

BT GROUP PLC
Form 6-K
May 27, 2009

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**SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

Form 6-K

Report of Foreign Private Issuer

Pursuant to Rule 13a-16 or 15d-16 of
the Securities Exchange Act 1934

Report on Form 6-K dated May 27, 2009

BT Group plc

(Translation of registrant's name into English)

BT Centre

81 Newgate Street

London EC1A 7AJ

England

(Address of principal executive offices)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.

Form 20-F X

Form 40-F o

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes o

No X

Enclosure: BT Group plc Annual Report and Form 20-F 2009 as sent to shareholders

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

BT Group plc

By: /s/ Alan

Name: Scott

Alan Scott

Title: Deputy
Secretary

Date: May 27, 2009

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BT GROUP PLC ANNUAL REPORT & FORM 20-F

BT GROUP PLC ANNUAL REPORT & FORM 20-F

BT Group plc
Annual Report
& Form 20-F
2009

BT Group plc is a public limited company registered in England and Wales and listed on the London and New York stock exchanges. It was incorporated in England and Wales on 30 March 2001 as Newgate Telecommunications Limited with the registered number 4190816. Its registered office address is 81 Newgate Street, London EC1A 7AJ. The company changed its name to BT Group plc on 11 September 2001. Following the demerger of O2 in November 2001, the continuing activities of BT were transferred to BT Group plc.

British Telecommunications plc is a wholly owned subsidiary of BT Group plc and encompasses virtually all the businesses and assets of the BT group. The successor to the statutory corporation British Telecommunications, it was incorporated in England and Wales as a public limited company, wholly owned by the UK Government, as a result of the Telecommunications Act 1984. Between November 1984 and July 1993, the UK Government sold all of its shareholding in British Telecommunications plc in three public offerings.

This is the Annual Report for the year ended 31 March 2009. It complies with UK regulations and is the Annual Report on Form 20-F for the US Securities and Exchange Commission to meet US regulations. This Annual Report has been sent to shareholders who have elected to receive a copy. A separate Summary financial statement & notice of meeting 2009 has been issued to all shareholders.

In this Annual Report, references to BT Group, BT, the group, the company, we or our are to BT Group plc (which includes the continuing activities of British Telecommunications plc) and its subsidiaries and lines of business, or any of them as the context may require.

References to a year are to the financial year ended 31 March of that year, eg 2009 refers to the year ended 31 March 2009. Unless otherwise stated, all non-financial statistics are at 31 March 2009. Please see cautionary statement regarding forward-looking statements on page 148.

A number of measures quoted in this Annual Report are non-GAAP measures. The Directors believe these measures provide a more meaningful analysis of the trading results of the group and are consistent with the way financial performance is measured by management. These include EBITDA, adjusted EBITDA, adjusted operating profit, adjusted profit before taxation, adjusted earnings per share, net debt and free cash flow. The rationale for using non-GAAP measures and reconciliations to the most directly comparable IFRS indicator are provided on pages 33 to 35, 39, 41, 47 and 48.

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FINANCIAL SUMMARY**

	2009	2008
	£m	£m
Revenue	£21,390	£20,704
EBITDA ^a		
adjusted ^{b,c}	£5,348	£5,784
reported	£3,301	£5,245
Profit (loss) before taxation		
adjusted ^{b,c}	£1,877	£2,506
reported	£(134)	£1,976
Earnings (loss) per share		
adjusted ^{b,c}	18.4p	23.9p
reported	(1.1)p	21.5p
Full year proposed dividend	6.5p	15.8p

Key performance indicators**Key points**

- 4 Revenue growth of 3%
- 4 EBITDA decline due to the unacceptable performance of BT Global Services
- 4 The rest of the business delivered a good performance in spite of the economic downturn
- 4 BT Global Services contract and financial review charges of £1.6bn and a specific item restructuring charge of £280m
- 4 Pension deficit payments of £525m per annum for the next three years

4 Full year proposed dividend of 6.5p per share

a EBITDA:

Earnings before interest, taxation, depreciation and amortisation.

b Items presented as adjusted are stated before contract and financial review charges recorded within BT Global Services and specific items.

c Adjusted EBITDA, adjusted profit before taxation, adjusted earnings per share and free cash flow are non-GAAP measures. The rationale for using non-GAAP measures and reconciliations to the most directly comparable IFRS indicators are provided in the Financial review on pages 33-35, 39, 41, 47 and 48.

