BT'S QUARTER THREE RESULTS 2006/2007

CEO - Ben Verwaayen

Good morning everybody and thanks for coming, weathering a snow storm like this not an easy task for many people here in Britain as the BBC reminded us this morning and the fact that you are here is a great testimony of the strength of this particular audience.

So let's quickly go the slide that you all know and you love and you care about and you read in your own time and therefore I think we can go to what you came for and where we came from.

We came from a past where you thought about BT as a Telco as a classical Telco and I think that we have evolved into something else. First of all, from a financial point of view, what we have evolved into is pretty predictable as an organisation. You have seen trends and we have delivered according to those trends. You have seen twelve consecutive quarters of revenue growth and you see the trend there. We have now eight consecutive quarters of EBITDA improvements of which four is EBITDA growth and you see the trend there and you have seen our earnings per share growth, nineteen consecutive quarters, and it all culminated in the beginning of this fiscal year by giving you guidance and said we are very confident that we know how to grow our revenues and our EBITDA and our earnings per shares and our dividend.

Here we are in February 2007 and I will say to you, we are very confident that we will grow our revenues, our EBITDA, our earnings per share and our dividend. Not just for this fiscal year but also for 2007/08. The trends are a clear indication where the Company is and what we do during this presentation is talk you through some of the trends.

These are the numbers that are very important to get the feel and the headline for this particular quarter, 5% group revenue up, EBITDA up 2.5%, profit before tax up 13%, earnings per share up 14% and nice to know that we have a £1 billion credit from the tax man.

So that fits in to this picture. This is the strategy picture that we have talked about many, many times and what we thought of doing this time is not talk about the strategy but the delivery. So if you look to the strategy of defending our core business and you look to the facts as we have presented them in this particular quarter you can see that defending the core is working. The decline we used to talk about 3 and 4% per quarter is now down to 1%. For the first time in sixteen quarters, four years, we are growing the number of voice customers again in BT, almost forty thousand. We know how to defend - we know it better than before - we know how to segment the market and do the right pricing and packaging.

The second thing that you need to know is how you built your relationship with your customers and how you do that in the long term, so you become more and more predictable. You have seen there is a rise in consumers under contract every quarter a percent or two up. We are now at 68% of our revenue under contract. If you look at the SME market, more than 50% of the Broadband contracts we signed is for longer than one year and if you look to the numbers in this quarter and you look to Global Services, two and a half billion orders received long term contracts, so we build as an organisation much more predictability into our numbers and the ability also to perform better on the margin lines because of that.

Now, growing the new. We have talked about it many times and here are two examples. Ten million broadband lines, can't get enough of that number, 10 million in the market is a fantastic number. Ten million customers going on broadband, that's 50% of households here in the UK in a four to five year period. The same as if you look to market share for BT Retail - 34% is an extremely good result. And 21CN, the underlining platform for building ourselves out of a Telco into a platform services company, has started in this quarter.

So, the profile of BT in defending the core and growing the new, is this. The profile is, the arrow is up when it comes to the new wave and the arrow is smaller and smaller down when it comes to our traditional business. We look to both elements. This trend is important in our new wave business and there are two core elements to that. We are a broadband company. If you add all the numbers in the quarter, you can see over half a billion in revenues on broadband and it's over 1.1 billion in revenue in networked IT services and these are the two corner stones in our new wave business. To look to these two elements will tell you that we are not selling to people end-to-end connectivity. We are selling to them a capability, either in lifestyle or in productivity or in globalisation.

The best way to look at this is, what do people buy from us? Well, they buy from Global Services in this particular quarter £2.5 billion in orders received, one and a half of that is networked IT services and you can see how that fits in to a pattern. This has been a very strong quarter but some people were worried about a certain weakness in the market. We are taking market share, and the best thing to look at is where the orders come from. These orders come from a wide variety of customers (231 new customers) new logos that we can add to a long list and you can see companies from all over the world. You can see that we are gaining market share not just on a geographical basis, also on a sectorial basis. So the strength is the depth of our order portfolio.

Now let's look to delivery, because it's one thing to win an order, the other thing is to make sure that you can deliver and therefore make your revenue and make your margin and deliver in a way that you built the platform for the next step. You see a whole list that you can read at your leisure of some of the contracts that we have won. Headline contracts, contracts that people talk about and how we are doing in delivery. The bottom line is we are doing excellent. But it is more important to find two or three examples to give you flavour. So I will leave aside the N3 we have talked about many times you know, the largest VPN network in Europe etc and we are ahead of time.

Let's look to Spine, transactional database. The transactional database was not the core competence of this company when we signed the contract. Today we have that capability - 11 million prescriptions run over it, two and a half million bookings made over it. It is running on a one and a half million prescriptions per month now so it is going very well and it is holding up against all kinds of measures. Of all the software drops that we had to give over the last 12 months we have a 100% on time or earlier than on time track record.

