Group performance
Group Finance Director's introduction

Our results this year have been significantly impacted by the findings from our investigation into our Italian business, Openreach's historical practices on Deemed Consent and the headwinds we face in the UK public sector and international corporate markets. The performance of our UK consumer, business and wholesale activities have been in line with our expectations and the integration of EE into the group is going well.

Our results for the year were below our expectations. We saw good performance from our UK consumer, business and wholesale activities but this was more than offset by what we found in our Italian business, Openreach's historical practices on Deemed Consent and the headwinds we face in the UK public sector and international corporate markets.

Reported revenue increased by 27% to £24.1bn. Our key measure of the group's revenue trend, underlying revenue[a] excluding transit adjusted for the acquisition of EE, was down 0.2%.

Our investigation into our Italian business identified £268m of prior year errors, for which we revised the prior periods, and a specific item charge of £260m in the current year for changes in accounting estimates and investigation costs. We've also recorded a specific item charge of £342m following Ofcom's investigation into Openreach's historical practices on Deemed Consent. Our reported operating profit, which includes specific items, was down 12%. Our adjusted[b] operating profit was up 8% reflecting a strong first year contribution from EE.

Reported profit before tax was down 19% to £2.4bn and adjusted[b] profit before tax was £3.5bn, up 5%. Reported EPS of 19.2 pence was down 33% and adjusted EPS of 28.9 pence was down 9%.

Net cash inflow from operating activities was £6.2bn, up 20%, whilst normalised free cash flow[c] was £2.8bn, down 10% which includes earlier than expected customer collections that will reverse next year.

In addition, we are also expanding and accelerating areas of our cost transformation programme. We are simplifying our central Group Functions and our internal service unit, Technology, Service & Operations. We are also restructuring the Global Services organisation and accelerating ongoing transformation programmes in other lines of business. We anticipate that these transformation programmes will cost around £300m over the next two years, with most of this being incurred in 2017/18. This restructuring cost will be treated as a specific item and will payback in about 2 years.

For 2017/18, we continue to expect underlying revenue excluding transit to be broadly flat year on year and adjusted EBITDA to be in the range £7.5bn to £7.6bn.

Simon Lowth

Simon Lowth
Group Finance Director
11 May 2017

Alternative Performance Measures
We assess the performance of the group using a variety of performance measures. These measures are not defined under IFRS and therefore termed 'non-GAAP' measures. A reconciliation from these non-GAAP measures to the nearest prepared measure in accordance with IFRS is presented on pages 252 to 254. The alternative performance measures we use may not be directly comparable with similarly titled measures used by other companies.

[a] Excludes specific items, foreign exchange movements and disposals and is calculated as though EE had been part of the group from 1 April 2015.
[b] Before specific items, which are defined on page 252.
[c] Before specific items, pension deficit payments and the cash tax benefit of pension deficit payments.

Group performance continued
Summary financial performance for the year

Performance against our outlook

We did not achieve the financial guidance we set out at the beginning of the year. We were in line with the revised guidance we issued in January 2017.

2016/17 performance against our outlook

	Outlook provided in May 2016	Outlook provided in January 2017	Result
Change in underlying revenue excluding transit[a]	Growth	Broadly flat	(0.2)%
Adjusted EBITDA[a]	c£7.9bn	c£7.6bn	£7.6bn
Normalised free cash flow[a]	£3.1bn – £3.2bn	c£2.5bn	£2.8bn
Dividend per share	≥10% growth	≥10% growth	15.40p, +10%
Share buyback	c£200m	c£206m	£206m

[a] Defined on pages 252 to 254.

Reported revenue increased by 27% to £24.1bn. Underlying revenue excluding transit adjusted for the acquisition of EE was down 0.2%, below our original outlook of growth. This was in line with the outlook we revised in January of broadly flat.

Adjusted EBITDA grew 18% to £7.6bn. This was below our original outlook of approximately £7.9bn and in line with the outlook we revised in January.

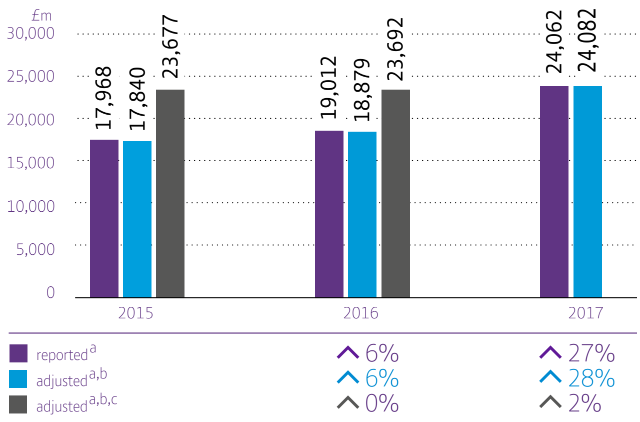
Normalised free cash flow was £2.8bn, down 10% and below our original outlook, but almost £300m above our revised outlook, due to early customer collections that will reverse in 2017/18.

Outlook for 2017/18

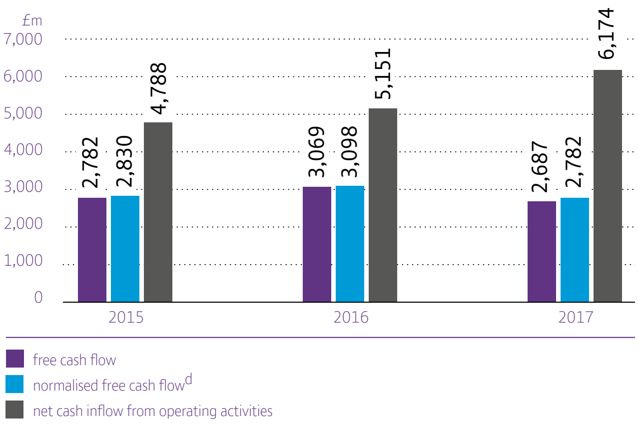
Change in underlying revenue excluding transit[a]	Broadly flat
Adjusted EBITDA[a]	£7.5bn – £7.6bn
Normalised free cash flow[a]	£2.7bn – £2.9bn
Dividend per share	Progressive
Share buyback	c£100m

[a] Defined on pages 252 to 254.

