

BT Q3 2010/11 Results

Conference Call Transcript

Attendance List:

Catherine Nash	(CN)
Ian Livingston	(IL)
Tony Chanmugam	(TC)
Gavin Patterson	(GP)
Jeff Kelly	(JK)
Sally Davis	(SD)
Steve Robertson	(SR)

CN I am Catherine Nash, Director of IR here at BT, and I would like to welcome you all to our Q3 results call. On the call today we have Ian Livingston, Chief Executive, and Tony Chanmugam, Group Finance Director. They will give a short presentation on the results and then we'll hand over to you for questions. On the call today we also have the Chief Executives of all our operating lines of business. Before we start, I would just like to draw your attention to the usual disclaimer on forward looking statements. Please see this slide that accompanies today's call and our latest Annual Report and Form 20F for examples of the factors that may cause actual results to differ from any forward looking statements we may make. So the slide and the Annual Report can be found on our website. And now I'll hand you over to Ian. Please go ahead.

IL Thank you Catherine and good morning to you and thank you all of you for coming on the call. I know it's a very busy day with the telecoms results and actually it's the reason it's an unusually late call. We did want to give you some time after the Vodafone conference call and also hopefully will help you out by making this a pretty quick run through the business. If I can ask you to turn to slide 4 for the Group results. Just the key headlines, revenue was down 3%, EBITDA up 7% in the quarter, earnings per share up 32%. The free cash flow, as you know, we have set a target relating to before specific items so to help we've given that number which is £569 million, up £43 million and for the year to date, we are just over £1.6 billion on that measure. After specific items, £515m and actually that's up £200 million. Net debt has improved by £1.4 billion, at £8.67 billion. I won't go through the group numbers in too much detail because Tony will run through them in his section. What I will do is to go through the individual lines of business in some more detail and first of all slide 5 and Global Services.

Global Services underlying revenue was down about 6%, that's 7% you see there but FX accounted for about 1% of that. We also saw a decline

in wholesale and mobile termination rates and, mobile termination rate decline will be a continued feature. We've seen probably a 2% to 3% of the decline relating to that factor. We have also seen a continued reduction in UK calls and lines and that's obviously something we want to focus on and try and improve on and finally, there is a one-off adjustment of around about £20 million to the numbers. What we try and do every quarter is just highlight to you if there is a particular up, a particular down that's not actually in the underlying numbers. We have also said that we expect next quarter to be slightly worse in terms of revenue decline and that's actually got a lot to do with the continuing position on MTRs but also if you recall last year we highlighted to you a large one off receipt and revenue item relating to a particular contract and we got to the anniversary of that and if you look at last year's numbers you can absolute see that in the trends.

In terms of net operating costs, we saw net operating costs decline by 8%, now part of that actually reflects the same position regarding transit and MTRs but underlying cost reductions as well and, overall, in terms of trends, EBITDA up 15%. For the year to date, operating cash inflow £49 million, reflecting the strong performance in Q3 and that's really, I think, reflecting a much improved working capital and that's quite important for a number of reasons. One is we've always said that cash is really the critical measure in Global Services, long term sustainable cash generation but also, you know, I think customer service reflects that because if customers aren't happy, you know they would tend not to pay you often and I think that the improved position represents also continuing progress we are making on customer service. We have always been highly regarded in Global Services compared to our competitors and that's a position we would like to continue to enhance. Also I think it reflects a more even cash profile during the year, it's something we said over a number of quarters to expect and we did actually see in Q3 a pull forward of some of the stuff we might expect in Q4 and that's why you expect, you obviously can't get it twice and that's why we've given you some guidance for the full year and critically what we've said is that in Global Services we are cash flow positive, round about £100 million for this financial year and that's a year earlier than we had originally guided so that's pretty reasonable news. Other item is order intake. Order intake £1.7 billion, up 8%. That means that year to date round about £7.6 billion so continued progress on that.

Now turning to Retail. Retail, I think, has shown good trends, revenue trends really pretty much across the piece. We have seen improving trends in consumer and business and enterprises. I'd actually like to start by highlighting BT Business and the chart on the right shows that this is a business whose revenue was running down 9% to 10% year 18 months ago and now actually we've gone to positive 1% and I think that reflects a less bad market but also it reflects our success in our strategy which is around providing not just communications but also IT and mobility for SMEs - and we've seen strong growth in both these areas for the

customer. Our Consumer was down 4% which is an improvement on Q2's number and a lot of the operating metrics have also improved and I'll run through that in the next slide in a second.

Net operating costs down 4%, Retail has been doing this for a number of years, I think we are probably 6 or 7 years into, that's 6 years into cost reductions and we are seeing across the piece, including our 6% decline in labour costs and I think it's worth mentioning that all units within Retail grew their EBITDA contribution. Our Consumer business, BTB Enterprises and actually interestingly enough our business in Ireland and that I think was a particularly notable performance given the economic conditions in the Republic of Ireland.

As I mentioned, I'll take you through the individual metrics in Consumer on slide 7. First of all, we did see an improvement in active customer losses a 35% reduction in quarter on quarter losses which is a step in the right direction. As always, more to do. Consumer ARPU continues to grow and that I think reflects very much more customers buying more services, well customers buying more services from us, particularly broadband. Probably one of the most notable metrics was the 53% share of broadband net adds or DSL net adds in the quarter, that's the best share for 8 years. 188,000 net adds out of total on the total BT Group Network of over 350,000 which in itself was a strong number. On Infinity, you see an increase, we've seen an increased level of take-up and we've seen actually in some of the individual areas, the cabinets are now getting into double digit take up in terms of percentage of households and that's encouraging and is actually better than we had expected. I think we have also seen the enthusiasm for Infinity and what we did on Race to Infinity, Race to Infinity was something we ran where we said to individual areas register your interest in Infinity and we actually got 365,000 registrations of interest which is, that's households, so that's a huge degree of interest and there we originally planned to enable five exchanges that otherwise would not have been enabled but, such was the level of interest and desire, actually we said well we think we can do 10 exchanges, so that's 10 exchanges that otherwise would not have been done and, you know, it's good to see people do seem genuinely interested in the service and the product.

On BT Vision, reasonable quarter in BT Vision. Increased net adds of 40,000 for the quarter and that's more than actually the previous two quarters combined. A lot of new innovations coming to Vision and we've talked about that in previous sessions but around BBC iPlayer and around, already we've rolled out much enhanced HD but more to come on that. What we call Vision 2.0 is going to come which is recommendation engine that I think that's going to help a lot given the vast range of the content we've got available. It's something to help people choose what they like and what they want, so a lot more to come to Vision as well as of course YouView coming. Also something actually not on the slide but mentioned is also wi-fi which appears to have been in

the news quite a bit recently. We've got now 2.6 million hot spots which is a few more I think than most people in the market, quite a lot more and an interesting thing is how much they are being used. Actually total minutes of usage were 881 million minutes last quarter alone and that compares with the previous quarter, this time the previous year was 335 million, we've gone from 335 million minutes in Q3 last year to 881 million minutes Q3 this year and I think whether it be smart phones, whether it be iPads, we've got a very successful iPad app, whether it be computers, people are finding wi-fi a very useful thing to use and we think the investment we have made over a long time in our hubs, this is just a little example of that strategy paying off.