Let's take another contract. Let's take Liverpool City Council. You are a city and you have to deliver to your citizens and you make a partnership with BT and after a few years CPA calls you excellent. For a city in its relationship with its customers, the best reward we got was an extension, a five year contract extension and it is the best proof that it is working.

Look to Fiat. It's a fantastic contract. 30 countries and, within a year, 80% of traffic is on the BT networks, so I think we know how to novate contracts. We know how to build capabilities and work with customers in very complex environments to deliver value to them. Therefore, we are always looking to how can we enhance the capabilities that we have and I use the word capabilities and not capacity. This is all about the capability. In the last seven days we have announced two acquisitions. One in the US, INS more than 600 billable consultants very much in the heart of our customer base. They serve half of the Fortune 1000, which is a very important part of what we want to serve and you can see what they do is very high level. These are very creative professionals that work in the space between IT and telecommunications - IT and networks. It will give us a better footprint not just in the US but around the globe with companies that they serve.

Then in India, we have acquired i2i, and I will leave this analysis with you. We need to look to the worlds, the different worlds and enhance our capabilities there. i2i will make us the largest global carrier in India. Of much more importance than that they have licences. They have capabilities on the ground and I think that their understanding of what we do as a business is based on the fact that for many years they have been the local representative of BT Infonet. So, I think this is a good expansion of our capabilities and this is what you do in an intelligent way, very tailored, very focussed, focussed on activities to enhance market spread and your ability to serve your customers. So that's networked IT Services.

The other one is Broadband, the 10 million. You are sick and tired of looking at this. I will frame it and hang it in my office so I don't have to bore you! Let's go to the next one.

Alright, this is also one to frame because it is pretty good, 34% growth. I remember the discussion we had last quarter when we said, "listen, this is a campaign driven market and this is a market that you have to work on value". You have to work - to let the customers understand what you are offering them. The two messages we gave you then, which I would like to repeat today, is that there is a market for price. That's in the left corner. Lots of people there. And there is a market for value in the right corner. That's where we are. Both have a reason to exist and we are doing extraordinarily well in that corner and we have value for our customers. The most important line here besides the 34% which is a great line, is the 60% buying option two and three, because this gives us the clear message of what people want. They want the capability that we offer. Broadband is not just access. It's a platform. Let me give you two examples.

We have the home IT services. So you don't want the hassle at home? If something goes wrong, you want to go directly into BT because we will take care of it. Whatever it is, our part or the IT part of what you have at home, 97% customer satisfaction, 97%, 25,000 contracts. If you look to what we do in the equivalent in the SME market, 20,000 companies signed up for a similar IT hassle free type of contract with BT. So you can see that broadband allows us to go into the market with a total different value proposition than we had in the old days. You see that VoIP was over one million, it's becoming an integral part of what people expect from a broadband platform. It's what people get used to. They have broadband and we go, of course, into the video part, it's voice, data and video and Vision has just got started but I think has good numbers. 80,000 people I think are registered, around 3,000 people now in day-to-day practice using it and we are going out every single day with our engineers to install. It tells you the story. This is a journey into the services business.

I can say the same thing about convergence, because convergence is the next logical step. You don't have stove piped part of your life, you have an integral part of your life. You don't have stove piped part of your business you have an integrated business. You want the things where you are and you want it in the way that you want it. Not how the supplier has decided you should get it and therefore mobility is not a separate part of what we do. It's an integrated part of what we do. WiFi is a fantastic standard to allow us to do that and you will see us having much more focus on WiFi than ever before. Simply for the reason that the phones are now here, that helps, you can sell them, I believe we have a Motorola phone now and we have a Nokia phone and a Samsung phone coming up. We have value proposition - not only in the consumer market but also in the business market. So I think this is a clue that helps us to bring the converged story to life where broadband and traditional services and new services in data and video all come together. The issue brings it hassle free!

Now the traditional business. Minus 1% is a pretty good number. And why is that? Well, because the red numbers are lower than you have seen in the past and the green numbers are approximately the same as they were. Therefore, the minus is smaller than you had in the past. It's as simple as that. We sell better… and how do we sell better? We sell better this way. You see two things here. You see that we are better in selling our packages to the market but remarkably this quarter, for the first time in four years, we gained voice customers. For the first time in four years, 37,000 is a good number. So, we have more customers coming back to us. By the way, this is the first quarter that CPS number is down - 83,000 down, this is the lowest quarter for WLR compared I think to the number around September 2004 and we are getting market share. So, if you take all that together, you will understand the trend in traditional. This is the trend and it's an important chart because, as we said with new wave and with all kinds of other elements, look to the trend. Not just look to the absolute number but look to the trend and it gives you the story of where we are.

Now, we have talked about our strategy many times and I think it is time that we look to our strategy again and add a number of dimensions. We have a great strategy in defending our traditional business and growing the new and building relationships and do that based on a platform. But the business is also evolving in two other ways.