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CHAIRMAN'S MESSAGE

The world looks a very different place than it did a year ago. Global trade has contracted for the first time in many decades. Financial markets have been in turmoil and trading conditions worldwide remain extremely challenging. Against this background, the importance of defending free trade and fighting for regulation that promotes investment and encourages competition has never been greater.

Our management team not only understands the challenges, but also sees the opportunities that lie ahead. Three out of our four principal divisions (BT Retail, BT Wholesale and Openreach) are delivering well. Management's highest attention is now directed towards returning BT Global Services, our one under performing division, to profitable growth.

We have agreed with the Trustee of the BT Pension Scheme the pension contributions for the next three years, enabling the Board to announce a sustainable dividend policy.

The proposed final dividend of 1.1p gives a full year dividend of 6.5p which rebases dividend payments to a level which we are confident is sustainable. The Board is committed to delivering attractive returns for shareholders and believes that the operational improvements in the business will generate sufficient cash flow to allow the dividend to grow at the same time as investing in the business, reducing debt and supporting the pension scheme.

Regulation

It is clear how important the 2005 Telecommunications Strategic Review by Ofcom has been in establishing the UK as the most competitive telecommunications market in the world. While the price of other utilities has soared, the price of communications has fallen sharply. New market entrants have flourished, encouraged by low wholesale prices and incentives to invest in unbundled local loops. Britain has more companies competing in the same space than any comparator country.

Now a healthy debate is underway about the investment needed to deliver the next generation of broadband services. These will be carried largely over fibre optic cables able to deliver speeds of up to 100Mb compared with a typical speed of 4-5Mb today. This investment will provide the UK with the world class IT infrastructure it will need to thrive as a knowledge-based society.

It is essential that the regulatory environment encourages investment. This means that BT and others must have the potential to make a return for shareholders that is commensurate with the risk involved. We need a level playing field in the UK's fast moving market which allows every company to compete on equal terms and makes sure that new monopolies are not allowed to emerge. We also need regulation to move at the same speed as the market is evolving.

In our overseas markets, particularly in the rest of Europe and in North America, regulators must do more to encourage fair competition. BT should be able to invest and compete in any other country, in the same unrestricted manner that overseas companies can invest and compete in the UK.

A sustainable business

BT has a proud record of contributing to the communities in which we work and of building a sustainable business. We believe our services are an important part of the solution to climate change.

Thousands of our people are involved in voluntary work and I am keen to build on this heritage and make sure that as a global business BT's Better World Campaign takes a genuinely global view.

Your Board

In December 2008, we welcomed Tony Chanmugam to the Board as Group Finance Director in succession to Hanif Lalani who had become Chief Executive, BT Global Services.

Since joining BT I have been extremely fortunate to have as my Deputy Chairman, Maarten van den Bergh who is stepping down from the Board at the conclusion of this year's AGM in July. Maarten has been a tremendous asset to the Board having served as senior independent director since 2006 and as Chairman of both the Board's Pension Scheme Performance Review Group and Remuneration Committee. I would like to thank him for almost nine years of distinguished service.

I would also like to express my gratitude to Matti Alahuhta who has decided to step down at the end of May having served as a non executive director for just over three years. His telecommunications industry and international

experience have been of great value to the Board and we wish him well.

I am working with the Nominating Committee to strengthen your Board following these departures and we will announce new appointments shortly.

My thanks also go to the rest of the Board for their extremely hard work during the last challenging months. I would also like to pay tribute to the BT staff. Everywhere I go I have been struck by their passion and commitment. I am confident in their ability to build on BT's many strengths in the future.

The future

BT is in business for the long-term. We invest billions of pounds into the UK's IT infrastructure for the long-term. We are seeking the regulatory certainty which will support long-term business decisions. And we want long-term relationships with our customers that are based on excellent service, and on our enduring commitment to helping them thrive in this fast changing world.

Sir Michael Rake

Chairman

13 May 2009

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OVERVIEW

CHIEF EXECUTIVE'S STATEMENT

The actions we have taken will enable BT to come out of this recession a stronger and better business.

There's no doubt about it, this has been a tough year. A tough year for BT Group, a tough year for the economy and a tough year for our shareholders.

But there are good reasons to look forward with optimism. Taken together, BT Retail, BT Wholesale and Openreach have delivered a resilient performance. That despite the economic downturn. However this success was overshadowed by the performance at BT Global Services. Because of this we have had to take a number of very substantial charges. These have not been comfortable, but were necessary to establish the solid foundations from which we can now build a profitable business.