Now moving on to Wholesale, Wholesale is doing what we said it would do, you know, in a stable business there are always going to be, you know, one-off items going in various directions. What we tried to do to help, you know, excluding transit and one-offs, is show you on the charts the underlying position for wholesale which is, give or take, broadly flat which of course is much, much better than a few years ago. And that's really as a result of the growth in managed network services so the revenue was up 9%. Held operating costs in the quarter and also it's worth mentioning a significant contract we gained with KCOM Group. The reason for mentioning that is KCOM was the start of, I think, the move into managed network services and you, those of you who follow KCOM I think will hear Bill Halbert talk very positively about this contract and what it has done for numbers of customers. It is good now they are adding on additional services and I think it shows it has been a good contract for us and a good contract for the customer and that actually is the whole thesis around Wholesale that we can use our scale and help our customers, not just in the UK, but on a more global basis.

Now turning to Openreach on slide 9. Openreach revenue overall was flat but external revenue was up 16%. That I think reflects continued growth in its external end users in the MPF and actually SMPF base this quarter and to a lesser extent, continued PoP build out. I think probably most interestingly and one of the most interesting numbers in all of this is actually what is happening with copper line base. If you look at the chart on the right, we are now showing growth in copper lines. And this is a new statistic we thought we'd give you because, from an Openreach point of view, what's important is how many physical pieces of copper or, over time, I'm sure we will say copper or fibre, get into our premises. For a long time, that was falling and actually at times falling quite significantly, and that's turned around and perhaps it says the death of the fixed line has been somewhat exaggerated and shows that customers, I think, are wanting broadband, are realising in order to get the sort of services they want, they need a broadband line. There will be some seasonality I'm sure involved there because Q3 is the quarter that students return to college so you will get some sort of kick up but, I think, you can see from the numbers that's certainly a significantly improved trend which will be helpful.

Net operating costs are down 8% in Openreach. A chunk of that is because of lower leaver costs, I think as Tony will mention later, we are very actively trying to manage the position of leaver costs by spending more money reinvesting in our workforce, retraining and redeploying them, so we are spending more money shall we say on ongoing labour costs and less on leaver costs and I think that's the right thing financially but it also is the right thing in terms of, you know, we are doing our best to protect our long term workforce as we can. On fibre roll out, we are back again making good progress on fibre roll out, you know I think last week we had about 80,000 homes. The week before that I think it was about 100,000. We did have a bit of a hiatus with the very bad weather which affected us in two ways. It affected us directly because, frankly, with the snow and ice, it was actually difficult to do the work that we needed to do but also particularly as the heavy rains affected us and repair, we did move some resources over there, so had a bit of hiatus in December and January but we are now back at a good pace and we would expect to hit the 5 million sometime in the Spring.

Finally, the final slide pensions. No BT presentation would be entirely complete without pensions but I think there is not a huge amount of new news. On IAS19 deficit, £2.7 billion. As you can see that's a significant improvement from last March. A large chunk of that is due to, the change to CPI. That was £2.9 billion gross not net so bearing in mind net obviously it was less than, net of tax. What we are seeing is continued strong performance of our asset base and the returns we are getting are substantially higher than we had assumed in terms of the actuarial or any other calculation. We, of course, made the £525 million deficit payment in December and pre-empting I think the question you might ask re pension regulator review is ongoing and I can't give you a date when exactly it will be finished but I think obviously the Pension Regulator has a lot of new information to absorb.

So turning to my final slide, as it were, my summary slide. I think in this quarter, we've seen some good stuff, we've seen good KPIs I think across most of the business, particularly in Retail and I think what's happening with copper base and it's nice to see BTB going positive. We are also pleased, you know, the previous quarter, previously we talked about hitting our £2 billion of free cash flow earlier than we said we would and therefore, and it being over £2 billion thereafter so that's a good tick in the box and then this quarter we said we are going to hit the GS cash flow positive a year earlier than we said we would and you know, grow it thereafter so we are making progress but, at the risk of being extraordinarily boring, I'm going to say, and I'll probably say it every quarter I speak to you, there is a lot more to do, we recognise that and the good news for BT is there is a lot more that can be done. With that, I'll pass you over to Tony.

TC

Thanks Ian and good morning everybody. I will now run through the results for Q3. Starting with slide 13, the key financial summary. Both reported and underlying revenue for the quarter were down 3% at just over 5 billion. Foreign exchange movements had no material impact on the group's revenue or EBITDA for the quarter. The revenue decline of 3% compares with 3% decline in Q2 and a 4% decline in Q1. Excluding the year on year impact of transit and mobile termination related revenues, revenue declined by 2% in the quarter, in line with the last quarter. Although any changes to mobile termination rates will have an impact on our top line revenue going forwards, I would emphasise that these are zero margin revenues to BT as we collect revenue on behalf of mobile operators. For our business in general, MTR cuts are good news for us and our customers. Transit revenues are very low margin and consequently have minimal impact on EBITDA. Next quarter we expect the Global Services decline in revenue to be slightly higher reflecting the increasing effect of mobile termination rate reduction this year and the one off benefit relating to a major contract milestone in the prior year. During this quarter, our incremental investment has helped reduce the level of active consumer line losses, delivered growth in Retail BT business revenue and increased our share of broadband net adds to 53%. As Ian said, the highest in 8 years. However, it is too early to assess the impact of the investment in Asia Pacific.

Adjusted EBITDA, that is before specific items but after leaver costs, increased by 7% over last year to near 1.5 billion. The growth reflects the continued focus of our cost transformation programmes across the group. Leaver costs were also £46 million lower than last year as increased focus is placed on ensuring that BT staff are utilised within the business, wherever possible.

Looking at slide 14, free cash flow. Free cash flow after specifics was an inflow of 515 million in the quarter, 210 million better than last year. Specific items accounted for 167 million of this improvement driven in the main by Global Services restructuring costs in the prior year, so pre specifics, free cash flow improved by 43 million against the prior year. Let me draw out some of the key movements. Cash outflow from capex in the quarter, was 670 million, an increase of 122 million against the prior year. This reflects the phasing of our key investment programmes such as the fibre roll out. The current level spend is in line with our expectations and we remain on course to invest around 2.6 billion of capital this financial year. There was an increased outflow of 50 million on tax payments driven by the historic increase in profit. As I mentioned at Q2, we expect to return to a more normal tax payment profile so this is in line with that expectation. For the first 9 months of this financial year, our effective tax rate has been 21.7%. Again this is in line with our expectations for the full year. The increase in tax payments has been offset by lower year on year interest payments of 47 million mainly due to timing between Q3 and Q4 and higher interest income relating to the resolution of some historic sales tax matters.