The first way is that we no longer have to talk about networks and IT. We have to talk about software enabled networks. We have to talk about capacity that gives people choices; how to mix our products and services with what they have from other people; and we have to talk about the fact that people make choices on a global basis, end-to-end. So, if you want to capture these three elements in words, this will add three important words to our vocabulary.

The first is “real time”. Many of our services are developed in our time, we will tell you how long it will take to get a new service and we will tell you how long it will take between services and we tell you how long it takes for us to produce, not for you to want, but for us to produce. If you want to make a radical shift and you want to say it’s not our time but your time, you have to be ready to bring the services to the market in their time - which is real time.

The way to do that is to shy away from hardware and go onto software. Everything that is hardware -where you use a screwdriver and somebody is in a car – that is coming out will cost time. The big shift, you will see that we, as a company, will become much more software driven in a way that we organise ourselves and create value. And we need to build the platforms that allow the software to sit on it so that you give real time experience to your customers. You must be able to enter an airline website and print your own airline tickets from home. You need to be able to create your own service as you see fit. Press the button, it’s there! That will make a shift from the hardware to the software. You just need the hardware platform to allow that to happen.

The second thing is, you need to be open. As with oil, which is an ingredient for productivity and a product by itself, but it’s an ingredient that you use. What we give to the market in the business sense is collaboration and communication tools that they will use in whatever sense they want. They will fold it in whatever service they have. So you can’t have propriety systems. You can’t have stove pipe systems. You must have an open system in architecture, in delivery, and to be honest, also in mindset. You have to work with many different partners. You have to make sure that you serve the market with the required speed and not by the slowest means while we are creating our own service. You have to make sure that you get the service capability from the best in the market.

The third element is “global”. We will all see later on when we talk about cost saving that we have to think on a global source basis. You have to think about creativity on a global basis and most of our customers want services end-to-end.

These are three new elements that will drive our investment criteria and drive how we are going to structure our market place to deliver in real time. Your time as a customer on a global basis, in a very open platform. The way to do that is to create the basis conditioned for that; 21C.

How are we doing on 21C? Thank you for asking. We are doing pretty good. We have live customers. We have delivered 10% of our network and I’d say pre-requisite. We are doing all kinds of stuff there in order of 2,300 kilometres of fibre in Wales in order to make this happen. There is 1,500 men years of software development in IT systems that we needed to do. 1,500 men years in order that we got started with this type of integrated services. We are working in Consult 21 with the rest of the market because it’s not just us. We have 400 WLR competitors in the market place…customers in the market place…and we have 20 plus LLU players. They all need to be accommodated and we are learning. This is not like laying an iron railway. You have a book and you say I go from A to B to C to D and it costs us in iron. We are looking to the market and we are listening to the market and for example we have seen that Ethernet is much more important to our customer base than we thought maybe 18 months ago. We have signed two contracts, Nortel and Siemens, in order to bring Ethernet into the frame. We want to be agile with our programming of the 21C and learning from what we see in the market place. I think that 21C is one of those projects that will enable us to change the way that we think about markets, technology and their interaction.

Now crucial to that is the performance of Openreach. I think Openreach has done a very good job. They had to do three things. They had to establish themselves as an entity and have done that. They had to deliver on the TSR, they have done it and, as you see in the numbers, that's not without its own expense and they had to bring a better reliable network to the market.

Now these are great numbers, 90,000 joints that are sealed and we can give you a lot of activity numbers. The fact that there are so many players in the market means there is a higher churn between those players and all activities that Steve and his team have to do and they have coped with that beautifully. The best test I think was when we had our worst rain after many years. Somebody calculated 60% more rain than on an average year. The fault rate went up 2% only. Many people say "ok so what?" For a network person, that is a phenomenal number and it shows that it's not working just on delivering one part of the equation. You have to deliver on every part of the equation. I think the best testimony for where we are today is the 1.5 million LLU lines. It is delivered early and I think it is a very vibrant part of our business and it's getting there step by step both on TSR as a more robust network.

Now, let's talk about costs. It is an important ingredient in our success model and it is there to stay, £400 million plus a year. Many of you have said "well, you have produced, so I believe you but it would be better to have a feel for it... where it's coming from?". Let me give you a few examples.

If I talk about supply management. Think about Global Services. Global Services on one hand will tell you it's great. We are now in 160 countries or so and territories but at the same time you have to realise, if you are in 160 countries and territories you will have stuff there. What do you do with the maintenance of that stuff? And where are the spare parts? Who is going to take care of that? That's a major cost item, now we have outsourced that with Alcatel-Lucent in a way that will be very positive for BT over the years and will save us a substantial amount of money and that will help to underpin the £400 million that Andy promised the market in September over three years. We have done things like outsourcing our post with TNT. We have looked to the printing of our phone book. We are looking to sourcing on a global basis as we deliver to our customers of the same capability.