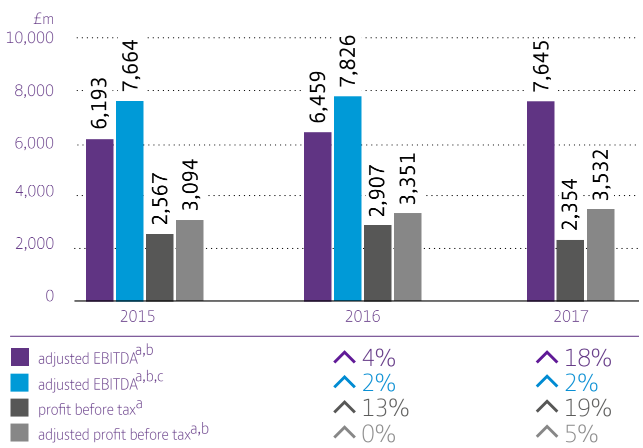
Revenue
Year ended 31 March



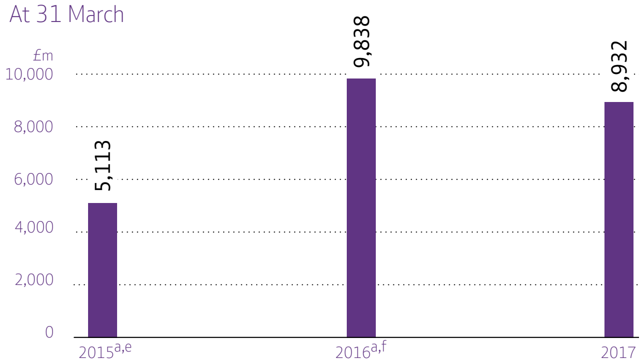
Cash flow
Year ended 31 March



Profit
Year ended 31 March



Net debt
At 31 March



[a] Certain prior year results have been revised to reflect the outcome of the investigation into our Italian business. See note 1 to the consolidated financial statements.
[b] Items presented as adjusted are stated before specific items. See page 252 for further details.
[c] Calculated as though EE had been part of the group from 1 April 2014. For 2016/17, no separate measure is shown as EE was part of the group for the full year and there is no difference to the adjusted measures.
[d] See definition on page 254 and summarised cash flow statement on page 96.
[e] Includes the impact of the £1.0bn equity placing we made in February 2015.
[f] Reflects the impact from EE.

For 2017/18, we continue to expect underlying revenue excluding transit to be broadly flat year on year. Adjusted EBITDA is expected to be £7.5bn - £7.6bn.

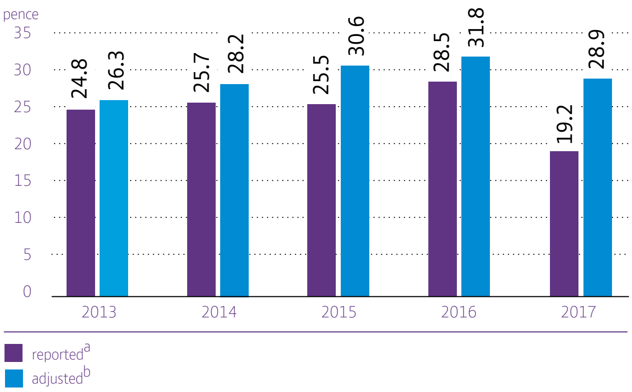
Our outlook for normalised free cash flow over the cumulative two year period 2016/17 and 2017/18 remains broadly unchanged. However, normalised free cash flow in 2016/17 of £2,782m was almost £300m above our outlook of around £2.5bn, due to early customer collections that will reverse in 2017/18. As such, normalised free cash flow in 2017/18 is now expected to be £2.7bn - £2.9bn, from £3.0bn - £3.2bn previously.

This outlook is provided on the basis of our existing investment plans. However, we continue to evaluate a range of additional investment opportunities. Our decision on whether to move forward with these will be affected by a number of factors, including the outcome of Ofcom's Wholesale Local Access Market Review, responses to Openreach's consultations and the results of any future spectrum auctions.

Our underlying dividend policy remains unchanged: to deliver progressive dividends while balancing the need to invest in the business, support the pension fund and maintain a strong balance sheet. The Board has concluded that a dividend increase of 10% in 2016/17 remains appropriate. However, given the importance of maintaining flexibility for additional investment and the range of potential outcomes, dividend growth in 2017/18 will be lower than the 10% previously anticipated. The rate of future dividend growth will reflect a number of factors, including underlying medium term earnings growth, the level of investment spending and other cash commitments. The Board believes that this dividend policy appropriately balances the interests of all stakeholders and provides a solid foundation for future growth, underpinned by an ongoing commitment to investment that delivers sustainable long-term value for customers and shareholders.

We expect to buy back around £100m of shares in 2017/18 to help counteract the dilutive effect of all-employee share option plans maturing in the year. This is below the £206m buyback we completed in 2016/17 reflecting the lower number of shares that are expected to be required for our share option plans.

Earnings per share
Year ended 31 March



Proposed full year dividend
Year ended 31 March

15.4p +10%
2017

14.0p
2016

Transforming our costs

Our integration of EE is going well. We've achieved around £150m of run-rate cost synergies in our first year, exceeding our target of £100m, as we've been able to realise synergies earlier than originally planned. We continue to expect cost synergies to reach a run-rate of around £400m in the fourth year. We've delivered savings this year through renegotiating supplier terms and reducing the number of head office employees. We've also insourced a number of activities where possible, including all roaming management, EE Facilities management and core mechanical and engineering field operations.

We are also expanding and accelerating areas of our cost transformation programme. We are simplifying our central Group Functions and our internal service unit, Technology, Service & Operations to improve the effectiveness and efficiency of the services and infrastructure delivered to our lines of business. We are also restructuring the Global Services organisation and accelerating ongoing transformation programmes in other lines of business. We anticipate that these transformation programmes will save in total around £300m over two years, with a restructuring charge of around £300m over the next two years, with most of this being incurred in 2017/18. This restructuring cost will be treated as a specific item. These changes will clarify accountabilities, remove duplication and improve efficiencies, removing around 4,000 roles mainly from managerial and back office areas. The cost savings will provide headroom to offset market and regulatory pressures and support increased investment in delivering great customer experience and leading networks.

Prior year revision and re-classifications

Investigation into our Italian business

Our investigations into our Italian business revealed inappropriate behaviour and improper accounting practices. We identified £268m of errors in relation to prior years and a specific items charge of £260m in the current year for changes in accounting estimates and investigation costs.

Revised presentation of cash pooling arrangements

We've also revised the presentation of our cash pooling arrangement following the release of an IFRIC clarification on IAS 32 'Financial instruments presentation offsetting and cash pooling arrangements' in April 2016. This requirement resulted in us grossing up cash and cash equivalents and short-term loans and other borrowings by £499m at 31 March 2016 and £414m at 31 March 2015 with no impact on the income statement.

EE purchase price accounting

Subsequent to our 29 January 2016 acquisition of EE, we've finalised our purchase price accounting within the period allowed under IFRS 3 'Business Combinations'. We also received £20m from the previous owners of EE as a result of the finalisation of the audit of the completion balance sheet. The changes after considering taxation resulted in an increase in goodwill of £29m as of 31 March 2016 with no material impact on the income statement.