Working capital and other inflows increased by 70 million driven by improved debt collection and timing on contract receipts being partly offset by a lower creditor balance as a result of lower costs and timing of supplier payments. We expect the cash impact of working capital and Other to be broadly neutral for the full year. Note that we received proceeds of 67 million in relation to the sale of the 5.5% stake in Tech Mahindra during the quarter but this is not included in our reported free cash flow which excludes disposals and acquisitions. Net debt of 8.7 billion shows a 1.4 billion improvement compared with last year. This is in line with Q2 as cash generated in the quarter has been offset by the outflow of the 525 million pension deficit payment. During the quarter our US dollar bond matured resulting in a repayment of 1.7 billion. This is funded through our existing cash and investment balances. We have further cash and investment balances of 1.2 billion on the 31st December and these will fund the 0.8 billion of repayments due during the course of Q4.

Moving on to slide 15, we have cost reductions. Total opex reductions of 235 million in the quarter are equivalent to a 6% reduction and in line with the level of reduction achieved in the first half. This headline reduction is after taking into account leaver costs which, as I mentioned, have reduced by 46 million year on year to 12 million. We continue to reduce our total labour costs which reduced by 3% overall in the quarter. Within this, the non BT labour cost reduced by 9%, a further reflection of our desire to protect BT permanent jobs wherever possible. On a cumulative basis, our cost reductions now stand at 722 million for the year and we are on track for our full year target of 900 million. The achievement in this quarter reflects the continued drive for cost transformation across the group through efficiency, effectiveness and renegotiating supplier contracts. Specific examples include improving field force productive through improvements in work scheduling and the setting of more rigorous performance standards. We are also delivering savings through greater automation and doing things right first time for our customers, therefore eliminating the cost of failure. However, we have also had increased levels of Openreach agency staff costs and overtime caused by the impact of the adverse weather in December and an increase in volumes. As I have said before, there remains plenty of opportunity to transform our cost base.

Finally, let me turn to slide 16, the outlook. Given our performance in Quarter 3, our group outlook remains unchanged for the full year with revenue expected to be around 20 billion, EBITDA around 5.8 billion and free cash flow at 2 billion. We now expect Global Services to be operating free cash flow positive this year at around 100 million, a year ahead of target and to generate around 200 million of cash in the next financial year. The improvement this year has been helped by some significant customer collections in the quarter and we would expect Q4 to be lower than last year as a result of our drive to smooth cash flows

between quarters. The projected 2 year cash profile demonstrates the progress made within Global Services. Our outlook for 2011/12 and 2012/13 is otherwise unchanged. Thanks for listening. I will now hand you back for questions.

Question and Answer Session

Chris Alliott

RBS

Good morning, thanks for that. Yeah, just two quick questions if I may. Firstly, on the copper line increase, I wonder if you could give a bit more detail on what you think may have driven those overall copper lines to have increased. Do you think that's just the fact that second lines have stopped being switched off and now you've got the situation where people are actually reactivating lines that had been switched off in new homes and what the split might be potentially between business and retail on those copper lines? And then, secondly, I wonder if you've got any flexibility on the pension to make prepayments into the pension ahead of the current schedule and whether that would actually be possible. Thanks.

IL

Thanks Chris. On copper line increases, it's difficult to say, I mean we did I think highlight last quarter that we had, we were seeing, a shift in what was happening which was encouraging and, you know, I don't want one swallow to make a complete summer but it's certainly a shift in the right direction. Part of that I think will be seasonal although if you compare to Q3 last year, the position is a lot better and the graph goes through to Q3 last year, but part of it is I think, I think we may be seeing movement, the assumption that you know, there was going to be a vast increase in mobile only households, I think may not be correct. I think people are finding that they are using broadband far more intensively than they did in the past and, frankly for that, you need a fixed line and what it can provide and I think that will be some of it also I think the competition in the market is helping to generate, you know Retail for instance has a very good up front line offer which is very good, particularly good value and I think that's attracted people. A lot of the other CPs also have got offers out there and so I think generally we seem to be seeing a good performance in the overall BT network and a lot of it may be because you've got lots of different providers advertising it and I think that change, a lot of it is happening when you've got a lot of different people now offering lines, not just calls and that maybe has stimulated the market and maybe also moved people away from other forms of communication, whether it be cable or mobile, but on the basis that I haven't seen anybody else's numbers, it would be difficult to comment and I've got no sense of the differences in business and corporate. In terms of flexibility of pension, yes we do have flexibility on pensions. I think it's a bit early to call that just now, we will have the next review at the end of this calendar year and that would start but, yes we do, you always have flexibility, I'm sure the trustees would not object if we decide to pay more money into the scheme but we'll have to take that, and we'd only do that if it made sense

from a financial point of view and as I said I think it's extremely unlikely we'd do anything, particularly this side of the next review in terms of that.

Nick Delfas

Morgan Stanley

One question just on customer service, can you share any statistics on how your customer service is developing because obviously the margins are very good but I'm just wondering if there is any evidence that service is suffering and, secondly, on leverage, you have avoided giving any kind of leverage targets and, obviously, you still have a review of the pensions to come and also the changes relating to operating leases from an accounting point of view, but is there anything more you can say on where you think the leverage of the company should go over the next 3 to 4 years?

IL

Taking the second one first, and I know that Tony will a bit more to it but I think he'll probably give you the same answer which is we don't have an eventual leverage target not least, you know, different market conditions do tell you different things. The great news is people are starting to ask the question because they see how much debt we are paying off and, you know, and it gives us long term options and that is what we have been trying to do in our business is give ourselves long term options rather than saying, oh well, here is a set target and hopefully over time you will see increased dividends, you will see opportunities and that is what we are going to carry on doing is generating the cash that allows you to ask that question. I don't know if Tony has anything to add to that.

On customer service, we've not had, we've not made the progress on customer service over the last few months we would have wanted to make. I made reference earlier to some of the impact of the weather but also volumes have been a big thing for us. We have seen a substantial increase in requirement for engineer visits for new provisions and it's coming out particularly from the LLU players but also we got hit hard by what was basically the worst weather I think for decades and so repair times aren't too bad and they are getting better, you know, put it in context, you know, we had probably about just over a day's worth of work on hand in terms of repair but the, in some of the areas, the lead times and provision are longer than we would like and we will be bringing that in and as I mentioned earlier, that we have moved some of our people off NGA back onto doing things from an engineering point of view to try and assist and it really has been a factor of combination of demand and the weather. Steve, I don't know if you have anything to add?

SR

No, I think that covers it. I just emphasise, we've been focusing on repair. We expect to get absolutely back to where we would expect to be in very good repair performance within the next couple of weeks and the extended lead times have really been purely down to demand. I would emphasise though our on-time delivery, so that when we do make a promise that we are going to deliver, we are still hitting very, very high levels of on-time delivery.