The other thing I would like to say, if you look to process improvements - it may not sound terrifically interesting to many people that 700,000 people do not need a paper bill any more. They trust the online service as their only way to communicate with us. It saves a lot of money and a lot of hassle and I think these real live examples show that we are confident we can deliver the £400+ millions and we would be happy to talk about the rest on this chart.

Now you have seen this one, 19 consecutive quarters of earnings per share growth. I have to be honest! It's not a trend, it's habit. You know habits are very hard to die.

So lets bring it together the story is very simple. We evolve our strategy and we understand how we translate the trends into the new steps that we need to take. We have a clear momentum in the market; we have an understanding of how to grow and how to take costs out and therefore we are confident to tell you that our revenues will grow. Our EBITDA growth or earnings per share will grow and our dividends will grow.

Thank you Hanif to you.

Hanif Lalani

Good morning everyone. We have just demonstrated that the positive, operational performance has been translated into strong financial results. This quarter showed the best top line performance in over five years, with a continued strong growth in new wave revenues helped by the lowest level of decline in traditional revenue that we have seen in recent times. This resulted in overall revenue growing by 5% or £244 million to £5.1 billion.

EBITDA pre leavers grew for the 4th consecutive quarter and at 2.5% growth, the improving trend has continued. Depreciation increased by £31 million, or 4% year on year, primarily driven by 13% increase in Global Services. Operating profit therefore grew by £4 million, to £698 million. Profit before taxation and specific items of £616 million was £71 million or 13% up on the prior year benefiting from a £67 million reduction in net finance costs due to higher pension credit and a lower net interest rate. The tax rate was 24.4% and the net result was that earnings per share before specific items increased by 14% to 5.6 pence or 5.8 pence pre leavers, the 19th consecutive quarter of year on year growth.

In addition, during the quarter there were a number of specific items, the most significant being a £1 billion one off tax credit that I will explain later in the presentation.

In the meantime, let's look through the P&L for each line of business starting with Global Services.

Revenue grew in the third quarter by 4% to £2.3 billion. New wave revenue was £1.8 billion, an increase of 8% year on year while UK traditional revenues declined by 6% driven by the continuing falls in Dial IP and voice related products.

This growth in revenues partially offset the impact of the changing mix resulted in gross margins being maintained at £653 million. During the quarter SG&A costs were cut by 2% as recent efficiency programmes began to deliver. EBITDA before leaver costs increased by £11 million to £238 million, a growth of 5% year on year.

Depreciation charges, which included the impact of bringing the NHS London assets into use, increased by 13% to £180 million. Consequently operating profit was down £9 million on last year at £58 million.

Let's move on to BT Retail. This is the first time in nearly four years that we have grown revenue in this part of the business. The growth of 1% reflects the success of Retail's strategy of innovative call pricing and value orientated Total Broadband propositions.

Gross profit rose 7% and gross margin increased by nearly 2 percentage points. The improvement was underpinned by a richer product mix, tighter margin management and the impact of cost efficiency programmes. These programmes also contributed to a 1% reduction in SG&A costs.

EBITDA before leaver costs, at £224 million was 22% higher than last year continuing the strong trend of growth we have seen in previous quarters. All units within BT Retail grew EBITDA with particularly strong growth in the business and in Enterprise units which together now account for more than half of Retails EBITDA. With depreciation growing by £7 million, the operating profit before leaver costs of £181 million was 23% higher than last year.

Let's focus on BT Wholesale. External revenue in the third quarter of £1 billion increased by 4% with revenue from new wave services increasing to £278 million, driven by the continued growth in broadband. Internal revenue increased by 4% to £895 million as broadband growth more than offset the impact of lower call volumes and lower regulated prices. Total revenue in the quarter of £1.9 billion was 4% higher year on year. Gross variable profit increased by 3% to £941 million. In addition, continuing efficiencies in the network and SG&A ensured that the cost growth was held to 1% despite increased Opex investment in 21CN. This resulted in EBITDA before leaver costs increasing by 4% to just over half a billion pounds. Depreciation has risen by 8% due to the ongoing replacement of legacy transmission assets by the roll out of 21CN. This combination has resulted in an operating profit of £210 million, half a percent lower than last year, pre-leavers.

Finally, Openreach. Strong market volume growth has more than offset WLR price reductions in the prior periods and lifted revenue 3% to £1.3 billion. External revenue increased by £106 million in contrast to the £70 million decline from other BT lines of business, reflecting the volume shift from internal to external channels.

Operating costs increased by 7% to £845 million due to the increased activity volumes and investment in service levels. This has resulted in EBITDA before leaver costs reducing by £19 million to £469 million.

Depreciation reduced by £19 million due to the lengthening of the economic life of copper at the start of the year. Operating profit was therefore maintained at last years' levels of £292 million.

