





**Pearson is a growing company.** In four years, we have more than doubled our annual revenues from £1.8 billion to nearly £4 billion and tripled our operating profit from £216 million to £686 million.

At the same time, we have built a simpler, more integrated media company and made each of our businesses a leader in its market. Today, in every part of the company, we continue to make the moves that will accelerate our long-term growth.

**PREFACE**

- 1 Financial highlights
- 2 Chairman's letter

**STRATEGY**

- 5 Chief executive's review

**GOALS**

- 11 The Pearson goals
- 12 Corporate measures
- 15 Operating measures
- 16 Internet enterprises

**PERFORMANCE**

- 17 The results
- 18 Pearson Education
- 22 The Penguin Group
- 26 The Financial Times Group
- 30 Recoletos
- 31 Financial review

**GOVERNANCE**

- 39 Board of directors
- 40 Directors' report
- 47 Personnel committee report

**FINANCIALS**

- 55 Index
- 56 Profit and loss
- 58 Balance sheet
- 59 Cash flow

**NOTES**

- 61 Auditor's report
- 62 Notes to the accounts
- 98 Five year summary
- 100 Shareholder information



**Pearson Education** • With the acquisition of NCS educational solutions companies, and the launch of a consumer education source on the internet, we are now a leading global education company. Our text books, online learning tools and digital content help to educate more than 100 million people around the world.



**Financial Times Group** • As we invest in international and online expansion, the reach and influence of the Financial Times brand continues to grow. Our network of business and financial newspapers and online services informs the daily decisions of more than four million business people and investors worldwide.



**Penguin** • By discovering a new generation of best selling authors and acquiring Dorling Kindersley, the leader in illustrated reference, Penguin has reinforced its position as one of the world's best-known publishers. It publishes an unrivalled range of fiction and non-fiction, bestsellers and classics, children's and reference works, read by people in 110 countries.

**UCLES**, one of the world's leading testing and assessment organisations, part of the Pearson Group of Learning Network, the most popular in the world. Through our work we have created the world's leading learning and assessment programmes used in schools and universities around the world every year.

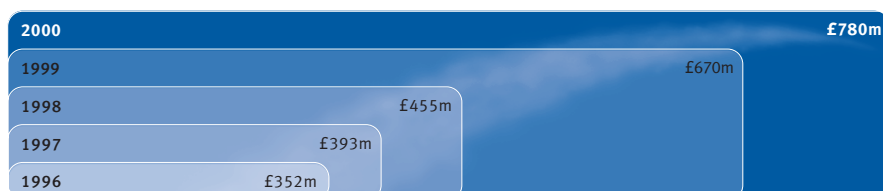
## FINANCIAL HIGHLIGHTS

### ADJUSTED EARNINGS per share



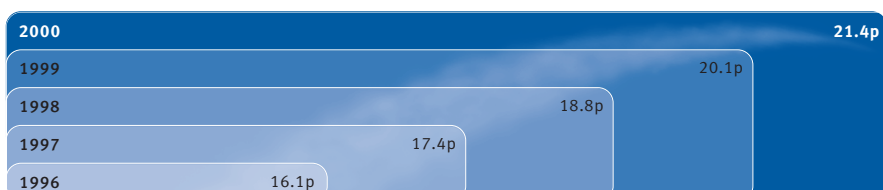
\*after internet enterprises † before internet enterprises

### EBITDA



earnings before interest, tax, depreciation and amortisation (before internet enterprises)

### DIVIDEND per share



	2000	1999
SALES	£3,874m	£3,332m
	\$5,850m	\$5,031m
OPERATING PROFIT before internet enterprises	£686m	£588m
	\$1,036m	\$888m
NET INVESTMENT in internet enterprises	£(196)m	£(39)m
	\$(296)m	\$(59)m
PRE-TAX PROFIT after internet enterprises	£333m	£402m
	\$503m	\$607m
ADJUSTED EARNINGS per share, before internet enterprises	54.6p	47.6p
	82.4¢	71.9¢
ADJUSTED EARNINGS per share, after internet enterprises	31.9p	43.3p
	48.2¢	65.4¢
DIVIDEND per share	21.4p	20.1p
	32.3¢	30.4¢

value of the dollar translated at \$1.51:£1 sterling

**note** - All charts are stated before goodwill, integration costs and non-operating items. Prior year earnings and dividend per share have been restated to reflect the rights issue.



## CHAIRMAN'S LETTER

**To:** Fellow shareholders

**From:** Dennis Stevenson

It has taken three years of hard work to turn Pearson from an attractive collection of diverse businesses into one company with a coherent strategy single-mindedly pursued by every part of Pearson. If you want to read not just about Pearson's future strategy but also an unusually down-to-earth and insightful view of the changing commercial environment, you should turn to Marjorie's report on page 5. I sum up that strategy in two simple statements:

- we want to make outstanding returns for our shareholders by creating, owning, applying and exploiting intellectual property;
- we want to do this in a way that is brave, imaginative and decent.

Last year we made a number of moves – the acquisitions of National Computer Systems (NCS) and Dorling Kindersley, the sale of Lazard, a major investment in our internet enterprises – that we knew, taken together, would suppress our earnings in 2000. We did so because we believe they put us in better shape to deliver longer-term growth across all our businesses. And we did so safe in the knowledge that we would continue to deliver on our key financial goals – sales, margins and cash – at the operating level.

As Marjorie makes clear, this focus on performance is at the heart of all we do. It matters not to us whether the activity could be described as 'old' or 'new' economy; what is important is what works in helping to deliver our strategy. Nothing is certain in this life but I am as confident as I can be that:

- we have a simple strategy that we all understand and believe in;
- we will steadily increase value for Pearson's shareholders.

My confidence stems from the conviction that our colleagues – and the way they feel about being part of Pearson – are the key to creating more value. Yes, competitive material rewards are crucial to motivating the people who work in our businesses. That is why, at this year's annual general meeting, we will be asking for your approval of a new long-term incentive plan. The plan is designed to ensure



LORD STEVENSON • CHAIRMAN

that our global business – anchored as it is, more than ever, in the United States of America – is able to compete worldwide for the very best talent.

But material rewards are only part of the answer. We are fortunate to be part of a company where many of our colleagues choose to make their careers with Pearson when (even following the implementation of our new long-term incentive plan) they could earn greater rewards elsewhere. One of the reasons they stay is because of the second part of our strategy – in every part of Pearson, in everything we do, we aspire to be brave, imaginative and decent (and we expect everyone who works with us to share those aspirations).

In the past year we have also been pleased to see a steady increase in the number of highly talented people – at all levels – who seek to join us. They are excited by our reputation and impressed by the quality of what we do.

I believe that, over the years, our values have ensured that, while being far from perfect, we have lived by ethical and environmental codes of which we can be proud. This year, for the first time, we include in the directors' report formal statements on labour standards, human rights and environmental policy. We will, in future years, report our performance against these policies. But we are also determined to ensure that we won't confuse our ability to 'tick the right box' in terms of our policies with the bigger task of ensuring that we remain true to the values and principles that have been at the heart of Pearson throughout its life.

Pearson is in the happy position of being able to draw on the experience and energy of a very committed group of non-executive directors, whom I thank wholeheartedly for their contribution to our many successes. After nine years as a non-executive director and nearly four years as Chairman of our Personnel Committee, Gill Lewis has decided to step down from the board of Pearson at the AGM. On behalf of the board I want to give particular thanks to Gill for the enormous contribution she has made.

## CHAIRMAN'S LETTER (CONTINUED)

Over the last few years we have been working hard to make Pearson a great place to work. The record performance we are reporting this year is built on the abilities and the creativity of 25,000 people across Pearson, led by a quite out-of-the-ordinary senior management corps. The board is enormously grateful to everyone in Pearson for their commitment, their talent and their hard work. They make this a very special company to work in and to invest in.



Dennis Stevenson



## CHIEF EXECUTIVE'S REVIEW

**Pearson is beginning to make sense. For the last four years we've been honing its strategy and simplifying its parts into a club of complementary businesses. Individually, those businesses lead their markets, and with each other they share assets and values and a consistent way of doing things. There's now a 'Pearson-ness' about us that was more theoretical than real before.**

This approach has helped us to another record year. More importantly, it underscores the fact that we now have a business and a strategy which we're confident will deliver a series of record years into the future.

That doesn't mean we've arrived, or even that we're at a rest stop. It just means we know where we're going. We are about education and enlightenment. About helping children succeed at school or adults succeed in their work. About helping politicians consider different points of view or business people divine markets. About inspiring people to take a fresh look – or enjoy a wry smile – at the world.

That may sound a little grandiose. We certainly recognise the challenges and our limitations. Take interpreting markets, for instance. Sometimes that work is a little close to home. Toward the end of 2000 and the beginning of 2001, it dawned on the world that there aren't two economies after all. Many people had suspected that all along, and suspected that what had been happening was just that markets – and human beings – were tending toward excess, as we always do.

So the trick was to stick with a set of basic principles, whatever your strategy. And we have. We believe

there's only one economy, and it demands to be fed sales and profits, and it thrives on growth. Keeping that in mind we focused our internet development on businesses that were integral to our main pursuits in education and in business information. We looked for ways to relate new ventures rather than spin them off into separate companies.

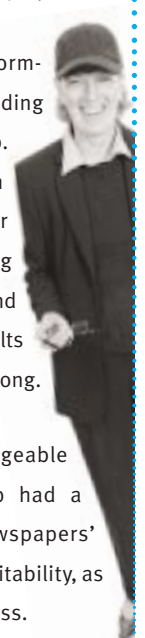
We weren't carried away by the internet euphoria, and we aren't carried away by the doom and gloom now either. Good businesses are still built on good ideas, well executed, and we believe technology can make both the ideas and the execution more powerful.

### THE YEAR 2000

In fact, we've been using the internet for several years to ignite and power our businesses, and last year it played a larger part than ever both in our success in the existing businesses and in the size of our investment in the new ones. But it was only a part.

We had another record operating performance at the same time as we were building our growth potential around the group. The results are discussed in detail on pages 11 to 38. The headlines are that our results were made up of strong operating contributions from all parts of Pearson, and that we've invested to make sure our results of the future will be just as reliable and strong.

**The Financial Times Group** • In a changeable economy, the Financial Times Group had a whopping year, spurred on by its newspapers' continuing growth in popularity and profitability, as well as their versatility and innovativeness.



MARJORIE SCARDINO • CHIEF EXECUTIVE

## CHIEF EXECUTIVE'S REVIEW (CONTINUED)



### BIRDS OF A FEATHER

BOOKS HAVE ALWAYS BEEN A GREAT WAY TO CONNECT PEOPLE – AND NOW PENGUIN IS CONNECTING WITH READERS IN WAYS NEVER POSSIBLE BEFORE. WE WEBCAST INTERVIEWS WITH BEST SELLING AUTHORS LIKE PATRICIA CORNWELL, USING QUESTIONS FROM LIVE AUDIENCES OR EMAILED FROM READERS. READING COMMUNITIES ARE SPROUTING UP EVERYWHERE, NURTURED BY PENGUIN'S ONLINE READERS GROUPS AND NETWORKS SUCH AS PENGUINCLASSICS.COM. IN LESS THAN A YEAR WE'VE BUILT DIRECT RELATIONSHIPS WITH MORE THAN 200,000 BOOK LOVERS, WHO ENJOY THE PENGUIN EXPERIENCE ONLINE AND GIVE US INFORMATION ABOUT THEIR READING HABITS.

Five years ago this group made about £100m in profit and was heavily dependent on one newspaper that sold 300,000 copies, most of them in its home market. In 2000, the FT Group logged a profit of more than £200m. That UK newspaper now exerts influence around the world, with two-thirds of its readers outside the UK. FT.com, its flagship web service, has begun to take on a life of its own, with impressive traffic and growing revenue, and the confidence to integrate itself into a more seamless relationship with the newspaper's editorial and advertising staff.

This kind of transformation was repeated in our other business information operations, too. *Les Echos* continued to be France's most profitable newspaper, with both advertising and circulation well up. At the same time, its business web service was the most popular one in the .fr space.

In Spain, *Expansión* made similar strides, adding to its roster of readers and of advertisers and developing *Expansiondirecto.com* into Spain's leading online business service. Likewise, our partnership paper and online service in Germany (*FT Deutschland*, the first non-English language publication that carries the FT name), as well as those in South Africa, Russia and Portugal, continued to gain ground in their markets. So did the world's best weekly news magazine, *The Economist*.

International, non-English-speaking markets form an increasingly important part of Pearson's strategy. Recoletos, our Spanish media company which, among other things, publishes *Marca*, the largest sports newspaper in Europe, offered part of its ownership to the public market on the Madrid stock exchange in 2000. This allows Recoletos to have a freely traded currency to fund other ventures in Spain and Latin America, as well as to gauge its

progress against its competitors by the market's response. With Recoletos' help, we will try to increase our complement of Spanish businesses in a world where Spanish is one of the three most spoken languages.

**Pearson Education** • Our largest business, institutional education, also took another giant step forward this year, in spite of the fact that it was already the world leader. Sales and profits increased in all businesses. At the same time, we invested in innovation, continuing to develop new online and print services and to build scale across the world in what may be the most important industry of our age.

One in three American children now use one of our math programmes. It is mathematically impossible to graduate from college in the US without being assigned one of our textbooks or online services. In 2000, we continued to improve these odds.

With our most successful reading programme for a decade, our US schools business held on to the market gains it made in 1999. Our US higher education business outperformed the market in its college business, though it was held back a bit by the flat consumer computer book market, in spite of having half the bestsellers in the category. Our share in international education markets, meanwhile, grew in double digits, based both on our business teaching the English language and on our local language programmes.

The September acquisition of NCS has already begun to revolutionise our education business. After seven months of ownership we are more confident than ever that it will make not only outstanding shareholder returns, but also a valuable contribution to the whole process of learning.

SO WHAT DID YOU DO AT SCHOOL TODAY?



IMAGINE HAVING YOUR CHILD'S ATTENDANCE RECORDS, HOMEWORK ASSIGNMENTS AND PROGRESS REPORTS AVAILABLE AT THE CLICK OF A MOUSE. NO MORE RUMMAGING IN THEIR BACKPACK TO FIND OUT HOW THEY'RE DOING AT SCHOOL. OUR NEW NCS4SCHOOL APPLICATION ENABLES PARENTS TO SEE RECORDS, COMMUNICATE WITH TEACHERS AND KEEP ABREAST OF THEIR CHILD'S ACADEMIC PERFORMANCE AND NEEDS, SO THAT THEY CAN PLAY A BIGGER PART IN THE LEARNING PROCESS.

## CHIEF EXECUTIVE'S REVIEW (CONTINUED)

NCS Pearson, as it's now called, is the leader in school software services, testing and data management. With Pearson Education's course content and NCS's ability to provide assessment and student data and connections between schools and homes, we can create educational programmes made to order for each student. Education can be customised. This is the revolution we hope to lead.

We also hope to serve learning needs broader than institutions alone. So in 2000 we launched a consumer learning business. Learning Network, an online network carried on the internet and on AOL, is designed for schools, parents, children, professionals and adults who want to keep on educating themselves. This network of sources, from inside and outside Pearson, provides a range of products and services to help each person assess his needs and fulfill them from something that can be used or bought online.

**Penguin** • Penguin published wonderful books while continuing to deliver the best margins and overall financial performance in the industry. We have been investing in its stock of would-be bestsellers, as well as in its classics and star authors, and this year both

groups turned in award-winning performances. Its list of hits has never been longer, nor has its list of awards for literary excellence.

To add to the glitter, in 2000 we acquired Dorling Kindersley, an entirely different kind of publishing company with a unique formula for exciting imaginations. DK has a store of largely home-grown or purpose-built content made of the artful marriage of beautiful pictures and quality text. Out of that marriage has come an imposing library of digitised images. So we'll be able not only to bring Penguin efficiency to bear on the DK business, we'll also be able to apply its content and images like magic around Pearson.

### ... AND BEYOND

In re-shaping our company, we've tried to take account of where the world is going, as well as our own aims and assets. Over the last two years, that world appeared to be twisted out of recognition by the invisible wire that connects us called the internet. We know that wire hasn't changed the rules of business, but something **has** changed. There has been something of a revolution in the



FT.COM'S AUDIENCE OF MANAGERS AROUND THE WORLD ARE AT THE TOP OR HEADED THERE. ITS NEW CAREER MANAGEMENT SERVICE FT-CAREERPOINT IS AN INVITATION TO SENIOR TALENT TO POST THEIR CVS, BROWSE HUNDREDS OF INTERNATIONAL

RECRUITMENT ADS AND APPLY FOR TOP JOBS ONLINE. RATHER THAN PORING THROUGH THOUSANDS OF CVS, BUSINESSES SAVE TIME USING FT-CAREERPOINT TO FIND THE MANAGERS OF THE FUTURE. THAT'S THE RIGHT CLIMBING PARTY TO JOIN.

world in which we're doing business. We see it in several trends:

**The customer is in charge – really** • This is no longer just a reminder that the customer is always right. It's a fundamental shift in the balance of power from producer to consumer. People can tailor their lives to their personal needs and tastes; create products from off-the-shelf components and block ads from their tv screens. They can have things their way.

**Business is now about services** • To sell printers, you need to sell printing services – theatre tickets, newspapers. The value is in what the product can do. We can't sell just textbooks; we have to sell applications that help teachers use the books to make lessons more engaging and more personal.

**Intellectual property isn't what it used to be** • The shift toward services also means that content is sometimes more valuable when it's paired with applications, or when it's shared in some way. We live in an age of alliances – with suppliers, customers, colleagues, even competitors. Information or assets shared with them may become richer and make our ways of working more efficient.

These trends have led us to begin to change a lot about what we're creating and how we're selling and distributing it, as you can see in the illustrations on these pages. Our emphasis is now on personalising our services; on connecting with our customers and connecting them with each other; and on looking for flexible ways to share our assets to widen our markets and accelerate our growth.

Nowhere are these trends more applicable than in education. We all learn at different paces, in different ways, with different motivations. Technology allows us to make the most of those differences. We can create personalised learning – dynamic courses with materials not bound by two-dimensional textbooks from only one source or teachers not bound by assumptions about what the class is learning. It allows us to assess each student's – or an entire class' – progress, add relevant data on the student, connect those who have an interest in the process (teachers, parents) and help everyone succeed in education. What's more, we can do this in a programme prescribed by an institution or chosen by a consumer in his own home.

**NOW PROFESSORS CAN ASK THE CLASS**



PEARSON'S MULTIMEDIA PACKAGES BRING A NEW DIMENSION TO COLLEGE EDUCATION. CHEMISTRY, THE CENTRAL SCIENCE, IS JUST ONE OF OUR TEXTBOOKS WHICH COMES WITH AN INTERACTIVE SERVICE WHERE STUDENTS CARRY OUT SIMULATED EXPERIMENTS OR COMPLETE TESTS ONLINE, GET THEIR RESULTS IMMEDIATELY AND

COLLABORATE ON ASSIGNMENTS WITH OTHER STUDENTS. AND ALL THE MATERIAL ALSO APPEARS ON A HANDHELD PC, SO THERE'S NO NEED TO TAKE A BOOK TO CLASS. PROFESSORS CAN ASK QUESTIONS IN CLASS, FIND OUT INSTANTLY WHAT THEIR STUDENTS ARE LEARNING AND CUSTOMISE LECTURES TO THEIR NEEDS.


## CHIEF EXECUTIVE'S REVIEW (CONTINUED)

These trends may change. There's certainly no time or room for complacency. We can still remember saying blithely that we were a 'content' company and thinking our rich stories and insights and ideas were enough. Our world-class brands could do the rest.

Now we need more. Now we have to provide the utility and connectivity that make our content special and give our brands personality. We have to help our customers use our content in a way that makes life easier for them. And whatever we do has to make a return for our shareholders. We've achieved record results this year and for each of the four years before that. That's a trend we plan to follow well into the future.

To succeed in all this requires imagination. And that can come from only one place in Pearson — from the

thousands of people here who every day do their jobs with self-confidence and creativity and respect for each other and those they do business with. In 2000, the people who work in Pearson once again went all out and produced wonderful products, exemplary marketing and delivery, unstinting support services and long-term value for shareholders. Thanks to all of you. Since most of you are already shareholders, you'll reap the value you've created and have the satisfaction of having done some very worthwhile things in the process.



Marjorie Scardino

DAVID BELL • DIRECTOR FOR PEOPLE



**WE'RE NOTHING WITHOUT OUR PEOPLE. WE THINK IT'S OUR JOB TO CHALLENGE AND INSPIRE THEM — AND TO HARNESS THEIR IDEAS ABOUT THE FUTURE OF PEARSON. IN FEBRUARY 2001, WE BROUGHT TOGETHER IN CALIFORNIA 140 OF OUR NEWEST, MOST PROMISING PEOPLE TO BRAINSTORM NEW STRATEGIES, IDENTIFY BUSINESS OPPORTUNITIES AND PLAN WAYS FOR OUR COMPANIES TO WORK TOGETHER MORE CLOSELY. ALL THE PHOTOS RUNNING THROUGH THIS REPORT WERE TAKEN AT THE CONFERENCE.**

NICK OUTLAW • PEARSON PLC



## THE PEARSON GOALS

**A review of Pearson's performance in 2000 needs first to be put in the context of our goals and targets. What are we trying to achieve? How do we measure progress? What are the rewards of success, and the penalties of failure? These goals provide the bridge between the group's strategic objectives which Marjorie has just outlined and the review of performance which follows.**

The starting point for all our targets is that we are aiming for faster growth and a higher quality of financial performance than our peers in the media industry, in Europe and the US, and than the broader stock market indices to which we belong.

We manage Pearson's operations with the help of a variety of key performance indicators which allow us to monitor performance against consistent criteria. Some of these are specific to individual businesses – only the FT Group need be concerned with the mix of circulation and advertising revenues for example – while others are relevant to every part of Pearson.

There are six financial measures which we track carefully and use to drive improvements in performance across Pearson. Three of them, the corporate measures, relate to the performance of Pearson as a whole. The others, the operating measures, provide the framework for the financial plans of each individual business.

The corporate measures directly align our targets with the preferred valuation criteria of our shareholders and support the requirement to fund a rising stream of dividend income. They are used to determine both short and long-term rewards for senior corporate management.

The operating measures form the basis of annual management bonus plans within each company. They are agreed as a package, so that excessive emphasis on cash generation does not jeopardise sales growth, or vice versa.

We have created separate measures for our internet enterprises, which we discuss towards the end of this section.





## CORPORATE MEASURES

### 1 • ADJUSTED EARNINGS

In 1997 we committed to increase adjusted earnings per share, the best definition of underlying earnings growth that we could find, at a double digit annual rate. The purpose was to deliver superior growth in the measure of performance most widely used by our shareholders and also to express our commitment to deliver this growth year in, year out. We subsequently excluded internet enterprises from this definition of earnings since it was clear that, in the early stages of their development, these enterprises were not being valued by our shareholders on the basis of earnings (or lack of them) and since the application of the double digit standard to our total adjusted earnings would have resulted in our internet enterprises being starved of much-needed investment.

We have achieved this double digit growth in each of the four years since the target was set. In 2000 adjusted earnings per share increased by 14.7% to 54.6p. This growth was helped by a two point reduction in the rate of tax used to calculate adjusted earnings (though we would have achieved our double digit target even without the benefit of this lower tax rate).

### 2 • EBITDA

In addition to earnings per share we focus on two corporate financial indicators which help us chart our course and, where appropriate, correct it. The first is EBITDA (earnings before interest, tax, depreciation and amortisation) which is a close proxy for operating cash flow but, like earnings per share, can be derived from a review of the profit and loss statement. As changes in accounting standards relating to deferred tax, goodwill amortisation and other non-trading items make it more difficult, in

our view, to track underlying changes in performance from year to year through earnings per share, we shall place greater emphasis on EBITDA as a measure of performance. It is increasingly used by analysts as a basis for valuing media companies such as Pearson.

The table illustrates progress over the past five years. Last year EBITDA (before internet enterprises and integration costs) increased by 16% to £780m, while over the whole five year period the compound rate of growth has averaged 22%.

### 3 • FREE CASH FLOW

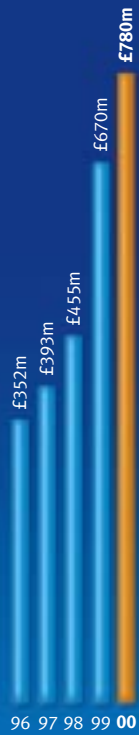
Free cash flow per share (operating cash flow less tax paid on operating profits and interest paid) is another highly relevant measure since it defines the capacity of the company to reinvest in the business and fund dividends to shareholders without incurring additional debt. The progress of free cash flow needs to be measured over a period of years however, since performance in any one year can be affected by large individual investment programmes or even by the timing of the collection of receivables from key customers.

2000 saw free cash flow of 49.1p per share, a modest increase on 1999 which was a year of exceptionally strong cash performance. Growth in free cash flow per share currently determines the award of Pearson Equity Incentives in the senior management reward plan (see p48).

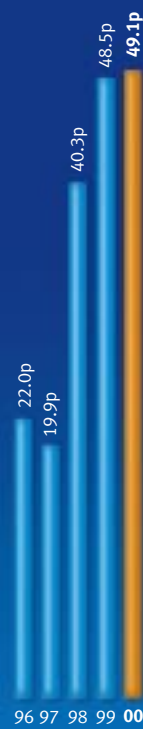




**1 • ADJUSTED EARNINGS**  
per share



**2 • EBITDA**



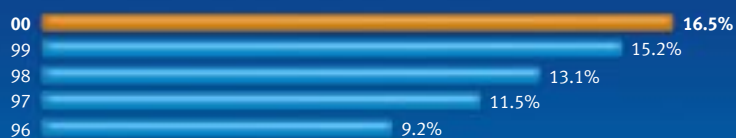
**3 • FREE CASH FLOW**  
per share

Before internet enterprises, goodwill, integration costs and non-operating items.  
Prior year earnings per share and free cash flow per share have been restated to reflect the rights issue.

#### 4 • UNDERLYING SALES GROWTH



#### 5 • TRADING MARGIN



#### 6 • CASH CONVERSION



Before internet enterprises, goodwill, integration costs and non-operating items.  
See page 99 for additional information.

## OPERATING MEASURES

### 4 • UNDERLYING SALES GROWTH

Achieving superior growth in sales, from both established and emerging markets, is critical to Pearson's success. We exclude from our calculation of sales growth the impact of acquisitions and disposals on the one hand and currency movements on the other. This gives us, we believe, the best proxy for underlying growth.

We have accelerated Pearson's underlying sales growth in each of the past four years due largely to a programme of internal investment across the company. At the same time we have changed the mix in the overall Pearson portfolio towards higher growth assets. Last year's underlying sales growth of 9.2% was the highest on record.

### 5 • TRADING MARGIN

Trading margin measures our ability to turn sales into profit. Since the sales contribution of associates and passive investments is not included in our consolidated revenue, we also exclude their profit contribution in arriving at a definition of trading profit.

The consistent strengthening of margins reflects increased levels of profitability in each of our key businesses. We believe that the FT Group, Pearson Education and Penguin are now achieving margins which are 'best in class' for their respective industries. The higher level of profitability reflects both attention to costs and the impact of higher sales growth on operating profit.

### 6 • CASH CONVERSION

We believe that Pearson should be able to convert at least 80% of its profit into cash flow after funding the working and fixed capital investments necessary to deliver superior growth. In 1998 and 1999 we exceeded that target by a healthy margin as the group benefited from a number of non-recurring cash items and timing variances.