Meeting our customers' needs

The markets in which we operate are changing fast and we need to move with them. In the UK we have the most competitive communications market in the world. Thanks largely to BT's investment, the UK now has some of the highest broadband availability and take up in the world as well as some of the lowest prices. Speeds are improving all the time, and our new fibre based services will deliver a next generation of super-fast broadband, bringing speeds of up to 100Mb to people's homes.

We have made real improvements in customer service, and we are going to do much more. Let me give you a couple of examples. Three years ago you could expect a fault on your telephone line once every nine years. That's now improved to once every 13 years. By the end of the financial year, 97% of our customers were getting through on their first call, complaints were down and customer satisfaction had improved significantly. And on Christmas Day 2008 we recorded our lowest ever number of outstanding network faults.

When our service improves, our customers are happy, more people want to do business with us, and also we can reduce our costs. That's because when we get our services right first time, the number of people phoning our call centres falls and the number of engineers we need to send out to fix things declines. That's just as true for the biggest customer of BT Global Services or BT Wholesale as it is for a family buying a broadband service from us. We have made significant progress, but this is most definitely not the end of our journey to make BT a leader in customer service.

New opportunities

Even in the most difficult economic circumstances a diverse and agile business will find opportunities to grow and improve the service it delivers to its customers. A really good example is BT Conferencing which is strongly growing both revenues and profits and is now the world's biggest provider of videoconferencing. Using the latest technology we are meeting the needs of companies all around the world. Helping customers save money by cutting travel costs and reducing their carbon footprint.

Another example is our Business One Plan service, which is the UK's first triple play of landline, mobile and broadband for small and medium-sized businesses. It launched three years ago and in 2009 added free calls within an organisation – even between offices and mobile workers – a significant saving. Over a million business lines are now using this service and more than 2,500 new customers sign up each week. In our consumer business the new BT Home Hub has been ordered by over 800,000 customers since its launch last June. It has the best wireless range on offer, and allows customers to save power by programming it to switch off when it's not being used.

These are just a few examples of BT seizing opportunities and delivering great service in the UK and around the globe. I was particularly pleased that Telemark Services, an industry analyst, has just rated BT Global Services the best operator in the world in its Customer Satisfaction Index with the highest score ever awarded.

A better business, a better future

In order to transform the company, we need to drive significant cost saving. Regrettably this has meant a reduction in our workforce. However, we have sought to retrain and redeploy permanent staff whenever we can. That has meant that in the past year only a third of the reduction came from our permanent staff, with the rest made up of contractors and third-party resource.

So in the past year we have taken some tough decisions and we have taken some bold decisions too. Like investing £1.5bn in fibre based super-fast broadband. There are certainly plenty of challenges, but I believe that the actions we have taken will enable BT to come out of this recession a stronger and better business.

Ian Livingston

Chief Executive

13 May 2009

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OVERVIEW

THIS IS BT

BT is one of the world's leading communications services companies. In the UK, we are the largest communications service provider to the residential and business markets. The BT brand is one of the most trusted in the UK. Around the world, we are a major supplier of networked IT services to government departments and multinational companies.

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OVERVIEW

HOW WE ARE STRUCTURED

We meet the needs of our different customer groups through four customer-facing lines of business, supported by two internal functional units. BT Retail, BT Wholesale and Openreach operate mainly in the UK. BT Global Services provides services in more than 170 countries around the world.

We believe that the way we are structured brings us closer to our customers, helps us get it right first time and enhances the customer experience, at the same time as helping us reduce our costs and drive value for our shareholders.

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BUSINESS AND FINANCIAL REVIEWS

BUSINESS REVIEW

Falling prices, rising data speeds and constant innovation continue to make the communications marketplace dynamic and intensely competitive. In 2009, we faced the additional challenges of the economic downturn and an unacceptable performance from BT Global Services.

Introduction

BT is a communications services company which operates in more than 170 countries worldwide. We are proud to serve customers that range from some of the largest multinational corporations and public sector organisations in the world, through the small business sector to millions of families and residential customers in the UK.

We are at the heart of a communications revolution which is continuing to improve the quality of people's lives and the effectiveness of their businesses. It is our job to bring together the best technology to create services that our customers need while offering them the very best value.

Our 2009 performance

In 2009, in spite of the economic downturn, three of our lines of business – BT Retail, BT Wholesale and Openreach have each performed well. Both BT Retail and Openreach delivered EBITDA growth while in BT Wholesale the rate of decline in revenue has slowed. This good performance was primarily due to the effective delivery of cost savings. However, these achievements were overshadowed by the unacceptable performance in BT Global Services.

