

## Pearson outlook 2007

---

We expect 2007 to be another good year for Pearson with continued margin improvement and growth ahead of our markets. We expect to achieve good underlying earnings growth, cash generation well ahead of our 80% threshold, and a further improvement in return on invested capital.

In 2007 we continue to invest in the growth and market-leading positions of our businesses, including:

- extending our lead in education, investing in new programmes for students in School and Higher Education and in testing and software services that help educators to personalise the learning process, both in the US and internationally;
- developing our fast-growing assessment businesses, which provide testing and related services to educational bodies;
- building the international reach of the *Financial Times* – both in print through its four editions worldwide and online through FT.com;
- developing a business concentrating on providing financial information services for financial institutions, corporations and their advisers;
- growing our position in consumer publishing, balancing our investment across our stable of bestselling authors, new talent and our own home-grown content.

## Pearson Education: overview

---

Pearson Education is the world's largest publisher of textbooks and online teaching materials. It serves the growing demands of teachers, students, parents and professionals throughout the world for stimulating and effective education programmes, in print and online.

In 2006 Pearson Education had sales of £2,877m or 65% of Pearson's total. Of these, £2.2bn (75%) were generated in North America and £0.7bn (25%) in the rest of the world. Pearson Education generated 68% of Pearson's operating profit.

Pearson Education competes with other publishers and creators of educational materials and services. These competitors include large international companies, such as McGraw-Hill, Reed Elsevier,

Houghton Mifflin Riverdeep Group and Thomson, alongside smaller niche players that specialise in a particular academic discipline or focus on a learning technology. Competition is based on the ability to deliver quality products and services that address the specified curriculum needs and appeal to the school boards, educators and government officials making purchasing decisions.

We report Pearson Education's performance by the three market segments it serves: School, Higher Education and Professional.

## Pearson Education: outlook 2007

We expect School to achieve underlying sales growth in the 4-6% range; Higher Education to grow in the 3-5% range; and Professional sales to be broadly level with 2006. We expect margins to improve again in School and Professional, and to be stable in Higher Education.

## School: overview

Our School business contains a unique mix of publishing, testing and technology products, which are increasingly integrated. It generates around two-thirds of its sales in the US.

In the US, we publish high quality curriculum programmes for school students covering subjects such as reading, literature, maths, science and social studies. We publish under a range of well-known imprints that include Scott Foresman in the elementary school market and Prentice Hall in secondary. Our school testing business is the leading provider of test development, processing and scoring services to US states and the federal government, processing some 40 million tests each year.

We are also the leading provider of electronic learning programmes for schools, and of 'Student Information Systems' technology which enables schools and districts to record and manage information about student attendance and performance.

In the US, more than 90% of school funds come from state or local government, with the remainder coming from federal sources. Our School company's major customers are state education boards and local school districts.

## School Key Performance Indicators

### US School sales growth versus industry

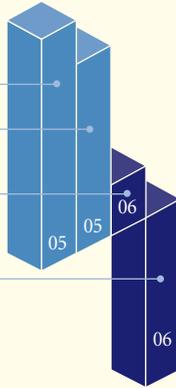
(i) Pearson: 12.1%

(ii) Industry: 9.9%

(i) Pearson: 2.7%

(ii) Industry: (8.8)%

(i) Pearson's total year on year sales growth in basal and supplementary product in the US (ii) the year on year sales growth of the US industry excluding Pearson.

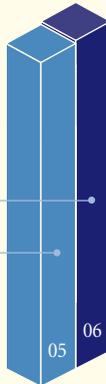


### Adoption cycle win rates

33.0%

32.5%

Pearson's market share by value of new business in US adoption states. Market share is quoted as a percentage of the total value of adoptions that we participated in.



### Testing contract win rates

41%

51%

The lifetime value of US school testing contracts won by Pearson this year as a percentage of the total lifetime value of contracts bid for this year.



Outside the US, we publish school materials in local languages in a number of countries. We are the world's leading provider of English Language Teaching materials for children and adults, published under the well-known Longman imprint. We are also a leading provider of testing, assessment and qualification services. Our key markets outside the US include Canada, the UK, Australia, Italy, Spain, South Africa, Hong Kong and the Middle East.

### School: 2006 performance

£ millions	2006	2005	Headline growth	Underlying growth
Sales	1,455	1,295	12%	6%
Adjusted operating profit	184	147	25%	17%

### Significant share gains in US School publishing

- Pearson US School publishing business up 3%, against an industry decline of 9% (excluding Pearson; 6% decline including Pearson) (source: Association of American Publishers), as we benefit from our sustained investment in new basal programmes and innovative digital services.
- Pearson takes the leading share of the new adoption market\*: 30% of the total market and 33% where we competed. #1 or #2 market share in reading, maths, science and social studies. Total new adoption opportunity of approximately \$670m in 2006, down from \$900m in 2005.
- Innovative digital programme for California takes #1 position and a 43% market share in elementary social studies. Digital curriculum services being developed for new adoptions.
- US School new adoption market expected to grow strongly over the next three years (estimated at \$760m in 2007; \$900m in 2008; \$950m in 2009).

