilities	<u>469</u>	<u>454</u>	<u>936</u>	<u>908</u>
Finance costs	<u>651</u>	<u>676</u>	<u>1,293</u>	<u>1,392</u>
Finance income before pension income	(22)	(58)	(46)	(115)
Expected return on pension scheme assets	<u>(574)</u>	<u>(518)</u>	<u>(1,146)</u>	<u>(1,035)</u>
Finance income	<u>(596)</u>	<u>(576)</u>	<u>(1,192)</u>	<u>(1,150)</u>
Net finance costs	<u>55</u>	<u>100</u>	<u>101</u>	<u>242</u>
Net finance costs before pensions	160	164	311	369
Interest associated with pensions	<u>(105)</u>	<u>(64)</u>	<u>(210)</u>	<u>(127)</u>
Net finance costs	<u>55</u>	<u>100</u>	<u>101</u>	<u>242</u>

<sup>1</sup>Finance costs in the second quarter and half year ended September 30, 2006 include a £4 million and £1 million net charge, respectively, arising from the re-measurement of financial instruments which under IAS 39 are not in hedging relationships on a fair value basis. Finance costs in the second quarter and half year ended September 30, 2005 included a £19 million and £7 million net credit respectively, arising from the re-measurement of financial instruments which were not in hedging relationships on a fair value basis. A component of these net credits was the fair value movement in, and realised gain arising from, the early redemption of the US dollar 2008 LG Telecom convertible bond amounting to £31 million for the second quarter and £27 million for the half year.

## 6 Dividends

	Half year ended September 30		Half year ended September 30	
	2006	2005	2006	2005
	Pence per share		£m	£m
Amounts recognised as distributions to equity holders in the period	<u>7.6</u>	<u>6.5</u>	<u>633</u>	<u>551</u>

The directors have declared an interim dividend of 5.1 pence per share (4.3 pence last year), payable on February 12, 2007 to the shareholders on the register at the close of business on December 29, 2006. This interim dividend, amounting to £423 million, has not been included as a liability as at September 30, 2006 (£361 million as at September 30, 2005). The final dividend for the year ended March 31, 2006 of 7.6 pence per share was approved at the Annual General Meeting on July 12, 2006.

## 7 Earnings per share

The basic earnings per share are calculated by dividing the profit attributable to shareholders by the average number of shares in issue after deducting the company's shares held by employee share ownership trusts and treasury shares. In calculating the diluted earnings per share, share options outstanding and other potential ordinary shares have been taken into account.

The average number of shares in the periods were:

	Second quarter ended September 30		Half year ended September 30	
	2006	2005	2006	2005
	millions of shares		millions of shares	
Basic	8,308	8,456	8,311	8,463
Diluted	8,483	8,589	8,466	8,579

## 8 (a) Reconciliation of profit before tax to cash generated from operations

	Second quarter ended September 30		Half year ended September 30	
	2006	2005	2006	2005
	£m	£m	£m	£m
Profit before tax	629	489	1,244	988
Depreciation and amortisation	703	692	1,406	1,401
Associates and joint ventures	(5)	(3)	(7)	(8)
Employee share scheme costs	27	25	47	37
Net finance costs	55	100	101	242
Profit on disposal of property assets and non current asset investments	(20)	-	(20)	-
Changes in working capital	(196)	(8)	(553)	(461)
Provisions movements, pensions and other	88	79	155	147
<b>Cash generated from operations</b>	<u>1,281</u>	<u>1,374</u>	<u>2,373</u>	<u>2,346</u>

## (b) Free cash flow

	Second quarter ended September 30		Half year ended September 30	
	2006	2005	2006	2005
	£m	£m	£m	£m
<b>Cash generated from operations</b>	1,281	1,374	2,373	2,346
Income taxes paid	(90)	(111)	(180)	(242)
<b>Net cash inflow from operating activities</b>	1,191	1,263	2,193	2,104
<b>Included in cash flows from investing activities</b>				
Net purchase of property, plant, equipment and software	(794)	(671)	(1,596)	(1,357)
Net sale of non current asset investments	-	(1)	-	(1)
Dividends received from associates	2	-	5	-
Interest received	22	59	37	96
<b>Included in cash flows from financing activities</b>				
Interest paid	(83)	(147)	(318)	(465)
<b>Free cash flow</b>	<u>338</u>	<u>503</u>	<u>321</u>	<u>377</u>