The issues in BT Global Services

During the 2009 financial year, the level of profitability in BT Global Services fell significantly. This was caused by a combination of higher costs, the slow delivery of cost reduction initiatives and worsening economic conditions. This led the Board to conclude that previous estimates of profitability for some of our major contracts were no longer likely to be achieved.

On page 10 we explain what actions the Board took as a result of these issues and how BT Global Services is being restructured to streamline and refocus the business.

Our focus

We aim to make BT a better business and drive shareholder value by delivering on our current strategic priorities better, faster and cheaper.

These are:

4 providing excellent customer service

4 building future networks

4 becoming more agile.

Providing excellent customer service

Our goal is to provide excellent service in every market in which we operate by putting our customers at the heart of everything we do.

Every part of BT is taking action to make substantial improvements to the delivery of our services. That means getting things right first time every time, keeping our promises to our customers and meeting or exceeding their expectations.

We continually track improvements that reflect the real experience of our customers from start to finish. We have made significant progress in the last 12 months across the whole range of our customers and we are determined to make further improvements. In the highly competitive markets in which we operate we believe that being recognised for outstanding customer service is a key differentiator for BT.

As an example of the progress we are making in the consumer market, the time taken to get through to an adviser fell by 65% in the past year. Our customers experienced a reduction of more than 20% in the number of line faults,

which means that a line will go wrong on average just once every 13 years. In the small business market, there was a 20% improvement in the average time to clear telephony network faults, while the average time to provide international multi-protocol label switching (MPLS) services to large business customers reduced by over 40%.

Building future networks

The digital revolution is opening up a world of new possibilities for all our customers. It means people can work together and collaborate more effectively than ever before. They can be entertained and informed in ways that would have been hard to imagine just a few years ago. We think this revolution has only just begun, and we are investing in our networks, systems and services to ensure that they are fit for the future.

In July 2008, we announced plans to make Britain's biggest ever investment in a fibre-based super-fast broadband network. We will spend £1.5bn making fibre based services available to around 40% of the UK's homes and businesses by 2012. This will deliver a range of services with top speeds of up to 100Mb, allowing customers simultaneously to run multiple bandwidth-hungry applications, such as high-definition movies, gaming, complex graphics and videos; all with greatly improved upload as well as download speeds.

These plans are conditional on our ability to make a proper return on our investment, and we have seen encouraging progress in establishing the right regulatory basis for this investment.

Super-fast broadband will run on BT's 21CN infrastructure. 21CN is our next generation global platform and has been at the heart of BT's transformation for some years.

We have now completed the new 21CN core network which is a unified software driven platform. It will help us meet our customers' needs faster and more efficiently whether they are delivered over copper or fibre. It will reduce the time it takes to get new services to market, eliminating duplication and reducing costs.

Our flagship MPLS network service provides coverage and support around the world from 875 BT managed points of presence and around 2,600 in partnership.

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Becoming more agile

Our goal is to combine the strengths of being a large company with the speed and flexibility of a small company. Our people are becoming more agile in the way they work together to serve customers. We are making our company more agile as well, cutting out any bureaucracy that can slow us down. As a result we will be more responsive to customer needs.

We are continuing to simplify our business to give people more authority and to allow them to do their jobs more effectively.

As we become a more agile organisation, we reduce our costs as well as the number of people we need to employ. In the past year we have reduced the number of full-time employees by around 5,000. In addition to this, the number of indirect employees working through agencies or third party contractors was reduced by around 10,000, giving a reduction in our total labour resource of some 15,000. We expect further reductions of a similar level in 2010. We have sought to retain our permanent workforce through redeployment and retraining, and will continue to do so. We continue our drive to reduce costs across the business, and made further progress in 2009 towards transforming our cost base.

Three out of four of our lines of business have made a strong contribution towards the delivery of cost savings, although BT Global Services still has to control costs more tightly and deliver greater savings.

Maintaining a sustainable business

BT is committed to contributing positively to the communities in which it works and to operating in a socially responsible way. We are using communications technology to help create a better, more sustainable world. Our goal is to help meet the challenge of climate change, to promote a more inclusive society and to enable sustainable economic growth.

We believe that being a recognised leader in the field of corporate responsibility contributes to shareholder value. It builds our brand and is central to the way we do business. It encourages the best people to want to work for BT. It is a powerful reason for customers to do business with us and stay loyal to us.