In 2000 we reverted to a more normal pattern but still exceeded the 80% threshold with a few percentage points to spare. The effective management of working capital, in particular, will remain a high priority for us in 2001 and beyond.

## CAPITAL ALLOCATION

In addition to the performance measures described above, we determine the allocation of capital within the company with the support of a financial model which relates the expected return on investment to the company's weighted average cost of capital, the two most important components being the cost of equity and the cost of debt. This model is used to appraise acquisition proposals as well as internal investments. We also employ it to analyse the subsequent performance of major acquisitions and investments.

### UNDERLYING SALES GROWTH ANALYSIS

TOTAL GROWTH	£542m
PORTFOLIO CHANGES	£115m
FOREIGN EXCHANGE	£125m
INTERNET ENTERPRISES	£38m
UNDERLYING GROWTH	£264m

## INTERNET ENTERPRISES

We substantially accelerated the pace of investment in our internet activities last year, although we also remained very selective about the projects and initiatives which we were prepared to support. The impact of this higher investment can be seen in both the sales and net investments attributable to our internet enterprises in the course of 2000.

Pearson's internet enterprises are discrete services which generate pure online revenues and which incur costs that are capable of separate identification. They are concentrated in the FT Group and education, and an analysis of their performance in 1999 and 2000 is shown below:

	2000	1999
REVENUES	£45m	£7m
NET INVESTMENT	£(196)m	£(39)m

The biggest area of investment last year was FT.com, which spent heavily on marketing in order to raise awareness of the brand. This strategy appears to have been successful, with substantial growth in both unique monthly users and in monthly page views (see page 28). We expect the net investment in FT.com to be substantially lower this year as revenues, and particularly non-advertising related revenues, should again show a dramatic increase, while costs associated with marketing and technology support will be much lower.

Our principal initiative in the education field is Learning Network, our consumer education portal. Learning Network's revenues were very small in 2000, as the portal was only launched towards the end of the year. We expect a much higher level of revenue in 2001 as Learning Network converts the already very substantial level of traffic to the site into customer relationships and revenue.

The accelerated investment is already driving up revenue in this area – last year internet enterprises contributed revenues of £45m and we are looking for a good deal more this year. Our confidence in the revenue growth prospects, coupled with our ability to manage costs aggressively at short notice, have encouraged us to project break-even for the FT Group's internet enterprises as early as the last quarter of next year, and break-even for Learning Network just 12 months after that.

We have established a number of specific performance indicators for these businesses. We focus heavily, for example, on the quality and loyalty of the internet audience as measured by the number of pages viewed during a visit, the average length of stay on the site and the frequency of return visits. We set targets by reference to these indicators and continue to fund the businesses only as the milestones corresponding to these targets are achieved.

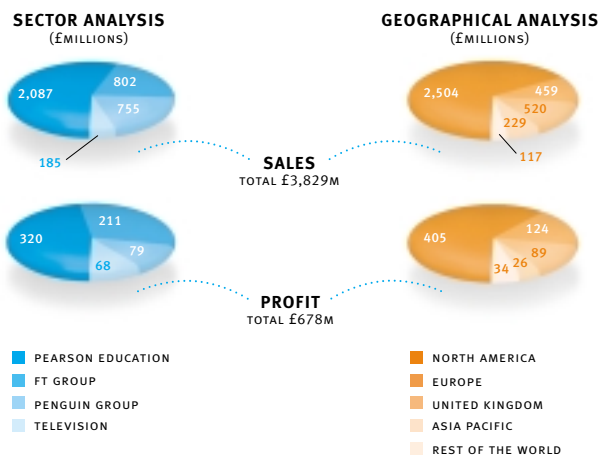
As these businesses become established and demonstrate their viability, the more familiar and traditional financial measures – revenue growth, profit and loss, and cash performance – become relevant and are used to assess performance. We have reported on the financial performance of our internet enterprises as a separate item within our operating profits, to provide greater transparency to shareholders. The internet is becoming increasingly integral to all our businesses. As our internet enterprises mature the distinction between them and our more established activities will become less appropriate.

## THE RESULTS

In 2000, sales grew from £3,332m to £3,874m and operating profit, before goodwill, internet enterprises and integration costs, increased from £588m to £686m.

Pre-tax profit, before goodwill, exceptional and non-operating items, fell from £402m to £333m, as we stepped up investment in our internet enterprises. The net costs of developing our internet enterprises increased from £39m in 1999 to £196m, as we accelerated their path to profitability. The net costs of developing these internet enterprises is expected to fall significantly in 2001.

The results also reflect a number of major strategic moves made during the year. We completed the disposal of our stake in the Lazard banking houses for £436m. We merged Pearson TV with CLT-Ufa and took a 22% stake in the RTL Group, which is Europe's largest television company and was valued at year-end at around £8bn. We made the £1.7bn acquisition, financed by a rights issue, of NCS, one of the leading commercial testing and educational services companies in the US. We acquired, for £318m, Dorling Kindersley, the worldwide illustrated reference publisher. We also made a number of smaller acquisitions and strategic investments. The net effect of these portfolio changes, which will allow us to accelerate revenue and earnings growth in 2001 and beyond, was to reduce operating profit by some £10m and pre-tax profit by around £20m in 2000.



continuing operations before internet enterprises, goodwill and integration costs

SHARON SILVER • PEARSON INC



WE HAVE ACCELERATED PEARSON'S UNDERLYING SALES GROWTH IN EACH OF THE PAST FOUR YEARS. LAST YEAR'S UNDERLYING SALES GROWTH OF 9.2% WAS THE HIGHEST ON RECORD.

## PEARSON EDUCATION • PROFILE

There has never been a better time to be in the business of education. While governments around the world invest more to educate their young people, individuals devote more of their personal hours (and finances) to help their children and to improve their own careers, earnings and life opportunities.

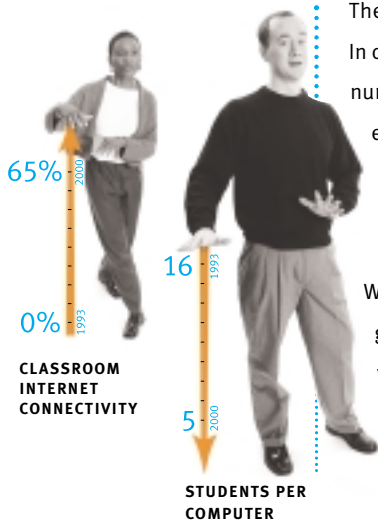
Over the past three years, through acquisitions, strategic alliances and organic growth, we have created the world's leading learning company. In the US, our largest single market, our educational publishing operations play a key role in meeting the demand for first-class curriculum, both in print and online. This market, valued at some \$8bn (a small proportion of the \$740bn invested in education in the US each year) is currently growing on average at around 8% per year.

With federal and state governments wanting both to measure academic progress against clear standards and modernise their school systems, we are seeing faster rates of growth in demand for testing and the enterprise software that powers many schools. The acquisition of NCS, completed in September 2000, means we can meet this demand and work with schools to embed assessment as part of the daily curriculum and to tailor learning to the needs of each student. And, as the internet becomes an integral part of both the home and the classroom, our Learning Network links teachers, parents and students in ways never possible before. In addition, by facilitating 'anytime, anywhere' learning, it enables us to take a leading role in the faster growing markets of online consumer learning and business education and management development.

The trends in the US are also playing out in developed countries around the world. In developing countries, school rolls are growing even more rapidly as an increasing number of students stays on longer at school. And, around the world, ownership of educational publishing and learning companies is often fragmented, creating major opportunities for consolidation and growth. As the world's most international education company, we are in a very good position to capitalise on these trends.

We have all the pieces – the most comprehensive range of educational programmes, leadership in testing, assessment and enterprise software and the very best in online consumer and professional learning – to participate in the learning revolution, and to profit from the growth it brings to the business of education.

KAREN MCLEAN • PEARSON EDUCATION



ERIC SVENDSEN • PEARSON EDUCATION

TEACHERS AND STUDENTS ARE LOGGING ON. IN THE US, THE NUMBER OF CLASSROOMS CONNECTED TO THE INTERNET AND THE NUMBER OF COMPUTERS PER CLASSROOM ARE GROWING FAST.

SOURCE: QUALITY EDUCATION DATA



### PEARSON EDUCATION

The acquisition of NCS has transformed Pearson Education into the world's leading integrated education company, linking curriculum, assessment and data management. The NCS operations have been integrated into our US school, US higher education & professional and international businesses.

#### US school

We are the leading K-12 (kindergarten to 12th grade) curriculum, testing and software company in the US. Our premier elementary (Scott Foresman) and secondary (Prentice Hall) imprints publish some of the very best school programmes, covering subjects such as reading, literature, math, science and social studies. We are a leading publisher of online assessment and digital courseware through NCSLearn (which combines Novanet with the Computer Curriculum Corporation) and the Waterford Early Reading Programme. We also publish supplementary teaching aids for both elementary and secondary schools. We are one of the leading commercial testing companies in the US, scoring and processing some 40 million student tests across the US every year. And more than 40,000 of the 110,000 schools use at least one of our suite of student curriculum, instructional management and financial software packages.

#### US higher education & professional

We are the leading higher education publisher in the US, with imprints such as Addison Wesley, Allyn & Bacon and Prentice Hall. We publish around one in three of all the text and online programmes studied on US campuses. Our professional and technology group publishes leading computer and information technology titles, with imprints such as Addison Wesley, Adobe Press, Cisco Press, New Riders, Peachpit, Prentice Hall, Que and Sams, complemented by Informat.com, our online information technology service. Our government solutions group manages and processes student grant applications on behalf of the US Department of Education and has a number of education related contracts with various government departments.

#### International

We are a leading publisher of text and online programmes in school, higher education and professional markets in countries all around the world. With our Longman imprint, more people learn English as a second language with our programmes than with those of any other publisher. We also create, manage and process student tests in countries all around the world.

#### FT Knowledge

In July 2000, we acquired The Forum Corporation, one of the top corporate training companies in the US, for £61m. It has combined with FT Knowledge to create one of the world's leading corporate training and elearning companies. The combined business provides learning solutions and training programmes in executive development, sales, customer service, management, leadership and finance for both corporations (our clients include 130 of the Fortune 500 companies) and individuals.

#### Learning Network

In September 2000, following the acquisition earlier in the year of Family Education Network for £96m (87% of the equity), we launched our Learning Network ([www.learningnetwork.com](http://www.learningnetwork.com); America Online Keyword: Learning Network). Learning Network is the leading consumer education source on the web, providing educational content and reference sources – as well as applications and services – for teachers, school students, parents and anyone interested in professional development and lifelong learning. By the summer of 2001, Learning Network will offer similar services to college professors and students.



OVER THE PAST FOUR YEARS, THROUGH ACQUISITIONS AND ORGANIC GROWTH, PEARSON HAS BECOME THE WORLD'S LEADING EDUCATION COMPANY.

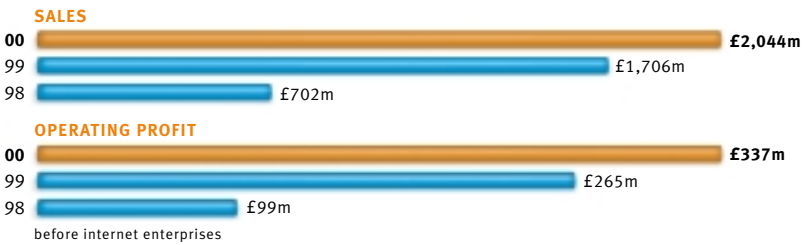
\* full year pro forma sales including NCS



BARBARA CUNSOLO • PEARSON EDUCATION

## PEARSON EDUCATION • PERFORMANCE

Sales at Pearson Education increased to £2,044m with underlying sales, held back by softness in the consumer technology markets, increasing by 5.4%. Underlying profits, boosted by integration benefits flowing through from the integration of the Simon & Schuster and AWL education businesses, increased by 13.4%.



After becoming part of Pearson Education on September 8, NCS contributed revenues of £146m and operating profit of £15m, meeting our revenue and profit expectations. It benefited from its leadership both in student testing and delivering enterprise software solutions to schools. The integration of NCS with Pearson Education is on track to deliver \$50m of annual cost savings by the end of 2002.

Our US school business increased sales by 10%, excluding revenues from NCS. Building on a very strong performance in 1999, we made significant market share gains in some key adoptions, benefiting from a range of new print and online programmes. In secondary science, Prentice Hall School took a 40% share in the major state adoptions including California and our new Scott Foresman reading programme grew market share from less than 5% to approximately 25% nationwide. We also continued to build on the success of our best selling math programmes and took the leading position in secondary social studies.

The US higher education and professional business increased sales by 9% (excluding revenues from NCS), gaining market share and growing margins. The college business delivered particularly strong growth in math, computer sciences, history and developmental English and continued to invest in combined text and online programmes. Its continued leadership in the college business helped to mitigate the impact of weakness in the consumer IT publishing market.

The international business increased sales by 18% (excluding revenues from NCS). Our major international operations all reported double digit revenue growth, with particularly strong progress in Latin America and English language training. We extended our lead in the international education market through a series of acquisitions in France, Brazil, Korea and Japan.



TRUC NGUYEN • FT KNOWLEDGE

PETER JOVANOVIĆ • CHIEF EXECUTIVE PEARSON EDUCATION

PEARSON EDUCATION STEPPED UP ITS MARKET SHARE IN READING IN THE US WITH THE LAUNCH OF SCOTT FORESMAN'S NEW PROGRAMME.



**OPERATING PROFIT ANALYSIS**

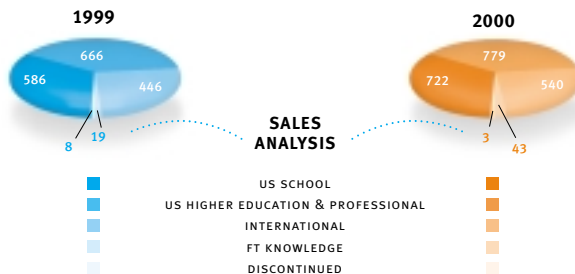
	2000	1999
PEARSON EDUCATION	£337m	£265m
FT KNOWLEDGE	£(17)m	£(8)m
<b>TOTAL</b>	<b>£320m</b>	<b>£257m</b>
INTERNET ENTERPRISES	£(83)m	£(3)m

The integration of the Simon & Schuster and Addison Wesley Longman businesses is now completed and in 2001 is expected to deliver the projected \$130m in annual cost savings. In the two years since the acquisition of the Simon & Schuster education businesses, our core US school and US college operations have increased revenues by an average of 8% per year on an underlying basis.

FT Knowledge made sales of £43m and losses of £17m as it invested in developing its corporate learning and executive education businesses in a market that is enjoying rapid worldwide growth. FT Knowledge merged successfully with The Forum Corporation; extended its financial training company, New York Institute of Finance, to Europe and Asia; launched FTdynamo, an online service focusing on world-class management thinking; and continued to develop online courses for the finance, investment and marketing professions.

Learning Network was launched successfully in September and is now established as one of the 50 most popular websites in the US. It is moving quickly to translate that traffic into the revenues which will ensure it breaks even by the end of 2003. At the same time, it is helping to drive revenue growth across Pearson's businesses.

Pearson Broadband, a new initiative to create interactive education television for K-12, higher education, professional and lifelong learning markets, will launch its first products in 2001.



JITKA BREJLOVA • INCS PEARSON

MONTH	VIEWS
SEPTEMBER	71m
OCTOBER	103m
NOVEMBER	88m
DECEMBER	71m
JANUARY	121m
FEBRUARY	134m

LEARNING NETWORK PAGE VIEWS HAVE INCREASED FROM 71 MILLION TO 134 MILLION IN SIX MONTHS.



## THE PENGUIN GROUP • PROFILE

As one of the most innovative names in consumer publishing, Penguin continues to seek to lead an industry valued at around \$15bn and growing at around 4% per year. Penguin aims to grow faster than the market by investing in great authors, targeting higher growth segments (such as children's publishing and illustrated reference) and building the Penguin brand, which is one of the most recognised media brands in the world.

We are one of the premier English language publishers, ranking in the top two in all our major markets. Three years ago, we set out to increase investment in building a bigger family of best selling authors and developing a new generation of literary talent. This investment is paying off with a record number of best selling titles, more first novels making it on to the bestseller lists and a host of major literary awards on both sides of the Atlantic.

We are also investing more in the technology and partnerships that enable us to connect with our readers. By developing companion websites, promoting author webcasts and forming online communities (around particular genres such as romance, science fiction and mystery), we can form closer, more direct relationships with our readers. This helps us to target our marketing, generating new sales across Penguin. At the same time, we are looking to the future, taking our titles into ebook format with a range of partners.

However, the biggest change at Penguin over the last year has been the acquisition of Dorling Kindersley, the world's premier family illustrated reference publisher. It gives us the ability to lift sales and profits as we bring Dorling Kindersley up to Penguin's best-in-class margins and use Penguin's marketing and distribution network to boost sales of Dorling Kindersley titles. We also aim to sprinkle the Dorling Kindersley magic right across Pearson to enhance the appeal of some of Pearson Education's leading school programmes, enrich the Lifelong Learning channel of our Learning Network and add to our new broadband education television properties.

It is one more example of how Penguin continues to follow new directions, finding better ways of getting things done at every stage of the publishing process. As we do so, we will focus on what we do best – publishing the very best books on any subject in any format.

NICOLA HARLE • PENGUIN UK





### PENGUIN

Penguin is one of the world's premier English language publishers – number one in the UK, Australia, New Zealand and India and number two in the US and Canada. It publishes the very best new fiction and non-fiction, literary prize winners and commercial blockbusters on subjects ranging from history and science to essential reference. Our imprints include Allen Lane, Avery, Berkley Books, Dutton, Hamish Hamilton, Michael Joseph, Plume, Putnam, Riverhead and Viking.

Our venture into ebooks is just beginning and we are pursuing a number of initiatives with our ebook fulfilment partner, Lightning Source. We've also joined with Gemstar, makers of ebooks, to distribute books by select best selling authors and we have hundreds of Penguin titles already on pilot programmes at Rocketbook, Softbook and Peanut Press.

### Children's

We are the world's leading children's publisher, helping characters such as Peter Rabbit, The Little Engine That Could and Spot capture the imagination of children all over the world. Our children's imprints include globally recognised names such as Puffin, Frederick Warne, Dutton, Grosset & Dunlap, Dial Books and Ladybird.

### Classics

The world has not changed so much that the best literature of several thousand years and countless cultures has lost its relevance. From the first history of Herodotus to the novels which shook the 20th Century, we are the leading publishers of classic literature in the world. With over 1,600 titles ranging from poetry to history, we have created the largest online resource dedicated to the world's classic literature at [penguinclassics.com](http://penguinclassics.com).

### Dorling Kindersley

We are now the world's premier illustrated reference publisher. Aiming to be a complete 'cradle to grave' publisher that families can grow up with, we produce books for children of all ages and books for adults covering a huge variety of subjects including childcare, health, gardening, food and wine, travel, business and sports. Designed to make complicated subjects simple, DK has built a unique and attractive graphic style which is now recognised around the world. Not only does our 'lexigraphic' design approach make our books easily translatable across cultures, but it's formed the basis of our library of 2.5 million wholly owned digital images which have many applications – in print or online.

REBECCA FOLLAND • PENGUIN UK  
THOMAS ABRAHAM • PENGUIN BOOKS INDIA



IN THE UK, 39 PENGUIN TITLES REACHED THE BOOKSELLER BOOKTRACK TOP 15 BESTSELLER LIST IN 2000 – UP 22% ON 1999.



IN THE US, 106 TITLES HIT THE NEW YORK TIMES BESTSELLER LIST – UP 56% ON 1999.

RICHARD PASCOCCIO • PENGUIN PUTNAM

## THE PENGUIN GROUP • PERFORMANCE

The Penguin Group (or Penguin Putnam as we are known in the US) posted its best ever performance in 2000. Underlying sales increased by 6.2% and underlying profits by 19.6%.



\* includes the Dorling Kindersley acquisition, completed on 9 May 2000. DK broke even on sales of £125m

Penguin's success was built on increased investment and development of new author talent and established best selling authors such as Tom Clancy, Patricia Cornwell, Clive Cussler, Spencer Johnson, Nora Roberts and many others.

In the US, Penguin Putnam achieved record revenues and profits and gained market share across all categories – adult hardcover, mass market, trade paperback and children's books. It landed 106 titles on the *New York Times* bestsellers lists, up 56% on 1999, including 13 titles that reached the number one position. Its adult hardcover and paperback titles spent a total of 600 weeks on the *New York Times* bestseller lists, up 36% on 1999. In the UK, Penguin had 39 titles in *The Bookseller* Booktrack top 15, with best selling authors including Alex Garland, Jeremy Paxman, Sue Townsend and Jamie Oliver, whose *Return of the Naked Chef* was the number one book for 16 weeks.

Penguin titles won some of the most prestigious industry awards, including the Whitbread Prize (Matthew Kneale's *English Passengers*), the Whitbread first novel award (Zadie Smith's *White Teeth*) and, in the US, a National Book Award for Non-fiction (Nathaniel Philbrick's *In the Heart of the Sea*). Our US children's publishing division published titles that won the 2001 Caldecott Award (Judith St George and David Small's *So you Want To be President?*), the 2001 Newbery Award (Richard Peck's *A Year Down Yonder*) and the 2001 Coretta Scott King Award (Joan Bauer's *Hope was Here*). It is the first time a single publisher has ever won all three awards in the same year.

DAVID WAN • PRESIDENT PENGUIN GROUP



FROM THE BEST COOKERY BOOKS TO THE MOST POPULAR FICTION, PENGUIN IS ALWAYS ADDING NEW AUTHORS TO ITS MIX. IN THE US, FOUR OF OUR FIRST-TIME AUTHORS BECAME MASS MARKET SUCCESSES IN 2000.

All the stars are aligned for an even stronger performance in 2001. We are publishing a raft of new books this year by existing best selling authors – among them Patricia Cornwell, Maeve Binchy, Amy Tan and Nick Hornby. Dorling Kindersley also has a powerful line-up of new books. And we are continuing to step up investment in publishing new authors. We are investing in online and ebook enterprises too, focused on securing long-term growth opportunities and creating more direct relationships with our readers. During the year, we developed hundreds of new author websites and staged interactive Yahoo! webcasts in the US with our best selling authors.

The integration of Dorling Kindersley went to plan. We consolidated DK's warehousing with Penguin, merged the finance systems and combined the UK sales and marketing functions. As a result, we have significantly improved operating efficiencies. We steered the business to break even in 2000 and we expect significant revenue and profit growth over the next few years. Dorling Kindersley is also opening new revenue opportunities across Pearson, creating new printed and online learning materials with Pearson Education and developing services for the lifelong learning market with Learning Network and Pearson Broadband.



MATTHEW BRODIN • FT GROUP

DK'S LIBRARY OF 2.5 MILLION BEAUTIFUL IMAGES OPENS UP MANY OPPORTUNITIES ACROSS PEARSON

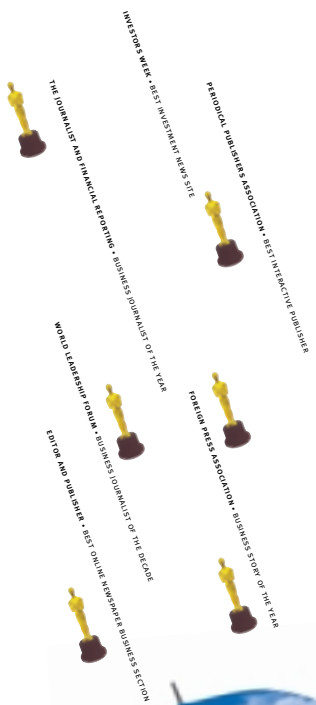
## THE FINANCIAL TIMES GROUP • PROFILE

With the rise of private investment, the increase in cross-border mergers, acquisitions and alliances, and the globalisation of business and investment, there is ever more demand for reliable business information and insight. While the US newspaper industry is expected to grow at 6% from 2000 to 2004, the online financial news sector is expected to grow at 15% per year (sources: Veronis Suhler/Simba). In Europe, JP Morgan predicts that the number of people using online investment services will grow from four million in 2000 to 18 million in 2003, an annual growth rate of 65%.

In 1997, convinced that the *Financial Times* was a very special international brand with unique and valuable content, we began to invest heavily in its growth. We have expanded internationally, launching a new edition for the US and extending our network of print sites around the world. Building on our network of national business newspapers, we have broken into new markets, with the launch of *Vedomosti* in Russia and *FT Deutschland* in Germany. And, with FT.com at the heart of our network of international business, investment and personal finance websites, we are expanding both our audience and our range of products and services.

This investment is paying off handsomely, with our business newspapers reaching record circulation and advertising growth and with our internet enterprises gaining huge popularity and moving towards profitability in their own right.

The FT Group will grow by continuing to do what we do best: providing authoritative news and analysis in a global context. We will continue to work hard both to beat the competition to major international business stories, and to ensure our journalism meets the very high standards that our readers expect. We will continue to provide the means by which many advertisers can communicate with a highly attractive and 'hard-to-reach' audience of international business people. And we will deliver the new premium products and services that will enable our customers to manage their businesses, careers and investments more effectively.



KIM HARRIS • FT BUSINESS

AWARDS ARE RAINING DOWN ON THE FINANCIAL TIMES GROUP'S NEWSPAPERS AND ONLINE SERVICES.



### FINANCIAL TIMES GROUP

The Financial Times Group, one of the world's leading business information companies, aims to provide a broad range of business information, analysis and services to a growing audience of internationally minded business people. The *Financial Times* newspaper is printed in 18 cities around the world and has one of the world's fastest growing international readerships. FT.com, the newspaper's internet partner, combines agenda-setting editorial with relevant financial data and discussion groups, as well as a broad range of business tools including the largest search function on the internet.

### European business newspapers & online services

Our pan-European network of national business newspapers and online services includes France's leading business newspaper and website, *Les Echos* and *lesechos.fr*, and Spain's leading business newspaper and website, *Expansión* and *Expansiondirecto.com*. In February 2000 we launched in partnership with Gruner + Jahr a new German language newspaper, *FT Deutschland*, with a fully integrated online business news and data service.

### Securities and specialist financial information

Through a controlling interest in Data Broadcasting Corporation, we are one of the world's leading sources of securities pricing and specialist financial information to global institutional, professional and individual investors. Our products include eSignal, an online real-time quotation service for brokers and active traders.

### Business information

FT Business produces specialist information on the retail, personal and institutional finance industries. It publishes the UK's premier personal finance magazine, *Investors Chronicle*, and *The Banker*, *Money Management* and *Financial Adviser* for professional advisers.

### Private investor information

FTMarketWatch, a joint venture with CBSMarketWatch, provides free, fast, incisive, real-time financial and market news to Europe's rapidly growing community of private investors. The FT Group owns a 34% interest in CBSMarketWatch, whose web properties (*BigCharts.com* and *CBSMarketWatch.com*) are the internet's most popular destinations for financial market news.

### Joint ventures and associates

We also have a number of other associates and joint ventures, including:

- A 50% interest in The Economist Group, which publishes the world's leading weekly business and current affairs journal;
- FTSE International, a joint venture with the London Stock Exchange;
- *Vedomosti*, Russia's leading business newspaper and a partnership venture with Dow Jones and Independent Media;
- A 50% interest in BDFM, publishers of South Africa's leading financial newspaper and magazine.