The effect on prior years' income statement, balance sheet and cash flow statements is set out in page 172 to 176 in note 1 to the financial statements.

Summarised income statement

Year ended 31 March Before specific items	2017 £m	2016[a] £m	2015[a] £m
Revenue	**24,082**	**18,879**	**17,840**
Operating costs[b]	(16,437)	(12,420)	(11,647)
EBITDA	**7,645**	**6,459**	**6,193**
Depreciation and amortisation	(3,510)	(2,631)	(2,538)
Operating profit	**4,135**	**3,828**	**3,655**
Net finance expense	(594)	(483)	(560)
Associates and joint ventures	(9)	6	(1)
Profit before taxation	**3,532**	**3,351**	**3,094**
Taxation	**(663)**	**(607)**	**(631)**
Profit for the year	**2,869**	**2,744**	**2,463**

[a] The comparative information of the current period results has been revised to reflect the outcome of the investigation into our Italian business.
[b] Excluding depreciation and amortisation.

Revenue
Reported revenue, which includes specific items, was up 27%. Adjusted revenue was up 28% at £24,082m. Both of these increases were driven by the impact of EE being part of the group for the full year.

We had a £522m positive impact from foreign exchange movements and a £64m reduction in transit revenue. Excluding these, underlying revenue excluding transit adjusted for the acquisition of EE was down 0.2% (2015/16: up 1.9%) which is consistent with our expectation of being broadly flat in the current year. This outlook was revised in our third quarter results following the challenging conditions in the UK public sector and international corporate markets and the impact of the issues in our Italian business.

Consumer revenue was up 7% with a 13% increase in broadband and TV revenue and a 4% increase in calls and lines. EE underlying revenue adjusted for the acquisition of EE was up 1% mainly due to the success of our 'more for more' pricing strategy. Openreach revenue was flat with the impact of regulatory price reductions offsetting the continued growth in fibre. Underlying revenue excluding transit adjusted for the acquisition of EE was down 3% in Wholesale and Ventures as a result of the continuing decline in Partial Private Circuits and call volumes. Business and Public Sector underlying revenue excluding transit adjusted for the acquisition of EE was down 6% due to the decline in UK public sector revenue. Global Services underlying revenue excluding transit adjusted for the acquisition of EE was down 2% and excluding revenue from our Italian business was flat.

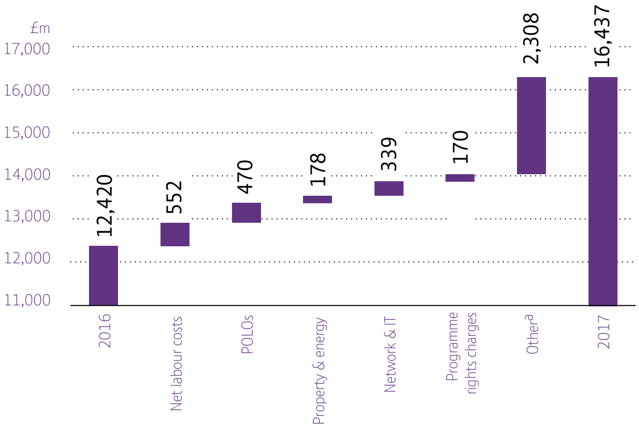
You can see a full breakdown of reported revenue by major product and service category in note 4 to the consolidated financial statements.

Operating costs
Reported operating costs were up 36% while adjusted operating costs before depreciation and amortisation increased 32%.

Our adjusted operating costs before depreciation and amortisation were £16,437m, up £4,017m (2015/16: £773m) driven by the acquisition of EE and adverse impact of foreign exchange. For the group, other operating costs were up £2,308m or 61%, primarily reflecting EE's subscriber acquisition and retention costs, and adverse foreign exchange movements.

Underlying operating costs excluding transit adjusted for the acquisition of EE were up 1%. This reflects additional UEFA rights costs and the new Premier League rights contract, increased investment in mobile handsets and continued investment in improving customer experience, offset by the benefits of our cost transformation programme.

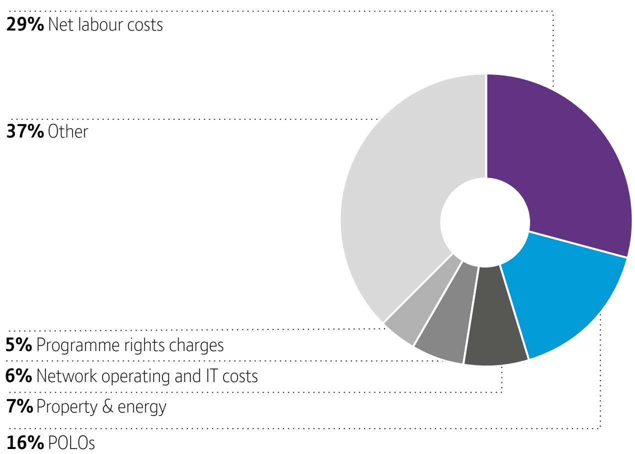
Operating costs before depreciation, amortisation and specific items
Year ended 31 March



[a] Includes all other movements in costs.

Programme rights charges increased £170m to £714m, primarily reflecting our investment in BT Sport. Property and energy costs were up 17%, payments to telecommunications operators (POLOs) were up 22% and network, operating and IT costs were up 53%, with these all being impacted by EE. Net labour costs increased by 13% despite a reduction in leaver costs of £23m (2015/16: £109m) due to the impact of EE.

2016/17 operating costs[a]



[a] Excluding depreciation, amortisation and specific items.

You can see a detailed breakdown of our operating costs in note 5 to the consolidated financial statements.

EBITDA

Adjusted EBITDA, which is before specific items, was £7.6bn which is in line with the 2016/17 outlook as revised in January.

Underlying EBITDA adjusted for the acquisition of EE was down 3%. This is mainly as a result of declines in UK public sector and our investment in improving customer experience.

You can see further details for EBITDA for the lines of business on pages 56 to 90.

Specific items

As we've explained on page 91, in this performance review we primarily explain our results before specific items. That's because this is how we measure the sustainable performance of our business.

The table below outlines items we've treated as specific items:

Year to 31 March	2017 £m	2016 £m	2015 £m
Specific revenue			
Italian business investigation (see page 6)	22	–	–
Regulatory matters	(2)	(203)	(128)
EE fair value adjustment	–	70	–
Specific revenue	**20**	**(133)**	**(128)**
Specific operating costs			
Regulatory matters (see page 7)	481	203	75
Italian business investigation (see page 6)	238	–	–
EE acquisition and integration costs	215	116	19
Out of period irrecoverable VAT	30	–	–
Profit on disposal of businesses	(16)	–	(6)
Property rationalisation costs	–	29	45
Restructuring charges	–	–	315
Profit on disposal of property	–	–	(67)
Specific operating costs	**948**	**348**	**381**
Specific net finance expense	**210**	**229**	**299**
Profit on disposal of interests in associates and joint ventures	**–**	**–**	**(25)**
Tax credit	**(217)**	**(166)**	**(121)**
Net specific items charged after tax	**961**	**278**	**406**

This year, specific items resulted in a net charge after tax of £961m (2015/16: £278m).