We commit a minimum of 1% of our pre-tax profits to activities that support society. We invested a total of £25m, comprising time, cash and in-kind contributions, in the community in 2009. Of this amount, £2.3m was in the form of charitable donations.

Measuring our performance

For 2009, the key performance indicators (KPI) against which we measured the delivery of our strategy were:

4 customer service

4 earnings per share

4 free cash flow.

Our customer service results were encouraging and we delivered significant improvements during the year. However, the unacceptable performance in BT Global Services impacted free cash flow and earnings per share, which were well below target.

Customer service

We set ourselves a group-wide stretching target in 2009 of improving right first time by 24%. We achieved an increase of 17%, compared with 9% in 2008 and we are targeting further improvements in 2010. We are now delivering excellent customer service levels in many areas.

Earnings per share

Adjusted basic earnings per share^{a,b} were 18.4p in 2009, compared with 23.9p in 2008 and 22.7p in 2007 (see **Financial review** page 39). The reported basic loss per share was 1.1p in 2009, compared with basic earnings per share of 21.5p and 34.4p in 2008 and 2007, respectively.

Free cash flow

Free cash flow^b in 2009 was £737m, compared with £1,503m in 2008 and £1,354m in 2007 (see **Financial review** page 41).

Outlook

We expect revenue to decline by 4% to 5% in the 2010 financial year, reflecting a continuation of the trends seen towards the end of the 2009 financial year, the impact of lower mobile termination rates, together with the impact of refocusing BT Global Services.

We expect to deliver a net reduction in group capital expenditure and operating costs of well over £1bn in 2010. Included within this is a reduction in group capital expenditure to around £2.7bn. As a result, we expect group free cash flow, before any pension deficit payments, but after the cash costs of the BT Global Services restructuring charges, to reach over £1bn in 2010 and beyond.

Earnings per share will be impacted by the movement of the net finance expense on the pension obligations which moves from a credit of £313m in the 2009 financial year to a charge of about £275m in 2010.

The proposed final dividend of 1.1p gives a full year dividend of 6.5p which rebases dividend payments to a level we are confident is sustainable. The Board is committed to delivering attractive returns for shareholders and believes that the operational improvements in the business will generate sufficient cash flow to allow the dividend to grow at the same time as investing in the business, reducing debt and supporting the pension scheme.

^a Items presented as adjusted are stated before contract and financial review charges and specific items.

^b Adjusted basic earnings per share and free cash flow are non-GAAP measures provided in addition to disclosure requirements defined under IFRS. The rationale for using non-GAAP measures is explained on pages 33, 47 and 48, and a reconciliation of adjusted basic earnings per share and free cash flow, to the most directly comparable

IFRS indicator,
is provided on
pages 39 and 41
respectively.

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BUSINESS AND FINANCIAL REVIEWS BUSINESS REVIEW

BT Global Services order intake (£m)

How we are structured

We have four customer-facing lines of business: BT Global Services, BT Retail, BT Wholesale and Openreach. These are supported by two internal functional units: BT Design and BT Operate.

BT Retail, BT Wholesale and Openreach operate mainly in the UK, where we are the largest communications services provider to the residential and business markets. BT Global Services operates in the UK and globally.

BT is one of Europe's largest and most successful communications wholesalers to other communications providers (CPs). In the UK we support CPs through BT Wholesale and Openreach, and internationally through Global Telecoms Markets, an operating unit of BT Global Services.

We have integrated our networks, IT and testing facilities which are managed by BT Design and BT Operate. Specifically, BT Design deploys platforms, IT systems and processes that support our products and services, while BT Operate is responsible for making sure they run smoothly. Neither generates external revenue.

Line of business financial performance

The financial performance of each of the lines of business for 2009, 2008 and 2007 is discussed in this **Business review**. We measure the financial performance of BT Retail, BT Wholesale and Openreach based on EBITDA and operating profit before specific items. For 2009, we measure the results of BT Global Services on an adjusted basis, being before the impact of contract and financial review charges and specific items. For further discussion of these items see pages 33 and 47 to 48. A reconciliation of adjusted EBITDA to group operating profit (loss) by line of business, and for the group, is provided in the table at the foot of pages 34 to 35.

BT Global Services

Business overview

BT Global Services is a provider of networked IT products, services and solutions. We aim to be the partner of choice for large enterprise and government customers in the UK and globally.

We have created a powerful combination of networked IT and professional services capabilities together with strong customer partnerships, investing and innovating together to build long-term value.

