Additional information

Alternative performance measures

Introduction

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

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

Specific items

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

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

In determining whether an event or transaction is specific, management considers quantitative as well as qualitative factors. Examples of charges or credits meeting the above definition and which have been presented as specific items in the current and/or prior years include significant business restructuring programmes such as the current group-wide cost transformation and modernisation programme, acquisitions and disposals of businesses and investments, charges or credits relating to retrospective regulatory matters, property rationalisation programmes, significant out of period contract settlements, net interest on our pension obligation, and the impact of remeasuring deferred tax balances. In the event that items meet the criteria, which are applied consistently from year to year, they are treated as specific items. Any releases to provisions originally booked as a specific item are also classified as specific. Conversely, when a reversal occurs in relation to a prior year item not classified as specific, the reversal is not classified as specific in the current year.

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

Reported revenue, reported operating costs, reported operating profit, reported net finance expense, reported profit before tax and reported earnings per share are the equivalent IFRS measures. A reconciliation from these can be seen in the group income statement on page 150.

Net debt and net financial debt

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

Currency-denominated balances within net debt are translated to sterling at swap rates where hedged. Fair value adjustments and accrued interest applied to reflect the effective interest method are removed. Amounts due to joint ventures held within loans and borrowings are also excluded.

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

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

Net debt and net financial debt are considered to be alternative performance measures as they are not defined in IFRS. A reconciliation from loans and other borrowings, lease liabilities, cash and cash equivalents, and current asset investments, the most directly comparable IFRS measures to net debt and net financial debt, is set out in note 27.

Return on Capital Employed

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

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

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

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

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

Additional information continued

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

Year ended 31 March	**2023 £m**	2022 £m
Reported operating profit for the period	2,619	2,885
Share of post tax profits (losses) of associates and joint ventures	(59)	–
Specific items (non-finance and tax)	556	287
Return for the period	**3,116**	**3,172**
Equity, debt and debt-like liabilities		
Loans and other borrowings	18,521	16,185
Lease liabilities	5,359	5,760
Retirement benefit obligations	3,139	1,143
BDUK grant funding deferral	427	488
Total equity	14,514	15,296
Adjust for balances used to hedge financial risk		
Cash and cash equivalents	(392)	(777)
Investments	(3,577)	(2,713)
Net derivative financial instruments	(1,096)	(221)
Adjust for tax balances		
Net deferred tax liabilities	911	1,671
Net current tax receivable	(349)	(406)
Capital employed	**37,457**	**36,426**
Return on capital employed	**8.3%**	**8.7%**

Adjusted EBITDA

In addition to measuring financial performance of the group and customer-facing units based on adjusted operating profit, we also measure performance based on adjusted EBITDA. Adjusted EBITDA is defined as the group profit or loss before specific items, net finance expense, taxation, depreciation and amortisation and share of post tax profits or losses of associates and joint ventures.

We consider adjusted EBITDA to be a useful measure of our operating performance because it approximates the underlying operating cash flow by eliminating depreciation and amortisation. Adjusted EBITDA is not a direct measure of our liquidity, which is shown by our cash flow statement, and needs to be considered in the context of our financial commitments.

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

Year ended 31 March	**2023 £m**	2022 £m
Reported profit for the period	**1,905**	**1,274**
Tax	(176)	689
Reported profit before tax	**1,729**	**1,963**
Net finance expense	831	922
Depreciation and amortisation, including impairment charges	4,818	4,405
Share of post tax losses (profits) of associates and joint ventures	59	–
Specific revenue	(12)	(5)
Specific operating costs before depreciation and amortisation	503	292
Adjusted EBITDA	**7,928**	**7,577**

Normalised free cash flow

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

Normalised free cash flow is defined as free cash flow (net cash inflow from operating activities after net capital expenditure) after net interest paid and payment of lease liabilities, before pension deficit payments (including their cash tax benefit), payments relating to spectrum, and specific items. It excludes cash flows that are determined at a corporate level independently of ongoing trading operations such as dividends paid, share buybacks, acquisitions and disposals, and repayment and raising of debt, cash flows relating to short-term funding arrangements with joint ventures, and cash flows relating to the Building Digital UK (BDUK) demand deposit account which have already been accounted for within normalised free cash flow. For non-tax related items the adjustments are made on a pre-tax basis.

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

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

Year ended 31 March	**2023 £m**	2022 £m
Cash generated from operations	**6,588**	**5,962**
Tax paid	136	(52)
Net cash inflow from operating activities	**6,724**	**5,910**
Net purchase of property, plant and equipment and intangible assets	(5,307)	(4,607)
Free cash flow	**1,417**	**1,303**
Interest received	41	6
Interest paid	(709)	(755)
Payment of lease liabilities	(727)	(659)
Dividends received from joint ventures, associates and investments	9	1
Net purchase of non-current asset investments	(5)	(8)
Add back pension deficit payments	994	1,121
Remove cash tax benefit of pension deficit payments	–	–
Add back net cash flow from specific items	404	606
Add back refund in respect of spectrum licence auction	–	(223)
Remove cash flows relating to the BDUK demand deposit account	(96)	–
Normalised free cash flow	**1,328**	**1,392**

Below we reconcile normalised free cash flow by unit:

Year ended 31 March	2023 £m	2022 £m
Consumer	1,147	917
Enterprise	522	791
Global	63	131
Openreach	211	448
Other	(615)	(895)
Normalised free cash flow	**1,328**	**1,392**

From FY24 we are updating our normalised free cash flow metric to reflect the ongoing evolution of the business:

– We will include the sale of cash flows of contract assets related to mobile handsets where the performance obligations have been substantially delivered to the customer. This is a financing cash flow in the cash flow statement as certain performance obligations in the contract need to be fulfilled before the right to consideration is unconditional, but we believe that it is appropriate to include these cash flows in our normalised free cash flow metric because the sale of these cash flows is part of our working capital management, as handset costs are incurred up front but recovered throughout the customer contract term. The corresponding operating cash inflow received from customers will be excluded from normalised free cash flow if it has previously been included at the time of the sale of the contract assets.

– We will include monies received as prepayment for the forward sale of future redundant copper. This is a financing cash flow in the cash flow statement as certain benefits of the asset have not yet been transferred to the buyer, but we believe that it is appropriate to include these cash flows in our normalised free cash flow metric because the forward sale of this asset is in line with our operating activities and is similar in nature to cash flows arising from the net purchase of property, plant and equipment which are already included within normalised free cash flow.

Sports JV pro forma basis

On 3 September 2022 BT Group and Warner Bros. Discovery announced completion of their transaction to form a 50:50 sports joint venture (Sports JV) combining the assets of BT Sport and Eurosport UK. On 18 October 2022 we published unaudited pro forma financial information estimating the impact on the group as if trading in relation to BT Sport had been equity accounted for in previous periods, akin to the Sports JV being in place historically.

Within this Annual Report we reference pro forma information relating to the years ended 31 March 2023 and 2022. The table below provides a bridge between financial information on a reported basis and a Sports JV pro forma basis.

	Reported basis		Sports JV pro forma adjustment		Sports JV pro forma basis		
Year ended 31 March	2023 £m	2022 £m	2023 £m	2022 £m	2023 £m	2022 £m	Change %
Adjusted revenue							
Consumer	9,737	9,858	(238)	(539)	9,499	9,319	2
BT Group	20,669	20,845	(238)	(539)	20,431	20,306	1
Adjusted EBITDA							
Consumer	2,623	2,262	71	205	2,694	2,467	9
BT Group	7,928	7,577	71	205	7,999	7,782	3

Cautionary statement regarding forward-looking statements

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