-
- IL And the performance is still way better than it was like say 4 or 5 years ago, to put it in context, you know, most repairs will be done next working day.
- Nick Delfas** Can I just ask quickly, is that why there's no update on the exact Infinity numbers, is that because of the weather?
- IL No, no, actually Infinity's gone fine, we've just decided, and there's a comment that the shareholders made to us that they say you are giving a lot of detail every single quarter and, you know, Infinity within this, you know, we are giving the overall broadband numbers and we're giving the overall Vision numbers, and it just seems to us that we've got lots of detail. We are making good, I just want to reassure people, we are making good progress on Infinity and demand so please do not interpret no Infinity numbers as meaning not good numbers. Actually we are very encouraged by progress on Infinity so no, it's not that, and Nick I notice that you obviously take advantage of the fact that questions are free on this occasion.
- Nick Lyall**
UBS Yeah, morning, it's Nick at UBS. It was actually on the fibre lines as well. When I try to strip out roughly the fibre line numbers, it looks like your underlying DSL ARPU is a bit weak this quarter. Are you having to make some discounts or is it bundling that's maybe forcing that? What is competition like in the market just now for the basic DSL products please? And then, secondly, on Retail, you mentioned the staff numbers and staff costs were down quite aggressively but also is SAC a contributor to this quarter, has SAC reduced quite a lot where investment in marketing reduced quite a lot quarter on quarter please.
- IL I'll let Gavin talk a little bit more about some of the things but, you know, bearing in mind we actually acquired a lot more customers this quarter so I don't think SAC has reduced, I mean, we acquired a lot more Vision customers, we acquired a lot more broadband customers and actually SAC, I imagine, is up. Marketing is down a bit, no question about that, and I'll let Gavin talk about that. Overall, our ARPU is very good and I'm not quite sure the unpacking number you referred to but...
- Nick Lyall** It may be wrong but because I've not got the fibre numbers it's a little bit difficult to work back to. It seems as if DSL APRU possibly was down a little bit sharper this quarter which is a bit of a concern.
- IL I don't think, no, I don't think we see that. We are pretty, I think we are pretty happy overall with ARPU, but I mean, you are right there is a lot more bundles being sold so I mean there is an element where the allocation of revenue to different bits is becoming less and less relevant as we do more bundles and it's something frankly we've got to look at with the KPIs over time, you know, it's absolutely right that we would give you ARPU but trying to split some of the revenue numbers between, if

you've got an all in one package, which of course we didn't use to be able to sell but we can now, you know, exactly the split between the different bits it's got a little bit of art to it but we've got no particular problems but Gavin is there anything you wanted to add.

GP

I mean bundling is working very well for us so we are increasingly selling customers onto bundles, we are finding that that's what customers generally want to buy from anybody in the market place so it's been a real opportunity for us because, as Ian said, it's only since we've been able to offer in the last year. I think elsewhere, I think we have a number of elements in our broadband strategy working very well for us so, Plusnet is working for us but the BT brand is growing very strongly as well so there isn't really change in the relative percentage between Plusnet and BT because I know that's a question sometimes that people have, are we just acquiring it through the Plusnet brand. No, both of them are growing and as Ian mentioned earlier, wi-fi is proving to be a very important differentiator for us. It's really growing very, very rapidly. Usage is growing rapidly. The number of customers using it every month is increasing rapidly as well and that's something that's certainly been a reason why people are coming to BT and away from competitors.

IL

I think Tony just wanted to add something about Retail cost just to add more colour

TC

The absolute level of Retail cost reduction, if we compare this quarter with the last quarter is roughly the same, so round about 4% decline. The increase in Retail EBITDA quarter on quarter is driven by improved performances on the margins which have been very effective.

Paul Sidney
Credit Suisse

I just have two questions please. Firstly, we are expecting some substantial MTR cuts in the UK this year. I was just wondering how should we think about the impact on BT in terms of line loss or perhaps cost savings, and the second question, we have seen a couple of price rises in the UK wireline market this week, particularly from yourselves and Virgin and I was just wondering, after seeing some price cuts over the past 12 months, are we moving into a more price inflationary environment? Thank you.

IL

On the second one, I don't think we are moving into a price inflationary environment. To put it in context, we have increased some of our prices but we also reduced some of our prices. For instance, you can get now unlimited calls for £4.70 per month which is I think about the cheapest in the market, and down 30p, and what you are actually seeing I think it's a lot of us, more and more, we are trying to move people to unlimited packages and you know, we want to make the marginal cost of a call basically zero because that is the way you make it, it's easier billing, it's peace of mind for the customer and you know we are very happy for the customer to want to make more calls and to see that as a cheap thing to

do so what you see in pricing is it's gone up in some places and down in others and certainly, it is a truism of our industry, that, price, you know customers tend to get more for their money and you might not see the level of price erosion but what you see is customers getting more for it and the classic case has to be fibre. We are seeing customers getting 80 times the speed that they were getting 8 years ago for half the price, in fact less than half the price and that probably has to represent one of the best bargains around. In terms of MTRs, I think we will see the impact of MTRs in a number of places. First of all, and it's got to be said, it is really good news particularly for our Retail business but also generally for fixed line business because MTRs represented a subsidy from our customers over to the mobile operators which they could then use in calls. It's not just MTRs, it's also things like, I think there will be changes, Ofcom have proposed changes on 0800 numbers, so a number of you who might have called an 0800 number today for this call, if you had called from a fixed line, it would have been free, if you had called from a mobile you might have paid 20p a minute for that 0800 and Ofcom have said that 0800 calls should be free and that will have an impact. So there are a number of things happening. I don't see it leading to line losses and I don't see it being the thing. I think it's actually good news for our Retail business and it gives us obviously the opportunity to package mobile calls more within the overall unlimited package which is something I would like to see and I think might cause a bit rebalancing in the industry. It will affect us however in our revenue number and that's what we try and indicate in places because whilst MTRs represent zero, are absolutely zero margin, our Wholesale numbers and our Global Services numbers do reflect carrying calls which have MTRs in them and so as MTRs come down, that number comes down but it's not, as you will, it doesn't represent any underlying real revenue because of course there is no margin attached to it so it's going to be complex, I think it has impacts on our Retail business and also on other parts of our business. Tony, do you have anything to add to that?

TC All I'm going to say is that we will give you more flavour and detail relating to transit and MTR revenues during the Q4 presentations as part of the guidelines then.

IL Yeah, because we'll know a bit more about what's happening and the timing. You've already seen something happening in Germany and that's what affected the top line for GS and as we get nearer the year end we'll know, obviously, a bit more detail about exact timings and therefore I can give you some more guidance when we've got it ourselves. Thanks very much.

Darren Ward
Echelon

Morning. Just a couple of questions about some of the trends in the direct employee cost piece. Firstly just a straightforward one, I couldn't see it anywhere, apologies if I've missed it, but could I just get a number of FTEs at the end of the year, that would be helpful, and the second part

of the question relates to capitalised costs on the direct labour. They're fairly sharply up year on year and have been for a couple of quarters now. I'm assuming that's the Infinity fibre roll-out but any other cover on that would be welcome, particularly in light of how little of that seemed to happen in the quarter with the weather, and are those costs going to stay at this sort of higher level, 180, 190 a quarter going forward.