The Gartner Group's research organisation recognises BT as a global leader in Gartner's Magic Quadrant for Network Service Providers, and industry analyst Telemark Services has given BT its platinum award, reflecting customer satisfaction with our delivery of global data virtual private network services, regarded as best in class.

Customer service improvements in 2009 included a reduction of more than 40% in the average time to provide international MPLS services and a 6% improvement in the delivery of international repairs within the target time. We have more than 3,400 points of presence in more than 170 countries. We are the largest supplier of networked IT services to -UK national and local government.

Despite these strengths, during 2009 the level of profitability in BT Global Services fell significantly.

As explained in the **Principal risks and uncertainties** section in this year's and previous years' annual reports, our pricing, cost and profitability estimates for major contracts generally include long-term cost savings that we expect to make over the life of the contract. In 2009, a failure to achieve these anticipated savings made a number of these contracts less profitable or even loss making, adversely impacting our profits.

Actions taken

The Board changed the senior management team within BT Global Services, with a new Chief Executive for the division appointed in October 2008. The new team's brief was to address the cost base, to bring greater focus to the profitability of new contract wins and to reduce shortfalls in delivery performance on existing contracts. The new management team undertook an extensive review of BT Global Services' financial position, contracts and operations. The financial review covered the financial performance of BT Global Services and its balance sheet position. The contract reviews covered the largest and most complex contracts and were conducted jointly with external advisors. Having completed the contract and financial reviews, a charge of £1.6bn was recognised, which includes £1.2bn relating to the two major contracts that are the subject of ongoing commercial negotiations. These charges reflect a more cautious view of the recognition of future cost efficiencies and other changes in underlying assumptions and

estimates, particularly in the light of the current economic outlook. £1.3bn of the total charge relates to contract costs which had been previously capitalised on the balance sheet.

BT Global Services management team is implementing a number of process improvements. Some of these were in place by the end of 2009, the rest are being implemented in 2010. These include undertaking more regular contract reviews to assess commercial risks and opportunities as part of a strengthened contract governance process that combines operational, financial and risk reporting. Additional scrutiny of contracts and cost transformation plans have been put in place and will continue to be conducted on a rigorous and regular basis involving strong independent oversight of assumptions and estimates for new and existing contracts. We are also placing greater focus on profitable sectors, setting stringent win criteria and enhancing due diligence around our ability and readiness to meet our delivery requirements on all major contracts.

Immediate action has also been taken to address the cost base, with particular focus on external procurement and total labour resource. We reviewed rates across our contractor base, and successfully reduced these rates by up to 35%. We have addressed spend of £450m with suppliers across seven categories of expenditure, including our contractor base, and have successfully

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BT Global Services new structure

renegotiated contracts, resulting in price reductions of 12% on average, and up to 35% in some categories. In addition, we have focused on a number of areas of significant discretionary expenditure including travel, consultancy and conferencing and have achieved reductions in these areas. These actions are expected to deliver sustainable cost reductions in the 2010 financial year.

How BT Global Services is changing

The operational review was completed towards the end of 2009, resulting in a revised operating model and restructuring plan which will reshape and refocus the business, further enhancing BT Global Services' ability to serve customers and establish a significantly lower cost base.

Under the new operating model, BT Global Services will focus on three customer segments:

- 4 being the number one provider of networked IT services to corporate and public sector customers in the UK, building on BT Global Services' strong market position and the group's 21CN products and services
- 4 providing networked IT services to key multinational customers, differentiating BT Global Services through seamless global connectivity and delivery of BT's core portfolio of products and services
- 4 creating a BT Global Services Enterprises unit consisting of a discrete portfolio of businesses addressing specific customer needs in key countries.

Significant structural changes are being implemented. The majority will be completed in 2010 in order to deliver the benefits of the new operating model which include:

- 4 integrated sales, marketing, professional services, account management and delivery capability, competing effectively in each target market
- 4 enhanced bid management and start-up processes to improve win rates on selected deals and ensure standardisation and quality of delivery
- 4 a single global service model, consolidating a large number of individual centres into a small number of larger operational hubs, which will provide a single point of customer contact and enable improved right first time customer service
- 4 continued rationalisation of systems and networks, reducing the number of systems by a third and halving the number of global networks, thereby removing duplication and enabling significant cost savings
- 4 restructuring corporate support functions to serve the three customer segments more efficiently and effectively
- 4 strategic partnering for sales, service and infrastructure.