From a Group perspective the operational performance from all the lines of business translate into the 4th quarter of consecutive EBITDA growth at 2.5% this quarter, and the 8th quarter in an improving trend.

Let's move on to cash flow. Net cash flow this quarter was an outflow of £525 million, primarily due to the £500 million paid into the pension fund during December. Year on year both capex and working capital outflows were higher.

Firstly, capital expenditure. In the quarter the actual cash invested amounted to £777 million. Expenditure is increasingly related to preparing exchanges for 21CN deployment.

In addition we are also investing in new systems development to ensure compliance with the Undertakings and in network infrastructure to meet LLU demand from other operators. We are successful in managing the legacy infrastructure on a much lower level of capital investment.

Over the coming quarters as we deliver on the Undertakings we expect capital expenditure on systems development to be higher. This will result in capex of around £3.2 billion for this year and next, before reducing towards the end of the decade.

Working capital. As you can see from the graph there is a seasonal cycle, reflecting Wholesale billing periods and customers' year ends. This means that 60-70% of our cash flow and working capital usually comes in Q4. I expect a similarly strong Q4 pick up this year, as we have had in prior years.

There are two significant areas we have reached agreement on this quarter, Pensions and Tax. The triennial pension funding valuation at December 2005 was concluded with BT agreeing to make deficiency payments equivalent to £280 million per annum for the next 10 years. The first three years will be paid up front and we pre-paid £500 million in December and the remaining £340 million will be paid by the end of April this year.

The IAS 19 pension obligation showed a net of tax deficit of £1.1 billion at December, that's £1.8 billion lower than 12 months ago.

Tax. We reached a settlement with Revenue and Customs which will result in the repayment to BT of just over £1 billion, including associated interest. This cash will be returned to BT in instalments, with around £250 million in Q4 and the remainder in the first half of next year. This repayment relates to the settlement of substantially all outstanding items in respect of the ten tax years through to March 2005.

This has resulted in the recognition in the P&L of a £1 billion tax credit as a specific item. Our current estimate of the effective tax rate is that it will remain at about 24.5% this year. And the effective rate for next year will be between 25-26%.

The momentum we have established over recent quarters in growing new wave revenues, implementing process improvements, delivering margin management and driving cost efficiencies allows us to be confident that we will continue to grow revenue, EBITDA, EPS, dividends both this year and next year.

Thank you.

Ben Verwaayen

Right, question time. Shall we start over there.

QUESTIONS AND ANSWERS

Question 1

Morning it's Mike Williams at Citigroup, a couple of questions please. Firstly a hypothetical question. If you did want to increase leverage for the Group and to do it at the subsidiary level, what are the main barriers you would need to overcome and how long will it take to do the ground work to actually be able to move to that position?   And secondly, you talk very positively about traditional revenue trends, I want to just test that confidence by asking if you can see sustainable revenue inflexion in traditional and if I can push my luck asking when might that occur? Thanks

Ben Verwaayen

You are pushing your luck many times in these questions.

Hanif Lalani

I'll take the first one, Mike's been looking for an answer to this question for the last year I think, but I think if you want to move debt to a subsidiary level then I think you are increasing the complexity and I think complexity takes time to bed in. So I think that if you try to do anything of that nature it's not going to happen instantaneously it will take you a period of time, may be up to a year.

Ben Verwaayen

Right and on the traditional business, Ian give it a try.

Ian Livingston

I think what we have seen is a significant improvement in the trend, it seems but a few quarters ago the inflexion word was being asked about the Group as a whole, after two quarters of decline. But as you know, our strategy is actually to move as many customers over into the new services, and that's not changed from dial IP into broadband, moving them from standard PSTN into VoIP, now we have got more than a million customers registered on our VoIP service, so we are pushing that very substantially in WiFi, for instance, we have got over a million hubs out there, so that trend's going to continue and that's going to eat in to traditional so I think increasingly the questions going to be forget the distinction between traditional and new wave - the things are merging together because we are very actively trying to move our customers over to new services.

Ben Verwaayen

Ok, we are going over there in the back.

Question 2

Hi, it's Simon Weeden from Goldmans. Two questions please. On the net pension credit as you now have the details of the triennial review and movements in the market and Bond yields, could you give us a view on how you see the net pension credit changing year over year in 07/08, and second could you tell us how much of the, or what the revenue impact was, from the price increase in retail calling at the beginning of October on the quarter just gone. Thanks.

Hanif Lalani

On the pension credit, I think that there are two factors to take in to account. Firstly the actuaries work with us to tell us what the returns are expected on the assets for the following year and they are not going to make that decision until the year end anyway so it's not something that's decided at the tri-annual funding evaluation. The second thing is if you are kind of looking at trends between this year and next year I am not expecting a significant change year on year so the best modelling that I could suggest to you is to keep it flat and I think the difference will be plus or minus point one of a pence on the second one.