IL Okay on FTE numbers, no is the answer to that question. You didn't miss it, we said that we wouldn't give it on a quarterly basis. What we have given you is the total labour cost which is way more important because that's the number that actually really we should be tracking. In terms of the capitalised labour, I mean overall provision activity is higher and I think I referred to that earlier as being something, and also as you said, NGA being a factor.

TC Just to come back on the labour costs, what we're trying to do on the labour costs is focus on the costs not the heads, and that's the most important thing, it's the cost, and within the cost we've tried to balance out safeguarding BT jobs, reducing the cost within the third party cost, so if you look and see we've taken out 3% of the total labour cost, that's after taking into account the inflation associated with pay increases. Within that 3% reduction we've taken out 9% of the non-BT staff costs and will continue to focus on that level of reduction.

Darren Ward Just to be clear, we should be expecting, given the ongoing NGA roll-out, we should be expecting the capitalised costs to stay up near this kind of level?

TC The capitalised cost is two component parts. One element certainly related to the NGA roll out, the second does relate to the volumes associated with the provisioning within Openreach and so long as those volumes stay robust, then the capitalised costs will stay equally robust.

**Maurice Patrick
Barclays Capital**

Two questions: first of all, you've given guidance on cash flow for Global Services this year and next year. Is that a sign of increased confidence in cost-management, or on the revenue opportunity, or both? Next question is, you've seen strong net adds on broadband without YouView. There's clearly a lot of press speculation about delays. Do delays or potential delays in YouView actually matter given the strong growth you've seen?

IL On Global Services, I think we said as we got nearer the time we would give you updates. I mean the fact we've given, we've said what we think it's going to be is a sign of confidence, I think it's a sign of confidence in our progress in Global Services and we want to give people something a bit more than it's going to be positive. It's nice we can say not only is it going to be positive this year but roughly here's a number and it is around about that number, be clear, and it's a sign of improved confidence, lots more to do, and that's net of a lot of investment we're making in Global

Services in growing the business, in rationalising it's networks, in areas such as that. So, I think people wanted to start treating Global Services as a normal business, and hopefully that as we start to talk 100 million, 200 million, people start to see that as opposed to we were always talking about cash outflows. And it's all a journey and Jeff, I don't know if there's anything you want to add about your journey?

JK Well, I would just add that it's a lot of different aspects of the business. We're very focused on free cash flow, we told you that at the beginning of the year. Our debt collections are much improved over the start of the year, our capital plan is very focused and much more efficient than it has been, also reflective of better deal structures, so there's a lot of aspects of that will improve cash.

IL Okay, thanks Jeff. And YouView, I mean you're right, we have had very good broadband numbers. I think the numbers on Vision are improved as well and there's a number of things we are doing and are highlighting in the presentation that we are doing irrespective of YouView that will, overtime, dovetail with YouView so I think we're doing pretty well anyway and we would be adding to our Vision proposition in any event, but YouView in the long term is important. Gavin is there anything you want to add?

GP No, I mean just to reiterate that YouView is important but it is only one part of our TV strategy and there are plenty of things around it that are going to help drive usage and attract customers this year, so nothing more to add.

**Morten Singleton
Investec**

Good morning gentlemen. Two quick questions if I may. First off on wi-fi, 2.6 million hotspots, that's about 600,000 more than I think you last reported, but could you give us some breakdown between the various elements, so how much of that would be BT Fon, how much of it is Openzone where businesses have opened up public access, and how much of it is your own constructed wi-fi hotspots? And the second question just concerns fibre, I understand you don't want to give a number for the number of people come on board for the Infinity product, but can you give us a flavour how attractive the proposition is proving in terms of the proportion of people showing an interest when their homes have been passed and they've been marketed?

IL On the second one I'll ask Gavin just to give a general sense of wi-fi, obviously the vast majority are Fon hot-spots but we also have a huge number of premium hot-spots, of Openzone hot-spots, but we were a bit puzzled about some of the comments of people talking about having doubled BTs number of hot-spots, which I think will be a challenge for them going for the 5.2 million from a standing start by 2013 which I think was a target, that was a bit puzzling, but I think one important thing is on wi-fi, was what I mentioned about that investment in the hub, because we

put quite a lot of development resource into not only how the hub looked but what it could do, and one of the things - it's only one of the things - was the ability to have this dual-channel secure access to allow you to do this open wi-fi, and you know this is real community broadband, maybe big society at its finest here, that people actually are opening up their wi-fi to allow other people to use it and gaining themselves, and the reason it's up 600,000 is of course the more people that get a hub, the more open it up and so therefore it's a self-generating community. But Gavin anything about the overall generalised split?

GP I'm not sure I really want to give any more detail than that. The 600,000 additional spots in the quarter are, the vast majority are from BT Fon open wi-fi hot-spots, but there's an awful lot of usage, in fact the majority of the usage does go through the BT Fon estate so that's probably all I would add. The other question was about Infinity and, I think Ian, do you want to...

IL Well, on Infinity, I think the numbers will compare favourably - just even the retail numbers alone to what Virgin had managed in their first year from their base. In terms of penetration, I mean we, as I said in the presentation, we're seeing a number of cabinets already at double digit penetration so areas of places like Basingstoke, a number of the areas within Basingstoke are already showing 12, 13% penetration and that's better than we had expected at this stage. Within exchange areas we're at high single digits in a number of places already, and we're encouraged by the numbers and I think more people are coming on to the NGA bandwagon. And you've got to remember there's fibre and then there's Infinity, Infinity is what Retail sell, and maybe it's a good thing that people will start to talk about it generically, and then of course our Wholesale business is allowing a number of smaller ISPs and there is quite a number now selling, people like Andrews & Arnold for instance, selling to their customers and we're also seeing quite a lot happening in places like Northern Ireland as being very strong, so yeah, so far so good would be the net answer.

Andrew Lee
Goldman Sachs

Good morning. Just a question on Retail, kind of just probing you a bit more on the success you've had in net adds there. I can see that a key differentiator of your Plusnet product has been the lower price point, but just wondered if you could give a bit more detail on what you think the key differentiators have been at the higher value segment of the market, I suppose importantly do you think that this higher end differentiator is sustainable through 2011 or do you expect market rationality that we've seen in UK broadband in 2009 and 2010 is going to become less stable in 2011? Thank you.

IL Well I think the rationality is actually in the consumer because they're getting great value actually for the high value product. We talked before about access to wi-fi hot-spots. If you actually look at how much that

would cost you to buy, as many people, do you're getting the broadband for very little money per month without even starting to talk about things like the extra phone line in your home, the access to BT vision, the n-class wi-fi, things like that. I mean I'm sure Gavin, who I'll put you over to, will tell you it represents an outstanding proposition in great marketing as to why we've done so well, but Gavin apart from outstanding marketing?