DAVID ALLOCK • FT.DYNAMO.COM



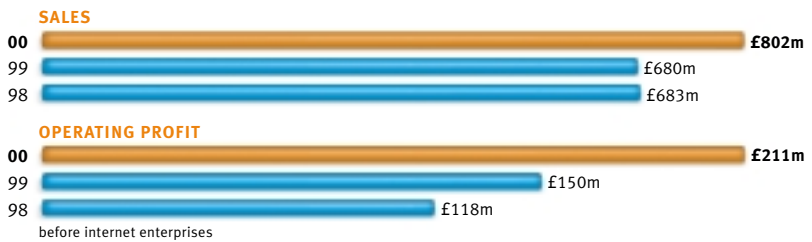
EUROPEAN BUSINESS PEOPLE ARE TWICE AS LIKELY TO READ THE FT AS THEY ARE TO READ ANY OTHER ENGLISH LANGUAGE BUSINESS PUBLICATION.

SOURCE: EBRIS.



## THE FINANCIAL TIMES GROUP • PERFORMANCE

The Financial Times Group had an outstanding year, with underlying revenue growing by 22% and underlying profit increasing by 40%. While circulation and advertising revenues hit record levels, we continued to invest in international expansion and new print and online products and services. Our internet enterprises also grew rapidly during the year, increasing revenues from £7m in 1999 to £42m in 2000. They are on track to break even by the end of 2002, two years ahead of our original expectations.



The *Financial Times* newspaper increased profits by 45% to £81m. Average daily sales in December increased to 485,000, up 10% year on year. Worldwide advertising revenues increased by 34%, with vigorous growth sustained throughout the year. The newspaper continued its successful expansion into North America, with circulation up 26% to 129,000. In the first two months of 2001, circulation and advertising revenues continued to increase.

FT.com continued to grow rapidly and by January 2001 had 1.7 million unique monthly users (up 55% on January 2000) and 39 million monthly page views (up 57%). The *Financial Times* newspaper and FT.com now have integrated editorial, advertising sales and support teams and a number of blue-chip international companies and financial institutions have run integrated advertising campaigns across the FT newspaper and FT.com. FT.com is also generating revenues by syndicating its content to an increasing number of customers and developing a range of premium services.

FTMarketWatch was launched successfully in June. It performed in line with our expectations, generating strong advertising and content licensing revenues. The business expanded further with the launch of a German language site in November, targeting Europe's largest community of private investors.

*Les Echos* increased its circulation by 5% to a record 154,000, and increased advertising revenues by 37%. Its online service, lesechos.fr, built on its position as France's leading newspaper website and grew advertising revenues by 180%. Lesechos.fr also established content partnership deals with a number of websites and launched a new personal finance portal, mesfinances.fr.

STEPHEN HILL • CHIEF EXECUTIVE FT GROUP



BETTY LIU • FINANCIAL TIMES

THE SUCCESS OF THE OF THE FT NEWSPAPER AND FT.COM ARE INTERTWINED, WITH CIRCULATION RISING 10% TO 485,000 AND TRAFFIC TO FT.COM INCREASING BY 55% TO 1.7 MILLION UNIQUE MONTHLY USERS.



*Expansión* grew its circulation to a new high of 63,000 and increased advertising revenues by 41%. *Expansiondirecto.com* more than doubled traffic and increased its advertising and e-commerce revenues.

FT Interactive Data, benefiting from the successful acquisition of Muller Data and subsequent merger with Data Broadcasting Corporation, enjoyed strong revenue and profit growth. FT Interactive Data streamlined its activities to focus on the institutional and retail businesses and, in the process, delivered earnings growth ahead of our expectations at the time of the merger.

FT Business had a strong year, with many of its leading financial titles delivering record revenues. *Investors Chronicle* grew its average sales by more than 20% to 75,000 copies and launched a new online service.

#### JOINT VENTURES AND ASSOCIATES

The Economist Group, in which Pearson has a 50% interest, had another excellent year and continued to invest in its two global brands, *The Economist* and *CFO*, both in print and online. Circulation at *The Economist* newspaper continued to grow with its worldwide circulation now averaging 762,000 copies, 5% higher than last year. The newspaper also benefited from strong advertising revenues. The *CFO* business also performed well and the international rollout of the *CFO* brand continues.

Profits from The Economist Group were more than offset by our share of the start-up costs of *FT Deutschland*, our joint venture with Gruner + Jahr. It reached a circulation of 66,000 just nine months after its launch and is running ahead of its advertising targets.

*Business Day* and *Financial Mail*, the South African titles in which we also own a 50% interest, maintained market share in a difficult economic environment. Average circulation at *Business Day* for the six months to the end of December was stable at approximately 44,000.

#### OPERATING PROFIT ANALYSIS

	2000	1999
FT NEWSPAPER	£81m	£56m
FT INTERACTIVE DATA	£59m	£31m
FT BUSINESS	£10m	£1m
LES ECHOS	£29m	£18m
FT BUSINESSES SOLD	£(1)m	£(2)m
RECOLETOS	£38m	£34m
JOINT VENTURES AND ASSOCIATES	£(5)m	£12m
<b>TOTAL</b>	<b>£211m</b>	<b>£150m</b>
INTERNET ENTERPRISES	£(113)m	£(36)m

RICHARD OSCROFT • FT GROUP

JOCELYN CRIPPS • FT GROUP



FT DEUTSCHLAND, THE FIRST NEW NATIONAL NEWSPAPER LAUNCHED IN GERMANY FOR 50 YEARS, GREW IN CIRCULATION FROM 0-66,000 IN JUST NINE MONTHS.

## RECOLETOS



Recoletos is a leading Spanish media group and is expanding both in Europe and in Spanish and Portuguese-speaking markets around the world. We publish the leading Spanish newspapers for business and sport as well as a number of lifestyle and specialist magazines. With our partners, our newspaper titles sell around 900,000 copies a day and we sell some 500,000 copies of our weekly and monthly magazines. Our websites draw over 90 million page views per month.

WE FLOATED RECOLETOS ON THE MADRID STOCK EXCHANGE, TO PROVIDE MORE FLEXIBILITY TO INVEST AND EXPAND INTO NEW MARKETS.



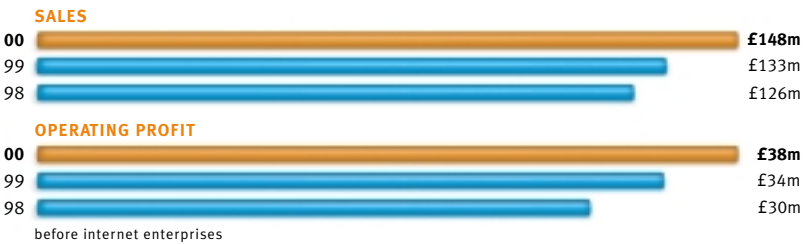
JUAN JOSE DIAZ • MARCA



MARTI SABALLS • ACTUALIDAD ECONOMICA



JAIME GARCIA • RECOLETOS



We publish *Expansión* and Expansiondirecto.com, Spain's leading daily financial newspaper and portal; *Marca* and *Marca Digital*, Europe's most popular sports daily and website; *Telva*, a leading women's magazine; *Diario Medico*, the top medical newspaper and other niche titles. We also own a 30% stake in Unedisa, publisher of *El Mundo*, one of Spain's leading daily newspapers, and a 50% stake in *Economica*, publisher of Portugal's leading business newspaper.

### PERFORMANCE

In 2000, Recoletos increased underlying profits by 27% to £38m. In addition to the strong performance of *Expansión*, *Marca* reached a circulation of 403,000, increased advertising revenues by 16% and more than quadrupled traffic to its website *Marca Digital* to 53 million monthly page views. *El Mundo* increased circulation to 292,000 and monthly page views to 43 million.

Recoletos also extended its position as Spain's leading multimedia business by winning licenses for digital free-to-air television and radio channels, which are being rolled out in 2001. Outside Spain, Recoletos built its presence in Latin America with the acquisition of *El Cronista*, Argentina's most influential business and financial newspaper. The public offering of 20% of Recoletos, completed in October, has enhanced the company's ability to move its business online and to expand in Spanish and Portuguese-speaking markets around the world.

## FINANCIAL REVIEW

### 2000 HIGHLIGHTS

The year 2000 was a period of intense activity for Pearson financially as well as operationally. We issued nearly £2bn in new equity, the bulk of it through the largest rights issue on the UK record books. And we transformed several subsidiary organisations into publicly quoted companies over which we exert either voting control or significant influence.

The balance sheet that we present to shareholders this year has been considerably strengthened by financial initiatives which have supported our public commitment to a minimum credit rating of BBB+ during a period of heavy investment in both acquisitions and organically grown enterprises.

### PORTFOLIO CHANGES

We have managed the development of the Pearson portfolio over the past five years with the twin objectives of achieving greater focus on a limited range of media activities and of securing a higher rate of sustainable growth for the whole company. Both these objectives were achieved during 2000. The sale of our shareholdings in the Lazard banking houses completed our withdrawal from non-media businesses, while all of our acquisitions strengthened our core media franchises and created growth opportunities for the future.

This portfolio strategy was executed at some short-term cost to earnings. The interest receipts from the cash proceeds of Lazard did not match the historical profit contribution of that investment, while the interest cost of acquiring Dorling Kindersley, for example, was not mitigated by any offsetting contribution of profits during the year of acquisition. We expect Dorling Kindersley to move into profit this year and to achieve margins comparable with those of Penguin as a whole by 2003, but it is a tribute to the underlying growth characteristics of our established businesses that we were able to deliver double digit growth in earnings per share last year despite these short-term portfolio effects.

### PEARSON TELEVISION/RTL GROUP

Pearson TV's merger with CLT-Ufa to create RTL Group was completed on 25 July 2000. Pearson now holds a 22% interest in the merged business, which is listed on the London Stock Exchange.

## FINANCIAL REVIEW (CONTINUED)

Up until 25 July, Pearson Television made sales of £185m and contributed £32m in profits. Our share of RTL Group's unaudited profit for the remainder of the year was £36m.

### FINANCING

We concluded early in 2000 that our accelerating investment in internet enterprises should be funded at least in part by new equity. These new initiatives offered greater growth opportunities, but also carried greater risks, than more traditional media investments, and we therefore considered it appropriate to finance their development with new equity. We successfully completed an equity placing of £250m in January of last year and earmarked the proceeds for the internet.

We returned to the equity market in August in order to finance the acquisition of NCS for £1.7bn (\$2.5bn) in cash. Until the NCS transaction, Pearson's acquisition programme had successfully been funded through a combination of disposals and additional debt. NCS gave us the opportunity to strengthen Pearson's capital base in support of a large strategic acquisition, and we raised all the funds required through a 3-for-11 rights issue to existing shareholders at a deep discount. The deep discount allowed us to reduce the transaction costs associated with the fund raising and the rights issue was well received. The acquisition of NCS had a neutral effect on earnings per share last year and should be positive from 2001 onwards.

Earnings and dividends for 1999 and previous years have been restated to reflect the bonus element of the rights issue.

### CAPITAL STRUCTURE

We also recognised last year that the growth opportunities of some of our businesses might best be realised through a partnership with public markets. Three of our companies finished the year with public company status:

**Pearson TV** • The merger between Pearson TV (PTV) and CLT-Ufa gave Pearson a 22% interest in RTL, a new public company with its primary listing in London. This transaction secured the future of PTV within Europe's largest free-to-air broadcasting company and provided a significant uplift in value to Pearson shareholders.

**FT Interactive Data** • In February of last year we completed the merger between FT Interactive Data, our information business serving the asset management industry, and Data Broadcasting Company (DBC), a NASDAQ-quoted company with complementary interests in financial information. Pearson now owns 60% of this successfully combined company.

**Recoletos** • Our Spanish media company floated on the Madrid Stock Exchange in October of last year. Pearson sold 20% of its interest at that time in order to provide Recoletos with the financial means to develop its strategy in new media markets and in Latin America.

While we do not expect any change in the status of our three principal operating divisions – FT Group, Penguin and Pearson Education – we see advantages in a more flexible approach to our capital structure so long as we can address the administrative and governance issues which arise.

### NYSE LISTING

We took the decision last year to list the company's shares on the New York Stock Exchange. This has increased the compliance burden on the company, as we are now registered with the US Securities & Exchange Commission and required to file our results in accordance with US GAAP, but it does allow us greater headroom in the development of share-based incentives for our 13,000 US employees. Our US colleagues and shareholders are also now able to follow the fortunes of the Pearson share price in a currency and format with which they are familiar.

### DIVIDEND POLICY

The company seeks to maintain a balance between the requirement of our shareholders, including our many private shareholders, for a rising stream of dividend income and the reinvestment opportunities that we see across the Group. This balance has been expressed in recent years as a commitment to increase our annual dividend faster than the prevailing rate of inflation while progressively re-investing a higher proportion of our distributable earnings in the business. We have also pegged the growth in our dividend to earnings before internet enterprises in order to reassure shareholders that their dividend will be protected during a period of exceptional investment. The 21.4p

dividend that we are recommending in respect of 2000 is consistent with that policy. It represents an increase of 6.5% on the adjusted 1999 dividend and is covered 2.6 times by adjusted before internet earnings per share, although only 1.5 times by earnings after internet investment. We expect to maintain this balance between dividend growth and investment in 2001 and beyond.

### ACCOUNTING DISCLOSURES AND POLICIES

We have expanded the description of our accounting policies this year in order to clarify the presentation of certain costs and balance sheet values specific to the publishing industry. These include our treatment of pre-publication costs, royalty advances and newspaper development costs. The notes to the accounts have also been expanded to provide separate identification of these items. The significant accounting policies of the group are shown on pages 62 and 63.

During the year we have adopted FRS 16, a standard relating to current tax. The main impact of this standard is to reflect UK dividend income net of UK tax credits. The new standard on tangible fixed assets, FRS 15, has also been adopted, although its impact on results and disclosures is not material.



## FINANCIAL REVIEW (CONTINUED)

### INTERPRETING THE FINANCIAL STATEMENTS

This section is designed to provide shareholders with background narrative on key elements of Pearson's financial statements.

#### INTEGRATION COSTS AND FAIR VALUE ADJUSTMENTS

Integration costs represent the cost of integrating our significant acquisitions into our existing businesses. These costs are separately identified and are excluded from our calculation of adjusted earnings. In 2000 £40m of integration costs were incurred, of which £27m related to the integration of Dorling Kindersley into the Penguin Group. In addition a further £9m was charged in respect of the Simon & Schuster acquisition, representing the final part of the integration process, and £4m was charged in respect of the NCS acquisition.

Provisional fair value adjustments amounting to £70m have been made to the net assets of the businesses acquired in the year. The most significant adjustments have been to harmonise certain Dorling Kindersley accounting policies with those of Penguin, together with the increase to market value of the carrying value of CBSMarketwatch, following the combining of the FT Interactive Data business with DBC.

#### GOODWILL AMORTISATION

The amortisation charge for goodwill, the difference between the price paid and the fair value of the net assets acquired, amounted to £239m in the year compared with £131m in 1999. This increase reflects the significant acquisitions made in the year, particularly Dorling Kindersley and NCS, and the combining of FT Interactive Data with DBC and our television business with CLT-Ufa to form the RTL Group.

#### NON-OPERATING ITEMS

Non-operating items remained significant in 2000 reflecting the sale of Lazard, which resulted in a non-operating profit of £231m, and the initial public offering of 20% of Recoletos, which resulted in a non-operating profit of £86m.

#### INTEREST

Net interest rose by £10m to £157m, with average net debt remaining largely constant. This increase in interest cost followed a general rise in interest rates during the year. A weighted three month LIBOR rate, reflecting the Group's borrowings in US dollars, euros, and sterling, rose by 110 basis points, or 1.1%. The effect of these rises on the Group was mitigated by its existing portfolio of interest rate swaps, which converted over half of its variable rate

#### DORLING KINDERSLEY PROVISIONAL FAIR VALUE ADJUSTMENTS

	BOOK VALUE	ACCOUNTING POLICY ALIGNMENT	REVALUATIONS	PROVISIONAL FAIR VALUE
FIXED ASSETS	20	(1)	(7)	12
WORKING CAPITAL	27	(36)	(19)	(28)
OTHER	(50)	—	(1)	(51)
TOTAL	(3)	(37)	(27)	(67)

#### NET TRADING ASSETS

INTANGIBLE ASSETS	£4,522m
TANGIBLE ASSETS	£524m
WORKING CAPITAL	£829m
OTHER NET ASSETS	£901m
<b>TOTAL</b>	<b>£6,776m</b>

#### CAPITAL EMPLOYED

SHAREHOLDERS' FUNDS	£4,044m
PROVISIONS & MINORITIES	£431m
NET DEBT	£2,301m
<b>TOTAL</b>	<b>£6,776m</b>

commercial paper and bank debt to a fixed rate basis. As a result, the Group's net interest rate payable averaged approximately 6.9%, rising 0.5% from the previous year.

#### TAXATION

The tax charge of £106m represents 37% of profit before taxation of £284m. Although the absolute amount of the tax charge was lower than in 1999, reflecting the reduced profit before taxation, the effective rate was little changed. There is limited tax relief available on goodwill amortisation, and this is the main reason why the effective tax rate is higher than the UK statutory rate of 30%. Profit before taxation was, of course, materially affected in 2000 by the increased losses from internet enterprises. To the extent that losses arose in the US we have generally not recognised tax relief given the existing tax losses available there. This factor was more than offset by the fact that the tax charge on non-operating profits was rather lower than the UK rate. This in turn largely reflected the fact that there was a relatively low effective rate of tax on the profit on disposal of our Lazard interests. In addition, integration costs, on which limited tax relief has been taken, were significantly lower in 2000 than in 1999.

Turning to the tax rate on adjusted earnings, this fell from 25% to 23%. As in 1999, the availability of tax losses in the consolidated tax group in the US meant that only a very limited tax provision was required on the Group's profits there, and this factor was again the largest single item accounting for the difference between the UK statutory rate and the effective rate on adjusted earnings. The effect was, however, diluted this year by the fact that DBC and its subsidiaries, including FT Interactive Data, are outside the consolidated tax group and as such their profits are not covered by the Group's US losses. As indicated in the analysis in note 8 on page 68, other factors, which had an adverse effect last year, were favourable to us this year. This largely reflected progress during the year in agreement of the company's affairs with the tax authorities.

#### MINORITIES

Minorities reflect the 20% interest in Recoletos following the initial public offering in September 2000 and the 40% interest in DBC following the combining of our asset valuation business with DBC in February 2000.

## FINANCIAL REVIEW (CONTINUED)

### MANAGING OUR FINANCIAL RISKS

This section explains the Group's approach to the management of financial risk.

#### TREASURY POLICY

The Group holds financial instruments for two principal purposes: to finance its operations and to manage the interest rate and currency risks arising from its operations and its sources of finance. The Group finances its operations by a mixture of cash flows from operations, short-term borrowings from banks and commercial paper markets, and longer term loans from banks and capital markets. The Group borrows principally in US dollars, euros and sterling, at both floating and fixed rates of interest, using derivatives, where appropriate, to generate the desired effective currency profile and interest rate basis. The derivatives used for this purpose are principally interest rate swaps, interest rate caps and collars, currency swaps and forward foreign exchange contracts.

The main risks arising from the Group's financial instruments are interest rate risk, liquidity and refinancing risk, counterparty risk and foreign currency risk. These risks are managed by the group finance director under policies approved by the board which are summarised below. These policies have remained unchanged, except as disclosed,

since the beginning of 2000. A treasury committee of the board receives reports on the Group's treasury activities, policies and procedures, which are reviewed periodically by a group of external professional advisers. The treasury department is not a profit centre, and its activities are subject to audit.

**interest rate risk** • The Group's exposure to interest rate fluctuations on its borrowings is managed by borrowing on a fixed rate basis and by entering into interest rate swaps, interest rate caps and forward rate agreements. In December 2000 the Group amended its policy objective to set a target proportion of its forecast borrowings (taken at the year end, with cash netted against floating rate debt) to be hedged (i.e. fixed or capped) over the next four years of 50% to 65% for the first two years, and 40% to 60% for the next two years. At the end of 2000 that ratio was 54%. On that basis, a 1% change in the Group's variable rate US dollar, euro and sterling interest rates would have a £10m effect on profit before tax.

**liquidity and refinancing risk** • The Group's objective is to procure continuity of funding at a reasonable cost. To do this it seeks to arrange committed funding for a variety of maturities from a diversity of sources. In May 2000 the Group amended its policy objectives so that the weighted average maturity of its core gross borrowings (treating short-term

#### NET BORROWINGS FIXED AND FLOATING RATES

	2000	1999
FIXED RATE	£1,239m	£1,155m
FLOATING RATE	£1,062m	£840m



**CASH INFLOW – OPENING NET DEBT £(1,995)m**

CASH FROM OPERATIONS	£580m
DISPOSALS	£550m
NEW EQUITY	£1,959m

**CASH OUTFLOW – CLOSING NET DEBT £(2,301)m**

INTEGRATION COSTS	£(61)m
INTERNET ENTERPRISES	£(198)m
INTEREST, TAXATION, DIVIDENDS AND OTHER	£(567)m
ACQUISITIONS	£(2,569)m

advances as having the final maturity of the facilities available to refinance them) should be between three and ten years, and that bank and non-bank sources should each provide at least £250m of such core gross borrowings.

In February 2000 the Group issued €650m of bonds due 2007. In July 2000 it put in place a \$2,500m syndicated bank facility maturing in 2005, which replaced a similar facility maturing in 2003. As a result, at the end of 2000 the average maturity of gross borrowings was 5.6 years and non-banks provided £1,565m (56%) of them (up from 5.1 years and 46% respectively at the beginning of the year). The proceeds of the bond issue were used to repay part of the group's syndicated bank facility.

The Group believes that ready access to different funding markets also helps to reduce its liquidity risk, and that published credit ratings and published financial policies improve such access. The Group manages the amount of its net debt, and the level of its net interest cover, principally by the use of a target range for net interest cover. All of the Group's credit ratings remained unchanged during the year. The long-term ratings are Baa1 from Moody's and BBB+ from Standard & Poor's, and the short-term

ratings are P2 and A2 respectively. The Group continues to operate on the basis that the board will take such action as is necessary to support and protect its current credit ratings. The Group also maintains undrawn committed borrowing facilities. At the end of 2000 these amounted to £609m, and their weighted average maturity was 4.5 years.

**counterparty risk** • The Group's risk of loss on deposits or derivative contracts with individual banks is managed in part through the use of counterparty limits. These limits, which take published credit limits (among other things) into account, are approved by the group finance director. In addition, for certain longer dated higher value derivative contracts the Group has entered into mark to market agreements whose effect is to reduce significantly the counterparty risk of the relevant transactions.

**currency risk** • Although the Group is based in the UK, it has a significant investment in overseas operations. The most significant currency for the Group is the US dollar, followed by the euro and sterling.

The Group's policy during the year on routine transactional conversions between currencies (for example, the collection of receivables, and the

settlement of payables or interest) remained that these should be effected at the relevant spot exchange rate. As in previous years, no unremitted profits were hedged with foreign exchange contracts.

The Group's policy is to align approximately the currency composition of its core borrowings in US dollars, euros and sterling with the split between those currencies of its forecast operating profit. This policy aims to dampen the impact of changes in foreign exchange rates on consolidated interest cover and earnings. Long-term core borrowing is

now limited to these three major currencies. However, the Group still borrows small amounts in other currencies, typically for seasonal working capital needs.

At the year end the split of aggregate net borrowings in its three core currencies was US dollar 63%, euro 14% and sterling 23%. These figures differed from the split of forecast operating profit, primarily because of temporary balances relating to the Pearson Television/RTL Group transaction and the Recoletos initial public offering.

<b>GROSS BORROWINGS</b>	<b>2000</b>	<b>1999</b>
<b>BANK DEBT</b>	<b>£1,252m</b>	<b>£1,254m</b>
<b>BONDS</b>	<b>£1,565m</b>	<b>£1,069m</b>
<b>GROSS BORROWINGS BY CURRENCY</b>		
<b>US DOLLARS</b>	<b>£1,782m</b>	<b>£1,795m</b>
<b>STERLING</b>	<b>£587m</b>	<b>£280m</b>
<b>EURO</b>	<b>£417m</b>	<b>£248m</b>
<b>OTHER</b>	<b>£31m</b>	<b>—</b>

## BOARD OF DIRECTORS

### CHAIRMAN

**Lord Stevenson** • chairman, aged 55, has been a non-executive director of Pearson since 1986 and became executive chairman in 1997. He is also chairman of Halifax plc and a non-executive director of Manpower Inc. in the US.

### EXECUTIVE DIRECTORS

**Marjorie Scardino** • chief executive, aged 54, joined the Pearson board in January 1997. She trained and practised as a lawyer, and published a weekly newspaper in the US. In 1985 she joined The Economist Group as president of its North American operations and was its chief executive from 1993 until joining Pearson. She is also a non-executive director of ConAgra Inc.

**David Bell** • director for people, aged 54, became a director of Pearson in March 1996. He is chairman of the Financial Times Group, having been chief executive of the *Financial Times* from 1993 to 1998. In July 1998 he was appointed Pearson's director for people with responsibility for the recruitment, motivation, development and reward of employees across the Pearson Group. He is also a non-executive director of VITEC Group plc and Zen Research plc and chairman of the Millennium Bridge Trust.

**John Makinson** • finance director, aged 46, joined the Pearson board and became finance director in March 1996. From 1994 to 1996 he was managing director of the *Financial Times*, and prior to that he founded and managed the investor relations firm Makinson Cowell. He is also a non-executive director of George Weston Limited in Canada.

### NON-EXECUTIVE DIRECTORS

**Lord Burns\*\*** • aged 56, was the government's chief economic adviser from 1980 until 1991 and Permanent Secretary of HM Treasury from 1991 until 1998. He is a non-executive director of Legal & General Group plc and The British Land Company PLC and non-executive chairman of Glas Cymru Limited. He was appointed a non-executive director of Pearson in May 1999.

**Gill Lewis†** • aged 57, is the managing partner of Heidrick & Struggles in the UK and in the Republic of Ireland. She became a non-executive director of Pearson in 1992.

**Reuben Mark\*\*** • aged 62, is chairman and chief executive of the Colgate Palmolive Company and a director of Citigroup Inc. and AOL Time Warner Inc. He became a non-executive director of Pearson in 1988.

**Vernon Sankey\*** • aged 51, is non-executive chairman of Gala Group Holdings plc and non-executive deputy chairman of Photo-Me International plc and Beltpacker plc. He is also a non-executive director of Zurich Financial Services AG. He became a non-executive director of Pearson in 1993.

**Rana Talwar** • aged 52, is group chief executive of Standard Chartered plc. He became a non-executive director of Pearson in March 2000.

\* a member of the audit committee.

† a member of the personnel committee.

## DIRECTORS' REPORT

*The directors are pleased to present their report to shareholders, together with the financial statements for the year ended 31 December 2000 on pages 56 to 60 and 62 to 97. Details of the businesses, the development of the Group and its subsidiaries and likely future developments are given on pages 11 to 30 of this annual report. Sales and profits of the different sectors and geographical markets are given on pages 64 and 65.*

**Results and dividend** • The profit for the financial year ended 31 December 2000 was £179m (1999: £294m). The profit retained for the year was £15m (1999: £156m) and has been transferred to reserves. A final dividend of 13.2p per share is recommended for the year ended 31 December 2000. This, together with the interim dividend already paid, makes a total for the year of 21.4p (1999: 20.1p). The final dividend will be paid on 1 June 2001 to shareholders on the register at the close of business on 16 March 2001, the record date.