As a result of this operational review, the group has recorded specific item restructuring charges of £280m in 2009, with further charges of approximately £420m in total expected to be recorded over the next two financial years, the majority in 2010. These charges predominantly arise from legacy networks and products rationalisation and restructuring costs associated with people and property. Further analysis of these charges, including their cashflow impact, is provided in the **Specific items** section of the **Financial review** on pages 36 to 37.

Market context

We believe that we have identified a clear path to a profitable and sustainable business, building on a strong market position.

The global networked IT services market is valued at around £600bn. We remain well placed to help our global customers reduce costs and streamline their businesses in a challenging market environment. We are seeing continued interest in network operational efficiency, workforce management, security, unified communications (including

Telepresence and conferencing) and global hosted contact centre solutions, as our customers respond to the current economic environment.

Operational performance

In the UK

We serve businesses in virtually every sector of British industry, from banking and finance to transport, logistics and the public sector. We have around 1,800 multi-site customers in the UK.

We continue to make progress on our N3, Spine and London Local Service Provider contracts with the National Health Service (NHS) National Programme for Information Technology (NPfIT), the largest non-military IT programme in the world.

Building on our work as the local service provider responsible for upgrading NHS IT systems in London, we have taken on the running of IT systems at eight acute hospitals in the South of England. In addition, we are working with a further four acute trusts in the South of England which have yet to roll out systems as part of NPfIT, as well as implementing 25 new systems in community and mental health trusts in the region.

We are deploying one of the world's largest converged IP networks for the Department for Work and Pensions to be completed in 2010.

Reinforcing our presence in the local government sector, we agreed a ten-year strategic partnership with South Tyneside Council, worth more than £180m for delivery of a number of key council services. We also won an extension to our existing arrangement with Liverpool City Council and a new contract with Sandwell Metropolitan Borough Council and two contracts with Norfolk County Council with a combined value of £40m to provide voice and data services and a schools internet service.

We are the official communications services partner for the London 2012 Olympic Games and Paralympic Games. This involves the provision and management of voice and data networks, internet access and land lines required at each of the London 2012 Games venues.

We signed a number of deals with major UK corporate sector customers including:

- 4 a seven-year, £160m outsourcing deal with Nationwide Building Society to manage its networked IT services

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4 a three-year contract extension with Manpower to provide fully managed global wide area network (WAN) infrastructure and managed services

4 a five-year contract with Carillion worth £32m for voice/hosted voice, IP data, conferencing and private automated branch exchange (PABX) maintenance.

Outside the UK

BT Global Services signed orders with 529 new customers outside the UK in 2009 and we continued to strengthen our business with large multinational corporations.

We signed a number of major deals in 2009, including:

4 a five-year, US\$526m contract with Procter & Gamble to provide and manage local area network (LAN) and WAN infrastructure in more than 80 countries

4 a contract with BMW to manage a large part of its communications infrastructure, including voice over IP (VoIP), contact centres, email services and videoconferencing

4 a three-year managed services contract with SWIFT to connect strategic offices across Europe, the US and Asia with BT's unified communications video solution

4 a three-year contract with Munich Re to provide security and network services in 33 countries

4 a contract with the Emirates airline to consolidate and manage its worldwide contact centres

4 a seven-year, 118m extension of current services provided to Syngenta for data and voice services plus deployment of IP telephony, managed LAN and BT OneVoice to 112 sites and the deployment of BT managed mobile services to 13 countries.

Successes in the public sector outside the UK included a contract with Barcelona City Council for 500 wireless broadband hot spots, providing free internet access across the city, and a contract with the Colombian government supporting digital inclusion under which BT will convert 755 public schools into telecentres and provide additional bandwidth to a further 1,150 schools.

We are also part of the Match consortium that won a 30m contract with the Dutch Ministry of Home Affairs for the housing and hosting of the national government's IT infrastructure.

Financial performance

	2009	2008	2007
	£m	£m	£m
Revenue	8,828	7,889	7,312
Adjusted gross profit ^a	2,576	2,839	2,759
Adjusted SG&A costs ^a	2,267	1,978	2,024
Adjusted EBITDA ^a	309	861	735
Contract and financial review charges	1,639		
EBITDA ^b	(1,330)	861	735
Operating (loss) profit ^b	(2,106)	117	70

a

Adjusted items
are before
contract and
financial review
charges and
specific items.

^b Before specific
items.

