

## Additional information

### Alternative performance measures

#### Introduction

We assess the performance of the group using a variety of alternative performance measures that are not defined under IFRS and are therefore termed non-GAAP measures. The non-GAAP measures we use are: adjusted revenue, adjusted operating costs, adjusted finance expense, adjusted EBITDA, adjusted operating profit, adjusted profit before tax, adjusted earnings per share, return on capital employed, normalised free cash flow and net debt. The rationale for using these measures, along with a reconciliation from the nearest measures prepared in accordance with IFRS, are presented below.

The alternative performance measures we use may not be directly comparable with similarly titled measures used by other companies.

#### Specific items

Our income statement and segmental analysis separately identify trading results on an adjusted basis, being before specific items. The directors believe that presentation of the group's results in this way is relevant to an understanding of the group's financial performance as specific items are those that in management's judgement need to be disclosed by virtue of their size, nature or incidence.

This presentation is consistent with the way that financial performance is measured by management and reported to the Board and the *Executive Committee* and assists in providing an additional analysis of our reporting trading results.

In determining whether an event or transaction is specific, management considers quantitative as well as qualitative factors, such as the frequency or predictability of occurrence.

Examples of charges or credits meeting the above definition and which have been presented as specific items in the current and/or prior years include acquisitions/disposals of businesses and investments, regulatory, historical insurance or litigation claims, business restructuring programmes, asset impairment charges, property rationalisation programmes, net interest on pensions and the settlement of multiple tax years. In the event that items meet the criteria, which are applied consistently from year to year, they are treated as specific items.

Details of items meeting the definition of specific items in the current and prior year are set out in note 9.

Reported revenue, reported operating costs, reported operating profit, reported net finance expense, reported profit before tax and reported earnings per share are the equivalent IFRS measures. A reconciliation from these can be seen in the group income statement on page 118.

### Net debt and net financial debt

Net debt consists of loans and other borrowings, lease liabilities (both current and non-current) less current asset investments and cash and cash equivalents, including items which have been classified as held for sale on balance sheet.

Our net debt calculation starts from the expected future undiscounted cash flows that should arise when our financial instruments mature. Currency-denominated balances within net debt are translated to sterling at swap rates where hedged. Fair value adjustments and accrued interest applied to loans and borrowings, current asset investments and cash equivalents to reflect the effective interest method are removed.

Net debt is a measure of the group's net indebtedness that provides an indicator of overall balance sheet strength. It is a key indicator used by management to assess both the group's cash position and its indebtedness. The use of the term 'net debt' does not necessarily mean that the cash included in the net debt calculation is available to settle the liabilities included in this measure.

Net financial debt is net debt excluding lease liabilities. It allows for the comparison to net debt measures reported before the introduction of IFRS 16 on 1 April 2019, and reflects a view that lease liabilities are operational debt in substance, rather than financing transactions.

Net debt and net financial debt are considered to be alternative performance measures as they are not defined in IFRS. A reconciliation from loans and other borrowings, lease liabilities, cash and cash equivalents, and current asset investments, the most directly comparable IFRS measures to net debt and net financial debt, is set out in note 26.

## Additional information continued

### Return on Capital Employed

We use a return on capital employed (ROCE) measure that serves as an indicator of how efficiently we generate returns from the capital invested in the business. It is a group KPI that is directly relatable to the outcome of investment decisions.

ROCE represents the group's returns as percentage of capital employed.

Returns are defined as adjusted earnings before interest and tax. We use an adjusted measure (before specific items) for the reasons explained in the 'specific items' section above.

Capital employed represents equity, debt and debt-like liabilities. We net the derivative financial instruments and cash and cash equivalent balances that we use to manage financial risk against gross debt, and exclude current and deferred tax balances as the measure is determined on a pre-tax basis.

While our long-term capital investment programmes such as our full fibre rollout deliver value-creating long term returns, they suppress ROCE in the short to medium term.

The following table sets out the calculation of our ROCE measure. In doing so it reconciles returns to operating profit, the most directly comparable IFRS measure, and presents the components of capital employed.

Year ended 31 March	2021 £m	2020 £m
<b>Reported operating profit for the period</b>	<b>2,587</b>	<b>3,283</b>
Share of post tax profits (losses) of associates and joint ventures	8	(33)
Specific items (non-finance and tax)	481	367
<b>Return for the period</b>	<b>3,076</b>	<b>3,617</b>
<b>Equity, debt and debt-like liabilities</b>		
Loans and other borrowings	16,685	19,334
Lease liabilities	6,152	6,560
Retirement benefit obligations	5,096	1,140
BDUK grant funding deferral	568	619
Total equity	11,679	14,763
<b>Adjust for balances used to hedge financial risk</b>		
Cash and cash equivalents	(1,000)	(1,549)
Investments	(3,683)	(5,112)
Net derivative financial instruments	48	(1,477)
<b>Adjust for tax balances</b>		
Net deferred tax liabilities	440	1,308
Net current tax receivable	(197)	(46)
<b>Capital employed</b>	<b>35,788</b>	<b>35,540</b>
<b>Return on capital employed</b>	<b>8.6%</b>	<b>10.2%</b>

### Adjusted EBITDA

In addition to measuring financial performance of the group and customer-facing units based on operating profit, we also measure performance based on EBITDA and adjusted EBITDA. EBITDA is defined as the group profit or loss before interest, taxation, depreciation and amortisation. Adjusted EBITDA is defined as EBITDA before specific items, net non-interest related finance expense, and share of post-tax profits or losses of associates and joint ventures. EBITDA is a common measure used by investors and analysts to evaluate the operating financial performance of companies, particularly in the telecommunications sector.