**Significant acquisitions and disposals** • Details of these transactions can be found in notes 27 and 28 to the accounts on pages 86 to 91.

**Transactions with related parties** • Details of transactions with related parties, which are reportable under FRS 8, are given in note 32 to the accounts on page 94.

**Capital expenditure** • The analysis of capital expenditure and details of capital commitments are shown in note 13 to the accounts on page 72.

**Directors** • The present members of the board, together with their biographical details, are shown on page 39. Michel David-Weill and David Verey resigned as directors on 3 March 2000. Rana Talwar was appointed a non-executive director on 20 March 2000. Details of directors' remuneration and interests in ordinary shares and options of the company are contained in the personnel committee report on pages 47 to 54. Three directors, David Bell, John Makinson and Vernon Sankey, will retire by rotation at the forthcoming Annual General Meeting (AGM) on 27 April 2001. All three, being eligible, will offer themselves for re-election. Details of directors' service contracts can be found on page 49. No director was materially interested in any contract of significance to the company's business.

**Corporate governance** • The board supports the principles of good governance and code of best practice expressed in the Combined Code (the Code) published in June 1998. This directors' report, including the personnel committee report which has been considered and adopted by the board, describes how the company has applied such principles and, apart from the two following exceptions, has complied with the provisions set out in section 1 of the Code. Given the small size of the board and the calibre and experience of the non-executive directors, the board does not believe the identification of a senior independent director is appropriate. Also, the board does not have a nomination committee for directors as it considers that the most formal and transparent procedure for the appointment of a new director is for this to be a matter for the whole board.

**The board** • The board currently comprises four executive directors, including the chairman, who is part-time, and five non-executive directors. All of the non-executive directors are independent of management and free from any business or other relationship which could materially interfere with the exercise of their independent judgement.

The board schedules six meetings each year and arranges to meet at other times as appropriate. There is a formal schedule of matters specifically reserved to the board for decision and approval, and the board is supplied in a timely manner with the necessary information to discharge its duties. A procedure exists for directors to seek independent professional advice in the furtherance of their duties, and all directors have access to the advice and services of the company secretary.

**Board committees** • The board of directors has established the following committees all of which have written terms of reference setting out their authority and duties:

*i* **Audit committee** • This committee is chaired by Vernon Sankey and its other members are Terry Burns and Reuben Mark. All are non-executive directors. The committee provides the board with the means to appraise Pearson's financial management and reporting, and to assess the integrity of the Group's accounting procedures and financial controls. The Group's internal and external auditors have direct access to the committee to raise any matter of concern and to report the results of work directed by the committee. The committee reports to the full board of Pearson.

**ii Personnel committee** • This committee is chaired by Gill Lewis and its other members are Terry Burns and Reuben Mark. All are non-executive directors. The committee meets regularly to decide the remuneration and benefits packages of the executive directors and the chief executives of the main operating companies, as well as recommending the chairman's remuneration to the board for its decision. It also reviews the Group's management development and succession plans. The committee reports to the full board and its report, which has been considered and adopted by the board, is set out on pages 47 to 54.

**iii Treasury committee** • This committee comprises Dennis Stevenson, John Makinson, Vernon Sankey and Rana Talwar. The committee sets the policies for the company's treasury department and reviews its procedures on a regular basis.

**Internal control** • Following the publication of guidance from the Turnbull Committee and its incorporation into the Listing Rules of the UK Listing Authority, the directors reviewed the effectiveness of the company's internal control processes in the light of the provisions of the Combined Code. There is now an ongoing process which has been in place during 2000 and up to the date of the approval of this annual report that is embedded into the company's integrated system of internal control, together with a formal reporting process to the board. The process accords with provision D.2.1 of the Combined Code.

The directors require the operating companies to undertake at least annual reviews to identify new or potentially under-managed risks. The results from these reviews are monitored within the existing quarterly reporting and annual budgeting processes. Annually, the Group control department provides a report to executive management and to the board. This system allows the board to report on the internal controls in accordance with the Financial Services Authority requirements.

The directors consider that the Group's system of internal control is appropriately designed to provide reasonable but not absolute assurance against material misstatement or loss. The main elements of this risk identification and internal control process are as follows:

**i Board** • The board of directors has overall responsibility for the Group's system of internal control and for reviewing its effectiveness, which it exercises through an organisational structure with clearly defined levels of responsibility and authority and appropriate reporting procedures. The board meets regularly and has a regular schedule of matters that are brought to it or its duly authorised committees for decision, aimed at maintaining effective control over strategic, financial, operational and compliance issues. This structure includes the audit committee which, with the finance director, reviews the effectiveness of the internal financial and operating control environment of the Group. The audit committee meets regularly and considers, inter alia, reports from internal and external auditors covering such matters.

**ii Operating company controls** • The identification and mitigation of major business risks is the responsibility of operating management. Each operating company maintains controls and procedures appropriate to its own business environment while conforming to Group standards and guidelines. These include procedures to identify and then mitigate all types of risks. The risks and mitigating actions are reported to the board through the quarterly reporting process.

**iii Financial reporting** • There is a comprehensive budgeting system with an annual budget approved by the board of directors. Monthly financial information, including balance sheets, cash flow statements, trading results and indebtedness, are reported against the corresponding figures for the budget and the previous year, with corrective action being taken by the directors as appropriate. In addition, these reports contain summary information of the major risks facing the operating companies, as well as the actions needed or taken either to mitigate or to take advantage of them.

**iv Treasury management** • The treasury department operates within policies approved by the board, and its procedures are reviewed regularly by the treasury committee. Major transactions are authorised outside the department at the requisite level and there is an appropriate segregation of duties. Frequent reports are made to the finance director and regular reports are prepared for the treasury committee.

**v Group control** • The Group control department has the central responsibility for risk control and internal audit which it exercises through teams located both in the UK and the US. The department reviews risks, processes and procedures in all main operating companies, agrees with operating companies their plans to eliminate or mitigate risks where possible, and to improve controls and processes. It monitors operating companies' progress and reports regularly to executive management and the audit committee and annually to the board.

## DIRECTORS' REPORT (CONTINUED)

**vi Insurance** • Insurance cover is provided either through Pearson's captive insurance subsidiary or externally, depending on the scale of the risk in question and the availability of cover in the external market.

**Going concern** • Having reviewed the Group's liquid resources and borrowing facilities, and the 2001 and 2002 cash flow forecasts contained in the Group budget for 2001, the directors believe that the Group and the company have adequate resources to continue as a going concern for the foreseeable future. For this reason, the financial statements have, as usual, been prepared on a going concern basis.

**Shareholder communication** • Management continues to develop, increase and improve communication with shareholders, large and small, institutional and private. This year's AGM will again include information about the Group's businesses, as well as the 2000 results and general AGM business. The company's website ([www.pearson.com](http://www.pearson.com)) includes a section focusing specifically on investor relations. We post all company announcements on the website as soon as they are made, and, where possible, we webcast all major investor presentations. In addition, Pearson has developed comprehensive programmes for communicating with institutional investors and with employee shareholders.

**People** • We have made good progress in the past year towards our goal of being the best employer in the world, though there is still a lot more to do.

On average there were 24,688 people in the company last year working in more than 60 countries. Almost all of them now own shares in Pearson; and many are saving to acquire more. We have expanded our training programmes at all levels and in all our companies, launched a new Pearson MBA in partnership with Duke University in North Carolina and introduced a new programme which makes it much easier for people to move between countries and between our companies.

This progress has been reflected in several surveys on both sides of the Atlantic in the past year. We were very pleased, for example, to be placed in the Top 100 Best Places to Work by the US magazine *Working Mother*. And earlier this year the British *Sunday Times* selected Pearson as the best place to work among the UK's top 100 companies. Partly for these reasons we have also had a steadily increasing number of high quality job applicants at all our businesses.

**i Employment** • The employment policies of the Group embody the principles of equal opportunity and are designed to meet the needs of operating companies and comply with local regulations in their areas of operation. The sole criterion for selection, training, development and promotion is the individual's suitability for the position of employment offered and his or her aptitudes and abilities. The company takes seriously its statutory obligations relating to disabled persons and seeks not to discriminate against current or prospective employees with disabilities because of a reason relating to their disability. Consideration is given to making reasonable adjustments to premises, or employment arrangements, if these substantially disadvantage a disabled employee, or prospective employee, compared to an able-bodied person.

**ii Training and development** • Pearson's commitment to training and development has further strengthened during 2000 with increased activities involving more people across the company and greater involvement from the individual businesses. With a core curriculum established in 1999, the portfolio has been extended to reflect Pearson's growing international population and now includes programmes in Europe, the US, Asia and Australia with further plans to focus on South America in 2001.

Pearson's Senior Management Programme has now taken place at INSEAD in France and Singapore as well as Harvard Business School. It has created a powerful team of top management better equipped to meet the challenge of change in their businesses. Regular skill updates for management cover leadership, finance, personal performance and project management with coaching and mentoring programmes in place at all levels.

In February 2000 Pearson brought together for the first time over 100 high potential people to work with top management on innovation and strategy, resulting in a CEO-led initiative offering the opportunity for individuals to participate in developing their own new business models. This initial event, FORUM 2000, has had a significant impact on the motivation and retention of key talent and, with FORUM 2001 bringing together a further 140 people, this will become a regular and critical key personal and organisational development event for Pearson.

In partnership with a leading US business school Pearson has sponsored ten managers on a new international MBA that minimises time away from work and maximises on-line study and tutoring. The well established Pearson graduate training scheme has been extended and further internationalised to enable newly qualified individuals from Pearson operating companies across the world to come to Europe to work on specific projects and to participate in management training before taking up positions in their home country.

The sharing of skills and expertise in the company is greatly enhanced through the adoption of a systematic and company wide process for moving individuals across businesses. Linked to personal development this offers the opportunity for people at all stages of their career to experience new and challenging environments. A central training facility at the new corporate centre will offer advice on career management and provide inter-cultural programmes as well as core skills and management development.

**iii Employee participation** • Share ownership lies at the heart of Pearson's remuneration philosophy and the directors believe that the very best way for our people to profit from Pearson's success is for them to become shareholders. Pearson operates both worldwide profit sharing and share acquisition plans in over 60 countries. For 2000, eligible employees, who make up the majority of all employees, will receive an award of 15 Pearson shares under a Group profit sharing plan. With more than half our people in the US, we have taken special care to make it easier for them to acquire shares in Pearson. The listing of our shares on the New York Stock Exchange in 2000 allowed us to launch a new US Employee Stock Purchase Plan which makes owning shares in Pearson more accessible to the majority of our employees.

**iv Employee communication** • Employee communication continues to be developed through regular Group-wide communication from the chief executive, Marjorie Scardino; wide-ranging presentations to staff around the world in connection with the publication of Pearson's results or other important events; the distribution of PearsonNow, the employee magazine; Pearsonville, the Group-wide intranet; and reports to participants in the various benefit plans. The various operating companies also have their own channels of communication such as briefing groups, videos, magazines and newsletters.

**v European employee forum** • Pearson has established a European Employee Forum with elected representatives from each of the Group's main operating companies and from countries in Europe where the Group's operations are of significant scale. The forum is intended to provide an arena for the exchange of relevant and appropriate information and to establish a constructive dialogue between management and employees on transnational issues which affect them. Two meetings of the forum were held in 2000.

**Labour standards and human rights** • During 2000, Pearson, along with other companies, signed a 'global compact' at the United Nations which sets out a series of principles on labour standards, human rights and the environment. Over the course of 2001 we are putting in place the ways to monitor our performance against these principles, and we will report on our progress in future years.

Some of the UN principles concern the environment and are covered by our environmental policy. Others refer to labour standards and human rights. They are:

#### **Labour standards**

- Freedom of association and the right to collective bargaining.
- The elimination of all forms of compulsory labour.
- The abolition of child labour.
- The elimination of discrimination in employment and occupation.

#### **Human rights**

- To support and respect international human rights within our sphere of influence.
- To ensure that we are not complicit in human rights abuses.

## DIRECTORS' REPORT (CONTINUED)

The following guidelines reflect the UN principles and show our key commitments:

### *i Labour standards*

- We try to offer equal employment opportunities to all. The people we recruit and promote are selected on merit and suitability, and will not be discriminated against because of gender, race, origin, background, religion, marital status, sexual orientation, age or political affiliation.
- We aim to comply with the relevant laws relating to employment and employment conditions in each country where we operate. Where such laws are lacking, we will introduce our own guidelines. Subject to any laws, we fully support the right of our people to freedom of association, collective bargaining and representation either through trades unions, works councils, or any other appropriate forum.
- We recognise that labour standards and conditions may vary from country to country. Pearson companies conduct business in many of the poorer countries of the world where living standards are low. Different attitudes to both adult and child labour prevail. Where Pearson companies directly control their activities in a country, we will ensure that our people have satisfactory wages and working conditions, and that there is no exploitation of labour. Working terms will take account of local economies.
- In addition we will expect those who provide us with goods and services to assure, and if necessary demonstrate to us, that their businesses at least comply with the UN standards set out above. We also expect third party suppliers to provide satisfactory working conditions for their employees.
- We will advise third party suppliers that we will positively support their efforts to comply with our guidelines to enable them broadly to adhere to the UN 'global compact', and we will expect them to do so within an agreed time frame.
- Operating in low cost environments has a financial benefit. It also carries a social responsibility. Any improvement in working conditions or pay agreed with a local supplier has to be pursued with care. There may be occasions when to insist on instant change could lead to instant and damaging unemployment; or it could create 'underground' employment which would be infinitely more dangerous and totally unregulated. In such instances, Pearson will agree a timetable for steady and sustained improvement.
- We recognise that there are great social, educational, health or safety problems in areas of the world where we do business and which affect our people. We will help, wherever possible, to educate our people in the workplace about such risks.
- We aim to prohibit physical and verbal abuse, or the threat of it, and any other form of intimidation within our workforce.
- In each country, our local subsidiary will be responsible for monitoring activity annually. These reports will be submitted to the director for people at Pearson by 31 January each year.

### *ii Human rights*

Pearson companies and people operate globally. Our products are produced and manufactured across the world and sold in many countries, often by companies we do not own which are operating on our behalf. We will, in the course of conducting business in 'high risk areas', ensure that we are not complicit in human rights abuses. This assurance can only come with regular monitoring. If we were to find ourselves inadvertently implicated in abuses of human rights, we would take immediate steps to rectify such a situation.

### *iii Board responsibility*

David Bell, as director for people, is the board director with overall responsibility for these issues.

**Environmental policy** • Pearson has had an environmental policy since 1992. In an ever-changing world, environmental issues concern the company and its shareholders, customers, staff and the general public alike. During 2000, we reviewed our policy and concluded that, although most of the original principles were still valid, we needed to enhance our efforts and measure them better.



Pearson does not directly operate in industries where there is a potential for serious industrial pollution. Our main products are based on intellectual property. However, in our normal operations we do things that have an impact on the environment in many ways.

The following policy guidelines show the principal commitments we have set for ourselves:

- We seek to comply with the relevant environmental laws and regulations applicable in each country in which we operate.
- We work with regulatory agencies and advisers as necessary in the implementation of effective environmental policies, and, where no regulations exist, we set our own guidelines.
- We take account of environmental issues when placing contracts with suppliers of goods and services.
- We will continue to introduce energy efficient systems into our buildings and to manage sensibly our energy requirements wherever we operate.
- We will introduce measures to monitor our progress and report on this annually.
- A senior executive has the responsibility for ensuring that our environmental principles are followed and we progress towards the targets we set ourselves. The board will take an active interest in our progress, and each of our operating companies will nominate a senior person to take responsibility for implementing our policy in those businesses. An annual report on our progress will be reviewed by the board.
- We will ensure that this environmental policy and our annual environmental report are available to everyone in Pearson through our website, and actively encourage people to participate and contribute to the development of environmental initiatives as they affect our business.

**Supplier payment policy** • Operating companies are responsible for agreeing the terms and conditions, including terms of payment, under which business transactions with their suppliers are conducted. It is Group policy that suppliers are made aware of such terms of payment and that payments to suppliers are made in accordance with these terms, provided that the supplier is also complying with all relevant terms and conditions. Group trade creditors at 31 December 2000 were equivalent to 34 days of purchases during the year ended on that date. The company does not have any significant trade creditors enabling it to produce creditor information for this purpose.

**External giving** • In 2000, Pearson's external giving totalled £1.79m (1999: £1.53m). This was split between the UK (£847,000; £967,000 in 1999) and the rest of the world (£938,000; £559,000 in 1999). About half of this went to education, arts, literacy and youth projects, including Children's Promise and Literacy Partners. The other half was given to Pearson's operating companies which take active roles in supporting their local communities. All of the operating companies match the funds raised by their employees for charities. The Financial Times Group continues to support schools and charities in its local London borough of Southwark including a programme where FT employees visit schools to help with reading programmes. Pearson does not make party political donations but it does support a number of independent research institutes across the political spectrum.

**Share capital** • Details of share issues are given in note 25 to the accounts on page 84. On 26 January 2000 Pearson announced the placing for cash of 11.5 million new ordinary shares representing approximately 2% of its then existing issued ordinary share capital. The shares were subscribed for by institutional investors at a price of £22 per share. The purpose of the placing was to fund its existing and new internet related businesses.

At the AGM held on 12 May 2000, the company was authorised, subject to certain conditions, to acquire up to 62 million of its ordinary shares by market purchase. This authority expires on the date of the forthcoming AGM. Although circumstances have not merited using this authority and there are no plans at present to do so, shareholders will be asked to renew this authority at the AGM on 27 April 2001.

In September 2000 Pearson completed a 3 for 11 rights issue of 170,528,278 new Pearson shares at a price of £10 per ordinary share. The purpose of the rights issue was to finance the acquisition of National Computer Systems, Inc.

## DIRECTORS' REPORT (CONTINUED)

At 5 March 2001, beneficial interests amounting to 3% or more of the issued ordinary share capital of the company notified to the company comprised:

	number of shares	percentage
Telefónica Media SA	38,853,403	4.86%

**Annual general meeting** • The notice convening the AGM to be held at 12 noon on Friday, 27 April 2001 at The Queen Elizabeth II Conference Centre, Broad Sanctuary, Westminster, London SW1P 3EE, is contained in a circular to shareholders to be dated 27 March 2001.

**Registered auditors** • In accordance with section 384 of the Companies Act 1985 (the Act) resolutions proposing the reappointment of PricewaterhouseCoopers as auditors to the company, at a level of remuneration to be agreed by the directors, will be put to the shareholders at the AGM.

**Statement of directors' responsibilities** • Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and Group as at the end of the year and of the profit or loss of the Group for that period. The directors are also responsible for the maintenance of adequate accounting records in compliance with the Act, for safeguarding the assets of the Group, and for preventing and detecting fraud and other irregularities. In preparing the financial statements on pages 56 to 60 and 62 to 97 inclusive, the directors consider that appropriate accounting policies have been used and applied in a consistent manner, supported by reasonable and prudent judgements and estimates, and that all relevant accounting standards have been followed.

**JULIA CASSON** • SECRETARY • 5 MARCH 2001

## PERSONNEL COMMITTEE REPORT

Pearson wants to be the best company to work for in the world and we have made further progress towards this goal in the past year. The personnel committee has been particularly pleased to see that this progress has been recognised in several surveys on both sides of the Atlantic which have singled Pearson out as a leader in its sector.

The personnel committee plays an important part in developing pay and benefits packages to help the company fulfil this goal. The committee is responsible for approving the pay and benefits packages of the executive directors and the chief executives of the main operating companies. It also recommends the chairman's remuneration to the board, reviews the company's management development and succession plans and monitors the operation of Pearson's various reward programmes.

The committee reviewed the company's approach to management development in the course of the year and welcomed the increased emphasis now being placed on this at all levels. The review concluded that the objectives set in 1999 had been largely met. These were to enhance the high-level skills of senior executives and to encourage them to develop a deeper understanding of the common challenges and opportunities facing the company. The committee was also pleased to see the increased investment in training and development being made within the company.

The company's objective is that everyone who works in Pearson should have a chance to own part of it and the company has made dramatic progress over the past four years in increasing the number of its people who own shares or are saving to acquire them. The company has also developed bonus and share ownership plans for executives which underline the fact that employees and shareholders have a common interest in success.

The company operates a profit sharing plan under which all employees (except executive directors) can, at the discretion of the board, receive a cash bonus and Pearson shares based upon the company's overall profitability. For the past three years, all employees worldwide have been able to acquire Pearson shares through a savings contract linked to a share plan. The company has also steadily increased the number of staff in receipt of awards under executive-type share option plans to approaching 4,000 this year compared with 185 in 1996.

In 2000, Pearson made one-off awards under a special share option programme which the board adopted and introduced on the recommendation of the committee to deal with competitive and employee retention issues in our internet and internet-related businesses.

**Composition and compliance** • The committee is chaired by Gill Lewis and its other members are Terry Burns and Reuben Mark. All are non-executive directors.

The Financial Services Authority requires companies to comply with the provisions of the Combined Code on corporate governance. The committee has considered the provisions in schedule A of the Code on the design of performance-related remuneration and schedule B on what should be included in this report and believes that the company has complied throughout the year.

In detail, the main components of the company's remuneration policy for executives are base salary, an annual bonus plan, long-term incentives, pension benefits and other market specific benefits. The current remuneration plans consist of:

**Base salary** • Base salaries are set at levels competitive with pay for directors and executives in similar positions in comparable companies.

**Annual bonus** • The maximum bonus that can be earned by executive directors and chief executives of the company's main operating companies is 100% of annual base salary. Maximum bonuses for other senior executives range downward from that level. Receiving the maximum requires the achievement of very challenging financial targets set by the committee. The targets for 2000 related to the company's stated goals of increasing earnings per share, revenue growth, margin improvement and cash generation. Performance is measured separately for each element and for executive directors for 2000 the thresholds before bonus became payable were increases of 10% in adjusted earnings per share and 7.5% in underlying sales and a cash conversion ratio of 80%. Based on performance against these measures, executive directors received a bonus of 85.9% of salary (out of a potential maximum of 100%).

## PERSONNEL COMMITTEE REPORT (CONTINUED)

The committee will continue to review the bonus plans and reserves the right to revise the bonus limits and targets in the future. The committee may also award individual discretionary bonuses, but none were awarded for 2000. Bonuses do not form part of pensionable earnings.

**Annual bonus share matching plan** • The annual bonus share matching plan permits executive directors and senior executives around the Group to take up to 50% of any after tax annual bonus in the form of Pearson shares which, if held and the company's adjusted earnings per share increases in real terms by at least 3% per annum, will be matched by the company on a gross basis of one share for every two held after three years and another one for two originally held (i.e. a total of one-for-one) after five years. Details of directors' matching awards are set out in tables 3 and 4 on pages 52 and 53 of this report.

**Long-term incentives** • Long-term incentive plans align the interests of directors and executives with those of shareholders. The committee's view is that if shareholders do well, this should be reflected in the remuneration of senior executives. The committee reviews the operation of long-term incentive plans on a regular basis, taking into account legislative and regulatory developments, particularly with regard to performance targets and evolving best practice.

Proposals for new long-term incentive arrangements are being put to shareholders at the AGM. Details of these have been set out in a separate circular to shareholders dated 27 March 2001. These arrangements have been designed to enable us to continue to recruit and retain the ablest managers worldwide and to ensure that their performance-related rewards are competitive in the markets in which we operate. As a result, we will be able to provide more focused reward opportunities for a wider group of managers, and to have greater flexibility in designing individual remuneration packages.

Details of Pearson's existing long-term incentive plans are set out below.

**i Reward plan** • The Pearson Reward Plan has had two elements: Pearson Premium Options (PPOs) linked to the rise in the Pearson share price over three to seven years and Pearson shares in the form of Pearson Equity Incentives (PEIs) linked to the three-year cumulative growth in Pearson's free cash flow (being operating cash flow less tax liabilities on operating activities and interest paid). Two awards have been made under this plan and the grants to executive directors are shown in tables 3, 4 and 5 on pages 52, 53 and 54 of this report.

In the circular to shareholders dated 30 March 1999, it was stated that the minimum rate of growth in free cash flow per share before any vesting of PEIs granted in 1999 took place would be very stretching and would require average growth greater than 10% per annum in excess of 1998 free cash flow. The committee has monitored free cash flow performance over the period and has concluded that the exceptionally high free cash flow for 1998 arising from a cash conversion performance of 102% made a double-digit increase target from the 1998 base unrealistic in the context of the plan. As a consequence, the committee has re-calibrated the targets for the 1999 to 2001 performance period based on the free cash flow for 1998 that would have derived from a good, but more normal, level of cash conversion. The minimum average growth rate of 10% per annum from this revised base remains.

Executive directors and managers covered by the reward plan were not eligible for grants of conventional share options in any year in which they received an award under the reward plan.

**ii Executive and special share option plans** • Options at market value at the date of grant have been granted to eligible employees not covered by the reward plan. Under the executive share option plan, awards are within the individual and overall limits authorised by shareholders. The exercise of options under this plan is subject to a real increase in the company's adjusted earnings per share of at least 3% per annum over a three-year period.

In the case of the special share option plan applied in 2000, no new shares will be issued to satisfy awards and executive directors were not eligible to participate in it.

**iii Incentive share plan** • The incentive share plan was introduced in 1993 to reward executives of the Group based on the performance of the company over the medium to longer term as measured by total shareholder return relative to the average of the FT-SE 100 total return index.

There is one outstanding award under this plan, relating to Lord Stevenson, covering the five-year performance period May 1997 to April 2002. No new awards have been or will be made under the incentive share plan.

**Service contracts** • All executive directors have agreements which can be terminated by the company on 12 months' notice. In the case of early termination of their contracts by the company without cause, these contracts provide for liquidated damages equivalent to 12 months' base salary, benefits and a proportion of bonus. During the year, no material changes were made to the service contracts of the executive directors. Non-executive directors do not have service contracts.

**Non-executive directors' remuneration** • Fees for non-executive directors are determined by the full board with regard to market practice and within the restrictions contained in the articles of association. Fees are reviewed annually with the help of outside advice. Non-executive directors receive no other pay or benefits (other than reimbursement for expenses incurred in connection with their directorship of the company) and do not participate in the company's long-term incentive plans.

Since January 2000, non-executive directors have received an annual fee of £35,000 each. One overseas-based director is paid a supplement of £7,000 per annum. The non-executive directors who chair the personnel and audit committees each receive an additional fee of £5,000 per annum. £10,000 of the total fee, or all of the fee in the case of Rana Talwar, is payable in the form of Pearson shares which the non-executive directors have committed to retain for the period of their directorships.

**Retirement benefits** • The highest paid director, Marjorie Scardino, has pension arrangements comprising defined benefit and defined contribution arrangements in the US. She participates in the funded, approved Pearson Inc. Pension Plan. This is a non-contributory final salary pension arrangement providing a lump sum convertible to a pension on retirement. The lump sum currently accrues at 6% of capped compensation. In addition, she participates in an unfunded, unapproved defined contribution arrangement, which provides a benefit based on an annual notional company contribution of 25% of base salary. This plan is non-contributory. The company also contributed \$5,100 to the Pearson Inc. funded, approved, defined contribution 401(k) arrangement and \$17,400 to the Pearson Inc. Excess Savings and Investment Plan.