There was a net charge of £260m (2015/16: nil) arising from changes in accounting estimates regarding the carrying value of the assets and liabilities of our Italian business, including professional fees incurred.

We've recognised a net cost of £479m (2015/16: £nil) in relation to regulatory matters. These are made up of the following:

– Deemed Consent: A charge of £342m was recognised (2015/16: £nil) in relation to Ofcom's March 2017 findings on our historical practices over the use of Deemed Consent. This includes a fine of £42m which has been imposed and we've also agreed to compensate Communication Providers, with the precise amount of the compensation to be determined but currently estimated at £300m.
– Re-assessment of other regulatory risks: We've also re-assessed our regulatory risks in light of recent regulatory decisions by Ofcom and the Competitions Appeals Tribunal. As a result we've increased our net provision by £137m (2015/16: £nil) in the year.
– Ladder pricing agreements: In 2016/17 we recognised revenue and costs of £8m (2015/16: £203m) being the prior year impacts of ladder pricing agreements with the other UK mobile operators.

We incurred £215m of EE integration costs (2015/16: EE acquisition-related costs £99m and integration costs of £17m). This includes a £62m (2015/16: £nil) specific amortisation charge relating to the write off of IT assets as we integrate the EE and BT IT infrastructure.

We recognised an out of period irrecoverable VAT charge of £30m during the year (2015/16: £nil) and a £1m interest expense. In addition to the above, we also treated a number of other items as specific, such as the net interest expense on pensions of £209m (2015/16: £221m). The decrease from 2015/16 mainly reflects a fall in the IAS 19 discount rate between 31 March 2016 and 31 March 2017.

We also recognised a tax credit of £63m (2015/16: £96m) for the re-measurement of deferred tax balances due to the upcoming changes in the UK corporation tax rate from 20% to 19% from 1 April 2017 and to 17% from 1 April 2020. The tax credit on specific items (excluding the re-measurement of deferred tax) was £154m (2015/16: £70m).

In 2015/16, we recognised a fair value adjustment on the acquisition of EE which reduced the amount of revenue recognised between acquisition and 31 March 2016.

You can see details of all revenue and costs that we have treated as specific items in the income statement in the last three years in note 8 to the consolidated financial statements.

Profit before tax

Reported profit before tax (which includes specific items) was down 19% to £2,354m while adjusted profit before tax was up 5% at £3,532m, due to the contribution from EE.

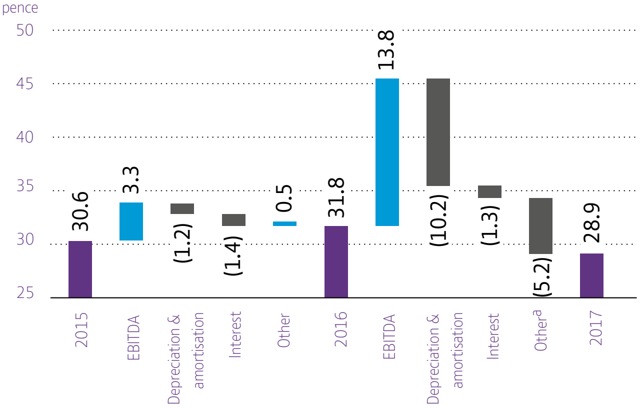
We discuss depreciation, net finance expense and tax in later sections of this performance review.

Earnings per share

Reported earnings per share, which includes specific items, was 19.2p, down 33%, while adjusted earnings per share decreased 9% to 28.9p.

Adjusted earnings per share is one of our key performance indicators (see pages 20 and 21) and has decreased by 6% over the past two years. The graph below shows the key drivers of this decrease.

Adjusted earnings per share
Year ended 31 March



[a] Other primarily reflects the impact of the change in the weighted average number of shares.

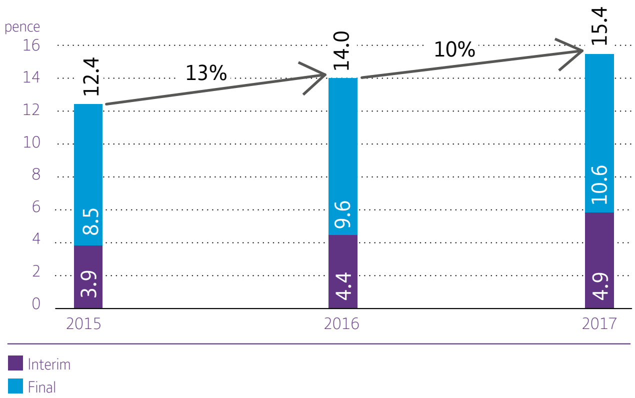
Dividends

The Board is proposing a final dividend to shareholders of 10.55p, up 10%. This brings the full year dividend to 15.40p, also up 10%, and compares with an increase in the 2015/16 full year dividend of 13%.

This year's dividend is in line with our outlook. It will be paid, subject to shareholder approval, on 4 September 2017 to shareholders on the register on 11 August 2017.

Dividends per share

Year ended 31 March



The Board has reviewed the group's dividend policy and continues to believe that a policy of paying progressive dividends is the most appropriate. The Board believes this best aligns with the group's financial objectives of growing sustainable profitable revenue growth and transforming the cost base in order to drive long-term growth in cash flows. In reaching this decision, the Board took into account forecasts for future debt reduction as well as the level of dividend cover expected over the medium-term. BT Group plc has sufficient distributable reserves to support the dividend policy.

We've set out our dividend expectations for 2017/18 in our Outlook on page 92.

Cash flow

We generated a net cash inflow from operating activities of £6,174m and normalised free cash flow of £2,782m, down £316m or 10%, which is above our outlook as revised in January of c£2.5bn for the year due to earlier than expected customer collections that we will now not receive next year.

Free cash flow

Normalised free cash flow decreased 10% to £2,782m, partly reflecting increased payments for the Premier League, UEFA Champions League and UEFA Europa League broadcast rights.

The net cash cost of specific items was £205m (2015/16: £232m). This included: EE acquisition and integration related costs of £111m (2015/16: £114m); restructuring costs of £51m (2015/16: £85m); and ladder pricing payments of £1m (2015/16: £41m receipts).