Ian Livingston

We actually if you recall made very substantial price reductions in August and being the sort of company that we are we gave our customers the reduction first, and we said we will delay some of the price rebalancing that we were going to do. These reductions, which have led to cutting Option 2 and Option 3 prices by about a third, have actually been the things that have driven the customer numbers and that's been the big thing, far more so than some of the rebalancing that started on 1st October. It has since had an effect, but the biggest effect we have seen is the customers moving in to the higher price packages because there is so much better value. I mean you now pay less than £10 for all you can eat calls any time of the week or any of you who are BT customers I would point out you get free evening and weekend calls, and if you are not BT customers you are also very welcome to sign up to that package for the next 12 months. We are sure that's going to help drive more and more customers to realise the value that BT provides.

Question 3

Hi it's Andrew Beale from Arete. Three questions if I can get away with it but.

Ben Verwaayen

We'll see, it depends.

Andrew Beale

You are confident enough to give guidance for the year ahead which is great but you have done it at Q3, which is slightly unusual. What is it that you have got planned for Q4, is that when you start to talk about the balance sheet and do you have any thoughts on that?

Secondly on Global Services M&A you have obviously done M&A for some capability expansion, some footprint expansion this time. What is the focus of Global Services M&A going forwards, do you actually, now that you have more scale, need a bit more network in some of your home markets, if I call that Europe, as well?

Then finally when do you think you, or when and how do you think you will get a price control in Openreach, because currently you have the price ceilings which don't really give you a huge amount of incentive to manage for lowest costs?

Ben Verwaayen

Right let me bring you into what we intend to do, what we are planning to do for Q4. So, we are planning to talk about great business performance in Q4, we are planning to talk about the year and we plan to talk about all the other issues to the Board has decided to talk about at the year end and I think that will cover basically the direction that we are looking at. So it's at year end always to talk about the performance of the quarter and the performance of the total year, so the presentation isslightly longer then. Your second question was about Andy's business and M&A.

Andy Green

Ok, so I think you know the strategy has definitely moved to services, so we saw Counterpane INS and i2i they are all basically about services. The footprint issue is more about people I think and being big where our customers needs to be big. We are globalising fast into Latin America, Asia Pacific and the whole world's doing that - we have to have the right resources there. I think the services piece is a bit more subtle, we have just done a deal with a subsidiary of Credit Lyonnais in Asia Pacific, a $20 million deal that is driven by the Counterpane acquisition you know on the West Coast of America and I think the whole thing here is to take fantastic Global Services capabilities and use our brand recognition and our reach to drive new business around the world and I think the heart of what we are doing with INS and Counterpane is (a) getting ourselves some strength in the US with the US multi-nationals there and (b) this ability to take those ideas and then cookie-cut around the world and you know it's very good to get that example of real life, what you can do to leverage those types of acquisitions.

Ben Verwaayen

Right Steve.

Steve Robertson

Yes, I get that the long term regulatory settlement is obviously something that is of interest. However if you look at the state of the market just now, it's still very very immature, very very volatile and there is quite a big slate of market reviews in place just now including the Broadband market review. So my anticipation is that we are going to get most of that out of the way in the course of the next year and will be coming back round the buoy for that. In terms of, in the meantime you know what incentives do we have to drive cost reduction. Well, if you were working for this man here (points to Hanif) you would probably find that he is more than an adequate substitute for a regulatory regime.

Ben Verwaayen

Right no comment there, now to the other side. Speak to you later…..

Question 4

Hi, it's Mark Cardwell at Bernstein, I would just like to pick up on the question that was just asked of Andy and asked specifically about India and China, do you perceive that you will need network assets at some point, and if so what type, you know sort of getting to customers, getting across backbones etc and separately on the Wholesale side you have had some deals with Vodafone and O2, I believe, to do Broadband, I am curious what you expect that to do to revenue in the sort of mid term and also the announcements today about some of the carriers starting to put their mobile networks together presumably that's negative to you, so I am just curious where you see the whole mobile business going putting the good stuff and the bad stuff, that's been happening lately together for you.

Andy Green

So the i2i acquisition took the number of nodes we have in India from 5 to 11 so you know that's important, it gives us a big capability but you would expect us to continue to go for multiple nodes. I think we are going to need like 3 or 4 nodes in cities like Delhi, just like you do in New York because you know there is going to be so much demand there and so much need for resiliency in those types of places. Now in China we have gone for an organic strategy - we are building out into the major cities, we are doing it with both carriers because we need really to have some tension there because it's very consumer focussed market and we have to focus their minds a bit more on the business market place. Concentrating on the financial sector around Shanghai and then Dalian for the business process outsourcing, which is where the customers are already going to, we are taking on two or three hundred extra people there. So far, I think those strategies are working fine but you know we will continue to look for anything there which makes you just better at doing business there than anybody else. That's the plan.