David Bell and John Makinson are members of a defined benefit section of the Pearson Group Pension Plan (the Plan), with a member contribution rate of 5% of pensionable salary. David Bell is eligible for a pension from the Plan of two-thirds of final base salary at normal retirement date due to his previous service with the Financial Times. It is anticipated that John Makinson will receive a pension of two-thirds of capped salary at normal retirement date (inclusive of benefits transferred from his previous pension plan). John Makinson is subject to the pensions earnings cap introduced by the Finance Act 1989. John Makinson participates in the company's Funded Unapproved Retirement Benefits Scheme (FURBS) arrangements, under which a contribution equivalent to 31.1% of his annual base salary is made by the Company to compensate him for pension benefits which cannot be provided from the Plan because of the pensions cap regulations.

All the UK executive directors are also eligible for dependants' pensions and a lump sum payment on death in service. Details of directors' pension arrangements are set out in table 2 on page 51 of this report.

## PERSONNEL COMMITTEE REPORT (CONTINUED)

**Remuneration of the directors** • Excluding contributions to pension funds and related benefits set out in table 2, directors' remuneration was as follows:

TABLE 1	2000				1999	
	salaries/fees	bonus	other*	3-year ISP (see table 4)	total	total
<i>all figures in £000s</i>						
<b>Chairman</b>						
Lord Stevenson	275	—	—	—	275	268
<b>Executive directors</b>						
Marjorie Scardino	475	408	55	—	938	2,517
David Bell	280	241	18	—	539	1,146
John Makinson	320	275	21	—	616	635
<b>Non-executive directors</b>						
Lord Burns	35	—	—	—	35	16
Michel David-Weill	4	—	—	—	4	25
Gill Lewis	40	—	—	—	40	30
Reuben Mark	42	—	—	—	42	32
Vernon Sankey	40	—	—	—	40	30
Rana Talwar	30	—	—	—	30	—
David Verey	4	—	—	—	4	25
<b>Total</b>	<b>1,545</b>	<b>924</b>	<b>94</b>	<b>—</b>	<b>2,563</b>	<b>4,724</b>
Total 1999 <sup>†</sup>	1,686	1,167	96	2,122	—	5,071

\* 'other' excludes pension contributions.

† Includes amounts to former directors.

**note** • Marjorie Scardino was the highest paid director in 2000. Her base salary increased by 2.2% from £465,000. Her total remuneration, including pension contributions, amounted to £1,081,182. For Marjorie Scardino, David Bell and John Makinson, 'other' emoluments include company car and health care benefits. Also included in 'other' emoluments for Marjorie Scardino is £34,660 in respect of housing costs.

TABLE 2

	age at 31 Dec 00	directors' contributions over the period £000 pa	increase in accrued pension over the period £000 pa	accrued pension at 31 Dec 00 £000 pa	other pension and related benefits costs to the company over the period £000 pa
<b>Directors' pensions</b>					
Marjorie Scardino	53	—	1.1	4.1	142.9
David Bell	54	14.0	9.8	149.3	—
John Makinson	46	4.5	2.0	16.5	104.5

**note 1** • The increase in accrued pension during the year excludes any increase for inflation. Accrued pension is that which would be paid annually on retirement at 62, the normal retirement age under the Pearson pension plan in the UK, based on service to 31 December 2000. As members of the UK plan, David Bell and John Makinson have the option to pay Additional Voluntary Contributions (AVCs). They did not pay any AVCs in 2000.

**note 2** • The column headed 'other pension and related benefits costs to the company over the period' comprises payments to FURBS and pension and insurance supplements for UK benefits. For US benefits, this includes life assurance, Group term life cover, company contributions to the Pearson Inc. 401(k) and excess savings and investment plans and notional contributions to Marjorie Scardino's notional defined contribution plan.

Further information relating to directors' pensions:

**Early retirement** • UK directors and other UK employees may retire before the normal retirement age of 62 and receive an immediate pension provided they have obtained company consent. In such cases, the pension entitlement from the UK plan will be scaled down to reflect the shorter service in accordance with normal actuarial practice. Early retirement reduction factors will also be applied to the accrued pension if retirement occurs before age 60. The earliest any director can retire and receive an immediate pension from the UK plan other than on ill-health grounds is age 50. Under the company's FURBS arrangements, early retirement is possible with company consent from age 50 onwards. The benefit payable will be the amount of the member's fund at the relevant date. In the US, Marjorie Scardino has a normal retirement age of 65 but may retire with company consent from age 55 with a reduced pension on a broadly equivalent actuarial basis.

**Dependants' pensions** • If a UK director dies while in employment before normal retirement age, a spouse's pension will be payable from the UK plan, or in the absence of a spouse to a financial dependant nominated by the member. The amount of the pension will be one-third of the director's annual base salary (capped in the case John Makinson). If a former director dies after leaving service but before retirement, a pension of 50% of the director's deferred pension will be payable to the spouse or nominated financial dependant. If John Makinson or David Bell die in retirement, the pension payable to their spouse or nominated financial dependant will be 60% of the director's pension. Children's pensions may also be payable to dependent children. As a member of the company's FURBS arrangements, John Makinson's member's fund would be paid to his dependants if he died before withdrawing it. Marjorie Scardino's US plan provides a spouse's pension on death in service from age 55 and death-in-retirement benefits broadly equivalent to 50% of the member's pension on early retirement.

**Pension increases** • John Makinson and David Bell are guaranteed post-retirement pension increases at the rate of 5% per annum or the Retail Price Index, if lower. The guaranteed increases relate to the non-Guaranteed Minimum Pension element of the pension. The plan has a recent history of providing discretionary pension increases at the full Retail Price Index rate. The US plans provide no guaranteed post-retirement pension increases for Marjorie Scardino.

## PERSONNEL COMMITTEE REPORT (CONTINUED)

TABLE 3 AT 31 DEC 00

	ordinary shares <sup>†</sup>	options - ordinary shares	incentive share and reward plans ordinary shares <sup>‡</sup>	annual bonus matching shares <sup>†</sup>
<b>Interests of directors were</b>				
Lord Stevenson	90,406	2,512	72,862	—
Marjorie Scardino	71,259	408,753	117,219	44,955
David Bell	44,087	134,873	58,595	16,135
Lord Burns	252	—	—	—
Gill Lewis	253	—	—	—
John Makinson	22,465	349,233	67,185	25,334
Reuben Mark	10,000	—	—	—
Vernon Sankey	253	—	—	—
Rana Talwar	913	—	—	—

TABLE 3 AT 1 JAN 00\*

	ordinary shares <sup>†</sup>	options - ordinary shares	incentive share and reward plans ordinary shares <sup>‡</sup>	annual bonus matching shares <sup>†</sup>
<b>Interests of directors were</b>				
Lord Stevenson	70,393	2,243	64,353	—
Marjorie Scardino	28,334	266,506	74,446	27,928
David Bell	14,208	97,879	37,051	8,717
Lord Burns	—	—	—	—
Gill Lewis	—	—	—	—
John Makinson	12,687	254,612	42,541	14,480
Reuben Mark	7,600	—	—	—
Vernon Sankey	—	—	—	—
Rana Talwar	—	—	—	—

\* Or date of appointment, if later.

† Amounts include shares acquired by individuals under the annual bonus share matching plan.

‡ The number of shares shown represents the maximum number of shares, including accumulated share dividends on incentive share plan shares but not on reward plan shares, which may vest, subject to the performance conditions being fulfilled.

† These shares are held in trust and represent the maximum award required to provide the company's matching contribution of shares in respect of that part of the bonus taken in shares by each director. The shares only vest if the performance and other conditions of the plan are met.

**note** • The number of shares as at 31 December 2000 reflects a rights issue of equity shares during 2000.

**note** • Executive directors of the company, as possible beneficiaries, are also deemed to be interested in Pearson Employee Share Trustee Limited, the trustee of which held 239,625 Pearson ordinary shares of 25p each at 31 December 2000 and also at 5 March 2001.

**note** • On 2 January 2001 Lord Burns, Gill Lewis and Vernon Sankey each acquired 93 shares in the company. On that date, Reuben Mark and Rana Talwar acquired 121 shares and 425 shares respectively. The shares were acquired as part of their directors' fees.

### Interests of directors in listed subsidiaries

At 31 December 2000 Marjorie Scardino, David Bell and John Makinson each held 1,000 shares in Recoletos Compañía Editorial, S.A., all purchased on 2 November 2000. Lord Stevenson held 8,660 shares purchased on 7 December 2000.



**TABLE 4**

	number of shares outstanding at 1 Jan 00	incentive share and reward plans*	annual bonus share matching plan	number of ISP shares vested and released	number of shares lapsed	rights issue adjustment	number of shares outstanding at 31 Dec 00
<b>Movements in directors' interests under the incentive share, reward and annual bonus share matching plans</b>							
Lord Stevenson	64,353	738	—	—	—	7,771	72,862
Marjorie Scardino	102,374	30,214	12,211	—	—	17,375	162,174
David Bell	45,768	15,267	5,689	—	—	8,006	74,730
John Makinson	57,021	17,448	8,141	—	—	9,909	92,519

\* The number of shares shown represents the maximum number of shares, including accumulated share dividends on incentive share plan shares but not on reward plan shares, which may vest, subject to the performance conditions being fulfilled.

**note** • The number of shares reflects a rights issue of equity shares during 2000 as shown.

**note** • Cash dividends may be paid on incentive share plan shares.

## PERSONNEL COMMITTEE REPORT (CONTINUED)

**TABLE 5**

	year of grant	01 Jan 00	granted	rights issue adjustment	exercised	31 Dec 00	option price (p)	market price (p)	gain on exercise (£)
<b>Movements in directors' interests in share options</b>									
Lord Stevenson	<b>b</b>	1998	2,243	—	269	—	2,512	687	—
Total			2,243	—	269	—	2,512	—	—
Marjorie Scardino	<b>a</b>	1998	157,640	—	18,916	—	176,556	974	—
	<b>a</b>	1998	5,660	—	—	—	5,660	1090	—
	<b>b</b>	1998	2,535	—	304	—	2,839	687	—
	<b>c</b>	1999	33,557	—	4,026	—	37,583	1373	—
	<b>c</b>	1999	33,557	—	4,026	—	37,583	1648	—
	<b>c</b>	1999	33,557	—	4,026	—	37,583	1922	—
	<b>c</b>	2000	—	33,022	3,961	—	36,983	2303	—
	<b>c</b>	2000	—	33,022	3,961	—	36,983	2764	—
	<b>c</b>	2000	—	33,022	3,961	—	36,983	3225	—
Total			266,506	99,066	43,181	—	408,753	—	—
David Bell	<b>a*</b>	1996	26,500	—	3,180	(29,680)	—	584	1886
	<b>b*</b>	1995	1,186	—	142	(1,328)	—	390	1634
	<b>a</b>	1998	18,300	—	2,196	—	20,496	974	—
	<b>b</b>	1996	596	—	71	—	667	517	—
	<b>b</b>	1997	581	—	69	—	650	530	—
	<b>b</b>	1998	448	—	53	—	501	687	—
	<b>b</b>	1999	165	—	19	—	184	913	—
	<b>c</b>	1999	16,701	—	2,004	—	18,705	1373	—
	<b>c</b>	1999	16,701	—	2,004	—	18,705	1648	—
	<b>c</b>	1999	16,701	—	2,004	—	18,705	1922	—
	<b>c</b>	2000	—	16,685	2,001	—	18,686	2303	—
	<b>c</b>	2000	—	16,685	2,001	—	18,686	2764	—
	<b>c</b>	2000	—	16,685	2,001	—	18,686	3225	—
	<b>b</b>	2000	—	181	21	—	202	1428	—
Total			97,879	50,236	17,766	(31,008)	134,873	—	402,953
John Makinson	<b>a*</b>	1994	50,000	—	6,000	—	56,000	567	—
	<b>a*</b>	1995	18,000	—	2,160	—	20,160	487	—
	<b>a*</b>	1996	32,800	—	3,936	—	36,736	584	—
	<b>a*</b>	1997	66,000	—	7,920	—	73,920	677	—
	<b>a</b>	1998	27,300	—	3,276	—	30,576	974	—
	<b>b</b>	1996	2,984	—	358	—	3,342	517	—
	<b>c</b>	1999	19,176	—	2,301	—	21,477	1373	—
	<b>c</b>	1999	19,176	—	2,301	—	21,477	1648	—
	<b>c</b>	1999	19,176	—	2,301	—	21,477	1922	—
	<b>c</b>	2000	—	19,068	2,288	—	21,356	2303	—
	<b>c</b>	2000	—	19,068	2,288	—	21,356	2764	—
	<b>c</b>	2000	—	19,068	2,288	—	21,356	3225	—
Total			254,612	57,204	37,417	—	349,233	—	—

**note** • The original subscription price has been adjusted (except where this was not permitted) to reflect a rights issue of equity shares during 2000 as shown.

**note** • The option prices and market prices have been rounded up to the nearest whole penny.

**note** • Shares under option on 31 December 2000 are designated as: **a** executive options; **b** Save for Shares options; **c** premium priced options; and **\*** where the options are exercisable.

Total combined gain on exercise of the options for all directors during 2000 amounted to £402,953. The register of directors' interests (which is open to inspection during normal office hours) contains full details of directors' shareholdings and options to subscribe for shares. The market price on 29 December 2000 was 1590p per share and the range during the year was 1465.2p to 2301.8p (rights adjusted). Subject to any performance conditions being met, outstanding executive and premium priced options become exercisable on the third anniversary of the date of grant and lapse if they remain unexercised after the tenth. Save for Shares options become exercisable on the third, fifth or seventh anniversary of the start of the contract and lapse if not exercised within six months after that anniversary.

## FINANCIAL STATEMENTS

Accounting policies	62 · 63
Acquisitions	86 · 87 · 88 · 89 · 90
Adjusted earnings per share	69
Associates	73 · 74 · 75
Auditors • Remuneration	66
Report to members	61
Balance sheet • Company	95
Group	58
Capital commitments	72
Capital employed	65
Capital expenditure	72
Cash flow	59
Cash at bank and in hand	77
Contingent liabilities	93
Corporate and operating measures	99
Creditors, other	82
Debtors	77
Deferred taxation	83
Depreciation	66 · 72
Diluted earnings per share	69
Disposals	91
Dividends	68
Earnings per share	69
Employee information	70 · 71
Fair values	86 · 87 · 88 · 89 · 90
Financial instruments	78 · 79 · 80 · 81 · 82
Five year summary	98
Fixed assets, tangible	72
Geographical analysis	64 · 65 · 70 · 73 · 74
Goodwill	71 · 74 · 86 · 89 · 90 · 91 · 92
Intangible assets	71
Interest	67
Investments	76 · 77
Joint ventures	72 · 73
Leases	94
Other operating income	66
Pensions	70 · 71 · 83
Principal subsidiaries and associates	97
Profit and loss account	56 · 57
Provisions	83
Recognised gains and losses	60
Related parties	94
Reserves	85
Sales	56 · 64
Sector analysis	64 · 65 · 70 · 73 · 74
Share capital and options	84
Shareholders' funds	60
Stocks	76
Taxation	68 · 83

## CONSOLIDATED PROFIT AND LOSS ACCOUNT

year ended 31 Dec 2000

	2000			1999 restated			note
	results from operations	other items	total	results from operations	other items	total	
<i>all figures in £ millions</i>							
<b>Sales (including share of joint ventures)</b>	3,537	–	3,537	3,332	–	3,332	
Less: share of joint ventures	(17)	–	(17)	–	–	–	
Continuing operations	3,520	–	3,520	3,332	–	3,332	
Acquisitions	354	–	354	–	–	–	
<b>Total sales</b>	<b>3,874</b>	<b>–</b>	<b>3,874</b>	<b>3,332</b>	<b>–</b>	<b>3,332</b>	<b>2</b>
Cost of sales	(1,633)	(8)	(1,641)	(1,414)	(10)	(1,424)	3
<b>Gross profit</b>	<b>2,241</b>	<b>(8)</b>	<b>2,233</b>	<b>1,918</b>	<b>(10)</b>	<b>1,908</b>	
Net operating expenses	(1,791)	(220)	(2,011)	(1,441)	(220)	(1,661)	3
<b>Operating profit analysed between:</b>							
Continuing operations – Group	446	(143)	303	477	(230)	247	
Acquisitions – Group	4	(85)	(81)	–	–	–	
<b>Total operating profit – Group</b>	<b>450</b>	<b>(228)</b>	<b>222</b>	<b>477</b>	<b>(230)</b>	<b>247</b>	
Share of operating loss of joint ventures:							
Continuing operations	(21)	–	(21)	–	–	–	
<b>Total share of operating loss of joint ventures</b>	<b>(21)</b>	<b>–</b>	<b>(21)</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>14</b>
Share of operating profit of associates:							
Continuing operations	25	(1)	24	24	(1)	23	
Acquisitions	28	(50)	(22)	–	–	–	
Discontinued operations	53	(51)	2	24	(1)	23	
	8	–	8	48	–	48	
<b>Total share of operating profit of associates</b>	<b>61</b>	<b>(51)</b>	<b>10</b>	<b>72</b>	<b>(1)</b>	<b>71</b>	<b>15</b>
Total operating profit analysed between:							
Operating profit before internet enterprises	686	(262)	424	588	(231)	357	2
Internet enterprises	(196)	(17)	(213)	(39)	–	(39)	2
<b>Total operating profit</b>	<b>490</b>	<b>(279)</b>	<b>211</b>	<b>549</b>	<b>(231)</b>	<b>318</b>	<b>2</b>

## CONSOLIDATED PROFIT AND LOSS ACCOUNT (CONTINUED)

year ended 31 Dec 2000

	2000			1999 restated			note
	results from operations	other items	total	results from operations	other items	total	
<i>all figures in £ millions</i>							
<b>Total operating profit</b>	490	(279)	211	549	(231)	318	
Continuing operations:							
(Loss)/profit on sale of fixed assets and investments	–	(4)	(4)	–	349	349	4
Profit/(loss) on sale of businesses and associates	–	30	30	–	(44)	(44)	5
Discontinued operations:							
Profit on sale of businesses and associates	–	231	231	–	–	–	5
	–	257	257	–	305	305	
Continuing operations:							
(Loss)/profit on sale of businesses and associates by an associate	–	(3)	(3)	–	1	1	15
<b>Profit before interest and taxation</b>	490	(25)	465	549	75	624	
<b>Net finance costs</b>							
Net interest payable – Group	(154)	–	(154)	(145)	–	(145)	6
Net interest payable – associates	(3)	–	(3)	(2)	–	(2)	15
Other net finance costs	–	(24)	(24)	–	–	–	7
<b>Total net finance costs</b>	(157)	(24)	(181)	(147)	–	(147)	
<b>Profit before taxation</b>	333	(49)	284	402	75	477	
Taxation	(87)	(19)	(106)	(100)	(77)	(177)	8
<b>Profit after taxation</b>	246	(68)	178	302	(2)	300	
Equity minority interests	(14)	15	1	(6)	–	(6)	
<b>Profit for the financial year</b>	232	(53)	179	296	(2)	294	
<b>Dividends on equity shares</b>			(164)			(138)	9
<b>Profit retained</b>			15			156	
<b>Adjusted earnings per equity share before internet enterprises</b>			54.6p			47.6p	10
<b>Adjusted earnings per equity share after internet enterprises</b>			31.9p			43.3p	10
<b>Earnings per equity share</b>			24.6p			43.0p	10
<b>Diluted earnings per equity share</b>			24.0p			42.4p	10
<b>Dividends per equity share</b>			21.4p			20.1p	9

1999 has been restated to reflect the adoption of FRS16 'Current Tax'. Earnings per equity share and dividends per equity share in 1999 have been restated to reflect the rights issue of equity shares during 2000.

There is no difference between the profit on ordinary activities before taxation and the retained profit for the year stated above and their historical cost equivalents.

## CONSOLIDATED BALANCE SHEET

as at 31 Dec 2000

<i>all figures in £ millions</i>	2000	1999	note
<b>Fixed assets</b>			
Intangible assets	4,522	2,457	12
Tangible assets	524	405	13
Investments: joint ventures			14
Share of gross assets	13	–	
Share of gross liabilities	(1)	–	
	12	–	
Investments: associates	1,024	234	15
Investments: other	155	99	16
	6,237	3,195	
<b>Current assets</b>			
Stocks	828	691	17
Debtors	1,217	1,132	18
Investments	12	4	19
Cash at bank and in hand	516	328	20
	2,573	2,155	
<b>Creditors – amounts falling due within one year</b>			
Short-term borrowing	(112)	(47)	21
Other creditors	(1,484)	(1,441)	22
	(1,596)	(1,488)	
<b>Net current assets</b>	977	667	
<b>Total assets less current liabilities</b>	7,214	3,862	
<b>Creditors – amounts falling due after more than one year</b>			
Medium and long-term borrowing	(2,705)	(2,276)	21
Other creditors	(34)	(32)	22
	(2,739)	(2,308)	
<b>Provisions for liabilities and charges</b>			
Deferred taxation	(9)	(21)	23
Other provisions for liabilities and charges	(257)	(206)	24
<b>Net assets</b>	4,209	1,327	
<b>Capital and reserves</b>			
Called up share capital	199	153	25
Share premium account	2,440	517	26
Profit and loss account	1,405	651	26
<b>Equity shareholders' funds</b>	4,044	1,321	
<b>Equity minority interests</b>	165	6	
	4,209	1,327	

The company balance sheet is shown in note 33.

The financial statements were approved by the board of directors on 5 March 2001 and signed on its behalf by  
**LORD STEVENSON • JOHN MAKINSON**

## CONSOLIDATED STATEMENT OF CASH FLOWS

year ended 31 Dec 2000

<i>all figures in £ millions</i>	2000	1999	note
<b>Net cash inflow from operating activities</b>	361	433	29
<b>Dividends from joint ventures and associates</b>	49	44	
Interest received	16	41	
Interest paid	(179)	(182)	
Debt issue costs	(4)	(5)	
Dividends paid to minority interests	–	(1)	
<b>Returns on investments and servicing of finance</b>	(167)	(147)	
<b>Taxation</b>	(90)	(156)	
Purchase of tangible fixed assets	(139)	(102)	
Sale of tangible fixed assets	22	36	
Purchase of investments	(132)	(24)	
Sale of investments	1	624	
<b>Capital expenditure and financial investment</b>	(248)	534	
Purchase of subsidiary undertakings	(2,276)	(249)	
Net cash acquired with subsidiary undertakings	(31)	–	
Purchase of joint ventures and associates	(108)	(54)	
Sale of subsidiary undertakings	158	44	
Net cash disposed with subsidiary undertakings	–	(3)	
Sale of associates	392	12	
<b>Acquisitions and disposals</b>	(1,865)	(250)	27/28
<b>Equity dividends paid</b>	(143)	(132)	
<b>Net cash (outflow)/inflow before management of liquid resources and financing</b>	(2,103)	326	
Liquid resources acquired	(16)	(9)	
Liquid resources disposed	–	10	
Collateral deposit placed	(118)	–	
<b>Management of liquid resources</b>	(134)	1	29
Issue of equity share capital	1,959	18	
Capital element of finance lease rentals	(10)	(11)	
Loan facility advanced	473	–	
Loan facility repaid	(735)	(1,112)	
Bonds advanced	411	608	
Loan notes advanced	134	–	
Net movement in other borrowings	63	202	
<b>Financing</b>	2,295	(295)	
<b>Increase in cash in the year</b>	58	32	29

## STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

year ended 31 Dec 2000

<i>all figures in £ millions</i>	2000	1999
Profit for the financial year	179	294
Other net gains and losses recognised in reserves:		
Currency translation differences	95	33
Taxation on currency translation differences – UK	(8)	3
<b>Total recognised gains relating to the year</b>	<b>266</b>	<b>330</b>

## RECONCILIATION OF MOVEMENTS IN EQUITY SHAREHOLDERS' FUNDS

year ended 31 Dec 2000

<i>all figures in £ millions</i>	2000	1999
Profit for the financial year	179	294
Dividends on equity shares	(164)	(138)
	15	156
Currency translation differences (net of taxation)	87	36
Goodwill arising on prior year acquisitions	1	–
Goodwill written back on business combinations	585	–
Goodwill written back	68	63
Shares issued	1,961	18
Replacement options granted on acquisition of subsidiary	6	–
Net movement for the year	2,723	273
Equity shareholders' funds at beginning of the year	1,321	1,048
<b>Equity shareholders' funds at end of the year</b>	<b>4,044</b>	<b>1,321</b>



## REPORT OF THE AUDITORS TO THE MEMBERS OF PEARSON PLC

We have audited the financial statements which comprise the profit and loss account, the balance sheet, the statement of cash flows, the statement of total recognised gains losses, and the reconciliation of movements in equity shareholders' funds, and the related notes (including additional disclosures within the Personnel Committee Report relating to the remuneration of directors of Pearson plc as specified for our review by the Financial Services Authority) which have been prepared under the historical cost convention and the accounting policies set out in the statement of accounting policies.

Respective responsibilities of directors and auditors • The directors are responsible for preparing the annual report. As described in the statement of directors responsibilities within the directors report, this includes responsibility for preparing the financial statements in accordance with applicable United Kingdom accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board, the Listing Rules of the Financial Services Authority and our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the United Kingdom Companies Act. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law or the Listing Rules regarding directors' remuneration and transactions is not disclosed.

We read the other information contained in the annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

We review whether the corporate governance statement in the directors report reflects the company's compliance with the seven provisions of the Combined Code specified for our review by the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or to form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

Basis of audit opinion • We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion • In our opinion the financial statements give a true and fair view of the state of affairs of the company and the Group at 31 December 2000 and of the profit and cash flows of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers • chartered accountants and registered auditors • London 5 March 2001

### Notes:

(a) The maintenance and integrity of the Pearson plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

(b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

## NOTES TO THE ACCOUNTS

### 1. ACCOUNTING POLICIES

Accounting policies have been consistently applied except that FRS16 'Current Tax' has been adopted and hence comparative figures have been restated to reflect that UK dividend income is now presented net of UK tax credits. In 1999 the taxation charge has been reduced by £3m and profit on the sale of fixed assets and investments has also been reduced by £3m. FRS15 'Tangible Fixed Assets' has also been adopted.

**a. Basis of accounting** • The accounts are prepared under the historical cost convention and in accordance with applicable accounting standards. A summary of the significant accounting policies is set out below.

**b. Basis of consolidation** • The consolidated accounts include the accounts of all subsidiary undertakings made up to 31 December. Where companies have become or ceased to be subsidiary or associated undertakings during the year, the Group profit includes profits for the period during which they were subsidiary or associated undertakings.

From 1 January 1998 goodwill, being either the net excess of the cost of shares in subsidiary undertakings and associated undertakings over the value attributable to their net assets on acquisition or the cost of other goodwill by purchase, is capitalised and amortised through the profit and loss account over its estimated useful life not exceeding 20 years. Estimated useful life is determined after taking into account such factors as the nature and age of the business and the stability of the industry in which the acquired business operates as well as typical life spans of the acquired products to which the goodwill attaches. Goodwill is subject to an impairment review at the end of the first full year following an acquisition and at any other time if events or changes in circumstances indicate that the carrying value may not be recoverable. Goodwill arising on acquisitions before 1 January 1998 has been deducted from reserves and is charged or credited to the profit and loss account on disposal or closure of the business to which it relates.

The profit of the Group includes the Group's share of the results of associated undertakings, and the consolidated balance sheet includes the Group's interest in associated undertakings at the book value of attributable net assets and attributable goodwill. The figures included in the financial statements have been based on unaudited management accounts for the period to 31 December.