GP Thanks for that feedback, Ian. You know, we're reasonably confident that these trends will continue going forwards. It's worth noting with the Plusnet brand, the vast majority of Plusnet customers take a line and calls with us as well, so they may be attracted by the very compelling price point on broadband, but it's the complete package that we try and encourage them to take. Then under the BT brand, the key differentiators for us are wi-fi, the fibre products, the things, the reasons why people are choosing us more than anything else.

IL Okay, thanks Gavin. And just one other point on Plusnet, actually I think the performance of BT Retail Total Broadband is even stronger in relative terms than Plusnet in the quarter, so just maybe thinking about some of the earlier comments. We've seen, actually, the high value do even better in relative terms, in terms of the quarter on quarter growth.

GP That's right, yeah. It's the mix between Plusnet and BT has not gone more towards Plusnet.

TC It's actually reduced slightly.

Andrew Lee Thank you. And I just had a quick follow up question on Global Services, you were talking about how the predictability and confidence of the business had improved and one of the things you mentioned or Jeff mentioned was best deal structures. I just wondered if you think the market place has improved to improve your predictability, given that yourselves and particularly Cable and Wireless Worldwide are now focused on free cash flow than perhaps you both had been four or five years ago?

IL Well I think when we look at our global customer base we don't, really we actually talk about competition with AT&T and OBS and Verizon not really Cable & Wireless to be honest, but I don't think it's the market, I think it's that we are more disciplined and doing better deals in the right way and bringing real value to our customers and building them up in a more effective way. Jeff, anything you want to add?

JK No, I would just agree with that. The focus in Global Services is well known, it's free cash flow, and there are a lot of mechanisms around the world to be able to be more efficient. I think as we approach deals we're better I think at talking customers through that towards the value of BT globally and having an asset conversation and getting to something that works for both of us.

IL Yeah, and be clear, we talk about free cash flow, what we mean is long term sustainable, measurable, growing free cash flow. This is not a short-term matter because the reason we're putting a lot of investment in for instance in Asia-Pac is to deliver that long-term. This is about sustainable and growable, it's one of the reasons we talked about £100 million this year, £200 million next year, you know, just to see that tracking. Okay, thank you, next question.

Paul Howard
JP Morgan
Cazenove

Thank you for that, a couple of questions. Ian, at Davos you were quoted as talking about Europe being due a painful adjustment, I think, in terms of consumer spending or in terms of the economy. I guess is there some hint there that you think the macro head-winds could get tougher over the next year or two? And then secondly, on Global Services I see for the nine months that your operating cash flow is basically EBITDA less capex and the working capital adjustments are sort of all evened out, is that what we should expect going forward, that EBITDA less capex is the free cash flow you report and there aren't big swings in working capital from one year to another?

IL I'll let Tony answer the second question, in a second. Just on Davos, I mean I was asked about the various economies, what I said is global corporations are doing pretty well because they're globalising, they're doing well in Asia and Latin America, and funnily enough we're doing well in Asia and Latin America, in particular. Also you seen the growth, particularly in Asian multi-nationals, that's good news for us, but if you talk about consumers you can't take the amount of money out of the economy without having some effect. I think it already is having an effect if you look at retailers' numbers generally. We are, to date, fortunate that we have something that a lot of people are interested in in terms of broadband, and a range of new services, and there has been a saying in consumer electronics, which is the product cycle can over-ride the economic cycle, I don't think you can do that forever but I wasn't trying to make any detailed comment about the future expectations for our business. Actually the next comment I made on that interview was about broadband and how it's seen to have become a core part of people's lives. Tony, whilst swings in working capital will happen quarter on quarter, just in the way of things anything you want to say about it.

TC One of the things I committed Paul two years ago was that we would even out our cash flow generation across the year. It's something that we've done reasonably well over the course of the last twelve months. No longer do we operate on the back of having our free cash all generated in Q4. That said, there will be some fluctuations in terms of working capital, based on reaching significant contract milestones, so there will be some movement on there but generally speaking, it'll be much smoother and as Jeff's said earlier on we'll manage the contracts so that the cash-flow generation is much more evenly distributed, it's

about cash management. So I'm reasonably optimistic that the levels of peaks and troughs will be lower, but this doesn't mean that there won't be peaks and troughs.

Paul Howard

But in terms of your guidance next year for Global Services an extra hundred million of cash flow is that pretty much all EBITDA?

TC

There will be a degree of EBITDA and there will be a degree of working capital.

**Guy Peddy
Macquarie**

Good morning all. Just a quick question: during the quarter you've probably benefitted from Orange coming back on to your network into a wholesale arrangement rather than an unbundled arrangement, so we can just give it some details of how we might see that through your KPIs please?

IL

Well, no. I'm sorry, not no I'm not going to answer it, but no in supposition, I think we moved the first Orange customer after the quarter end. It's not going to affect the Retail KPIs at all, it's just a wholesale movement, and it's - I mean Sally, I don't know if you want to answer it but you're not really going to see movement in the KPIs apart from some revenue, I guess, and Wholesale, Sally?

SD

I think that's correct, and it'll take a couple of quarters for that to come through, so you won't see it rapidly but, you'll see it in the broadband numbers.

IL

It's Wholesale running the network rather than Orange doing it so it doesn't have any effect on our end and it's not particularly - it's not particularly substantial, so it'll just be sold by Wholesale on behalf of - Orange will sell it provided by Wholesale as opposed to Orange selling it provided by Openreach.

TC

To be clear, it won't be in our broadband net adds.

IL

No. There'll be no change, no change in that sense. Okay? Thanks.

**Stuart Gordon
Berenberg**

Good morning, just two questions. You mentioned about the MTR cuts actually being a positive for BT. As I recall you still don't pass those MTR cuts on directly to your customers. Could you give us some guidance on the tailwind benefits from the MTR cuts and EBITDA? And the second question in Global Services, you've spoken about the last quarter trend potentially being worse than the trend we saw in the quarter just past, and this reflects the sort of one-off payments that we saw that were sort of migrated from the first quarter into the fourth quarter last year as I recall. But really if you look at the trends in the first half of the year, are we to read the economic environment may be getting worse in Global Services

or is this just a focus on better quality business that will help with the cash flow? Thanks.

IL Right, on MTRs actually we do pass a lot of our MTRs, I mean what I said - we've already got substantially lower prices, particularly for customers who sign up to our mobile package, our mobile calling package, a special plan that makes actually the prices quite cheap. We tried to anticipate a fair chunk of MTR reductions in that, and as I said what we would like to do is move more and more people into all you can eat. If you take our BT Business for instance you've already got for £15 Gavin, a month, all your calls to mobiles, all your calls to fixed lines, all your calls to how many countries is it?

GP I think 25.