## 8 (b) Free cash flow *continued*

Free cash flow is defined as the net increase in cash and cash equivalents less cash flows from financing activities (except interest paid), less the acquisition or disposal of group undertakings and less the net sale of short term investments. It is not a measure recognised under IFRS but is a key indicator used by management in order to assess operational performance.

## (c) Cash and cash equivalents

	At September 30		At March 31
	2006	2005	2006
	£m	£m	£m
Cash at bank and in hand	397	475	511
Short term deposits	<u>596</u>	<u>1,252</u>	<u>1,454</u>
Cash and cash equivalents	993	1,727	1,965
Bank overdrafts	<u>(72)</u>	<u>(195)</u>	<u>(181)</u>
	<u>921</u>	<u>1,532</u>	<u>1,784</u>

## 9 Net debt

Net debt at September 30, 2006 was £8,079 million (September 30, 2005 - £8,133 million, March 31, 2006 - £7,534 million).

Net debt consists of loans and other borrowings less current asset investments and cash and cash equivalents. Loans and other borrowings are measured at the net proceeds raised, adjusted to amortise any discount over the term of the debt. For the purpose of this analysis current asset investments, cash and cash equivalents are measured at the lower of cost and net realisable value. Currency denominated balances within net debt are translated to sterling at swapped rates where hedged.

This definition of net debt measures balances at the future cash flows due to arise on maturity of financial instruments and removes the balance sheet adjustments made for the re-measurement of hedged risks under fair value hedges and the use of the amortised cost method as required by IAS 39. In addition, the gross balances are adjusted to take account of netting arrangements amounting to £67 million. Net debt is a non GAAP measure since it is not defined in IFRS but it is a key indicator used by management in order to assess operational performance.

## 9 (a) Analysis

	At September 30		At March 31
	2006	2005	2006
	£m	£m	£m
Loans and other borrowings	9,677	12,838	9,935
Cash and cash equivalents	(993)	(1,727)	(1,965)
Other current financial assets <sup>1</sup>	<u>(768)</u>	<u>(2,996)</u>	<u>(365)</u>
	7,916	8,115	7,605
Adjustments:			
To retranslate currency denominated balances at swapped rates where hedged	437	399	121
To recognise borrowings at net proceeds and unamortised discount	(274)	(383)	(192)
Other	<u>-</u>	<u>2</u>	<u>-</u>
<b>Net debt</b>	<u><b>8,079</b></u>	<u><b>8,133</b></u>	<u><b>7,534</b></u>

After allocating the element of the adjustments which impact loans and other borrowings, gross debt at September 30, 2006 was £9,760 million (September 30, 2005 - £12,586 million, March 31, 2006 - £9,686 million).

<sup>1</sup>Excluding derivative financial instruments of £10 million, £221 million and £69 million at September 30, 2006 and 2005 and March 31, 2006, respectively.

## (b) Reconciliation of net cash flow to movement in net debt

	Second quarter ended		Half year	
	September 30		ended September 30	
	2006	2005	2006	2005
	£m	£m	£m	£m
Net debt at beginning of period	7,727	8,121	7,534	7,893
Increase in net debt resulting from cash flows	326	125	448	360
Net debt assumed or issued on acquisitions	-	-	9	1
Currency movements	36	(10)	99	(24)
Other non-cash movements	<u>(10)</u>	<u>(103)</u>	<u>(11)</u>	<u>(97)</u>
Net debt at end of period	<u><b>8,079</b></u>	<u><b>8,133</b></u>	<u><b>8,079</b></u>	<u><b>8,133</b></u>