We consider EBITDA and adjusted EBITDA to be useful measures of our operating performance because they approximate the underlying operating cash flow by eliminating depreciation and amortisation. EBITDA and adjusted EBITDA are not direct measures of our liquidity, which is shown by our cash flow statement, and need to be considered in the context of our financial commitments.

A reconciliation of reported profit for the period, the most directly comparable IFRS measure, to EBITDA and adjusted EBITDA is set out below.

Year ended 31 March	2021 £m	2020 £m
<b>Reported profit for the period</b>	<b>1,472</b>	<b>1,734</b>
Tax	332	619
<b>Reported profit before tax</b>	<b>1,804</b>	<b>2,353</b>
Net interest related finance expense	773	750
Depreciation and amortisation	4,347	4,274
<b>EBITDA</b>	<b>6,924</b>	<b>7,377</b>
EBITDA specific items	481	350
Net other finance expense	18	147
Share of post tax losses (profits) of associates and joint ventures	(8)	33
<b>Adjusted EBITDA</b>	<b>7,415</b>	<b>7,907</b>

### Normalised free cash flow

Normalised free cash flow is one of the group's key performance indicators by which our financial performance is measured. It is primarily a liquidity measure. However, we also believe it is an important indicator of our overall operational performance as it reflects the cash we generate from operations after capital expenditure and financing costs, both of which are significant ongoing cash outflows associated with investing in our infrastructure and financing our operations.

Normalised free cash flow is defined as free cash flow (net cash inflow from operating activities after net capital expenditure) after net interest paid and payment of lease liabilities, before pension deficit payments (including their cash tax benefit), payments relating to spectrum, and specific items. For non-tax related items the adjustments are made on a pre-tax basis. It excludes cash flows that are determined at a corporate level independently of ongoing trading operations such as dividends, share buybacks, acquisitions and disposals, and repayment and raising of debt.

Normalised free cash flow is not a measure of the funds that are available for distribution to shareholders.

A reconciliation from cash inflow from operating activities, the most directly comparable IFRS measure, to free cash flow and normalised free cash flow, is set out below.

Year ended 31 March	2021 £m	2020 £m
<b>Cash generated from operations</b>	<b>6,251</b>	<b>6,481</b>
Tax paid	(288)	(210)
<b>Net cash inflow from operating activities</b>	<b>5,963</b>	<b>6,271</b>
Net purchase of property, plant and equipment and intangible assets	(4,818)	(3,889)
<b>Free cash flow</b>	<b>1,145</b>	<b>2,382</b>
Interest received	6	30
Interest paid	(770)	(736)
Add back pension deficit payments	955	1,274
Remove cash tax benefit of pension deficit payments	(181)	(434)
Dividends from associates	5	1
Add back net cash flow from specific items	390	112
Add back net sale of non-current asset investments	(11)	33
Add back prepayment in respect of spectrum licence auction	702	–
Remove payment of lease liabilities	(782)	(651)
<b>Normalised free cash flow</b>	<b>1,459</b>	<b>2,011</b>

## Cautionary statement regarding forward-looking statements

Certain information included in this Annual Report is forward-looking and involves risks, assumptions and uncertainties that could cause actual results to differ materially from those expressed or implied by forward-looking statements. Forward-looking statements cover all matters which are not historical facts and include, without limitation, projections relating to results of operations and financial conditions and the company's plans and objectives for future operations. Forward-looking statements can be identified by the use of forward-looking terminology, including terms such as 'believes', 'estimates', 'anticipates', 'expects', 'forecasts', 'intends', 'plans', 'projects', 'goal', 'target', 'aim', 'may', 'will', 'would', 'could' or 'should' or, in each case, their negative or other variations or comparable terminology. Forward-looking statements in this Annual Report are not guarantees of future performance. All forward-looking statements in this Annual Report are based upon information known to the company on the date of this Annual Report. Accordingly, no assurance can be given that any particular expectation will be met and readers are cautioned not to place undue reliance on forward-looking statements, which speak only at their respective dates. Additionally, forward-looking statements regarding past trends or activities should not be taken as a representation that such trends or activities will continue in the future. Other than in accordance with its legal or regulatory obligations (including under the UK Listing Rules and the Financial Conduct Authority's Disclosure Guidance and Transparency Rules), the company undertakes no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise. Nothing in this Annual Report shall exclude any liability under applicable laws that cannot be excluded in accordance with such laws.