IL All your calls to a lot of countries induced in the package price, so you know that's what we intend to do is actually put the money into the packages. I think that will be the main thing, you know, as well as I'm sure you will see some prices in the calls to mobiles. So, I think I'd say you're not right in your initial assumption. In Global Services you sort of gave me an either or to which I'm going to say neither. What happened in Global Services is, for next quarter, that we recognised about £100 million of revenue because we hit a contract milestone. Anniversarying that, you'll always have some sort of contract milestones hit in quarters, I guess particularly in Q4, but you'll be very substantially less, that plus having a sort of full quarter effect, particularly I think in the German MTR situation, that will be the delta. If you take these out, the underlying position between first half and second half is pretty much unchanged so there's not a, this is not a worsening economic position, it's not a low number of contracts, actually if you look at our order book, you know, in the last two quarters our orders have been up year on year, so it is what we said it is which is we anniversary the big number in Q4, and if you look at Q4 last year, that was I think our best revenue performance for some time and we were very clear to call out the reason for it, and hopefully you've seen that we are trying our best when you've got, in particular a positive item, we call it out so you know what the underlying position is, and we very much called that out, so it's anniversarying that and MTR, that's the key item. Okay, thanks.

Simon Weeden
Citi

Thank you very much. Three relatively quick ones I think, first one may be a bit longer. Just on Wholesale, I notice the costs are flat there this quarter as it happens. Can you elaborate at all on whether there is opportunity to do more there going forwards especially as you presumably carry on seeing an increase in Ethernet in the mix relative to the other business lines. Second quick question on when you expect the net debt raising event - the next net debt - sorry, the next debt raising event needs to come by. And finally just on your hotspots of 2.6 million, I

wondered if you could split them for us between people who are at home who've allowed their hub to be opened up versus public areas.

IL I think on the last one we tried to say that we wouldn't give an exact number but probably the vast majority are going to be Fon hot-spots but we have the largest estate by some distance in the country of Openzone sites and I'd just say to you, wander around central London and you will see particularly, you'll wander around on your Ipad having downloaded the app for it and you will just see the number of Openzone spots and you can travel for a long distance in central London and be connect to Openzone, so we've got by far and away the largest, but numerically of course, with 2.6 million that the vast majority will represent Fon. In terms of Wholesale costs being flat we did see actually, good, transit revenue was pretty robust. I'm never quite sure whether to use the word "good" because it is low margin so the cost - the cost goes with it which is pretty flat this quarter so it's slightly different. Sally anything else you want to say about your future cost reduction plans?

SD Absolutely, there is always more to do, and there is always more opportunity. We just continue to streamline the business, take out complexity, which of course has costs attached to it, and that will continue to drive our cost reduction programme.

IL And Tony, net debt raising?

TC We don't need to raise any net debt. We've got £700 million to pay down in terms of bonds that mature during the quarter, we've got £1.2 billion in cash. No bonds maturing next financial year, we have sufficient cash. Doesn't - this year and next year - doesn't mean that we won't actually go to the market but there's absolutely no need for us to do so.

IL So it would be purely opportunistic if we did.

Simon Weeden Thanks a lot.

IL Apologies to any bankers listening in, sorry.

John Karidis
MF Global

Good morning to you. Just a couple of questions please. Firstly when you were allowed to increase temporarily the rates for local loop unbundling come the next fiscal year, did you know at that time that Ofcom was thinking of weighted average costs of capital for Openreach approximately 150 basis points less than before, and then completely separately, it's a little bit disappointing to hear that YouView is being delayed. It would be really nice to get a straight answer as to how long that delay will be and has there been any other delay on things like, for example, the next generation hub or the Smartphone for the home that we heard about now three quarters ago, should we expect to see those hitting the high street before the end of your current financial year?

IL Yeah, well I mean on the second thing hub three is sitting proudly in my office and it's a very nice looking hub as well and so that will be coming out very shortly, yeah, started shipping hub three and it I think, we started out having the best looking and the best functioning and the best capability hub in the market and we've increased that lead with hub three, so that's going really well. There's a number of things we're doing on Vision irrespective of YouView, and I made that point. I can't give you an update on YouView just now, you've seen some market speculation but I think it's up to the YouView team to say well what do they think and when it's going to happen. Irrespective of YouView there is a number of things we're bringing to the market and, you know, in terms of HD, in terms of iPlayer, so that will continue. I think, in terms of our overall performance on broadband you do see all of these things are feeding in to our overall performance on broadband.

John Karidis Yeah, I'm sorry. Can I ask with regards to the iPlayer for example should we hope to see that on BT Vision due before 31st March this year?

IL Well, thousands of customers already have it, so it's in trial and I think, in probably early spring we'll start rolling it out but there's thousands of customers that already have it so we want to do is go through a bit of a trial thing and the customers who have it really like it, really have been using it a lot so that's coming along. In terms of your comments about temporarily increasing prices I don't quite think we see it that way, but is it a surprise Ofcom did a review of WACC, no because they would, is that final answer on WACC, no it's not because it's a discussion paper, but also we have to look at RAV as well, so when they come to the conclusion about what are they going to do on overall prices for LLU for instance, one of the things like the RAV adjustment has to be looked at and also the price of ducts, because clearly the cost of ducts has gone up. Also things like the cost of copper has gone up, they're very high, so there are a number of issues that have to be looked at, so the WACC whatever it finally is, is only one bit of it and we'll be both making points about the level of the WACC assumptions but also about the level of the net asset value and both of them need to go into, plus efficiency assumptions etc to calculate the final price of LLU or indeed anything else.

Robert Grindle
Deutsche Bank

Good morning. What's the level of interest so far in the trialling of your new duct and pole access product, and then, separately Global Services is very diverse and of course in the UK you've got a government issue, but your average domestic corporate customer in the UK, how are they feeling about the world? Are they sitting tight still or are they starting to think about spending a bit more on telco services in this year, be it hosting or cloud computing, etc, etc, how is the regular average sort of UK domestic corporate thinking at this time?

IL I think it depends which sector on that last point really. I think cloud is always a danger of being a cliché as I keep on saying to a lot of our people. Our customers don't tend to buy clouds. What they buy is things that are better, faster, cheaper and more flexible, stuff like that. The fact that it may have a cloud infrastructure behind them, like our hosted services in a number of areas, is great but most customers shouldn't have to worry about that. I don't think most customers also start off by saying what I want to do this year is spend more on telecom services. What they may wish to do however is expand or they may want to have a more flexible workforce, they may want to have more people on the move, they may want to have new services, and we'll help them. But also a number of them want someone else to run it all for them and I think certainly in some sectors we're seeing people say, you know something, this is getting, from a security point of view, flexibility, resilience point of view, we really shouldn't be running it ourselves, we should really get someone else to do so and that presents opportunities for us, but against that you know there's unquestionably the corporate community, they've got pricing pressures as well, but Jeff I don't know if there's anything you want to add about the general corporate market?

JK I'd say it's all service line related so there's a lot of interest in security, globally, as well in the UK, as unified comms, we're seeing some pick-up in unified comms, with some interest, but nothing really other than that.