## 10 Statement of changes in equity

	Half year ended September 30		Year ended
	2006	2005	March 31
	£m	£m	£m
Shareholders' funds	1,555	45	45
Minority interest	<u>52</u>	<u>50</u>	<u>50</u>
	1,607	95	95
Effect of adoption of IAS 32 and IAS 39	<u>-</u>	<u>(209)</u>	<u>(209)</u>
<b>Fund (deficit) at beginning of period</b>	1,607	(114)	(114)
Total recognised income for the period	641	1,500	2,906
Share based payment	27	26	65
Issues of shares	12	4	4
Net purchase of treasury shares	(108)	(108)	(344)
Dividends on ordinary shares	(633)	(551)	(912)
Minority interest	<u>(5)</u>	<u>(1)</u>	<u>2</u>
Net changes in equity for the financial period	(66)	870	1,721
<b>Equity at end of period</b>			
Shareholders' funds	1,494	707	1,555
Minority interest	<u>47</u>	<u>49</u>	<u>52</u>
	<u>1,541</u>	<u>756</u>	<u>1,607</u>

## 11 Earnings before interest, taxation, depreciation and amortisation (EBITDA)

	Second quarter ended		Half year	
	September 30		ended September 30	
	2006	2005	2006	2005
	£m	£m	£m	£m
Operating profit	659	586	1,318	1,222
Specific items (note 4)	23	70	23	82
Depreciation and amortisation (note 3)	<u>703</u>	<u>692</u>	<u>1,406</u>	<u>1,401</u>
EBITDA before specific items	<u>1,385</u>	<u>1,348</u>	<u>2,747</u>	<u>2,705</u>

Earnings before interest, taxation, depreciation and amortisation (EBITDA) before specific items is not a measure recognised under IFRS, but it is a key indicator used by management in order to assess operational performance.

## 12 United States Generally Accepted Accounting Principles (US GAAP)

The results set out above have been prepared in accordance with the basis of preparation as set out in note 1. The table below sets out the results calculated in accordance with US GAAP.

	Second quarter ended September 30		Half year ended September 30	
	2006	2005	2006	2005
Net income attributable to shareholders (£m)	509	191	923	583
Earnings per ADS (£)				
- basic	0.61	0.23	1.11	0.69
- diluted	0.60	0.22	1.09	0.68

Each American Depositary Share (ADS) represents 10 ordinary shares of BT Group plc.

Shareholders' equity, calculated in accordance with US GAAP, is a £52 million deficit at September 30, 2006 (September 30, 2005 - £615 million deficit, March 31, 2006 - £158 million deficit).

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### **Forward-looking statements – caution advised**

Certain statements in this results release are forward-looking and are made in reliance on the safe harbour provisions of the US Private Securities Litigation Reform Act of 1995. These statements include, without limitation, those concerning: continued growth in revenue, EBITDA, earnings per share and dividends; growth in new wave revenue, mainly from networked IT services, broadband and mobility growth; implementation of BT's 21<sup>st</sup> Century Network; the introduction of next generation services: and improving shareholder returns.

Although BT believes that the expectations reflected in these forward-looking statements are reasonable, it can give no assurance that these expectations will prove to have been correct. Because these statements involve risks and uncertainties, actual results may differ materially from those expressed or implied by these forward-looking statements.

Factors that could cause differences between actual results and those implied by the forward-looking statements include, but are not limited to: material adverse changes in economic conditions in the markets served by BT; future regulatory actions and conditions in BT's operating areas, including competition from others; selection by BT and its lines of business of the appropriate trading and marketing models for its products and services; fluctuations in foreign currency exchange rates and interest rates; technological innovations, including the cost of developing new products, networks and solutions and the need to increase expenditures for improving the quality of service; prolonged adverse weather conditions resulting in a material increase in overtime, staff or other costs; developments in the convergence of technologies; the anticipated benefits and advantages of new technologies, products and services, including broadband and other new wave initiatives, not being realised; and general financial market conditions affecting BT's performance. BT undertakes no obligation to update any forward-looking statements whether as a result of new information, future events or otherwise.