In 2009, BT Global Services revenue increased by 12% to £8,828m (2008: £7,889m, 2007: £7,312m), compared with growth of 8% in 2008. Revenue in 2009 includes the impact of foreign exchange rate movements of £588m and acquisitions of £368m. Excluding these, underlying revenue was £7,872m, compared with reported revenue of £7,889m in 2008. Revenue from outside the UK has increased to 47% of BT Global Services total revenue (2008: 40%, 2007: 36%), reflecting the impact of organic growth as well as the impact of foreign exchange rate movements and overseas acquisitions.

Revenue from managed network solutions increased by 17% to £5,328m, compared with growth of 10% in 2008. The increase was driven by growth in revenue from both networked IT services and MPLS and reflects the impact of foreign exchange rate movements and acquisitions, together with substitution of UK calls and lines. Revenue from calls and lines decreased by 8% to £1,095m, compared with a decline of 6% in 2008. The decrease was due to the gradual decline in this revenue stream as customers switch to more email, IP network and conferencing products as shown by the growth in managed network solutions. Other revenue increased by 12% to £2,049m, compared with a growth of 11% in 2008. The increase was mainly driven by growth in revenue from the global carrier business and reflects the impact of foreign exchange rate movements and acquisitions. During the year, we won new networked IT services contracts worth £5.5bn (2008: £5.0bn, 2007: £5.2bn). Networked IT services contracts represent 68% of our total order value of £8.0bn (2008: £8.0bn, 2007: £9.3bn).

Adjusted gross profit decreased by 9% to £2,576m in 2009 (2008: £2,839m, 2007: £2,759m), compared with an increase of 3% in 2008, primarily due to high costs and the continued decline in higher margin UK business. Including the impact of the contract and financial review charges of £1.6bn, gross profit in 2009 decreased by 66% to £965m.

Gross profit is revenue less costs directly attributable to the provision of products and services reflected in revenue in the period. Selling, general and administrative (SG&A) costs are those costs that are ancillary to the business processes of providing products and services and are the general business operating costs.

Adjusted SG&A costs increased by 15% to £2,267m in 2009 (2008: £1,978m, 2007: £2,024m), compared with a decrease of 2% in 2008. SG&A costs include the impact of foreign exchange rate movements of £221m and acquisitions of £170m. Excluding these, underlying adjusted SG&A costs decreased by 5% to £1,876m, reflecting the renewed focus from the new management team on total labour resource, supplier negotiation and discretionary and general overhead expenditure in the second half of 2009. Including the impact of the contract and financial review charges of £28m included within SG&A costs, SG&A costs increased by 16% to £2,295m.

The decrease in gross profit together with the impact of higher SG&A costs resulted in adjusted EBITDA of £309m, a reduction of £552m compared with 2008. In 2008, EBITDA increased by 17% to £861m. Depreciation and amortisation increased by 4% to £776m

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Average annual revenue per consumer household (£)

(2008: £744m, 2007: £665m), compared with an increase of 12% in 2008. The increase reflects the increased investment in our global infrastructure, customer related capital expenditure and the impact of acquisitions, as well as the impact of foreign exchange movements.

The above factors resulted in an operating loss of £2,106m, compared with an operating profit of £117m in 2008 (2007: £70m).

BT Retail

Business overview

BT Retail aims to help its customers enhance the way they live their lives and run their businesses. At home we enable our customers to keep in touch with friends and families and to enjoy fast, reliable, secure and safe connection to the internet. We are bringing broadband to the TV and TV to broadband so that people can watch what they want when they want. At work we serve small and medium-sized enterprises (SMEs) (typically with up to 1,000 employees, although some are significantly larger) and enable them to cut their costs and improve their service by using communications and IT services that were once available only to the largest businesses. We do this by taking the drudgery out of implementing new technologies so our customers can focus on doing what they do best.

There are four divisions in BT Retail: BT Consumer, BT Business, BT Ireland and BT Enterprises.

We are the UK's largest communications provider, with 20.7m fixed lines and 4.8m broadband lines.

Market context

Market conditions have been challenging: the rate of growth in demand for broadband has been slowing as the market matures and competition intensifies, both from local loop unbundlers with large customer bases to whom they can sell broadband, and from the mobile operators who are now offering mobile broadband as well as mobile voice. At the same time the economic downturn is causing business and personal customers to shop around for the very best value.

We have responded by offering customers complete packages that meet their needs and deliver great value for money.

Operational performance

BT Consumer

Voice

We offer value for money services with three main packages of calls and lines – Unlimited Weekend Calls, Unlimited Evening and Weekend Calls and Unlimited Anytime Calls. All offer competitive terms but customers who