**c. Sales** • Sales represent the amount of goods and services, net of value added tax and other sales taxes, and excluding trade discounts and anticipated returns, provided to external customers and associated undertakings.

Revenue from the sale of books is recognised when the goods are shipped. Anticipated returns are based on historical return rates. Circulation and advertising revenue is recognised when the newspaper or other publication is published. Subscription revenue is recognised over the life of the subscription.

**d. Pension costs** • The regular pension cost of the Group's defined benefit pension schemes is charged to the profit and loss account in order to apportion the cost of pensions over the service lives of employees in the schemes. Variations arising from a significant reduction in the number of employees are adjusted in the profit and loss account to the extent that the year's regular pension cost, reduced by other variations, exceeds contributions payable for that year. Other variations are apportioned over the expected service lives of current employees in the schemes.

**e. Post-retirement benefits other than pensions** • Post-retirement benefits other than pensions are accounted for on an accruals basis to recognise this obligation over the expected service lives of the employees concerned.

**f. Tangible fixed assets** • The cost of tangible fixed assets other than freehold land is depreciated over estimated economic lives in equal annual amounts. Generally, freeholds are depreciated at 1% to 5% per annum, leaseholds at 2% per annum, or over the period of the lease if shorter, and plant and equipment at various rates between 5% and 33% per annum.

**g. Leases** • Finance lease rentals are capitalised at the net present value of the total amount of rentals payable under the leasing agreement (excluding finance charges) and depreciated in accordance with policy f above. Finance charges are written off over the period of the lease in reducing amounts in relation to the written down carrying cost. Operating lease rentals are expensed as incurred.

**h. Fixed asset investments** • Fixed asset investments are stated at cost less provisions for diminution in value.

**i. Stocks** • Stocks and work in progress are stated at the lower of cost and net realisable value.

## 1. ACCOUNTING POLICIES (CONTINUED)

**j. Pre-publication costs** • Pre-publication costs represent direct costs incurred in the development of titles prior to their publication. These costs are carried forward in stock where the title has a useful life in excess of one year. These costs are amortised over estimated economic lives of five years or less, upon publication of the title, with a higher proportion of the amortisation taken in the earlier years.

**k. Royalty advances** • Advances of royalties to authors are included within debtors when the advance is paid less any provision required to bring the amount down to its net realisable value. The royalty advance is expensed at the contracted royalty rate as the related revenues are earned.

**l. Newspaper development costs** • Revenue investment in the development of newspaper titles consists of measures to increase the volume and geographical spread of circulation. These measures include additional and enhanced editorial content, extended distribution and remote printing. These extra costs arising are expensed as incurred.

**m. Deferred taxation** • Deferred taxation is provided, using the liability method, at the expected applicable rates, on all timing differences between accounting and taxation treatments which are expected to reverse in the foreseeable future.

**n. Financial instruments** • The Group uses derivative financial instruments to manage its exposure to interest rate and foreign exchange risks. These include interest rate swaps, currency swaps and forward currency contracts. Amounts payable or receivable in respect of interest rate derivatives are accrued with net interest payable over the period of the contract. Where the derivative instrument is terminated early the gain or loss is spread over the remaining maturity of the original instrument. Foreign currency borrowings and their related derivatives are carried in the balance sheet at the relevant exchange rates at the balance sheet date. Gains or losses in respect of the hedging of overseas subsidiary undertakings are taken to reserves. Gains or losses arising from foreign exchange contracts are taken to the profit and loss account in line with the transactions which they are hedging. Premiums paid on contracts designed to manage currency exposure on specific acquisitions or disposals are charged to the profit and loss account.

The company participates in offset arrangements with certain banks whereby cash and overdraft amounts are offset against each other.

**o. Foreign currencies** • Profit and loss accounts in overseas currencies are translated into sterling at average rates. Balance sheets are translated into sterling at the rates ruling at 31 December. Exchange differences arising on consolidation are taken directly to reserves. Other exchange differences are taken to the profit and loss account where they relate to trading transactions and directly to reserves where they relate to investments.

The principal overseas currency for the Group is the US dollar. The average rate for the year against sterling was \$1.51 (1999: \$1.61) and the year end rate was \$1.49 (1999: \$1.61).

**p. Liquid resources** • Liquid resources comprise short-term deposits of less than one year and investments which are readily realisable and held on a short-term basis.

**q. Retained profits of overseas subsidiaries and associates** • No provision is made for any additional taxation, less double taxation relief, which would arise on the remittance of profits retained where there is no intention to remit such profits.

## NOTES TO THE ACCOUNTS (CONTINUED)

### 2A. ANALYSIS OF SALES

<i>all figures in £ millions</i>	2000			1999		
	sales	internet enterprises	total sales	sales	internet enterprises	total sales
<b>Business sectors</b>						
Pearson Education	2,087	3	2,090	1,725	–	1,725
FT Group	802	42	844	680	7	687
The Penguin Group	755	–	755	565	–	565
Television	185	–	185	355	–	355
Continuing operations	3,829	45	3,874	3,325	7	3,332
<b>Geographical markets supplied</b>						
United Kingdom	520	13	533	539	5	544
Continental Europe	459	7	466	516	2	518
North America	2,504	24	2,528	1,990	–	1,990
Asia Pacific	229	1	230	200	–	200
Rest of world	117	–	117	80	–	80
Continuing operations	3,829	45	3,874	3,325	7	3,332
<i>all figures in £ millions</i>	total by source	inter-regional	total sales	total by source	inter-regional	total sales
<b>Geographical source of sales</b>						
United Kingdom	837	(29)	808	820	(52)	768
Continental Europe	352	(7)	345	394	(6)	388
North America	2,453	(19)	2,434	1,991	(18)	1,973
Asia Pacific	204	(3)	201	159	(4)	155
Rest of world	88	(2)	86	50	(2)	48
Continuing operations	3,934	(60)	3,874	3,414	(82)	3,332

**note** • The table above analyses sales by the geographical region from which the products and services originate. Inter-regional sales are those made between the Group companies in different regions. The Pearson Education business sector includes sales of £146m in respect of National Computer Systems and The Penguin Group business sector includes sales of £125m in respect of Dorling Kindersley, both of which were acquired during 2000.

### 2B. ANALYSIS OF OPERATING PROFIT

<i>all figures in £ millions</i>	2000				
	results from operations	internet enterprises	integration costs	goodwill amortisation	operating profit
<b>Business sectors</b>					
Pearson Education	320	(83)	(13)	(157)	67
FT Group	211	(113)	–	(53)	45
The Penguin Group	79	–	(27)	(14)	38
Television	68	–	–	(15)	53
Continuing operations	678	(196)	(40)	(239)	203
Discontinued operations	8	–	–	–	8
	686	(196)	(40)	(239)	211
<b>Geographical markets supplied</b>					
United Kingdom	89	(90)	(16)	(22)	(39)
Continental Europe	124	(8)	–	(14)	102
North America	405	(97)	(21)	(203)	84
Asia Pacific	26	–	(3)	–	23
Rest of world	34	(1)	–	–	33
Continuing operations	678	(196)	(40)	(239)	203
Discontinued operations	8	–	–	–	8
	686	(196)	(40)	(239)	211

## 2B. ANALYSIS OF OPERATING PROFIT (CONTINUED)

1999

<i>all figures in £ millions</i>	results from operations	internet enterprises	integration costs	year 2000 costs	goodwill amortisation	operating profit
<b>Business sectors</b>						
Pearson Education	257	(3)	(95)	(2)	(121)	36
FT Group	150	(36)	–	(2)	(9)	103
The Penguin Group	65	–	–	(1)	–	64
Television	68	–	–	–	(1)	67
Continuing operations	540	(39)	(95)	(5)	(131)	270
Discontinued operations	48	–	–	–	–	48
	588	(39)	(95)	(5)	(131)	318
<b>Geographical markets supplied</b>						
United Kingdom	46	(34)	(14)	(2)	–	(4)
Continental Europe	110	(1)	(2)	–	(4)	103
North America	340	(4)	(72)	(3)	(127)	134
Asia Pacific	29	–	(6)	–	–	23
Rest of world	15	–	(1)	–	–	14
Continuing operations	540	(39)	(95)	(5)	(131)	270
Discontinued operations	48	–	–	–	–	48
	588	(39)	(95)	(5)	(131)	318

**note** • Integration costs include costs in respect of the Simon & Schuster acquisition in 1998 and the Dorling Kindersley and National Computer Systems acquisitions in 2000. Discontinued operations relate to the withdrawal of the Group from the banking business following its disposal of Lazard in March 2000. Analyses of the profits of joint ventures and associates are shown in notes 14 and 15. Internet enterprises consists of the Group's discrete internet operations, principally FT.com and Learning Network. The Pearson Education business sector (results from operations) includes £15m in respect of National Computer Systems and The Penguin Group business sector (results from operations) includes £nil in respect of Dorling Kindersley, both of which were acquired during 2000. Of the exceptional expense of £40m charged to the profit and loss account in 2000, £21m was charged against provisions.

## 2C. ANALYSIS OF CAPITAL EMPLOYED

*all figures in £ millions*

	2000	1999
<b>Business sectors</b>		
Pearson Education	4,864	2,877
FT Group	542	408
The Penguin Group	569	193
Television	801	(78)
Continuing operations	6,776	3,400
Discontinued operations	–	149
	6,776	3,549
<b>Geographical location</b>		
United Kingdom	379	(30)
Continental Europe	1,038	313
North America	5,217	3,023
Asia Pacific	39	22
Rest of world	103	72
Continuing operations	6,776	3,400
Discontinued operations	–	149
	6,776	3,549
<b>Reconciliation of capital employed to net assets</b>		
Capital employed	6,776	3,549
Less: deferred taxation	(9)	(21)
Less: other provisions	(257)	(206)
Less: net debt	(2,301)	(1,995)
Net assets	4,209	1,327

## NOTES TO THE ACCOUNTS (CONTINUED)

### 3. ANALYSIS OF CONSOLIDATED PROFIT AND LOSS ACCOUNT

*all figures in £ millions*

	2000	1999
<b>Cost of sales</b>	<b>(1,641)</b>	<b>(1,424)</b>
Distribution costs	(180)	(157)
Administration and other expenses	(1,913)	(1,602)
Other operating income (see below)	82	98
<b>Net operating expenses</b>	<b>(2,011)</b>	<b>(1,661)</b>
Analysed as:		
Net operating expenses – before exceptional items and goodwill amortisation	(1,791)	(1,446)
Net operating expenses – exceptional items	(32)	(85)
Net operating expenses – goodwill amortisation	(188)	(130)
<b>Net operating expenses</b>	<b>(2,011)</b>	<b>(1,661)</b>

**note** • The following amounts are included in the 2000 totals in respect of acquisitions: cost of sales £211m and net operating expenses £224m. The exceptional expense of £40m in 2000 (1999: £95m) is included within cost of sales £8m (1999: £10m) and administration and other expenses £32m (1999: £85m) (see note 2).

*all figures in £ millions*

	2000	1999
<b>Other operating income</b>		
Income from other investments:		
Unlisted	3	3
BSBH loan stock interest	–	1
Other operating income (mainly royalties, rights and commission income)	79	94
	<b>82</b>	<b>98</b>
<b>Profit before taxation is stated after charging:</b>		
Amortisation of pre-publication costs	155	134
Depreciation	100	82
Operating lease rentals:		
Plant and machinery	16	22
Properties	75	61
Other	14	12
Year 2000 compliance costs	–	5
Auditors' remuneration:		
Audit	2	2
Non-audit – UK (company £nil; 1999: £nil)	1	2
Non-audit – Other	5	2

**note** • In addition to the non-audit fees (UK) of £1m (1999: £2m), consultancy fees of £1m (1999: £6m) have been incurred in respect of systems development. These fees have been capitalised. Fees of £1m (1999: £2m) were also incurred in the UK in respect of acquisitions and disposals. These fees have also been capitalised. Audit fees of the company amounted to £0.1m (1999: £0.1m).

#### 4. (LOSS)/PROFIT ON SALE OF FIXED ASSETS AND INVESTMENTS

<i>all figures in £ millions</i>	2000	1999 restated
Continuing operations:		
Profit on disposal of interest in BSB Holdings Ltd	–	345
Net (loss)/profit on other investments and property interests	(4)	4
	(4)	349
Taxation	3	(90)

#### 5. PROFIT/(LOSS) ON SALE OF BUSINESSES AND ASSOCIATES

<i>all figures in £ millions</i>	2000	1999
Continuing operations:		
Profit on sale of 20% of Recoletos	86	–
Loss on closure of Dorling Kindersley Family Learning business	(16)	–
Net loss on sale of other businesses and associates	(40)	(44)
	30	(44)
Discontinued operations:		
Profit on sale of Lazard (see note 15)	231	–
	261	(44)
Taxation	(51)	5

#### 6. NET INTEREST PAYABLE – GROUP

<i>all figures in £ millions</i>	2000	1999
<b>Interest payable and similar charges:</b>		
On borrowing repayable wholly within five years not by instalments	(110)	(155)
On borrowing repayable wholly or partly after five years	(67)	(29)
	(177)	(184)
<b>Interest receivable and similar income:</b>		
On deposits and liquid funds	21	29
On discounted proceeds on businesses held for resale	–	7
Amortisation of swap proceeds (see note 22)	2	3
<b>Net interest payable</b>	<b>(154)</b>	<b>(145)</b>

#### 7. OTHER NET FINANCE COSTS

The amortisation of an arrangement fee in respect of a borrowing facility has been accelerated due to the early redemption of the facility resulting in a charge of £16m. An £8m premium was paid in respect of a forward currency option in connection with the acquisition of National Computer Systems.

## NOTES TO THE ACCOUNTS (CONTINUED)

### 8. TAXATION

<i>all figures in £ millions</i>	2000	1999 restated
<b>UK</b>		
Corporation tax for the period at 30% (1999: 30.2%)	40	116
Adjustments in respect of prior periods	(13)	(11)
	27	105
Double taxation relief	(1)	(1)
	26	104
Deferred taxation (see note 23)	(1)	6
Joint ventures	(6)	–
Associates	6	9
<b>Overseas</b>		
Overseas taxation for the period	70	52
Deferred taxation	(3)	–
Associates	14	6
	106	177

<i>all figures in percentages</i>	2000	1999 restated
<b>Tax rate reconciliation</b>		
UK tax rate	30.0	30.2
Effect of overseas tax rates	2.2	3.0
Effect of utilisation of tax losses in the US	(7.8)	(9.8)
Other items	(1.4)	1.6
Tax rate reflected in adjusted earnings (before internet enterprises)	23.0	25.0
Effect of internet enterprises	3.1	–
Tax rate reflected in adjusted earnings (after internet enterprises)	26.1	25.0
Effect of profits/(losses) excluded from adjusted earnings	11.2	12.1
<b>Tax rate reflected in earnings</b>	37.3	37.1

**note** • The Group has significant tax losses available in the US which are not recognised in the accounts and hence the tax rate reflected in adjusted earnings is lower than the UK tax rate.

### 9. DIVIDENDS

	2000		1999	
	pence per share	£m	pence per share restated	£m
Interim paid	8.2	58	7.7	53
Final proposed	13.2	106	12.4	85
Dividends for the year	21.4	164	20.1	138

**note** • 1999 interim and final and 2000 interim dividends per share have been restated to reflect the rights issue of equity shares during 2000 (see note 25). Dividends in respect of the company's shares held by employee share trusts (see note 16) have been waived.



## 10. EARNINGS PER SHARE

In order to show results from operating activities on a comparable basis two adjusted earnings per equity share are presented. First, an adjusted earnings per share is presented which excludes profits or losses on the sale of fixed assets and investments, businesses and associates (see notes 4 and 5) which in 2000 relate primarily to the sale of Lazard and the sale of 20% of Recoletos. Also excluded are Year 2000 compliance costs, integration costs in respect of the acquisitions of Simon & Schuster, Dorling Kindersley and National Computer Systems (NCS) (see note 2), the accelerated amortisation of a financing arrangement fee following the early redemption of a borrowing facility, the premium paid in respect of a forward currency option in connection with the acquisition of NCS (see note 7) and goodwill amortisation. Due to a significant level of expenditure on internet enterprises, a second adjusted earnings per equity share is presented in which the results of these are also excluded from earnings.

	2000		1999 restated	
	£m	earnings per share (p)	£m	earnings per share (p)
<b>Profit for the financial year</b>	179	24.6	294	43.0
Adjustments:				
Loss/(profit) on sale of fixed assets and investments: continuing operations (see note 4)	4	0.5	(349)	(51.0)
(Profit)/loss on sale of businesses and associates: continuing operations (see note 5)	(30)	(4.0)	44	6.4
(Profit) on sale of businesses and associates: discontinued operations (see note 5)	(231)	(31.7)	–	–
Loss/(profit) on sale of businesses and associates by an associate: continuing operations	3	0.4	(1)	(0.1)
Internet enterprises (see note 2)	196	26.9	39	5.7
Interest on internet enterprises	9	1.2	–	–
Goodwill amortisation (see notes 12/15)	239	32.9	131	19.2
Integration costs (see note 2)	40	5.5	95	13.9
Other net finance costs (see note 7)	24	3.3	–	–
Year 2000 compliance costs	–	–	5	0.7
Taxation on above items	(18)	(2.5)	67	9.8
Minority interest share of above items	(18)	(2.5)	–	–
<b>Adjusted earnings before internet enterprises</b>	397	54.6	325	47.6
Internet enterprises	(196)	(26.9)	(39)	(5.7)
Interest on internet enterprises	(9)	(1.2)	–	–
Taxation on internet enterprises	37	5.0	10	1.4
Minority interest share of internet enterprises	3	0.4	–	–
<b>Adjusted earnings after internet enterprises</b>	232	31.9	296	43.3
Profit for the financial year	179	24.3	294	42.5
Taxation on the conversion of ordinary shares	(2)	(0.3)	(1)	(0.1)
<b>Diluted earnings</b>	177	24.0	293	42.4
Weighted average number of equity shares (millions) – for earnings and adjusted earnings	727.7		683.4	
Effect of dilutive share options	8.4		7.8	
Weighted average number of equity shares (millions) – for diluted earnings	736.1		691.2	

**note** • The weighted average number of shares in 1999 has been restated to reflect the rights issue of equity shares during 2000.

## NOTES TO THE ACCOUNTS (CONTINUED)

### 11. EMPLOYEE INFORMATION

The details of the emoluments of the directors of Pearson plc are shown on pages 47 to 54 and form part of these audited financial statements.

<i>all figures in £ millions</i>	2000	1999
<b>Staff costs</b>		
Wages and salaries	792	702
Social security costs	82	75
Post-retirement costs	22	26
	<b>896</b>	<b>803</b>

	UK	US	other	total
<b>Average number employed 2000</b>				
Pearson Education	1,517	9,180	2,888	13,585
FT Group	2,166	1,413	1,892	5,471
The Penguin Group	1,630	2,310	768	4,708
Television	390	60	247	697
Other	168	59	–	227
Continuing operations	<b>5,871</b>	<b>13,022</b>	<b>5,795</b>	<b>24,688</b>
<b>Average number employed 1999</b>				
Pearson Education	1,407	7,229	2,042	10,678
FT Group	2,158	1,034	1,790	4,982
The Penguin Group	749	1,866	614	3,229
Television	617	105	550	1,272
Other	171	51	–	222
Continuing operations	<b>5,102</b>	<b>10,285</b>	<b>4,996</b>	<b>20,383</b>

<i>all figures in £ millions</i>	2000	1999
<b>Post-retirement costs</b>		
Defined benefit pension schemes		
UK Group plan: regular pension cost	8	8
UK Group plan: amortisation of surplus	(8)	(3)
Net pension charge	–	5
Other defined benefit pension schemes	13	11
Defined contribution pension schemes	5	6
Medical benefits	4	4
	<b>22</b>	<b>26</b>

**Pension schemes** • The Group operates a number of pension schemes throughout the world. The major schemes are self-administered and the schemes' assets are held independently of the Group. Pension costs are assessed in accordance with the advice of independent qualified actuaries. The principal schemes are primarily of the defined benefit type. There is also a closed defined benefit scheme in the UK, which now receives neither employers' nor members' contributions, and a number of other defined benefit and defined contribution schemes, principally overseas.

The most recent full actuarial valuation was performed as at 1 January 1999, using the projected unit method of valuation. The market value of the assets of the scheme at this date was £1,038m. The actuarial assumptions used to determine the SSAP24 charge are shown on page 71. The net assets of the UK Group plan at 31 December 2000 are included in the pension plan accounts at £1,185m (unaudited).

## 11. EMPLOYEE INFORMATION (CONTINUED)

	UK group plan
Real return on investments per annum	3.9%
Real increase in earnings per annum	1.9%
Real increase in pensions in payment per annum	0.0%
Real increase in dividends per annum	1.25%
Level of funding•	112%

• Actuarial value of assets expressed as a percentage of the actuarial value of the liabilities.

In view of these results, all employers' contributions remain suspended for the time being and the valuation surplus is being apportioned, in accordance with SSAP24, on a mortgage basis over the expected remaining service lives of the current employees.

The total market value of the assets of other defined benefit schemes (mainly in the US), valued this year, was £93m (1999: £64m).

**Other post-retirement benefits** • The Group provides certain health-care and life-assurance benefits principally for retired US employees and their dependants. These plans are unfunded. Retirees are eligible for participation if they meet certain age and service requirements. Plans that are available vary depending on the business division in which the retiree worked. Plan choices and retiree contributions are dependent on retirement date, business division, option chosen and length of service.

The principal assumptions affecting the provision for other post-retirement benefits were: medical inflation rates of between 5% and 7% and a discount rate of 8%.

## 12. INTANGIBLE ASSETS

*all figures in £ millions*

	goodwill
<b>Cost</b>	
At 31 December 1999	2,599
Exchange differences	162
Additions (see note 27)	2,206
Television assets contributed	(70)
Disposals (see note 28)	(37)
<b>At 31 December 2000</b>	<b>4,860</b>
<b>Amortisation</b>	
At 31 December 1999	(142)
Exchange differences	(12)
Television assets contributed	2
Disposals (see note 28)	2
Provided in the year	(188)
<b>At 31 December 2000</b>	<b>(338)</b>
<b>Net carrying amount</b>	
At 31 December 1999	2,457
<b>At 31 December 2000</b>	<b>4,522</b>

## NOTES TO THE ACCOUNTS (CONTINUED)

### 13. TANGIBLE FIXED ASSETS

<i>all figures in £ millions</i>	freehold & leasehold property	plant & equipment	assets in course of construction	total
<b>Cost</b>				
At 31 December 1999	235	537	21	793
Exchange differences	8	20	1	29
Reclassifications	14	8	(22)	–
Owned by subsidiary undertakings acquired	71	134	–	205
Television assets contributed	(34)	(54)	–	(88)
Capital expenditure	24	102	3	129
Owned by subsidiary undertakings disposed	–	(4)	–	(4)
Disposals	(17)	(67)	(1)	(85)
<b>At 31 December 2000</b>	<b>301</b>	<b>676</b>	<b>2</b>	<b>979</b>
<b>Depreciation</b>				
At 31 December 1999	(81)	(307)	–	(388)
Exchange differences	(2)	(13)	–	(15)
Impairment in value	–	(1)	–	(1)
Provided in the year	(12)	(88)	–	(100)
Owned by subsidiary undertakings acquired	(12)	(46)	–	(58)
Television assets contributed	6	26	–	32
Owned by subsidiary undertakings disposed	–	1	–	1
Disposals	9	65	–	74
<b>At 31 December 2000</b>	<b>(92)</b>	<b>(363)</b>	<b>–</b>	<b>(455)</b>
<b>Net book value</b>				
At 31 December 1999	154	230	21	405
<b>At 31 December 2000</b>	<b>209</b>	<b>313</b>	<b>2</b>	<b>524</b>

**Freehold and leasehold property** • Net book value includes: freehold of £154m (1999: £113m) and short leases of £56m (1999: £41m).

**Capital commitments** • The Group had capital commitments for fixed assets, including finance leases, already under contract amounting to £24m at 31 December 2000 (1999: £20m).

**Other notes** • The net book value of Group tangible fixed assets includes £11m (1999: £23m) in respect of assets held under finance leases. Depreciation on these assets charged in 2000 was £1m (1999: £2m).

### 14. JOINT VENTURES

<i>all figures in £ millions</i>	2000		1999	
	valuation	book value	valuation	book value
Unlisted joint ventures	12	12	–	–

**note** • The valuations of unlisted joint ventures are directors' valuations as at 31 December 2000. If realised at these values there would be no liability for taxation. The Group had no capital commitments to subscribe for further capital and loan stock.

<i>all figures in £ millions</i>	equity	reserves	total net assets
<b>Summary of movements</b>			
At 31 December 1999	–	–	–
Transfer from associates	8	(2)	6
Owned by businesses acquired	2	–	2
Additions	19	–	19
Retained loss for the year	–	(15)	(15)
<b>At 31 December 2000</b>	<b>29</b>	<b>(17)</b>	<b>12</b>

#### 14. JOINT VENTURES (CONTINUED)

	2000	
	operating profit	total net assets
<i>all figures in £ millions</i>		
<b>Analysis of joint ventures</b>		
<b>Business sectors</b>		
FT Group	(21)	10
The Penguin Group	–	2
Continuing operations	(21)	12
<b>Geographical markets supplied and location of net assets</b>		
United Kingdom	(2)	3
Continental Europe	(19)	9
Continuing operations	(21)	12

	2000
<i>all figures in £ millions</i>	
<b>Reconciliation to retained loss</b>	
Operating loss of joint ventures	(21)
UK taxation	6
<b>Retained loss for the year</b>	<b>(15)</b>

#### 15. ASSOCIATES

	2000		1999	
	valuation	book value	valuation	book value
<i>all figures in £ millions</i>				
Partnership interests	–	–	410	149
Listed associates	1,895	948	–	–
Unlisted associates	341	72	426	18
Loans	4	4	67	67
	<b>2,240</b>	<b>1,024</b>	<b>903</b>	<b>234</b>

**note** • Principal associates are listed on page 97. The valuations of unlisted associates are directors' valuations as at 31 December 2000. If all associates were realised at these values there would be an estimated liability for taxation, at year end rates, of £153m. The Group had no capital commitments to subscribe for further capital and loan stock.

## NOTES TO THE ACCOUNTS (CONTINUED)

### 15. ASSOCIATES (CONTINUED)

<i>all figures in £ millions</i>	equity	share of loans	reserves	total	goodwill	total net assets
<b>Summary of movements</b>						
At 31 December 1999	98	67	43	208	26	234
Exchange differences	2	–	2	4	15	19
Transfer to joint ventures	(8)	–	2	(6)	–	(6)
Additions	18	13	–	31	58	89
Combination of television interests:						
– Television assets contributed	(4)	(64)	51	(17)	(48)	(65)
– Share of combined television interests	183	–	–	183	633	816
Combination of Asset Valuation interests						
– DBC	5	–	–	5	117	122
Disposals	(104)	(12)	(45)	(161)	–	(161)
Retained loss for the year	–	–	(14)	(14)	–	(14)
Goodwill written back on disposal	41	–	–	41	–	41
Goodwill amortisation	–	–	–	–	(51)	(51)
<b>At 31 December 2000</b>	<b>231</b>	<b>4</b>	<b>39</b>	<b>274</b>	<b>750</b>	<b>1,024</b>

<i>all figures in £ millions</i>	2000		1999	
	operating profit	total net assets	operating profit	total net assets
<b>Analysis of associates</b>				
<b>Business sectors</b>				
Pearson Education	7	18	6	7
FT Group	(30)	175	14	63
Television	25	831	3	15
Continuing operations	2	1,024	23	85
Discontinued operations	8	–	48	149
	10	1,024	71	234
<b>Geographical markets supplied and location of net assets</b>				
United Kingdom	3	(3)	–	2
Continental Europe	29	874	10	56
North America	(36)	135	8	14
Rest of world	6	18	5	13
Continuing operations	2	1,024	23	85
Discontinued operations	8	–	48	149
	10	1,024	71	234

**note** • Operating profit from continuing operations before goodwill amortisation is analysed as Pearson Education £7m, FT Group £7m and Television £39m.