Summarised cash flow statement

Year ended 31 March Before specific items	2017 £m	2016[a] £m	2015[a] £m
EBITDA	7,645	6,459	6,193
Capital expenditure[b]	(3,119)	(2,431)	(2,403)
Net interest	(622)	(541)	(573)
Taxation[c]	(661)	(459)	(415)
Working capital movements	(382)	(12)	(150)
Other non-cash and non-current liabilities movements	(79)	82	178
Normalised free cash flow	**2,782**	**3,098**	**2,830**
Cash tax benefit of pension deficit payments	110	203	106
Specific items	(205)	(232)	(154)
Free cash flow	**2,687**	**3,069**	**2,782**
Pension deficit payments	(274)	(880)	(876)
Dividends	(1,435)	(1,075)	(924)
Disposals and acquisitions	51	(3,379)	10
Share buyback programme	(206)	(315)	(320)
Proceeds from issue of own shares	70	90	1,201
Reduction (increase) in net debt from cash flows	893	(2,490)	1,873
Net debt at 1 April	(9,838)	(5,113)	(7,023)
Reduction (increase) in net debt from cash flows	893	(2,490)	1,873
Non-cash movements	13	(2,235)	37
Net debt at 31 March	**(8,932)**	**(9,838)**	**(5,113)**

[a] Certain prior year results have been revised to reflect the outcome of the investigation into our Italian business. See note 1 to the consolidated financial statements.
[b] Net of government grants.
[c] Excluding cash tax benefit of pension deficit payments.

Free cash flow, which includes specific item outflows of £205m (2015/16: £232m) and a £110m (2015/16: £203m) tax benefit from pension deficit payments, was £2,687m (2015/16: £3,069m).

We made pension deficit payments of £274m (2015/16: £880m) and paid dividends to our shareholders of £1,435m (2015/16: £1,075m).

We spent £206m (2015/16: £315m) on our share buyback programme to help counteract the dilutive effect of our all-employee share option plans maturing. Exercises of share options generated proceeds of £70m (2015/16: £90m).

Non-cash movements within net debt in the prior year primarily reflect £2,107m of net debt acquired with EE.

You can see a reconciliation to normalised free cash flow from the net cash inflow from operating activities, the most directly comparable IFRS measure, on page 254.

Capital expenditure

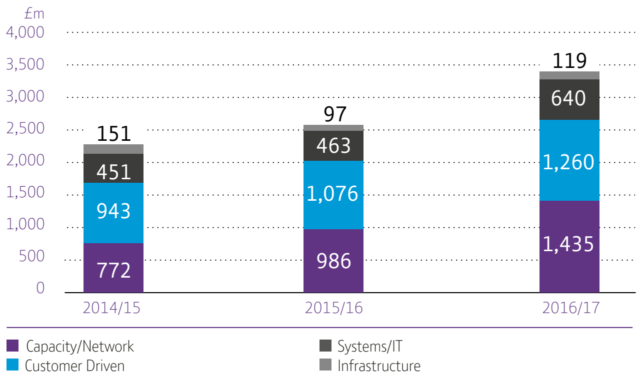
We continue to make significant investments in line with our strategy including a focus on improving customer experience.

The Design Council is accountable to the *Operating Committee* for delivering an efficient and optimised investment plan, aligning investment decisions across our networks, systems, platforms and products so that they are directed towards our strategic priorities.

2016/17 is the first full year including EE. Capital expenditure therefore includes the investment EE is making to expand coverage, improve network speed and performance while continuing to offer innovative products and excellent customer experience. We're also investing in the integration of EE into the wider group to drive both revenue and cost synergies.

For the year, our capital expenditure, inclusive of net grant deferral was £3,454m (2015/16: £2,622m, 2015/14: £2,317m). The table below shows the split of our investments by major category.

Capital expenditure
Year ended 31 March



In recent years we've prioritised our capital expenditure to underpin our strategy to deliver sustainable revenue growth, and to expand coverage and capacity while enhancing speed and resilience of both our fixed access network and our mobile network. Key investments this year include:

Capacity/network investments

- increasing the footprint of our superfast fibre broadband network, including extending the reach of superfast broadband to rural areas under the BDUK programme. We've now passed more than 26.5m homes and businesses;
- the launch of our Ultrafast broadband trial now with 500K premises passed;
- enhancing and expanding our mobile network coverage, including the delivery of the ESN contract; and
- continued investment in convergence of fixed and mobile services.

Customer driven investments

- continued development of customer contract-specific infrastructure for our global clients; and
- deployment of Ethernet, including reduction in the existing workstack, and copper/fibre connections to homes and businesses.

Systems/IT investments

- improving customer experience by enhancing our online contact systems, order and repair journeys as well developing new products, such as our nuisance calls blocker.

Non-network infrastructure

- Investment in our property estate, including integration of EE and BT people into the same locations.

Capital expenditure was £3,454m (2015/16: £2,622m). This consists of gross expenditure of £3,426m (2015/16: £2,731m) which has been increased by net grant deferral of £28m (2015/16: £109m decreased by net grant funding) mainly relating to deferral of grant funding in the BDUK programme. This is driven by the base-case assumption for take-up in BDUK areas being increased to 39% of total homes passed following our review of the level of customer take-up. While we have recognised gross grant funding of £160m (2015/16: £338m) in line with network build in the year, we have also deferred £188m (2015/16: £229m) of the total grant funding to reflect higher take-up levels on a number of contracts. The increase in take-up assumption shows the high demand on our fibre network driven by customers taking advantage of faster speeds to consume more data. To date we have deferred £446m (2015/16: £258m).

Of the total group capital expenditure £69m (2015/16: £5m) related to the integration of EE. Additionally, £272m, (2015/16: £248m, 2014/15: £231m) arose outside the UK. Capital expenditure contracted but not yet incurred was £889m at 31 March 2017 (2015/16: £922m, 2014/15: £507m).

Depreciation and amortisation

Depreciation and amortisation has increased by 33% to £3,510m (2015/16: £2,631m, 2014/15: £2,538m) due to the inclusion of EE depreciation and amortisation for the full financial year.

Net debt

Net debt decreased by £906m to £8,932m, reflecting strong cash generation by the business.

We have achieved this while making investments for the future of our business including research and development, and sports and TV content, supporting our pension fund and funding our share buyback programme. We have also paid progressive dividends to our shareholders.