\* In the US, 20 'adoption' states buy textbooks and related programmes on a planned contract schedule or 'adoption' cycle. The level of spending varies from year to year with this schedule, depending on the number of adoptions in the largest states and subjects. In 'open territory' states, school districts or individual schools buy textbooks according to their own schedules, rather than on a statewide basis.

### *Strong growth and continued share gains in school testing*

- US School testing sales up in the high single digits (after 20%+ growth in 2005), benefiting from further contract wins, market share gains and leadership in onscreen marking, online testing and embedded (formative) assessment.
- Acquisition of National Evaluation Systems (NES), the leading provider of customised assessments for teacher certification in the US, with contracts in 16 states including Florida (won in 2006) and California (renewed in 2006). NES expands our testing capabilities in an attractive adjacent market.

### *School technology business broadened*

- Acquisition of Chancery and PowerSchool enhances our leading position in the US Student Information Systems (SIS) market. Integration on track and good growth prospects as schools upgrade information systems to manage and report data on student attendance and performance.
- Organic growth and margin improvement continues in digital curriculum business, Pearson Digital Learning. Continued investment in new generation digital products to meet demands of school districts for personalised classroom learning.
- Four product nominations in six categories, more than any other education company, for the Software and Information Industry Association 'Codie' awards. The products are: *Prosper*, a formative assessment tool for 'at-risk' students; *Write to Learn*, a web-based tool for learning to read and write; *Chancery SMS*, a student information system for middle and large school districts; and *California History-Social Studies*.
- Our technology now touches the lives of many students. The SIS business provides assessment, reporting and business solutions to over 29,000 schools servicing more than 25 million students. PDL's digital curriculum solutions have helped raise the achievement levels of over 20 million students. We have around 3 million students and teachers registered to use one of our online school learning platforms in the US.

### *Good growth in international school*

- International testing businesses continue to benefit from technology leadership. In the UK, we have marked over 9 million GCSE, AS and A-Level scripts on screen. In 2007 we will roll out *Results Plus* across the UK, providing students, teachers and parents with online access to question-level examination performance data.
- In school publishing, UK launch of ActiveTeach technology provides multimedia resources for maths and science teaching and brings market share gains. Market-leading school companies in Hong Kong and South Africa outperform their markets.
- Acquisition of Paravia Bruno Mondadori (PBM), one of Italy's leading education publishers. Good progress in integrating publishing, sales and marketing, distribution and back office operations with our existing Italian business, and in sharing content and technology.
- Successful launch of regional adaptations of *English Adventure* (with Disney), our worldwide English Language Training programme for elementary schools, in Asia and Latin America.

### **Higher Education: overview**

Pearson is the US' largest publisher of textbooks and related course materials for colleges and universities. We publish across all of the main fields of study with imprints such as Prentice Hall, Addison Wesley, Allyn & Bacon and Benjamin Cummings. Typically, professors or other instructors select or 'adopt' the textbooks and online resources they recommend for their students, which students then purchase either in a bookstore or online. Today the majority of our textbooks are accompanied by online services which include homework and assessment tools, study guides and course management systems that enable professors to create online courses. We have also introduced new formats such as downloadable audio study guides and electronic textbooks which are sold on subscription. In addition, we have a fast-growing custom publishing business which works with professors to produce textbooks and online resources specifically adapted for their particular course.

## Business Review *Continued*

In 2006, our Higher Education business generated approximately 80% of its sales in the US. Outside the US, we adapt our textbooks and technology services for individual markets, and we have a growing local publishing programme. Our key markets outside the US include Canada, the UK, Benelux, Mexico, Germany, Hong Kong, Korea, Taiwan and Malaysia.

### Higher Education: 2006 performance

£ millions	2006	2005	Headline growth	Underlying growth
Sales	795	779	2%	4%
Adjusted operating profit	161	156	3%	3%

### Steady growth momentum

- US Higher Education up 4%, ahead of the industry once again.
- Over the past eight years, Pearson's US Higher Education business has grown at an average annual rate of 7%, compared to the industry's average growth rate of 4%.