## 15. ASSOCIATES (CONTINUED)

*all figures in £ millions*

	2000
<b>Reconciliation to retained loss</b>	
Operating profit of partnerships and other associates (before goodwill amortisation)	61
Loss on sale of business by an associate	(3)
Net interest payable of associates	(3)
UK taxation	(6)
Overseas taxation	(14)
Distributions receivable in respect of the year from partnership interests	(35)
Dividends (including tax credits) from unlisted associates	(14)
<b>Retained loss for the year</b>	<b>(14)</b>

The aggregate of the Group's share in its associates, excluding the Group's interest in the RTL Group, and Lazard in 1999, is shown below.

<i>all figures in £ millions</i>	2000	1999
Sales	384	299
Fixed assets	42	72
Current assets	132	165
Liabilities due within one year	(73)	(105)
Liabilities due after one year or more	(32)	(73)
<b>Net assets</b>	<b>69</b>	<b>59</b>

In July 2000 the Group combined its television business with CLT-Ufa and retained a 22% shareholding in the new combined business, the RTL Group. The Group's share in the sales and net assets of the RTL Group is shown below.

<i>all figures in £ millions</i>	2000
Sales	271
Fixed assets	241
Current assets	348
Liabilities due within one year	(324)
Liabilities due after one year or more	(60)
<b>Net assets</b>	<b>205</b>

The Group's interest in Lazard Partners Limited Partnership and the three Lazard Houses for the year ended 31 December 1999 is shown below. On 3 March 2000, the Group sold its interests in Lazard Partners Limited Partnership and the three Lazard Houses for £436m comprising £40m in respect of dividends and partnership distributions and proceeds of £396m, less costs of £4m, giving rise to a profit on sale of £231m before tax estimated at £34m.

<i>all figures in £ millions</i>	2000	1999
Profit before tax	8	48
Taxation	(2)	(7)
Profit after taxation	6	41
Fixed assets	–	26
Current assets	–	3,399
Liabilities due within one year	–	(2,819)
Liabilities due after one year or more	–	(457)

## NOTES TO THE ACCOUNTS (CONTINUED)

### 16. OTHER FIXED ASSET INVESTMENTS

<i>all figures in £ millions</i>	2000		1999	
	valuation	book value	valuation	book value
Listed	82	82	51	16
Unlisted	73	73	83	83
	155	155	134	99

**note** • The valuations of unlisted investments are directors' valuations as at 31 December 2000. If all investments were realised at valuation there would be no liability for taxation.

<i>all figures in £ millions</i>	own shares held	other	total
<b>Cost</b>			
At 31 December 1999	10	89	99
Exchange differences	–	5	5
Additions	71	61	132
Owned by subsidiaries acquired	–	38	38
Television assets contributed	–	(75)	(75)
Transfers	–	(14)	(14)
Disposals	(1)	(15)	(16)
<b>At 31 December 2000</b>	<b>80</b>	<b>89</b>	<b>169</b>
<b>Provision</b>			
At 31 December 1999	–	–	–
Transfer from other creditors	6	–	6
Disposals	(1)	–	(1)
Provided during the year	9	–	9
<b>At 31 December 2000</b>	<b>14</b>	<b>–</b>	<b>14</b>
<b>Net book value</b>			
At 31 December 1999	10	89	99
<b>At 31 December 2000</b>	<b>66</b>	<b>89</b>	<b>155</b>

**note** • The Pearson Employee Share Trust and Pearson plc Employee Share Ownership Trusts hold 4.2m (1999: 1m) Pearson plc ordinary shares which had a market value of £66m at 31 December 2000 (1999: £19m). These shares have been acquired by the trusts, using funds provided by Pearson plc, to meet obligations under various executive and employee option and restricted share plans. Under these plans the participants become entitled to shares after a specified number of years and subject to certain performance criteria being met. Pearson aims to hedge its liability under the plans by buying shares through the trusts to meet the anticipated future liability. The anticipated future liability is regularly re-assessed during the year and additional shares are purchased when required to meet an increase in this liability. The cost of funding and administering the trusts are charged to the profit and loss account in the period to which they relate. The cost of the shares is being amortised over the performance period of the associated plans. Dividends on the shares held by the trusts have been waived.

### 17. STOCKS

<i>all figures in £ millions</i>	2000	1999
Raw materials	29	35
Work in progress	68	62
Finished goods	383	310
Pre-publication costs	348	284
	828	691

**note** • The replacement cost of stocks is not materially different from book value.



## 18. DEBTORS

*all figures in £ millions*

	2000	1999
<b>Amounts falling due within one year</b>		
Trade debtors	809	807
Associates	99	10
Royalty advances	88	83
Other debtors	95	84
Prepayments and accrued income	58	82
	1,149	1,066
<b>Amounts falling due after more than one year</b>		
Royalty advances	48	54
Other debtors	19	6
Prepayments and accrued income	1	6
	68	66
	1,217	1,132

## 19. CURRENT ASSET INVESTMENTS

<i>all figures in £ millions</i>	2000		1999	
	valuation	book value	valuation	book value
Listed	8	8	–	–
Unlisted	4	4	4	4
	12	12	4	4

**note** • The valuations of unlisted investments are directors' valuations as at 31 December 2000. If all investments were realised at valuation there would be no liability for taxation.

*all figures in £ millions*

### Summary of movements

At 31 December 1999	4
Transfers	9
Disposals	(1)
<b>At 31 December 2000</b>	<b>12</b>

## 20. CASH AT BANK AND IN HAND

<i>all figures in £ millions</i>	2000		1999	
	Group	company	Group	company
Cash, bank current accounts and overnight deposits	425	–	288	–
Certificates of deposit and commercial paper	15	–	22	–
Term bank deposits	76	56	18	7
	516	56	328	7

## NOTES TO THE ACCOUNTS (CONTINUED)

### 21. FINANCIAL INSTRUMENTS

A full discussion on treasury policy is given in the Financial Review on pages 36 to 38. Short-term debtors and creditors have been excluded from all the following disclosures, other than currency risk disclosures.

#### a. Maturity of borrowings and other financial liabilities

The maturity profile of the Group's borrowings and other financial liabilities is shown below.

<i>all figures in £ millions</i>	2000		1999	
	Group	company	Group	company
<b>Maturity of borrowings</b>				
<b>Short-term</b>				
Bank loans and overdrafts	112	225	47	130
Total due within one year	112	225	47	130
<b>Medium and long-term</b>				
Loans or instalments thereof repayable:				
From one to two years	100	–	155	155
From two to five years	1,626	905	1,617	906
After five years not by instalments	979	813	504	351
Total due after more than one year	2,705	1,718	2,276	1,412
<b>Total borrowings</b>	<b>2,817</b>	<b>1,943</b>	<b>2,323</b>	<b>1,542</b>

**note** • At 31 December 2000 £1,134m (1999: £547m) of debt, including commercial paper, currently classified from two to five years would be repayable within one year if refinancing contracts were not in place. The short-term bank loans and overdrafts of the Group are lower than those of the company because of bank offset arrangements.

<i>all figures in £ millions</i>	2000			1999		
	Group finance leases	Group other financial liabilities	Group total	Group finance leases	Group other financial liabilities	Group total
<b>Maturity of other financial liabilities</b>						
Amounts falling due:						
In one year or less or on demand	6	5	11	5	–	5
In more than one year but not more than two years	3	16	19	7	11	18
In more than two years but not more than five years	6	14	20	3	4	7
In more than five years	1	10	11	–	1	1
	<b>16</b>	<b>45</b>	<b>61</b>	<b>15</b>	<b>16</b>	<b>31</b>

#### b. Borrowings by instrument

<i>all figures in £ millions</i>	2000		1999	
	Group	company	Group	company
<b>Unsecured</b>				
10.75% Sterling Bonds 2002	100	–	100	–
9.5% Sterling Bonds 2004	130	–	120	–
4.625% Euro Bonds 2004	356	356	345	345
7.125% US Dollar notes 2006	166	–	153	–
6.125% Euro Bonds 2007	441	441	–	–
10.5% Sterling Bonds 2008	100	100	100	100
7% Sterling Bonds 2014	272	272	251	251
Variable rate loan notes	74	74	–	–
Bank loans and overdrafts and commercial paper	1,178	700	1,254	846
<b>Total borrowings</b>	<b>2,817</b>	<b>1,943</b>	<b>2,323</b>	<b>1,542</b>

## 21. FINANCIAL INSTRUMENTS (CONTINUED)

### c. Undrawn committed borrowing facilities

all figures in £ millions

	2000	1999
Expiring within one year	–	–
Expiring between one and two years	–	155
Expiring in more than two years	609	362
	609	517

note • All of the above committed borrowing facilities incur commitment fees at market rates.

### d. Currency and interest rate risk profile

	2000				
	borrowings £m	total variable rate £m	total fixed rate £m	fixed rate borrowings weighted average interest rate %	weighted average period for which rate is fixed – years
<b>Currency and interest rate risk profile of borrowings</b>					
US dollar	1,782	721	1,061	6.2	4.1
Sterling	587	447	140	8.4	4.8
€uro	417	379	38	5.4	4.2
Other currencies	31	31	–	–	–
	2,817	1,578	1,239		

	1999				
	borrowings £m	total variable rate £m	total fixed rate £m	fixed rate borrowings weighted average interest rate %	weighted average period for which rate is fixed – years
<b>Currency and interest rate risk profile of borrowings</b>					
US dollar	1,795	790	1,005	6.1	4.6
Sterling	280	130	150	8.5	5.0
€uro	248	248	–	–	–
	2,323	1,168	1,155		

note • The figures shown in the tables above take into account interest rate, currency swaps and forward rate contracts entered into by the Group. Variable rate borrowings bear interest at rates based on relevant national LIBOR equivalents.

	2000		
	other financial liabilities	total fixed rate	total no interest paid
<b>Currency and interest rate risk profile of other financial liabilities</b>			
US dollar	48	11	37
Sterling	13	5	8
	61	16	45

## NOTES TO THE ACCOUNTS (CONTINUED)

### 21. FINANCIAL INSTRUMENTS (CONTINUED)

#### d. Currency and interest rate risk profile (continued)

*all figures in £ millions*

		1999	
	other financial liabilities	total fixed rate	total no interest paid
<b>Currency and interest rate risk profile of other financial liabilities</b>			
US dollar	21	14	7
Sterling	9	–	9
Other currencies	1	1	–
	31	15	16

**note** • Variable rate financial liabilities bear interest at rates based on relevant national LIBOR equivalents.

	2000			
<i>all figures in £ millions</i>	cash at bank and in hand	short-term deposits	other financial assets	total
<b>Currency and interest rate risk profile of financial assets</b>				
US dollar	223	56	21	300
Sterling	6	15	9	30
€uro	69	3	1	73
Other currencies	127	17	–	144
	425	91	31	547
Floating rate	326	7	–	333
Fixed rate	50	84	2	136
No interest paid	49	–	29	78
	425	91	31	547

**note** • Floating rate cash and deposits earn interest based on relevant national LIBID equivalents. Fixed rate cash and deposits earn interest at rates between 4.5% and 12%. Of the total financial assets earning interest at fixed rates, £94m are US dollar denominated.

	1999			
<i>all figures in £ millions</i>	cash at bank and in hand	short-term deposits	other financial assets	total
<b>Currency and interest rate risk profile of financial assets</b>				
US dollar	183	7	1	191
Sterling	5	17	2	24
€uro	61	14	1	76
Other currencies	39	2	–	41
	288	40	4	332
Floating rate	221	1	–	222
Fixed rate	48	35	–	83
No interest paid	19	4	4	27
	288	40	4	332

**note** • Floating rate cash and deposits earn interest based on relevant national LIBID equivalents. Fixed rate cash and deposits earn interest at rates between 3% and 8.4%.

## 21. FINANCIAL INSTRUMENTS (CONTINUED)

### e. Currency exposures

The table below shows the extent to which Group companies have monetary assets and liabilities in currencies other than their local currency.

<i>all figures in £ millions</i>	2000				total
	US dollar	net foreign monetary assets/ sterling	euro	(liabilities) other	
Functional currency of entity:					
US dollar	–	1	–	6	7
Sterling	10	–	12	19	41
€euro	–	2	–	–	2
Other currencies	–	(1)	–	–	(1)
	10	2	12	25	49

<i>all figures in £ millions</i>	1999				total
	US dollar	net foreign monetary assets/ sterling	euro	(liabilities) other	
Functional currency of entity:					
US dollar	–	(4)	2	9	7
Sterling	21	–	6	14	41
Other currencies	5	(3)	–	–	2
	26	(7)	8	23	50

### f. Fair values of financial assets and financial liabilities

The table below shows the book value and the fair value of the Group's financial assets and financial liabilities.

<i>all figures in £ millions</i>	2000		1999	
	book value	fair value	book value	fair value
<b>Primary financial instruments held or issued to finance the Group's operations</b>				
Other financial assets	31	31	4	4
Other financial liabilities	(61)	(61)	(31)	(31)
Cash at bank and in hand	425	425	288	288
Short-term deposits	91	91	40	40
Short-term borrowings	(112)	(112)	(47)	(47)
Medium and long-term borrowings	(2,705)	(2,683)	(2,276)	(2,307)
<b>Derivative financial instruments held to manage the interest rate and currency profile</b>				
Interest rate swaps	–	(4)	–	23
Currency swaps	–	20	–	10
Foreign exchange contracts	–	2	–	1

**note** • Other financial assets, other financial liabilities, cash at bank and in hand, short-term deposits and short-term borrowings: the fair value approximates to the carrying value due to the short maturity periods of these financial instruments. Medium and long-term borrowings: the fair value is based on market values or, where these are not available, on the quoted market prices of comparable debt issued by other companies. Interest rate swaps: the fair value of interest rate swaps is based on market values. At 31 December 2000 the notional principal value of these swaps was £2,057m (1999: £1,818m). Currency swaps: the fair value of these contracts is based on market values. At 31 December 2000 the Group had £890m (1999: £473m) of such contracts outstanding.

## NOTES TO THE ACCOUNTS (CONTINUED)

### 21. FINANCIAL INSTRUMENTS (CONTINUED)

#### g. Hedges

The Group's policy on hedges is explained on page 36. The table below shows the extent to which the Group has off-balance sheet (unrecognised) and on-balance sheet (deferred) gains and losses in respect of financial instruments used as hedges at the beginning and end of the year. It also shows the amount of such gains and losses which have been included in the profit and loss account for the year and those gains and losses which are expected to be included in next year's or later profit and loss accounts.

<i>all figures in £ millions</i>	unrecognised		total net gains/(losses)	deferred gains
	gains	losses		
<b>Gains and losses on hedges at 31 December 1999</b>	51	(17)	34	4
Gains and losses arising in previous years that were recognised in 2000	(8)	1	(7)	(2)
<b>Gains and losses arising before 31 December 1999 that were not recognised in 2000</b>	43	(16)	27	2
Gains and losses arising in 2000 that were not recognised in 2000	(2)	(7)	(9)	–
<b>Unrecognised gains and losses on hedges at 31 December 2000</b>	<b>41</b>	<b>(23)</b>	<b>18</b>	<b>2</b>
Of which:				
Gains and losses expected to be recognised in 2001	2	–	2	2
Gains and losses expected to be recognised in 2002 or later	39	(23)	16	–

### 22. OTHER CREDITORS

*all figures in £ millions*

	2000	1999
<b>Amounts falling due within one year</b>		
Trade creditors	426	473
Taxation	255	294
Social security and other taxes	3	28
Other creditors	121	74
Accruals and deferred income	567	482
Obligations under finance leases	6	5
Dividends	106	85
	<b>1,484</b>	<b>1,441</b>
<b>Amounts falling due after more than one year</b>		
Trade creditors	–	2
Other creditors	21	10
Accruals and deferred income	3	10
Obligations under finance leases	10	10
	<b>34</b>	<b>32</b>

**note** • Accruals and deferred income includes £2m (1999: £4m) relating to the unamortised profit arising out of the unwinding of a sterling interest rate swap in 1994. The swap was arranged in 1992 in connection with the issue of £100m 10.75% Sterling Bonds 2002. The profit is being amortised over the remaining life of the bonds. None of the amount falls due after more than one year.

### 23. DEFERRED TAXATION

*all figures in £ millions*

	2000
<b>Summary of movements</b>	
At 31 December 1999	21
Subsidiary undertakings acquired/disposed	(8)
Television assets contributed	(8)
Transfers	8
Net release in the year	(4)
<b>At 31 December 2000</b>	<b>9</b>

*all figures in £ millions*

	2000	1999
<b>Deferred taxation derives from</b>		
Capital allowances	4	1
Taxation on unremitted overseas earnings	19	18
Other timing differences	(14)	2
	<b>9</b>	<b>21</b>
<b>Deferred taxation not provided</b>		
Relating to revalued assets and timing differences	4	4
Relating to gains subject to roll-over relief	1	1
	<b>5</b>	<b>5</b>

**note** • The Group has calculated deferred tax not provided on rolled over gains in 2000 taking into account the indexation allowance which would be deductible on a disposal of the asset into which the gain was rolled.

### 24. OTHER PROVISIONS FOR LIABILITIES AND CHARGES

<i>all figures in £ millions</i>	post- retirement	deferred consideration	integration	reorganisations	leases	other	total
At 31 December 1999	95	29	24	6	25	27	206
Exchange differences	7	2	1	–	1	–	11
Subsidiary undertakings acquired/disposed	1	5	14	8	(3)	1	26
Deferred consideration arising on acquisitions	–	39	–	–	–	–	39
Television assets contributed	(2)	(14)	–	–	(1)	(2)	(19)
Transfer from creditors	1	–	3	1	1	(1)	5
Released	(2)	–	–	(1)	–	(3)	(6)
Provided	24	–	21	6	–	–	51
Utilised	(15)	(5)	(24)	(4)	(3)	(5)	(56)
<b>At 31 December 2000</b>	<b>109</b>	<b>56</b>	<b>39</b>	<b>16</b>	<b>20</b>	<b>17</b>	<b>257</b>

**note**

- a. Post-retirement provisions are in respect of pensions, £46m and post-retirement medical benefits, £63m.
- b. Deferred consideration. Included within the balance is £30m which relates to the purchase of Forum in 2000 which will be paid in 2001.
- c. Integration. During the year £21m has been provided (see note 2) mainly in respect of the acquisitions of Dorling Kindersley and NCS. £24m has been utilised mainly in respect of the integration of Simon & Schuster following its acquisition in 1998. The balance is expected to be utilised in the year ended 31 December 2001.
- d. Reorganisations. Included in the balance is £7m in respect of the acquisition of Forum which is expected to be utilised in the year ended 31 December 2001.
- e. Lease commitments. These relate primarily to onerous lease contracts, acquired as part of the purchase of subsidiary undertakings, which have expiry dates up to 2010. The provision is based on current occupancy estimates and it has been assumed that the properties will not be sub-let.
- f. Other. Included within other is £9m (1999: £12m) in respect of warranty and legal claims, the timing of the settlement of which is unknown. The balance, which relates to a number of small items, is expected to be utilised over varying time periods.

## NOTES TO THE ACCOUNTS (CONTINUED)

### 25. SHARE CAPITAL

	number (000s)	£m
<b>Authorised</b>		
Ordinary shares of 25p each		
<b>At 31 December 2000</b>	916,000	229
<b>Called up, allotted and fully paid</b>		
At 31 December 1999	612,670	153
Issued under share option and employee share schemes	2,895	1
Issued under placing	11,500	3
Issued under rights issue	170,528	42
<b>At 31 December 2000</b>	797,593	199

**note** • The consideration received in respect of shares issued during the year was £1,961m (1999: £18m). In January 2000 Pearson placed 11,500,000 ordinary shares and raised approximately £250m, after expenses, to fund its existing and new internet-related businesses. In September 2000 Pearson completed a 3 for 11 rights issue of 170,528,278 new Pearson shares at a price of £10 per ordinary share. The purpose of the rights issue was to finance the acquisition of National Computer Systems, Inc.

	when granted	number of shares (000s) restated	original subscription price (p) restated	exercise period
<b>Options outstanding at 31 December 2000</b>				
Worldwide Save for Shares plans	1994	70	455	1999 – 02
	1995	89	390	2000 – 03
	1996	345	517	2001 – 04
	1997	284	530	2000 – 05
	1998	922	687	2001 – 06
	1999	1,407	913 – 970	2001 – 07
	2000	728	688 – 1,793	2000 – 08
		3,845		
Executive share option plans	1991	34	337 – 365	1994 – 01
	1992	43	293 – 380	1995 – 02
	1994	196	567 – 635	1997 – 04
	1995	271	487 – 606	1998 – 05
	1996	484	584 – 683	1999 – 06
	1997	1,801	664 – 758	2000 – 07
	1998	2,838	847 – 1,090	2001 – 08
	1999	3,234	1,081 – 1,285	2002 – 09
	2000	7,757	100 – 2,481	2000 – 10
		16,658		

**note** • The subscription prices have been rounded up to the nearest whole penny. The number of shares and the original subscription price have been restated to reflect the rights issue of equity shares during 2000. The 2000 figures include replacement options granted to employees of Dorling Kindersley and the Family Education Network following their acquisition during the year.



## 26. RESERVES

*all figures in £ millions*

	share premium account	profit and loss account
<b>Summary of movements</b>		
At 31 December 1999	517	651
Exchange differences	–	87
Premium on issue of 185m equity shares	1,923	(8)
Goodwill arising on prior year acquisitions	–	1
Goodwill written back on business combinations	–	585
Goodwill written back	–	68
Replacement options granted on acquisition of subsidiary		
– at acquisition	–	5
– post acquisition	–	1
Profit retained for the year	–	15
<b>At 31 December 2000</b>	<b>2,440</b>	<b>1,405</b>
<b>Analysed as:</b>		
Joint ventures and associates	–	22
Group excluding joint ventures and associates	2,440	1,383

**note** • Cumulative goodwill relating to acquisitions made prior to 1998, which was deducted from reserves, amounts to £1,307m (1999: £1,870m). During 2000 Pearson plc received £27m on the issue of shares in respect of the exercise of options awarded under various share option plans. Employees paid £19m to the Group for the issue of these shares and the balance of £8m comprised contributions to the qualifying employee share ownership trust (QUEST) from subsidiary undertakings. The Group has taken advantage of the exemption available by UITF abstract 17 and has not incurred a charge on options granted at a discount to market value for its Inland Revenue approved SAYE schemes. At 31 December 2000 £2m of proceeds on the issue of shares were in transit.

## NOTES TO THE ACCOUNTS (CONTINUED)

### 27. ACQUISITIONS

In May 2000 the Group acquired Dorling Kindersley plc and in September 2000 the Group acquired National Computer Systems Inc (NCS). In February 2000 the Group combined its Asset Valuation business with Data Broadcasting Inc (DBC) and retained a 60% shareholding in the new combined business. In July 2000 the Group combined its television business with CLT-Ufa and retained a 22% shareholding in the new combined business, the RTL Group. All acquisitions and combinations have been consolidated applying acquisition accounting principles.

#### a. Acquisition of subsidiaries and businesses

						2000	1999
<i>all figures in £ millions</i>	Dorling Kindersley	NCS	DBC	RTL	other	total	total
Tangible fixed assets	10	115	11	–	11	147	(4)
Joint ventures	2	–	–	–	–	2	–
Associates	–	–	122	183	–	305	–
Fixed asset investments	–	29	8	–	1	38	–
Stocks	38	32	–	–	11	81	(2)
Debtors	40	102	9	–	24	175	9
Current asset investments	–	–	–	–	–	–	27
Creditors	(106)	(71)	(31)	–	(47)	(255)	(20)
Provisions	(2)	(20)	(1)	–	(10)	(33)	10
Deferred taxation	–	–	6	–	2	8	1
Net borrowing acquired	(49)	9	31	–	(4)	(13)	–
	(67)	196	155	183	(12)	455	21
Equity minority interests	–	–	(99)	–	(2)	(101)	32
Net assets acquired at fair value	(67)	196	56	183	(14)	354	53
Fair value of consideration:							
Cash	(317)	(1,709)	(2)	–	(232)	(2,260)	(267)
Television assets contributed	–	–	–	(284)	–	(284)	–
Deferred cash consideration	–	(3)	–	–	(36)	(39)	(4)
Costs accrued	(1)	(1)	–	(20)	(1)	(23)	(2)
Net prior year adjustments	–	–	–	–	4	4	33
Replacement options granted	–	–	–	–	(5)	(5)	–
	(318)	(1,713)	(2)	(304)	(270)	(2,607)	(240)
Goodwill previously written off on businesses combined	–	–	(73)	(512)	–	(585)	–
Total consideration	(318)	(1,713)	(75)	(816)	(270)	(3,192)	(240)
<b>Goodwill arising</b>	<b>385</b>	<b>1,517</b>	<b>19</b>	<b>633</b>	<b>284</b>	<b>2,838</b>	<b>187</b>
Analysed as:							
Goodwill written off to reserves	–	–	–	–	(1)	(1)	–
Goodwill attributable to associates	–	–	–	633	–	633	–
Goodwill attributable to subsidiaries	385	1,517	19	–	285	2,206	187
	385	1,517	19	633	284	2,838	187

**note** • Goodwill written off to reserves relates to acquisitions made before 1 January 1998.

						2000
<i>all figures in £ millions</i>	Dorling Kindersley	NCS	DBC	RTL	other	total
<b>Acquisition fair values</b>						
Book value of net assets acquired/combined	(3)	178	52	147	11	385
Fair value adjustments	(64)	18	103	36	(23)	70
Fair value to the Group	(67)	196	155	183	(12)	455

**note** • Other fair value adjustments comprise the revaluation of net assets.

## 27. ACQUISITIONS (CONTINUED)

### b. Dorling Kindersley

<i>all figures in £ millions</i>	book value at 9 May 2000	accounting policy alignment	revaluations	provisional fair value 31 Dec 2000
Tangible fixed assets	18	(1)	(7) <sup>a</sup>	10
Joint ventures	2	–	–	2
Stocks	85	(35)	(12) <sup>b</sup>	38
Debtors	48	(1)	(7) <sup>c</sup>	40
Creditors	(106)	–	–	(106)
Provisions	(1)	–	(1)	(2)
Net borrowing	(49)	–	–	(49)
<b>Net liabilities acquired</b>	<b>(3)</b>	<b>(37)</b>	<b>(27)</b>	<b>(67)</b>

**note** • Dorling Kindersley was acquired in May 2000. All fair value adjustments are provisional. These adjustments will be finalised in the 2001 financial statements when a detailed review of fair values has been completed.

#### Accounting policy alignment

The accounting policies of Dorling Kindersley have been changed to bring them into line with the accounting policies of Penguin. The most significant changes are to expense internal pre-publication costs, which were carried in stock until the publication of a title, and to align policies on stock provisioning.