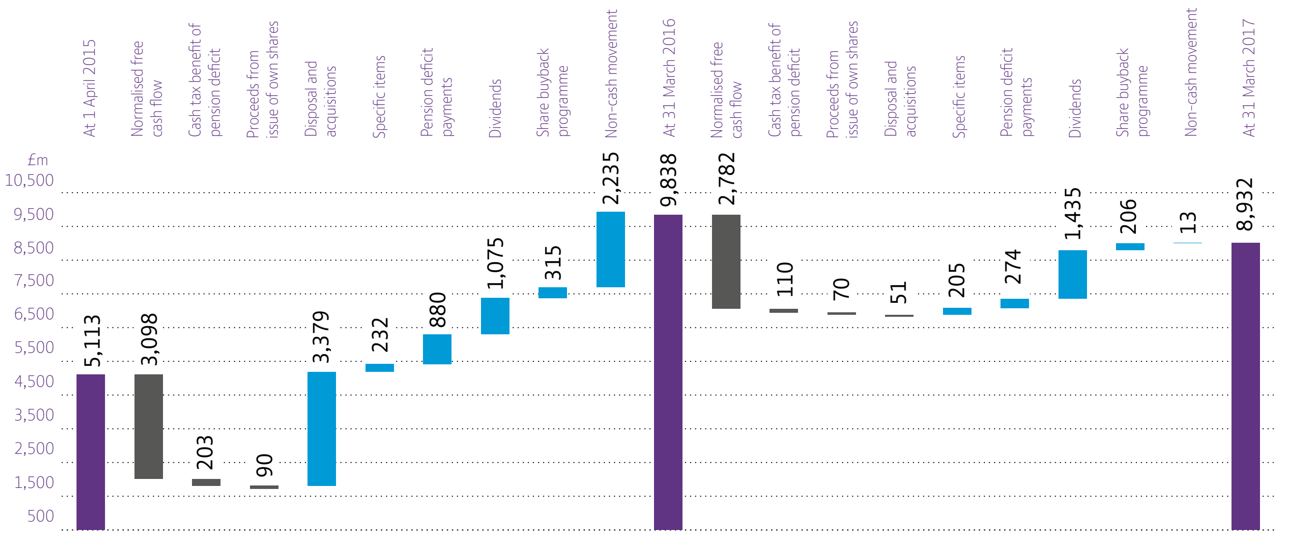
Gross debt, translated at swap rates and excluding fair value adjustments, at 31 March 2017 was £10,980m. This comprises term debt of £9,680m, finance leases of £229m, bank loans of £350m, and other loans of £721m.

Bond maturities in June 2016, December 2016 and February 2017 resulted in a total cash outflow of £1,787m.

We have decreased our current investments and cash and cash equivalent by £1,866m, reflecting the funding of bond maturities and cash requirements of the business.

The table below shows the key movements in net debt over the past two years.

Movements in net debt



The table below shows the key components of our net debt and of the £906m decrease this year.

£m	At 1 April 2016	Term debt issuance/ (maturities)	Other cash flow	Fair value move-ments	Foreign exchange	Transfer to within one year	Other move-ments	**At 31 March 2017**
Debt due within one year[a]	3,736	(1,787)	(1,038)	–	333	1,399	(11)	2,632
Debt due after one year	11,025	–	4	(29)	471	(1,399)	9	10,081
Impact of cross-currency swaps[b]	(652)	–	–	–	(767)	–	–	(1,419)
Removal of accrued interest and fair value adjustments[c]	(357)	–	–	29	–	–	14	(314)
Gross debt	**13,752**	**(1,787)**	**(1,034)**	**–**	**37**	**–**	**12**	**10,980**
Less:								
Cash and cash equivalents	(996)	–	505	–	(38)	–	1	(528)
Current assets investments	(2,918)	1,787	(364)	–	(29)	–	4	(1,520)
Net debt	**9,838**	**–**	**(893)**	**–**	**(30)**	**–**	**17**	**8,932**

[a] Including accrued interest and bank overdrafts.
[b] Retranslation of debt balances at swap rates where hedged by cross-currency swaps.
[c] Removal of accrued interest applied to reflect the effective interest rate method and removal of fair value adjustments.

The impact of foreign exchange on net debt includes the impact of translation on finance leases, short-term borrowings, investments and cash balances. This also includes the benefit of translating our debt balances to Sterling at swap rates.

Financing and debt maturity

The main source of our cash inflow in recent years has been the cash generated from our operations.

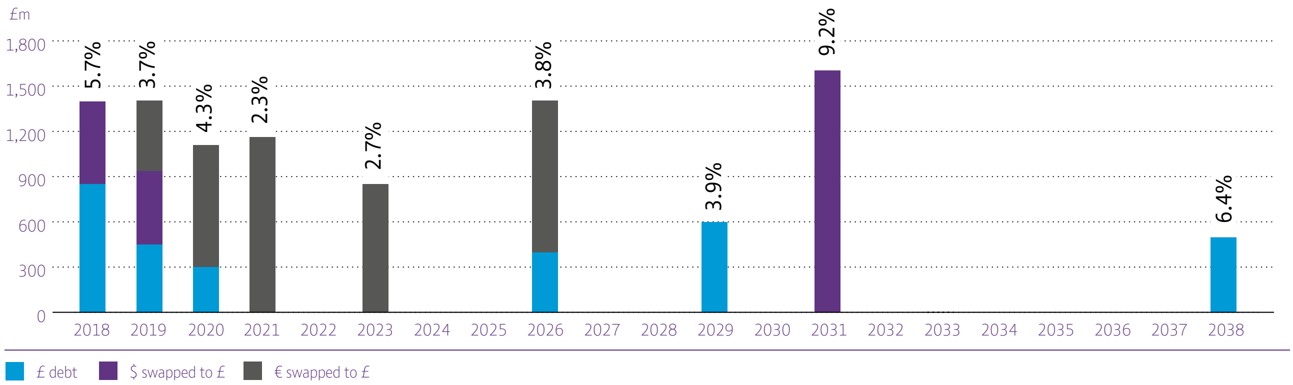
We increased our undrawn revolving committed credit facility from £1.5bn to £2.1bn in June 2016. This facility has been extended by one year and will now mature in September 2021. In addition, we entered into a new 364-day revolving bridge facility of £1.5bn maturing in March 2018, with the option to renew to March 2019. The bridge facility contains mandatory prepayment and cancellation clauses in certain circumstances, such as the issuance of public debt securities. This facility was undrawn as at 31 March 2017.

In July 2016 the remaining £181m of the EE acquisition facility was repaid.

We have term debt of £1,399m, at swap rates, and other debt of £735m maturing in 2017/18.

Maturity profile of term debt and average coupon rate

At 31 March



Net finance expense

Reported net finance expense has increased £92m to £804m. Adjusted net finance expense of £594m increased by £111m due to our average net debt being higher than last year as a result of our acquisition of EE.

We've shown below an overview of our average gross debt, investments and cash balances, and net debt and the related weighted average interest rates over the past three years. The weighted average interest rate on net debt reduced from 7.4% to 5.9% as the new debt issuances and debt acquired from EE are at lower interest rates than the average rate of the existing debt.

You can see a reconciliation of net finance expense to net interest cash outflow in note 26 to the consolidated financial statements.