IL Yeah, on ducts, I mean ducts are not a silver bullet, duct access, but we certainly come up with a proposition which prices notably cheaper than the European average. Steve, have you been knocked over in the rush for people to start spending money on fibre or is it only BT who's meant to do that?

SR Not quite yet. I mean we were really pleased to get the reference offer out on time, it's just been out for a couple of weeks. Should emphasise that both the duct and pole access is purely for the purposes of next generation access, so it's not a generic passive offer. In terms of a level of interest, all of the infrastructure players have shown a degree of interest, nobody has formally committed to trialling it yet, but as I say it's very, very early days, the reference offer's literally only come out in the last couple of weeks.

IL I'm sure somebody will, although I think there's also been a lot of people that said if only you open, if BT opens their ducts, they would spend billions of pounds and then when it comes to it funnily enough their money isn't exactly where their commitments are. But we shall see.

Stephen Howard
HSBC

I was just wondering about Openreach and Retail strategy with the Infinity fibre product. I suppose my question really boils down to in how much of a hurry are you? Is the most important thing to get people on to the platform quickly which obviously might imply being a bit more aggressive

on the pricing or alternatively are you just taking a view that there's no rush here, you're simply willing to let the appeal of the platform become apparent over time as services like YouView and over the top video and so on make the compelling nature of fibre clearer, and just as a follow on, I think you're in the project of launching a CDN platform in the Wholesale division, I was just wondering if you were getting much traction with that, do you think you can displace the likes of Akamai and so on? Thanks.

IL

On the strategy on Infinity, we already have got a very aggressive price point both at an Openreach and Wholesale level and also at Retail level and yeah, we want to go for volume. We want to make it an easy decision for customers. You know, we're not saying to customers you have to spend £30, £40 or £50 a month to get this, which makes it a niche product, we want to have a good base, and you will get more and more services but I think already the Openreach division has gone aggressively hoping to get lots of people and we've had really very little pushback from customers - from Openreach customers about the rental price which is remarkable and I think at Retail level Gavin and the team have decided to embrace it aggressively. On CDN, I'm not sure we are looking to replace Akamai quite yet, but some interest Sally?

SD

Yes, absolutely, and what we're doing is really rather complementary to many of the CDN players because we have the opportunity to go through deeper into networks, working with the service providers to really minimise their cost of backhaul and to provide them with options for quality of service and providing differentiated options and tiering of services. So what we're doing is actually very different and yes it is gaining some interest in the market.

IL

More to follow I think in that over time.

Andrew Beale
Arete

A couple of questions. First of all on GS cash flow, obviously your projections are very encouraging to see the improvement and the predictability, but can you tell us what we should deduct in terms of cash specific items or provision movements to get to, if I can call it, actual cash, and secondly on Retail, obviously you have some additional competition coming with the TalkTalk roll out of 93% LLU and maybe a bit more Sky for LLU, just wondering if that's something you think you can offset with Infinity and other Retail products so that we don't see too much of an effect from that. Thanks.

IL

Well, I think people have been predicting that Retail would struggle in terms of net adds for a very long time. I guess if you wait long enough there'll be a quarter in which they're right, but I've been pleased by the consistency, we've gone from over 20% net adds in the quarter to 30% to over 40%, but I'm not guaranteeing we'll stay over 50% but I think we feel we've got lots of things we can do and of course the competition is intense, there's no doubt about it, the UK is the most competitive market

in the world, and that's great for the customer but we seem to be doing pretty well in it, and we note some of our competitors have said their strategy now is not to grow their base and that's not our strategy. We think that there's lots of things we're going to bring to the marketplace, but we'll have to see. You know, each quarter is - each quarter is a battle, there's no question about that, and more LLU will certainly make a battle but you know it's - we're talking fairly small percentages of the country now, there's a lot of exchanges to be done get to to 90% of the country, no question about it. In terms of GS specific items, Tony?

TC

Yeah. If you look at the cash flow we're projecting next year, there's no impact in relation to specific items. It's before that and that's the way we make our projections.

David Strauch
Natixis

Thank you. I would like to know if you could share any progress in your discussion with the Pensions Regulator or any idea of timing for the outcome, and also I was wondering if you see potential substantial change in the ULL tariffs from the WACC change or if it would really be limited to the very different items you were mentioning?

IL

Well in terms of ULL tariff, what because of the WACC? I wasn't quite clear when you talked about a much different tariff in the ULL.

David Strauch

Yes, I was wondering the change in WACC could have a substantial impact on the ULL tariff, or as you were mentioning different items in the discussion with Ofcom, you expect whatever the case the change will be limited.

IL

Yeah, it won't have a huge impact. We said the change in the WACC, if you took it across the full range of regulated products, would be some tens of millions of pounds across the group and of course ULL would be only part of that and that is without taking account of any changes towards the asset values in an upward direction, so I'm sure we will have a long and interesting discussion, I use the word in the widest possible sense, about ULL and other pricing with the regulator and that's - I don't think that's going to be a huge item in terms of the overall Group. In terms of the Pensions Regulator, regretfully I can't really tell you much more. The Pensions Regulator have a lot to look into given the - given what's happened on the Guarantee, given that you'll have had the confirmation of the state guaranteeing virtually all of the people in it and also on CPI they've got quite a lot on their plate to look into so we'll have to see how they take it, and when we know, don't worry, we will tell the market.

Jerry Dellis
Jefferies

Two questions please. The first one on Retail, I think in the past you've talked about the expectation of steady quarter on quarter improvements. Given the bit of a step change this quarter, is that still the outlook that you

see on the Retail side? Then just in terms of your sort of up trading of customers be it onto BT Vision or to fibre or to the Sky TV service, when you look at where those customers are really coming from, is there anything you can say about how the mix divides between sort of your installed base between customers who were previously customers of the unbundlers and maybe people coming off cable?

IL I'm not sure, on Retail, that we said steady improvement. I think we would see improvement in Retail trends is what - when you do releases quarterly you have movements around the place and a different number of days in quarters etc, nothing is entirely steady when we're talking about a -2 or a -3 or a -4%, but we would overall expect to see improving trends in Retail and what you see in BT Business and actually Consumer this quarter is a sign of that, and it's also why the KPIs are important because they also feed through to the revenue trends. In terms of, Gavin, of where are the customers who are taking Infinity coming from and things like Vision and things like that, do you want to say?

GP I mean Infinity customers, you won't be surprised, it's a mix between existing customers upgrading it when they come to the end of a contract, but we've been quite pleased at how attractive it's been to new customers. I'm not going to give the split, as we're trying not to give too much, too many data points, but it's a mixture of both and we've been encouraged by the attraction to new to BT customers.

IL Yeah, I see in overall numbers we must be winning customers from other providers because of the sheer scale of our adds and you know ourselves and Sky combined, there must be clearly some losers somewhere in the market place. And with that look thank you all on a very busy day, appreciate your time, and have a very good day. Thank you.