#### Revaluations

a Fixed assets have been reduced to write down certain back office software development costs to their recoverable amount.

b Work in progress and finished goods amounting to £12m have been written off in respect of obsolete product to bring the value down to its net realisable value.

c Debtors have been reduced by £7m to bring the value down to its net realisable value.

<i>all figures in £ millions</i>	1 July 1999 to 9 May 2000	1 July 1998 to 30 June 1999
<b>Dorling Kindersley financial information</b>		
Sales	151	198
Operating (loss)/profit	(26)	12
Exceptional operating items	(28)	–
Non-operating items	–	(1)
(Loss)/profit before taxation	(56)	11
Taxation	1	(4)
(Loss)/profit for the financial period	(55)	7
Other net gains and losses recognised in reserves	–	(1)
Total recognised (losses)/gains relating to the period	(55)	6

**note** • The above results are based on the accounting policies of Dorling Kindersley prior to acquisition.

## NOTES TO THE ACCOUNTS (CONTINUED)

### 27. ACQUISITIONS (CONTINUED)

#### c. National Computer Systems

<i>all figures in £ millions</i>	book value at 8 Sept 2000	revaluations	provisional fair value 31 Dec 2000
Tangible fixed assets	114	1	115
Fixed asset investments	29	–	29
Stocks	31	1	32
Debtors	104	(2)	102
Creditors	(108)	37 <sup>a</sup>	(71)
Provisions	–	(20) <sup>b</sup>	(20)
Deferred taxation	(1)	1	–
Net cash	9	–	9
<b>Net assets acquired</b>	<b>178</b>	<b>18</b>	<b>196</b>

**note** • NCS was acquired in September 2000. All fair value adjustments are provisional. These adjustments will be finalised in the 2001 financial statements when a detailed review of fair values has been completed.

#### Revaluations

a Current taxation payable has been reduced to reflect the receipt of £29m post acquisition which related to pre-acquisition items. Creditors of £6m have been moved to provisions to more accurately reflect the nature of the liability and creditors of £2m no longer required have been released.

b Additional provisions have been made of which £8m relates to severance obligations existing at the acquisition date, £3m relates to various outstanding claims and £3m relates to deferred consideration in respect of earlier acquisitions.

<i>all figures in £ millions</i>	30 Jan 2000 to 8 Sept 2000	1 Feb 1999 to 29 Jan 2000
<b>NCS financial information</b>		
Sales	308	417
Operating profit	27	46
Profit before taxation	26	45
Taxation	(10)	(17)
Profit for the financial period	16	28
Other net gains and losses recognised in reserves	–	1
Total recognised gains relating to the period	16	29

**note** • The above results are based on the accounting policies of NCS prior to acquisition.

## 27. ACQUISITIONS (CONTINUED)

### d. Data Broadcasting Corporation Inc – combination of assets

On 29 February 2000 the Group combined its Asset Valuation business with Data Broadcasting Corporation Inc (DBC) and retained a 60% shareholding in the new combined business. The difference between the value of the net assets of the Group's Asset Valuation business contributed and the fair value of the Group's share of the net assets of the DBC business acquired has been taken to goodwill.

<i>all figures in £ millions</i>	book value at 29 Feb 2000	revaluations	provisional fair value 31 Dec 2000
Associates	20	102	122
Other net assets	32	1	33
<b>Net assets of DBC</b>	<b>52</b>	<b>103</b>	<b>155</b>
DBC assets not attributable to Pearson (40%)			(62)
Share of Asset Valuation business assets no longer attributable to Pearson			(37)
			(99)
			56

**note** • All fair value adjustments are provisional. These adjustments will be finalised in the 2001 financial statements when a detailed review of fair values has been completed.

#### Revaluations

The carrying value of the associate, CBSMarketwatch, has been increased to reflect its market value, based on the quoted share price, at the date of acquisition.

<i>all figures in £ millions</i>	2000
<b>Goodwill arising on combination</b>	
Share of net assets of DBC attributable to Pearson (60% of £155m)	93
Share of net assets of Asset Valuation business contributed (40% of £92m)	(37)
Goodwill previously written off to reserves	(73)
Costs	(2)
	(112)
<b>Goodwill arising</b>	<b>19</b>

**note** • The net assets of the Group's Asset Valuation business contributed amounted to £92m.

<i>all figures in £ millions</i>	1 Jan 2000 to 29 Feb 2000	1 Jan 1999 to 31 Dec 1999
<b>DBC financial information</b>		
Sales	23	110
Operating loss	(1)	(3)
Non-operating items	(4)	(14)
Loss before taxation	(5)	(17)
Taxation	(1)	(6)
Loss for the financial period	(6)	(23)
Other net gains and losses recognised in reserves	(1)	–
Total recognised losses relating to the period	(7)	(23)

**note** • The above results are based on the accounting policies of DBC prior to acquisition.

## NOTES TO THE ACCOUNTS (CONTINUED)

### 27. ACQUISITIONS (CONTINUED)

#### e. RTL – combination of assets

On 25 July 2000 the Group combined its television business with CLT-Ufa and retained a 22% shareholding in the new combined business, the RTL Group. The difference between the value of the net assets of the Group's television business contributed and the fair value of the Group's share of the net assets of the CLT-Ufa business acquired has been taken to goodwill.

<i>all figures in £ millions</i>	book value at 25 July 2000	revaluations	provisional fair value 31 Dec 2000
<b>Share of net assets</b>	147	36	183

**note** • All fair value adjustments are provisional. These adjustments will be finalised in the 2001 financial statements when a detailed review of fair values has been completed.

#### Revaluations

Fixed assets have been revalued to their fair market value.

<i>all figures in £ millions</i>	2000
<b>Television assets contributed</b>	
Intangible assets	(68)
Tangible fixed assets	(56)
Associates	(65)
Fixed asset investments	(75)
Stocks	(63)
Debtors	(95)
Creditors	150
Provisions	19
Deferred taxation	8
Equity minority interests	1
Net cash	(40)
Net assets of Group's television business contributed	(284)
Goodwill previously written off to reserves	(512)
Costs	(20)
Share of net assets of RTL Group attributable to Pearson	183
<b>Goodwill arising</b>	633

#### f. Cash flow from acquisitions

<i>all figures in £ millions</i>	2000	1999
Cash – current year acquisitions (see page 86)	2,260	267
Deferred payments for prior year acquisitions and other items	16	(18)
<b>Net cash outflow</b>	2,276	249

**note** • Contributions to the cash flow from acquisitions in 2000 are as follows: net cash outflow from operating activities £(44)m, returns on investments and servicing of finance £(1)m, taxation £(3)m and capital expenditure and financial investment £1m.

## 28. DISPOSALS

*all figures in £ millions*

	2000	1999
<b>Disposal of subsidiaries and businesses</b>		
Intangible assets	(35)	(1)
Tangible fixed assets	(3)	(14)
Stocks	(18)	(4)
Debtors	(4)	(20)
Creditors	–	22
Provisions	7	5
Deferred taxation	–	1
Equity minority interest	(50)	–
Net cash	–	(3)
Net assets disposed of	(103)	(14)
Proceeds received	192	57
Costs	(27)	(19)
Net prior year adjustments	(5)	(5)
Profit on sale	57	19
Goodwill written back from reserves	(27)	(63)
<b>Net profit/(loss) on sale</b>	<b>30</b>	<b>(44)</b>

*all figures in £ millions*

	2000	1999
<b>Total goodwill written back from reserves</b>		
On disposal of subsidiaries	27	63
On disposal of associates (see note 15)	41	–
	<b>68</b>	<b>63</b>

*all figures in £ millions*

	2000	1999
<b>Cash flow from disposals</b>		
Cash – current year disposals	192	57
Costs paid	(27)	(9)
Deferred receipts and payments from prior year disposals and other amounts	(7)	(4)
<b>Net cash inflow</b>	<b>158</b>	<b>44</b>

**note** • Contributions to the cash flow from disposals in 2000 are as follows: net cash outflow from operating activities £(8)m and taxation £(3)m.

## NOTES TO THE ACCOUNTS (CONTINUED)

### 29. NOTES TO CONSOLIDATED STATEMENT OF CASH FLOWS

<i>all figures in £ millions</i>	2000			1999		
	continuing	discontinued	total	continuing	discontinued	total
<b>a. Reconciliation of operating profit to net cash inflow from operating activities</b>						
Operating profit – total	203	8	211	270	48	318
Share of operating loss/(profit) of joint ventures and associates	19	(8)	11	(23)	(48)	(71)
Depreciation charges	100	–	100	82	–	82
Goodwill amortisation	188	–	188	130	–	130
(Increase) in stocks	(97)	–	(97)	(57)	–	(57)
Decrease/(increase) in debtors	53	–	53	(71)	–	(71)
(Decrease)/increase in creditors	(119)	–	(119)	127	–	127
(Decrease) in operating provisions	(4)	–	(4)	(33)	–	(33)
Other and non-cash items	18	–	18	8	–	8
<b>Net cash inflow from operating activities</b>	<b>361</b>	<b>–</b>	<b>361</b>	<b>433</b>	<b>–</b>	<b>433</b>
Purchase of fixed assets and finance lease payments	(149)	–	(149)	(113)	–	(113)
Sale of operating tangible fixed assets	22	–	22	24	–	24
Dividends from associates	11	38	49	12	32	44
Other	(8)	–	(8)	8	–	8
<b>Operating cash flow</b>	<b>237</b>	<b>38</b>	<b>275</b>	<b>364</b>	<b>32</b>	<b>396</b>
Analysed between:						
Operating cash flow before internet enterprises and other items	542	38	580	508	32	540
Cash effect of other items:						
Dorling Kindersley exceptional payments	(46)	–	(46)	–	–	–
Integration costs:						
Simon & Schuster	(27)	–	(27)	(110)	–	(110)
Dorling Kindersley	(25)	–	(25)	–	–	–
NCS	(9)	–	(9)	–	–	–
Cash effect of internet enterprises	(198)	–	(198)	(34)	–	(34)
<b>Operating cash flow</b>	<b>237</b>	<b>38</b>	<b>275</b>	<b>364</b>	<b>32</b>	<b>396</b>

**note** • The Dorling Kindersley exceptional payments are in respect of creditors on the acquisition balance sheet beyond normal trading terms.



## 29. NOTES TO CONSOLIDATED STATEMENT OF CASH FLOWS (CONTINUED)

<i>all figures in £ millions</i>	cash	over-drafts	sub-total	short-term deposits	debt due within one year	debt due after one year	finance leases	total
<b>b. Analysis of net debt</b>								
At 31 December 1999	288	(38)	250	40	(9)	(2,276)	(15)	(2,010)
Exchange differences	14	(7)	7	(1)	(1)	(122)	(1)	(118)
Acquired with subsidiary*	–	–	–	–	–	–	(11)	(11)
Television assets contributed*	–	–	–	(82)	–	60	2	(20)
Debt issue costs	–	–	–	–	–	4	–	4
Other non-cash items	–	–	–	–	–	(17)	(1)	(18)
Net cash flow	123	(65)	58	134	8	(354)	10	(144)
<b>At 31 December 2000</b>	<b>425</b>	<b>(110)</b>	<b>315</b>	<b>91</b>	<b>(2)</b>	<b>(2,705)</b>	<b>(16)</b>	<b>(2,317)</b>
At 31 December 1998	305	(67)	238	40	(5)	(2,552)	(19)	(2,298)
Exchange differences	(23)	3	(20)	1	–	(30)	(1)	(50)
Disposed with subsidiary*	–	–	–	–	–	–	1	1
Debt issue costs	–	–	–	–	–	5	–	5
Other non-cash items	–	–	–	–	–	(5)	(7)	(12)
Net cash flow	6	26	32	(1)	(4)	306	11	344
<b>At 31 December 1999</b>	<b>288</b>	<b>(38)</b>	<b>250</b>	<b>40</b>	<b>(9)</b>	<b>(2,276)</b>	<b>(15)</b>	<b>(2,010)</b>

\* Excluding cash and overdrafts.

**note** • Finance leases are included within other creditors in the balance sheet (see note 22).

<i>all figures in £ millions</i>	2000	1999
<b>c. Reconciliation of net cash flow to movement in net debt</b>		
Decrease in net debt from net cash flow	58	32
Decrease/(increase) in net debt from management of liquid resources	134	(1)
(Increase)/decrease in net debt from other borrowings	(346)	302
Decrease in finance leases	10	11
Television assets contributed	(20)	–
Acquired with subsidiary	(11)	–
Disposed with subsidiary	–	1
Debt issue costs	4	5
Other non-cash items	(18)	(12)
Exchange differences	(118)	(50)
Movement in net debt in the year	(307)	288
Net debt at beginning of the year	(2,010)	(2,298)
<b>Net debt at end of the year</b>	<b>(2,317)</b>	<b>(2,010)</b>

**d. Tax paid** includes £30m (1999: £100m) relating to items excluded from operating profit.

## 30. CONTINGENT LIABILITIES

There are contingent Group and company liabilities in respect of indemnities, warranties and guarantees in relation to former subsidiary undertakings and in respect of guarantees in relation to subsidiaries and associated undertakings. In addition there are contingent liabilities of the Group in respect of legal claims. None of these claims is expected to result in a material gain or loss to the Group.

## NOTES TO THE ACCOUNTS (CONTINUED)

### 31. COMMITMENTS UNDER LEASES

At 31 December 2000, the Group had commitments under leases other than finance leases, to make payments in 2001 as follows:

<i>all figures in £ millions</i>	land and buildings	other
<b>For leases expiring:</b>		
In 2001	7	3
Between 2002 and 2005	37	14
Thereafter	61	1
	105	18

### 32. RELATED PARTIES

**Joint ventures and associates** • Loans and equity advanced to joint ventures and associates during the year and at the balance sheet date are shown in notes 14 and 15. Amounts falling due from joint ventures and associates are set out in note 18. Dividends receivable from joint ventures and associates are set out in notes 14 and 15. Details of individually significant transactions are shown below.

**a.** During 2000, the Group combined its television business with CLT-Ufa and retained a 22% stake in the new combined business, the RTL Group. Significant related party transactions in respect of the television business were as follows.

**Channel 5 Television Group Ltd** • During the year the Group provided £22m (1999: £31m) of programming to Channel 5 Broadcasting Ltd, a wholly owned subsidiary of Channel 5 Television Group Ltd, and undertook transmission to the value of £2m (1999: £3m) for Channel 5 Engineering Services Ltd, a subsidiary of Channel 5 Television Group Ltd. At 31 December 1999 £6m was outstanding. During the year the Group paid £4m (1999: £4m) in respect of consortium relief.

**Grundy associates** • During the year the Group received £2m (1999: £3m) for management fees, format rights and royalties from a number of associates of Grundy Worldwide Ltd, of which £2m was outstanding at 31 December 1999. No individual transactions were material to the Group.

**Magyar-RTL** • During the year the Group provided programmes and services to the value of £nil (1999: £1m) none of which was outstanding at 31 December 1999.

**b. Lazard Partnership** • During the year the Group sold its interests in the three Lazard Houses.

The Group periodically placed funds on deposit with the Lazard Houses. The investments were made on an arm's-length basis and no transactions were individually material in the context of the Group treasury transactions. The Group also used the Lazard Houses to provide professional advice. Fees for such services for the period were not material to either party.

### 33. COMPANY BALANCE SHEET as at 31 Dec 2000

all figures in £ millions

	2000	1999	note
<b>Fixed assets</b>			
Tangible fixed assets	7	–	34
Investments: subsidiaries	2,586	2,401	34
Investments: own shares held	64	8	34
	<b>2,657</b>	<b>2,409</b>	
<b>Current assets</b>			
Debtors:			
Subsidiaries – due within one year	2,841	2,233	
Associates – due within one year	65	–	
Subsidiaries – due after more than one year	2,289	1,403	
Taxation	15	–	
Other debtors	11	6	
Prepayments and accrued income	4	1	
Cash at bank and in hand	56	7	20
	<b>5,281</b>	<b>3,650</b>	
<b>Creditors – amounts falling due within one year</b>			
Short-term borrowing	(225)	(130)	21
Subsidiaries	(983)	(1,844)	
Taxation	–	(20)	
Other creditors	(9)	(4)	
Accruals and deferred income	(20)	(30)	34
Dividends	(106)	(85)	
	<b>(1,343)</b>	<b>(2,113)</b>	
<b>Net current assets</b>	<b>3,938</b>	<b>1,537</b>	
<b>Total assets less current liabilities</b>	<b>6,595</b>	<b>3,946</b>	
<b>Creditors – amounts falling due after more than one year</b>			
Medium and long-term borrowing	(1,718)	(1,412)	21
Subsidiaries	(468)	(280)	
Accruals and deferred income	–	(3)	34
<b>Provisions for liabilities and charges</b>			
Deferred taxation	–	(1)	34
Other provisions for liabilities and charges	(2)	(2)	
	<b>(2,188)</b>	<b>(1,698)</b>	
<b>Net assets</b>	<b>4,407</b>	<b>2,248</b>	
<b>Capital and reserves</b>			
Called up share capital	199	153	25
Share premium account	2,440	517	34
Special reserve	397	397	34
Other reserves	50	50	34
Profit and loss account	1,321	1,131	34
<b>Equity shareholders' funds</b>	<b>4,407</b>	<b>2,248</b>	

The financial statements were approved by the board of directors on 5 March 2001 and signed on its behalf by  
**LORD STEVENSON • JOHN MAKINSON**

## NOTES TO THE ACCOUNTS (CONTINUED)

### 34. NOTES TO THE COMPANY BALANCE SHEET

*all figures in £ millions*

	2000	1999
<b>Tangible fixed assets (leasehold property)</b>		
Cost	8	1
Depreciation	(1)	(1)
<b>Net book value</b>	<b>7</b>	<b>–</b>

**note** • The company had capital commitments for fixed assets already under contract of £10m.

*all figures in £ millions*

<b>Investment in subsidiaries</b>	
At 31 December 1999	2,401
Acquisitions	318
Subscription for additional share capital in subsidiaries	193
Disposals	(318)
Provision for diminution in value	(8)
<b>At 31 December 2000</b>	<b>2,586</b>

**note** • Shares are stated at cost less provisions for diminution in value or directors' valuations.

*all figures in £ millions*

<b>Deferred taxation</b>	
At 31 December 1999	(1)
Credit for the year	1
<b>At 31 December 2000</b>	<b>–</b>

**Own shares held** • Amounts included within own shares held relate to Pearson plc ordinary shares held in respect of the Pearson plc Employee Share Ownership Trusts (see note 16).

**Accruals and deferred income** • Accruals and deferred income includes £2m (1999: £4m) relating to the unamortised profit arising out of the unwinding of a sterling interest rate swap in 1994. The swap was arranged in 1992 in connection with the issue of £100m 10.75% Sterling Bonds 2002. The profit is being amortised over the remaining life of the bonds. None of the amount falls due after one year.

*all figures in £ millions*

	share premium account	special reserve	other reserves	profit and loss account	total
<b>Reserves</b>					
<b>Summary of movements</b>					
At 31 December 1999	517	397	50	1,131	2,095
Premium on issue of 185m equity shares	1,923	–	–	–	1,923
Replacement options granted on acquisition of subsidiary	–	–	–	6	6
Profit for the financial year	–	–	–	348	348
Dividends	–	–	–	(164)	(164)
<b>At 31 December 2000</b>	<b>2,440</b>	<b>397</b>	<b>50</b>	<b>1,321</b>	<b>4,208</b>

**note** • The special reserve represents the cumulative effect of cancellation of the company's share premium account. As permitted by section 230(4) of the Companies Act 1985, only the Group's profit and loss account has been presented.

## PRINCIPAL SUBSIDIARIES AND ASSOCIATES

as at 31 Dec 2000

country of  
incorporation  
or registration

### Subsidiaries

The principal operating subsidiaries are listed below. They operate mainly in the countries of incorporation or registration, the investments are in equity share capital and they are all 100% owned unless stated otherwise.

#### Pearson Education

Addison Wesley Longman Inc.	US
Addison Wesley Educational Publishers Inc.	US
Macmillan USA Inc.	US
Pearson Education Ltd	England
Prentice Hall Inc.	US
NCS Pearson Inc.	US

#### FT Group

Financial Times Group Ltd*	England
Financial Times Business Ltd	England
Data Broadcasting Inc. (60%)	US
Les Echos SA	France
Recoletos Compañía Editorial SA (78.97%)	Spain

#### The Penguin Group

Penguin Putnam Inc.	US
The Penguin Publishing Co Ltd	England
Penguin Books Australia Ltd	Australia
Dorling Kindersley Holdings Ltd*	England

\*Direct investment of Pearson plc.

	country of incorporation or registration	class of share	beneficial interest %	accounting year end
<b>Associates</b>				
<b>FT Group</b>				
The Economist Newspaper Ltd	England	Ord 5p	50	March
		'B' 5p	100	
		'A' 5p	Nil	
		Trust 5p	Nil	
<b>Television</b>				
RTL Group SA	Luxembourg	Ord voting	21.6	December

## FIVE YEAR SUMMARY

<i>all figures in £ millions</i>	1996	1997	1998	1999	2000
Sales – continuing operations	1,830	2,011	2,251	3,332	3,874
Sales – underlying growth (%)	5.6	6.5	6.7	7.3	9.2
EBITDA* – before internet enterprises	352	393	455	670	780
Trading margin – before internet enterprises (%)	9.2	11.5	13.1	15.2	16.5
Operating profit before internet enterprises, goodwill and other items					
Pearson Education	60	60	99	257	320
FT Group	89	108	118	150	211
The Penguin Group	27	58	48	65	79
Television	40	26	61	68	68
Continuing operations	216	252	326	540	678
Internet enterprises investment					
Pearson Education	–	–	–	(3)	(83)
FT Group	–	–	–	(36)	(113)
	–	–	–	(39)	(196)
Adjusted eps – before internet enterprises**	27.3p	31.2p	37.5p	47.6p	54.6p
Adjusted eps – after internet enterprises**	27.3p	31.2p	37.5p	43.3p	31.9p
Dividends per share**	16.1p	17.4p	18.8p	20.1p	21.4p
Net assets	393	156	1,084	1,327	4,209
Deferred taxation and other provisions	189	212	273	227	266
Net debt	430	707	2,279	1,995	2,301
Capital employed	1,012	1,075	3,636	3,549	6,776
Free cash flow per share* – before internet enterprises**	22.0p	19.9p	40.3p	48.5p	49.1p

\*Before goodwill, integration costs and non-operating items.

\*\*Restated to reflect the rights issue of equity shares during 2000.

## CORPORATE AND OPERATING MEASURES

### Sales – underlying growth

Sales growth excluding the impact of acquisitions and disposals and movements in exchange rates.

<i>all figures in £ millions</i>	2000
Underlying increase	264
Portfolio changes	115
Foreign exchange	125
Internet enterprises	38
Total sales increase	542
Underlying increase	9.2%

### EBITDA\* – before internet enterprises

Earnings before interest, taxation, depreciation and amortisation, seen to be a close proxy for operating cash flow.

<i>all figures in £ millions</i>	2000
Operating profit (before internet enterprises)	686
Depreciation (before internet enterprises)	94
EBITDA	780

### Trading margin – before internet enterprises

Trading profit (operating profit excluding profit from joint ventures, associates and investments) as a proportion of sales.

<i>all figures in £ millions</i>	2000
Total operating profit – Group	450
Internet enterprises – Group	183
Investment income	(3)
Trading profit	630
Sales	3,829
Trading margin	16.5%

### Adjusted eps – before internet enterprises

Earnings excluding non-trading or recurring items (see note 10 for a full definition) divided by the weighted average number of shares in issue.

<i>all figures in £ millions</i>	2000
Adjusted earnings	397
Weighted average number of shares in issue (millions)	727.7
Adjusted eps	54.6p

### Free cash flow per share\* – before internet enterprises

Operating cash flow less taxation paid on operating profits and interest paid, divided by the weighted average number of shares in issue.

<i>all figures in £ millions</i>	2000
Operating cash flow	580
Taxation paid on operating profits	(75)
Interest paid	(148)
Free cash flow	357
Weighted average shares in issue (millions)	727.7
Free cash flow per share	49.1p

\*Before goodwill, integration costs and non-operating items.

## SHAREHOLDER INFORMATION

**Payment of dividends to mandated accounts** • Where shareholders have given instruction for payment to be made direct into a bank or building society, this is done through the Bankers Automated Clearing System (BACS), with the associated tax voucher showing the tax credit attributable to the dividend payment sent direct to the shareholder at the address shown on our register. If you wish the tax voucher to be sent to your bank or building society, please inform our registrar, Lloyds TSB Registrars, The Causeway, Worthing, West Sussex BN99 6DA. Telephone 0870 600 3986 or, for those shareholders with hearing difficulties, textphone number 0870 600 3950.

**Dividend reinvestment plan (DRIP)** • The plan provides the benefit of giving shareholders the right to buy the company's shares on the London stock market with the cash dividend. If you would like further information about the DRIP, please contact Lloyds TSB Registrars. Telephone 0870 241 3018.

**Personal Equity Plans (PEPs) and Individual Savings Accounts (ISAs)** • The government no longer permits investment to be made in PEPs, although existing PEPs may be continued. Existing Corporate PEP and Single Company PEP holders who require further information about their PEPs should ring the Halifax helpline on 0870 606 6417. Lloyds TSB Registrars now offer ISAs in Pearson shares. They can be contacted for information on 0870 242 4244.

**Low cost share dealing facility** • A postal facility, which provides a simple, low cost way of buying and selling Pearson shares, is available through the company's stockbroker, Cazenove & Co., 12 Tokenhouse Yard, London EC2R 7AN. Telephone 020 7588 2828.

**Information about the Pearson share price** • The current price of Pearson ordinary shares can be obtained from Financial Times CityLine. Telephone 0891 433620. Calls are charged at 60p per minute.

**American Depositary Receipts (ADRs)** • Pearson's ordinary shares are now listed on the New York Stock Exchange in the form of ADRs and traded under the symbol PSO. Each ADR represents one ordinary share. Voting rights as a shareholder may be exercised through The Bank of New York, ADR Department, 101 Barclay Street, New York, New York 10286, telephone 800 BNY ADRS (toll free within the US) or (1) 908 769 9835 (outside the US). All enquiries regarding ADR holder accounts and payment of dividends should be directed to The Bank of New York, the authorised depository bank for Pearson's ADR programme, at the address given above. Pearson will file with the Securities and Exchange Commission a report on Form 20-F that will contain a US GAAP reconciliation.

**Advisers** • *auditors* PricewaterhouseCoopers • *bankers* HSBC Bank Plc • *broker* Cazenove & Co. • *financial advisers* Lazard Brothers & Co. Limited, J. Henry Schroder & Co. Limited • *solicitors* Freshfields Bruckhaus Deringer, Herbert Smith and Morgan, Lewis & Bockius.

### FINANCIAL CALENDAR FOR 2001

EX-DIVIDEND DATE	Wednesday	14 March
RECORD DATE	Friday	16 March
ANNUAL GENERAL MEETING	Friday	27 April
LAST DATE FOR DIVIDEND REINVESTMENT ELECTION	Thursday	17 May
PAYMENT DATE FOR DIVIDEND AND SHARE PURCHASE DATE FOR DIVIDEND REINVESTMENT	Friday	1 June
INTERIM RESULTS	Monday	30 July
INTERIM DIVIDEND	Friday	26 October