Ben Verwaayen

Right then on the Wholesale market, actually I respectfully disagree with you that it's bad news. I think it is excellent news because the message that it gives loud and clear to everybody is that managed services is the way to go forward. In the old days the differentiation was that you needed to be totally vertical separated and duplication therefore was the name of the game in the market. Who could build as fast as possible, masts out in the market and networks out in the market and the differentiation was in hardware stuff - the differentiation is shifting totally to the consumer and therefore is a vast market that is much less sensitive on managed services than ever before. You see that in the trends of BT Wholesale business and I have to say this was music to my ears when I heard it because it means common sense may break out in the market in the first place. This is a very very good trend because it replaces, duplication with the economy of scale. Right we will go back here and then we go back there. It's Laura first.

Question 5

Morning, it's Laura Janssens from Merrill - I have three as well if that's ok?

First of all, on the sort of headline financials. The revenues looked a bit stronger than we were all expecting but that didn't seem to drop down to EBITDA despite the out performance in traditional. Can you give us a bit of clarity, for example, about whether you had things like greater subscriber acquisition costs in broadband in the quarter? Secondly on broadband - obviously a very good Retail share but the Wholesale number looked a little bit lighter than I'd expected given that we normally see a seasonal up lift in Q4, maybe you can comment on that.

Then lastly, just picking up a comment that Hanif made about preparing the local exchanges for 21CN. Can you give a little bit more colour on what exactly that means and specifically whether it means that you need less space in some of these local exchange buildings? Thanks.

Hanif Lalani

On revenue to EBITDA I think that the key message I think you probably heard was there are a number of factors that drive it. Firstly is investment in service. We are investing in service in Retail, we are investing in service in Openreach, we are investing in service in Wholesale and in Global Services, so in all lines of business we are investing in service to ensure the experience for our customers is absolutely fantastic. Also yes, acquisition costs if you are going to have a 34% market share you will see an increase in acquisition costs, so part of the drop down in to EBITDA does come through part of it is consumed by service and the other by acquisitions.

Ben Verwaayen

Second part of the questions was …

Hanif Lalani

Was DSL connections for Wholesale. Two hundred and forty thousand connections - stronger than last quarter, I think that while LLU picks up and people migrate we are going to see lower volumes than we did last year but I still think 240,000 is a fantastic performance.

Ben Verwaayen

And I think 700,000 Broadband customers to be accurate 697,000 is a very strong number and people have said you know you will hit the ceiling, I don't see that at all. I think that there is a, this is a market that can grow and will grow, so you know it's a matter of perception, I thought the number was pretty good.

Hanif Lalani

You will have to tell us what the third one was Laura.

Oh, 21CN.

Oh exchange place. Oh, yes I'll tell you what that is, this is a terrific one. If you look. Bloomberg said I was a Marketing Director, now I am a technology man.

A couple of things happening. First is when we went from analogue to digital we had to clear out the exchanges, you are kind of seeing a similar transformation happening within the exchanges. We are having to clear up how the cabling is done in the exchange, we are looking at where the MDF is located, how the power works, ultimately with 21CN coming in there will be less requirement for space for equipment, there will be actually in the short term an increase in power consumption but over the long term it should come down. So you are right, yes there will be less requirement for space in the exchanges and we have over 6,000 exchanges and that creates and gives an opportunity with that.

Ben Verwaayen

So the answer could have been yes. Right next one, ok. Paul

Question 6

Thank you it's Paul Howard at Cazenove. Couple of questions. Firstly on Global Services and your ambitions there. You have obviously made a number of small acquisitions in the past - is there a sense that large acquisitions could be contemplated to sort of transform some of your capabilities globally? What sort of size would you be comfortable with? And what's the financial criteria in that respect? Then secondly, on spectrum. Quite a lot of spectrums becoming available now over the next year or two, again could you give us a size of your ambitions in that respect?

Ben Verwaayen

I am very ambitious for Global Services. I remember the first advice I got from some of you in the room that we should get rid of Global Services five years ago, I think we will all agree now that it's a great asset they are growing the business and they are doing it mostly organically and mostly it is because other customers tell other customers that it's a great experience that we have. I think that is the most important element of our confidence that we can bring them to customers that we have to convince them that we can deliver what we promised. We will always be looking to expand our capabilities but I think our past is a great indication for the view to the future. Now you can never say never, you know that phrase, but basically I would say assumption wise we have learnt our lessons how to integrate business always better than we said and faster and it has to do with culture, understanding of the market place and size. I think we are becoming pretty good in doing this stuff and that's a help and you have to think three times if we changed that habit in to doing another trick. So great ambitions, also great belief in the formula that we have.

On spectrum well, you know it's true, there is spectrum becoming available, the same thing as another part of our business, we will look at it, we will look at it seriously but everything has its price and it is depending on the price and depending on what we can do with it. We are not desperately depending on any of that but you know some looks good and some not so good. We will see. Over there.

Question 7

Yes, thank you I am Hannes Wittig from JP Morgan.