Year ended 31 March Before specific items	**2017** **£m**	2016 £m	2015 £m
Average gross debt	12,217	9,030	9,007
Weighted average interest rate on gross debt	4.6%	5.4%	6.0%
Average investments and cash balances	2,817	2,616	2,446
Weighted average interest rate on investments	0.3%	0.4%	0.4%
Average net debt	9,400	6,414	6,561
Weighted average interest rate on net debt[a]	5.9%	7.4%	8.1%

[a] Excludes interest relating to unwinding of discount on provisions and derivatives not in a designated hedge relationship.

Taxation

Our effective tax rate before specific items was 18.8% (2015/16: 18.1%). We paid income taxes of £551m (2015/16: £256m).

Our tax contribution

We are proud to be a major contributor of taxes to the UK economy. In 2016 we bore UK taxes of £893m and collected £2,985m of taxes. The One Hundred Group 2016 Total Tax Contribution Survey ranked us as the 5th highest contributor in the UK.

We paid UK corporation tax of £471m. We benefited from £117m of EE's historical tax losses (2015/16: £20m) and £110m from tax deductions associated with employee pension and share schemes (2015/16: £208m).

Our approach to tax

We seek to ensure that our business develops in a tax-efficient manner that embodies our wider corporate purpose. In doing this we, comply with the tax rules of the countries where we do business and deal with their tax authorities in an open and constructive manner. We take the benefit of widely claimed tax incentives and apply OECD principles.

Tax governance

We maintain a limited appetite for tax risk by requiring a strong connection between tax planning and our business, and by requiring reasonably likely publicity to be neutral in nature. We seek out opportunities that meet these requirements where there is reasonable tax technical merit and we are confident that we can manage any organisational complexities.

We have a framework for managing taxes that is set centrally and agreed by the Board. We employ suitably qualified professionals to manage the operation of this framework, who report to the group finance director. Compliance with this framework is tested by our internal audit function.

Tax expense

Our tax expense recognised in the income statement before specific items was £663m (2015/16: £607m). In addition we recognised a £445m tax credit (2015/16: tax charge of £235m) in the statement of comprehensive income, principally in relation to our pension scheme.

We expect our income statement effective tax rate before specific items to be around the UK rate of corporation tax, as the majority of our business occurs in the UK. In the current year, our rate is lower than this because we recognised tax credits in respect of historical overseas tax losses and prior period tax items.

The UK tax rate fell to 19% on 1 April 2017 and will fall to 17% on 1 April 2020, which should reduce our expected effective tax rate. Recognition of further deferred tax assets on historical overseas tax losses would also reduce our future rate. Changes to our estimates of uncertain tax positions may increase or reduce our future rate.

Year ended 31 March Before specific items	2017 %	2016 %	2015 %
Tax at UK statutory rate	20.0	20.0	21.0
Non-UK results taxed at different rates	0.3	(0.2)	0.6
Net permanent differences	0.7	0.3	–
	21.0	**20.1**	**21.6**
Changes to prior year estimates	(1.1)	(2.5)	(1.1)
Deferred tax accounting for non-UK losses	(1.1)	0.5	(0.1)
Effective tax rate	**18.8**	**18.1**	**20.4**

We have booked a tax benefit of £39m in respect of UK patent incentives (2015/16: £37m). We do not expect this to be affected materially by the OECD's Base Erosion and Profit Shifting project.

Key tax risks

Our key uncertainties are whether EE's tax losses will be available to us, whether our intra-group trading model will be accepted by a particular tax authority and whether intra-group payments are subject to withholding taxes.

Additionally we have extensive and long standing UK operations that necessarily require the use of estimates. We routinely work with HMRC to validate these estimates.

Tax losses

We have an asset of £270m relating to tax losses on our balance sheet. This relates mainly to historical tax losses acquired with EE. We expect to be able to use this against future profits of EE.

In addition we have £4.2bn of income tax losses that we've not given any value to on our balance sheet. We might be able to use these losses to offset future profits, however we currently do not consider this probable. We also have £17.0bn of UK capital losses, which we have no expectation of being able to use.

We've given more details in note 9 to the consolidated financial statements.

Summarised balance sheet

Our balance sheet reflects our significant investment in the network infrastructure assets that are the foundation of our business, as well as the working capital with which we manage our business day by day. It also reflects the longer-term strategy with which we finance our investment, and our obligation to the pension fund.

At 31 March	2017 £m	2016[a] £m	Movement £m
Property, plant & equipment, software and telecommunications licences	20,884	20,531	353
Goodwill and other intangible assets	10,643	10,890	(247)
Other non-current and current assets	3,067	2,288	779
Trade and other receivables	4,195	4,196	(1)
Investments, cash and cash equivalents	2,048	3,914	(1,866)
Total assets[b]	**40,837**	**41,819**	**(982)**
Loans and other borrowings	(12,713)	(14,761)	2,048
Trade and other payables	(7,437)	(7,418)	(19)
Other current and non-current liabilities	(2,398)	(2,288)	(110)
Provisions	(1,161)	(743)	(418)
Deferred tax liability	(1,240)	(1,262)	22
Pensions, net of deferred tax	(7,553)	(5,235)	(2,318)
Total liabilities	**(32,502)**	**(31,707)**	**(795)**
Total equity	**8,335**	**10,112**	**(1,777)**

[a] Revised. See note 1 to the consolidated financial statements.
[b] Excluding deferred tax asset relating to BT's defined benefit pension schemes.

Our core fixed and mobile network infrastructure is included within property, plant and equipment, software and telecommunications licences. These assets were held at a net book value of £20.9bn at 31 March 2017. The net increase of £353m in the year primarily reflects capital expenditure of £3,454m exceeding the related depreciation and amortisation charge of £3,189m, and a net foreign exchange gain of £87m.

Goodwill and other acquisition-related intangible assets decreased by £247m, primarily reflecting the impact of foreign exchange translation of overseas non-current assets. This also reflects the outcome of our re-assessment of the provisional assets and liabilities fair values recognised in our 31 March 2016 financial statements as part of the acquisition of EE.

We review the recoverable amounts of goodwill annually across our cash generating units which hold goodwill, which are Consumer, EE, Business and Public Sector, Global Services, and Wholesale and Ventures, and are satisfied that these support the carrying value of goodwill (see note 12 to the consolidated financial statements).

Other non-current and current assets and liabilities relate primarily to our financial instruments, which we've described in note 27 to the consolidated financial statements. It also includes inventories which have increased by £38m as outlined in note 16 to the consolidated financial statements.

Trade and other receivables decreased by £1m to £4,195m while trade and other payables of £7,437m were £19m higher. Despite these movements, the unwinding of the effects of improper working capital transactions in our Italian business resulted in a working capital outflow of £382m. Investments, cash and cash equivalents, loans and other borrowings are reconciled to net debt of £8,932m in note 25 to the consolidated financial statements. We've discussed net debt on pages 97 to 98.