### Rapid growth in online learning and custom publishing

- Approximately 4.5m US college students using one of our online programmes. Of these, approximately 2.3m (up almost 30% on 2005) register for an online course on one of our 'MyLab' online homework and assessment programmes.
- 16 subject-specific 'MyLab' online homework and assessment programmes now available supporting more than 200 titles. Research studies show significant gains in student success rates and productivity improvements for institutions.
- Strong market share, student performance and institutional productivity gains in college maths, supported by MyMathLab.
- In psychology and economics, two of the three largest markets in US higher education, Pearson publishes successful first edition bestsellers: Cicarrelli's *Psychology* together with MyPsychLab and Hubbard's *Economics* together with MyEconLab. Cicarrelli's *Psychology* increases

Pearson's market share by 3% to 25% and is the bestselling launch of a first edition in the discipline in the past decade.

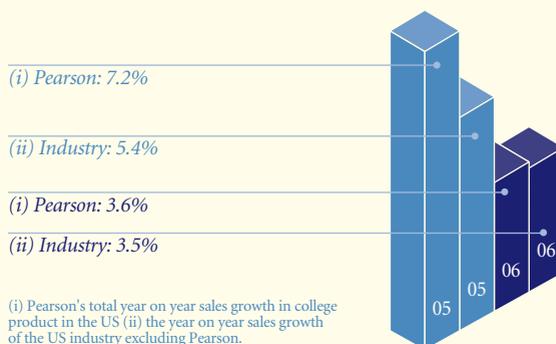
- Continued strong double digit growth in custom publishing – which builds customised textbooks and online services around the courses of individual faculties or professors.

### Good progress in international markets

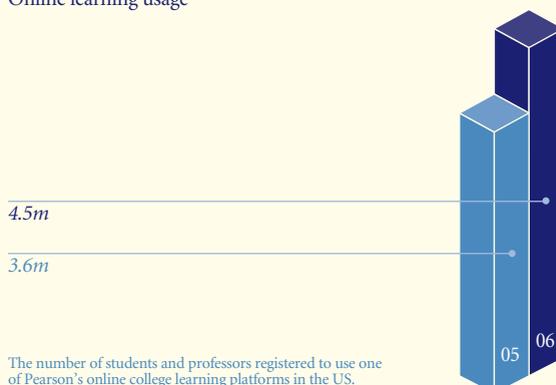
- Good growth in local language publishing programmes. Increasing focus on custom publishing and technology based assessment services with the MyLab suite of products.

### Higher Education Key Performance Indicators

US College sales growth versus industry



### Online learning usage



### Professional: overview

Our Professional education business\* publishes educational materials and provides testing and qualifications services for adults. Our publishing imprints include Addison Wesley Professional, Prentice Hall PTR, Cisco Press (for IT professionals), Peachpit Press and New Riders Press (for graphics and design professionals), Que/Sams (consumer and professional imprint) and Prentice Hall Financial Times (for the business education market). We have a fast-growing Professional Testing business, Pearson VUE, which manages major long-term contracts to provide qualification and assessment services through its network of test centres around the world. Key customers include major technology companies, the Graduate Management Admissions Council, the National Association of Securities Dealers and the UK's Driving Standards Agency. We also provide a range of data collection and management services, including scanners, to a wide range of customers.

### Professional: 2006 performance

£ millions	2006	2005	Headline growth	Underlying growth
Sales	627	589	6%	3%
Adjusted operating profit	60	45	33%	29%

Note: includes Government Solutions

### Professional Testing: rapid organic sales and profit growth

- Professional Testing sales up more than 30% in 2006 (and have doubled over the past two years). Approximately 4m secure online tests delivered in more than 5,000 test centres worldwide in 2006.
- Successful start-up of the worldwide Graduate Management Admissions Test. 220,000 examinations delivered in 400 test centres in 96 countries, in first year of new contract.
- Professional Testing moves from around breakeven in 2005 to profitability in 2006.
- Successful integration of Promissor, acquired in January 2006. Combination brings together two leading international professional testing companies and takes Pearson into new US state and federal regulatory markets.

### Professional publishing: further margin improvement

- Technology publishing profits up as further cost actions offset continued industry weakness.
- Strong performance from Wharton School Publishing and FT Press imprints, aided by Pearson's global distribution and strong retail relationships. 41 titles published in 2006 including Jerry Porras, Stewart Emery and Mark Thompson's *Success Built To Last* (the sequel to *Built To Last*) and Jeffrey Gitomer's *The Little Red Book of Sales Answers*, *The Little Gold Book of Yes Attitude*. Three *Wall Street Journal* business bestsellers, two *BusinessWeek* bestsellers and one *New York Times* bestseller in 2006.

### Government Solutions: sale completed in February 2007

- Sale of Government Solutions to Veritas Capital for £560m in cash, £40m in preferred stock and a 10% interest in the company completed in February 2007.
- Government Solutions contributed £286m of sales and £22m of operating profit to Pearson in 2006.

\* Professional education is not technically a segment under IFRS and therefore has no segment specific key performance indicators.