I have two questions. One is on the tax situation. Just wanted to see if the settlement sort of exhausts your capital gains loss carried forward or what sort of basis of the settlement is and, if you could, maybe give us a bit of tax guidance that may be beyond the year 2007/8 that would be appreciated.

The second area is on the subject of fibre. I think we know what you have said in the past on that subject, just want to see if things is thinking changes all the time as the subject changes. Are there any new thoughts and if so would you consider VDSL in the UK or would you rather think that it is a sort of something that could be leap frogged as we see in France?

Hanif Lalani

Ok on tax, I think that the way to look at it is, capital losses that we have in excess of £16 billion are still there. In terms of tax guidance we said 24.5% this year between 25/26% next year and I would say between 27/28% in the medium term.

Regards the settlement, the settlement really closes out all of the tax items we had over the 10 years up to March 2005 which means that some of the litigation we are involved in is no longer necessary and this was much more about a rapid conclusion that avoids costs and time on both sides.

Ben Verwaayen

Right on fibre we have talked about this issue many many times, it's about the service it's not about the way you transport the service. I sometimes are amazed to see that it's almost a religious subject for some people that it has to be fibre. Well we are testing 24mb as you saw on one of the slides in the market, that gives capability to customers and that is what really matters. If we need fibre for that well time will tell, I mean we are not shying away from fibre, Steve put 2,300 kilometres of fibre in Wales but that is something else than the fibre story. So press us on the service story but how we get the service we will do it in the best possible way for the cheapest possible price. Over there, then you.

Question 8

Hi, Chris Fremantle from Morgan Stanley. Can I just ask you a quick question on BT Retail and specifically on some of the new services. Do you think at some stage, some sort of High Street distribution is going to become necessary, either owned or not as a result of the new services that you have put together?

Ian Livingston

Well I think, distribution will come in a number of ways. I mean Dabs.com for instance is having a tremendous time which shows that maybe we, BT Retail, isn't so bad at doing retail, I mean 25% growth in Dabs.com is not bad in the PC and electronics market and it's selling a number of BT services. We have also been doing some things in shopping centres, for instance, I was in Bray Head recently which for those of you down in London is in Scotland. Scotland - that's the place to North of Newcastle, and you know we had a great place there that we were showing the operation of a number of our services. I am not convinced at this point that a BT shop itself makes sense, because actually it's about customers not about what we want to show. Customers are really interested in our services when they are shown in retailers, whether it's a retail experience in itself is another matter and you will see in places like John Lewis you will see BT services being shown, you see in Phones4U, we will be putting the Fusion phone and you will see in a number of stores BT services being made available. Having 15 stores around the country I am not convinced it's going to make a massive difference to our life but we will carry on looking at it. We have got some people who have some background in retail so maybe they will help us.

Question 9

Hi Tim Jagger, RBS Credit Research. Clearly your thinking on the balance sheet is evolving and in my experience securitisations are notoriously complex transactions. Earlier Hanif you mentioned that you were looking at moving debt potentially into a subsidiary, ie Openreach I think that everybody would think that's the way it is going to work. Is that the way existing bond holders should think about this process right now?

Hanif Lalani

I think I answered the theoretical question for Mike and I still think it is theoretical.

Ben Verwaayen

Right last question over there.

Question 10

Hi it's Steven Howard at HSBC.

A couple of questions. Firstly obviously a very strong performance in the consumer segment, I was wondering to what extent you felt that might have been boosted by NTL holding back on customer acquisition in the fourth calendar quarter as they migrated the systems away from legacy. I wonder if you felt that had any impact, and just more generally what you think of the threat they represent as of today with all the re-banding, and just a quick follow up on the revenue line. Could you perhaps specify roughly what the inorganic boost is to the top line at present because obviously you have done a number of small acquisitions.

Ian Livingston

Last bit first. There was only one acquisition in there which was Dabs which accounted for 1% … something like that… the other acquisitions haven't yet impacted that I can think of and PlusNet won't be in the numbers till this quarter. In terms of NTL holding back. NTL have been holding back for quite a long time now if you look at their numbers! So I am not quite sure that's entirely a planned hold back and if you look at our Broadband numbers in terms of net adds we actually did more than TalkTalk and Sky combined so it wasn't a bad quarter. But unquestionably we are going to see it, be very aggressive not just NTL, Telewest, Virgin combined relaunch and I think they are going to have more than just change their name and there is a lot of things around that but we will also see the reaction to it. I bet in today's newspaper it's absolutely full of Sky and ourselves and all acting and reacting to it so it's going to be interesting next couple of quarters but we are pretty pleased over 3.4 million Broadband customers if you put in PlusNet and certainly we have been adding faster than anyone else over the last few quarters. But we are going to have to carry on upping our game both in service and in propositions because the market certainly isn't going to get any easier.

Ben Verwaayen

Right and on that high note thank you very much and see you next time.