Provisions increased by £418m to £1,161m mainly due to an increase in regulatory provisions which was treated as a specific item. We have a significant property portfolio which includes both office buildings and former telephone exchanges (see page 31). Property provisions, which mainly comprise onerous lease provisions, amounted to £292m. There are also asset retirement obligations of £83m relating to leased mobile sites forming part of the EE network. You can find more information about these provisions in note 19 to the consolidated financial statements.

We've shown deferred tax movements in note 9 to the consolidated financial statements. Pensions, net of deferred tax, increased by £2.3bn to £7.6bn and are discussed below. Equity has deteriorated compared with the prior year due to the actuarial losses relating to retirement benefit obligations, being more than the profit for the year.

Pensions

Overview

We provide a number of retirement plans for our employees:

– The BT Pension Scheme (BTPS), a defined benefit plan in the UK, is the largest of these plans. Although closed to new members, the BTPS still has around 32,500 active members, 199,500 pensioners and 64,000 deferred members.
– The BT Retirement Saving Scheme (BTRSS) is a contract-based, defined contribution arrangement operated by Standard Life. This is the current arrangement for UK employees who joined BT after 1 April 2001. It has around 32,500 active members.
– EE operates the EE Pension Scheme (EEPS), which has a defined benefit section that is closed to future accrual and a defined contribution section which has around 11,000 active members.
– We also maintain retirement arrangements around the world with a focus on these being appropriate for the local market and culture.

The BTPS, BTRSS and EEPS are not controlled by the Board. The BTPS and EEPS are managed by separate and independent Trustee bodies while savings in the BTRSS are managed directly by members.

Details of the governance of the BTPS, its financial position and the performance of its investments are available in the BTPS Annual Report published by the Trustee in December 2016, on the BTPS Trustee website (www.btpensions.net).

We've given more information on our pension arrangements and on the funding and accounting valuations in note 20 to the consolidated financial statements.

BTPS funding valuation and future funding obligations

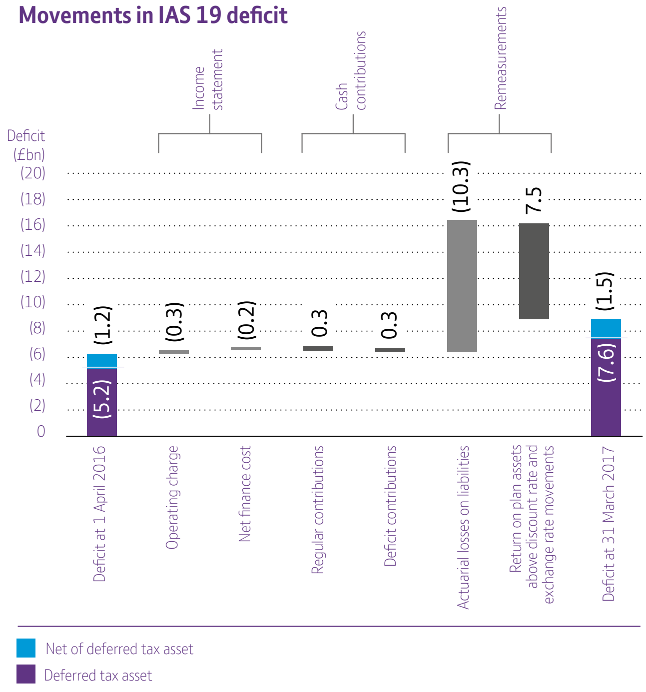
The funding of the BTPS is subject to legal agreement between BT and the Trustee of the BTPS and is determined at the conclusion of each triennial valuation. The most recent triennial funding valuation at 30 June 2014 and the associated deficit contribution plan was agreed with the Trustee in January 2015. At 30 June 2014, the market value of assets was £40.2bn and the funding deficit was £7.0bn. There is a wide range of assumptions that could be adopted for measuring pension liabilities. Legislation requires that this deficit is based on a prudent view – for example, assuming a lower future investment return than might be expected in practice.

A 16-year deficit contribution plan was agreed reflecting BT's long-term and sustainable cash flow generation. Under this plan, we made deficit payments of £875m in March 2015, £625m in April 2015 and £250m in March 2016 and March 2017.

Accounting position under IAS 19

The accounting deficit, net of tax, rose over the year from £5.2bn to £7.6bn. The movements in the deficit for the group's defined benefit plans are shown below.

Movements in IAS 19 deficit



The actual investment return in the year to 31 March 2017 of around 21% was higher than the discount rate assumption at 31 March 2016 of 3.30%, leading to a reduction in the deficit recognised as a remeasurement in other comprehensive income. The return reflects strong asset performance across all asset classes, in particular equities and government bonds which increased by c16% and c23% respectively.

The actuarial losses on liabilities in 2016/17 primarily reflect a fall over the year in the real discount rate from 0.44% to 0.78%.

Contractual obligations and commitments

We've shown in the table below our principal contractual financial obligations and commitments at 31 March 2017. You can see further details on these items in notes 20, 25 and 30 to the consolidated financial statements.

At 31 March 2017	**Total £m**	Less than 1 year £m	Between 1 and 3 years £m	Between 3 and 5 years £m	More than 5 years £m
Loans and other borrowings[a]	**12,334**	2,618	2,756	1,281	5,679
Finance lease obligations	**229**	14	24	26	165
Operating lease obligations	**7,160**	650	1,168	1,037	4,305
Capital commitments	**889**	811	77	–	1
Other commitments	**367**	231	127	9	–
Device purchase commitments	**423**	423	–	–	–
Programme rights commitments	**2,644**	–	641	1,405	598
Pension deficit obligations	**7,686**	710	1,460	1,410	4,106
Total	**31,732**	**5,457**	**6,253**	**5,168**	**14,854**

[a] Excludes fair value adjustments.

We have unused committed borrowing facilities totalling £3.6bn. We expect that these resources and our future cash generation will allow us to settle our obligations as they fall due.

Adoption of IFRS 15 'Revenue from Contracts with Customers'

IFRS 15 'Revenue from Contracts with Customers' will be effective for BT on 1 April 2018. We are planning to adopt this new standard retrospectively, applying it to each prior reporting period presented in our 2018/19 financial statements, namely 2016/17 and 2017/18. On adoption in 2018/19, this will require a cumulative transitional adjustment at 1 April 2016. We are still in the process of quantifying the implications of this standard and the financial impact is not yet reasonably estimable, but we anticipate that the resulting accelerated revenues and deferred costs are likely to significantly exceed deferred revenues, and there will be a resulting cash tax impact in 2018/19 and 2019/20.

More detail over our approach to this new standard as well as others is outlined in note 1 to the consolidated financial statements.